THE KENYA MICROINSURANCE POLICY FRAMEWORK PAPER
ABSTRACT

The Microinsurance Policy Paper maps out the Insurance Regulatory Authority's (IRA) future path in the regulation and supervision of microinsurance in Kenya. It spells out the strategic approach chosen, and the principles and key elements underlying this process.

In so doing, the Paper makes policy recommendations that lay the foundations for the drafting of a legal and regulatory framework aimed at enabling the microfinance market to develop in a sound and customer-oriented environment. Microinsurance is insurance that is adapted to meet the requirements and needs specific to low-income households. It is considered to have considerable potential for helping low-income households to manage their financial risks, for assisting insurers and intermediaries to expand their markets and for providing governments with a way to rely on privately-driven insurance in place of state funding schemes.

Microinsurance is an emerging trend in the Kenyan market and as such its regulation has not been provided for in the existing insurance law. It is provided by a variety of institutions, and should be delivered in a way appropriate to low-income households with the products being designed as commercial insurance products that are fully funded by the premiums paid.

Microinsurance should be managed by insurers and other providers in accordance with generally accepted insurance principles and practices as it forms part of the broader insurance market. However, it is distinguished by its focus on the low-income sector which has a number of repercussions for the way that it is provided and accessed.

Microinsurance offers affordable premiums; has limited risk cover; uses easily understood contracts; has few exclusions; uses appropriate delivery channels; provides fast and efficient claims settlement and is a commercial product. It is not a national insurance or a social programme; simply a low level of insurance covers or funded by a general loan loss provision
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ABBREVIATIONS

For purposes of this policy, unless otherwise stated, the following abbreviations shall apply:

A2II - Access to Insurance Initiative
AKI - Association of Kenya Insurers
Cenfri- Centre For Financial Regulation and Inclusion
FANAF - Fédération des Sociétés d'Assurances de Droit National Africaines
FSD - Financial Sector Deepening
IAIS - International Association of Insurance Supervisors
ICT - Information, Communication and Technology
ILO - International Labour Organization
IRA - Insurance Regulatory Authority
IT - Information Technology
JWG - Joint Working Group
MDG - Millennium Development Goals
MFI - Micro Finance Institution
MI - Micro Insurance
MIN - Micro Insurance Network
NGO - Non Governmental Organization
NHIF - National Hospital Insurance Fund
NSSF - National Social Security Fund
R&D - Research and Development
SACCO- Savings and Credit Society
SME - Small and Medium Enterprises
US$ - United States Dollar
WB - World Bank
EXECUTIVE SUMMARY

This paper considers the potential role, opportunities and challenges for developing a microinsurance policy framework for the Kenyan market. Kenya currently does not have a separate definition for microinsurance; accordingly, the regulatory framework and Proclamation do not make any concessions to microinsurance. Microinsurance is defined as insurance that is accessible to the low-income population, potentially provided by a variety of providers and managed in accordance with generally accepted insurance practices. This means that it should be funded by premiums and managed based on generally accepted risk-management principles. It therefore excludes social welfare as well as emergency assistance provided by governments.

The need for Microinsurance regulatory framework arose out of the concerns about the risk of consumers exposed to the unregulated products and services which target the most vulnerable strata of the population. Various scenarios have been looked at. According to the Landscaping Study of the Microinsurance Centre, about 3.5 million people in Africa have access to microinsurance. In most sub-Saharan countries less than 2% of the poor and vulnerable have access to Microinsurance. Africa, a continent with many infectious diseases, limited infrastructure, largely agrarian populations and fragile economies, low-income people are exposed to a multitude of risks that keep them in, or push them back into, poverty. Illness, death, natural disasters, damage to and loss of property, and accidents all can have devastating effects on livelihoods without a buffer to help people mitigate the financial impact of these events.

As opposed to people in developed countries, most individuals in Africa cannot count on government safety nets to successfully mitigate significant portions of

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1 The Landscape of Microinsurance in the 100 poorest Countries, MicroInsurance Centre (2007)
their risks. Despite emergence of potentially effective government schemes in a few African countries, outreach is still very low (ILO 2008, Leppert 2009) and it is unlikely that those schemes would provide effective protection in the medium term. Failure of informal schemes and government-led programs opens a significant window of opportunity for Microinsurance to decrease low-income households’ vulnerability to risks and help smooth their way out of poverty.

In regard to other initiatives, the G20 commitment to financial inclusion recognises the more than two billion adults who do not have access to formal or semi-formal financial services and the millions of micro, small and medium-sized firms that also face a serious lack of access to finance.

The International Association of Insurance Supervisors (IAIS) together with the Microinsurance Network (MIN), constituted a Joint Working Group (JWG) to serve as a global dialogue platform for identifying issues, undertaking studies and sharing knowledge on micro insurance. This culminated in the launch of the Access to Insurance Initiative (A2II)\(^2\) in 2010. The purpose of the Initiative is to strengthen the capacity of policymakers, regulators, and supervisors seeking to advance insurance market access.

The Kenya Insurance Industry is characterized by a small market focused on corporate and asset markets which gives rise to stiff competition. Insurers have not focused on widespread growth in the untapped market. A different concept of insurance is therefore necessary to facilitate the required growth by tapping into the potential existing in the informal sector.

It is increasingly being recognized that the Microinsurance agenda is inevitable as a form of financial inclusion and avenue for increasing insurance penetration.

\(^2\) The Access to Insurance Initiative is a global partnership between the IAIS, the German Ministry of Economic Cooperation and Development (BMZ) together with the German Technical Cooperation (GTZ) who acts on its behalf (and who hosts the Secretariat of the Initiative), the CGAP, the International Labour Organisation (ILO) and the South Africa-based FinMark Trust. (www.access-to-insurance.org)
Majority of the insured Kenyans are drawn from the formal sector which accounts for about 5% of the total population. This therefore means that most of the Kenyan population is in the informal sector that is not adequately provided for by the conventional insurance. Insurance penetration is specifically low – around 3%.

Although piecemeal amendments have been done over the years on the Insurance Act, Cap 487, Microinsurance is still regulated under miscellaneous class of insurance business in the Act. This paper therefore seeks to entrench Microinsurance as a tool for socio-economic empowerment and risk management for low income households in Kenya by setting an appropriate policy for harmonizing, facilitating, and encouraging provision of the services in a well managed and regulated environment. In working towards these objectives, the policy framework is underpinned by the National agenda of Financial Inclusion as contained in the Vision 2030 principles to reform the financial system. Access to microinsurance by the poor and disadvantaged population would contribute significantly to the achievement of the Millennium Development Goals, particularly eradicating extreme poverty and hunger (MDG 1), promoting gender equality and empowering women (MDG 3) and developing a global partnership for development (MDG 8) and specifically promote the development of the insurance sector.

The objective of financial inclusion is that individual consumers, particularly low-income consumers currently excluded from using formal financial sector services, must be able to access and on a sustainable basis use financial services that are appropriate to their needs and provided by registered financial service providers.

It is in recognition of the foregoing that towards the end of 2010 the Insurance Regulatory Authority formed a Steering Committee to drive the Microinsurance
agenda. This Committee has worked round the clock to develop this Framework paper.

Various factors affect the development of the microinsurance market. These include factors relating to the demand side, supply side and regulatory environment. On the demand side, an individual will only buy insurance if the perceived value of the insurance product exceeds the perceived opportunity cost of purchasing it. The features of the low-income and currently uninsured market were captured in the findings of the 2009 FinAccess survey.

Subsequently, Centre for Financial Regulation and Inclusion (Cenfri) analysed the low-income market’s experience of risk, as well as their perceptions of and demand for insurance products. Differences between the insured and uninsured from FinAccess survey showed that the insured are more affluent than their uninsured counterparts. The key demand factors discussed in the paper are Risk experience & perceptions and Consumer education & awareness.

Supply side factors suggest that the likelihood of positive discovery amongst low income clients depends on the distribution channel or business model used to deliver microinsurance. There are twelve factors which have been identified and discussed as affecting the supply of Microinsurance currently.

On the enabling environment various regulatory obstacles to the development of Microinsurance in Kenya were identified and discussed in the paper. It is generally agreeable that regulatory approaches are not supportive of microinsurance development.

The broad objective of this policy paper to “provide a framework for entrenching Microinsurance as a tool for socio-economic empowerment and risk management for low income households in Kenya”. Other specific objectives relating to consumer protection; stability; sound claims management; market development and appropriate regulation have also been addressed.
The paper further identifies available opportunities for the development of microinsurance as:

- Focusing on the high ratio of uninsured population
- Focusing on anchor risks like health, funeral and agricultural risks on value chains and networks
- Focusing on Banks and emerging networks
- Focusing on consumer education and awareness campaigns.
- Focusing on the available consumer protection initiatives.

To accelerate the growth of the microinsurance market in Kenya, recommendations are made in order to improve financial access by the low income population as outlined in the vision 2030. These are:

- Adoption of this proposed Microinsurance policy framework paper
- Amendment to the Insurance Act, Cap 487 as appropriate to accommodate Microinsurance;
- Drafting and gazettement of Microinsurance Regulations.
- Consider supportive registration requirements and supervision for Microinsurance players.
- Development of appropriate consumer protection initiatives
- Enhancement of Microinsurance Consumer education and awareness
- Product innovations through Research & Development
- Encouragement of creating a flexible and low-cost intermediation (Distribution channels) regime
- Development of strategic partnerships.
- Embrace Information Communications Technology (ICT)
- Development of good Corporate Governance principles
- Recognition of the role of Actuarial assessment
- Development of appropriate Reinsurance arrangements

In conclusion, socio-economic empowerment and risk management for low income households in Kenya is important to the development of the economy
as a whole and in order to encourage its’ development in the insurance industry, a supportive regulatory and legal framework is required. This policy framework paper therefore summarises the proposed regulatory framework for microinsurance in Kenya that is to be incorporated into the regulatory architecture through amendment to the existing insurance legislation. These proposals are intended to support the Government’s financial sector policy objectives of financial stability, consumer protection, financial inclusion, improved regulatory coordination, and regulatory comprehensiveness as outlined in the Vision 2030. With an emphasis on improving the access of poorer and economically vulnerable households to financial services, delivering upon these objectives is expected to ensure that the financial services sector better supports economic and employment growth and the alleviation of poverty. The microinsurance proposals highlighted here importantly reinforce this broader strategy.
1.0 INTRODUCTION

The need for enhanced access to insurance at affordable rates to the poor and low end market is well set out in the Kenya Vision 2030 and other government policy documents. Compared to some other regions in Africa, the microinsurance market in Kenya is not developed\(^3\) although commercial insurers are becoming active, and informal “insurers” are expanding with some seeking integration into the formal insurance system. With access to insurance especially micro insurance being limited, Kenya like many other developing countries has identified microinsurance as having great potential for enhancing financial inclusion and mitigating risks.

Microinsurance is specifically designed for the protection of low-income people\(^4\), with affordable insurance products to help them cope with and recover from common risks. It is a market-based mechanism that promises to support sustainable livelihoods by empowering people to adapt and withstand stress. Two-thirds of the population living in extreme poverty is classified as women often living on less than $1 per day. This category is therefore quite vulnerable to risks and without adequate mitigation measures, the probability of lapsing into a vicious cycle of poverty in high.

According to the Landscaping Study of the Microinsurance Centre, about 3.5 million people in Africa have access to microinsurance. In most sub-Saharan countries less than 2% of the poor and vulnerable have access to Microinsurance\(^5\).

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\(^3\) Access to Microinsurance is generally very limited. Even in countries with established microfinance institutions – a common delivery channel for Microinsurance – only few Microinsurance schemes are available.

\(^4\) What happens when a poor family’s breadwinner dies, when a child in a disadvantaged household is hospitalized, or the home of a vulnerable family is destroyed by fire or natural disaster? Every serious illness, every accident and every natural disaster threatens the very existence of poor people and usually leads to deeper poverty. That’s where “Microinsurance” comes in.

\(^5\) The Landscape of Microinsurance in the 100 poorest Countries, MicroInsurance Centre (2007)
A study by FinAccess conducted in 2009 revealed that only 7% of the Kenyan population has any form of insurance. It further revealed that majority of the insured are drawn from the formal sector which accounts for about 5% of the total population. This therefore means that majority of Kenyans are in the informal sector that is not adequately provided for by the conventional insurance.

Currently, the majority of insurance users are clustered in the KSh22,500 (US$ 299)- KSh40,000 (US$ 530) a month income groups, with the distribution spread evenly around this income band when including NHIF and National Social Security Fund (NSSF) usage. When excluding NHIF and NSSF, insurance usage tends to be skewed towards incomes above the KSh22,500 (US$ 299) - KSh40,000 (US$ 530) income band.

With growing markets and new players, an enabling policy environment is a prerequisite for Microinsurance to develop. Sound policies and regulations for Microinsurance encourage innovation, investment, sustainability and growth in the insurance sector while protecting consumers and the soundness of institutions. While the private sector is a key driver of Microinsurance market development, the policy framework is a crucial element.

Microinsurance is a low-price, high-volume business and its success and market sustainability is dependent on keeping the transaction costs down. Hardly any satisfactory state-run programme of insurance benefits is now available for poor population groups, people working in the informal sector and other disadvantaged individuals—and private-sector programmes are even rarer.

A number of constraints make Microinsurance look unattractive, including a lack of political will, scarcity of public funds and absence of a viable business
model. The costs of marketing and processing appear to be too high and, in view of the extremely low purchasing power of the consumer base; it cannot be easily apportioned to the target group. Such constraints make Microinsurance unattractive at the cursory level.

Findings of a study conducted in 2009 by the International Labour Organization’s (ILO’s) Microinsurance Innovation Facility and the Microinsurance Centre in collaboration with the African Insurance Organization, the Fédération des Sociétés d'Assurances de Droit National Africaines (FANAF), the ILO’s STEP Programme defines Microinsurance as an insurance product that is accessible to low-income households. Mandatory health mutual schemes for the formal sector (no option to opt-out) are not taken into account.

Such social security schemes cover over 5 million people in both Ghana and Rwanda. In addition, South Africa, Tunisia, Libya and Egypt, among others, provide some social security for health and disability risks; these systems were also excluded from the sample.

1.1 Status of Micro insurance in Africa

Low-income households are vulnerable to risks, a fact that is widely recognized as one of key drivers of underdevelopment (World Bank 2001). In Africa, a continent with many infectious diseases, limited infrastructure, largely agrarian populations and fragile economies, low-income people are exposed to a multitude of risks that keep them in, or push them back into, poverty. Illness, death, natural disasters, damage to and loss of property, and accidents all can have devastating effects on livelihoods without a buffer to help people mitigate the financial impact of these events.
As opposed to people in developed countries, most individuals in Africa cannot count on government safety nets to successfully mitigate significant portions of their risks. Despite emergence of potentially effective government schemes in a few African countries, outreach is still very low (ILO 2008, Leppert 2009) and it is unlikely that those schemes would provide effective protection in the medium term. Failure of informal schemes and government-led programs opens a significant window of opportunity for Microinsurance to decrease low-income households’ vulnerability to risks and help smooth their way out of poverty.

Policymakers and insurance supervisors in emerging markets and developing economies are increasingly becoming aware of the need to seek a healthy balance to regulation and enhancing access to quality insurance services while protecting policyholders and other beneficiaries. Governments are increasingly aware of the benefits to having inclusive insurance markets to poverty reduction and social and economic development.

Regulated insurers and a variety of intermediaries\(^6\) are increasingly recognizing the business potential of the low-income population and have been offering innovative products and distribution models. At the same time, informal entities grow in size and numbers. Governments are realizing that they lack the capacity needed for expanding the regulatory perimeter for consumer protection and market development for this population segment.

### 1.2 Other initiatives

At the Pittsburgh Summit in September 2009, G20 Leaders committed to improving access to financial services for poor people, through supporting the “safe and sound spread of new modes of financial service delivery capable of reaching the poor” and the “scale up [of] the successful models of small-and medium-sized enterprise (SME) financing”. In June 2010, G20 Finance Ministers and Central Bank Governors made a “call on relevant international

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\(^6\) Intermediaries refers to any natural person or legal entity that engages in insurance intermediation.
standard setting bodies to consider how they can further contribute to encouraging financial inclusion, consistent with their respective mandates”. In Toronto, Leaders stated that they “developed a set of principles for innovative financial inclusion, which were to form the basis of a concrete and pragmatic action plan for improving access to financial services amongst the poor. This action plan was released at the Seoul Summit.”

The G20 commitment to financial inclusion recognises the more than two billion adults who do not have access to formal or semi-formal financial services and the millions of micro, small and medium-sized firms that also face a serious lack of access to finance.

Increasing financial inclusion reduces the economic vulnerability of households, promotes economic growth, contributes to alleviating poverty and improves the quality of people’s lives. Encouraging implementation of the G20 Principles for Innovative Financial Inclusion was an important first step towards building a framework to improve access to a full range of financial services for excluded individuals, micro, small and medium enterprises.

The International Association of Insurance Supervisors (IAIS) together with the Microinsurance Network (MIN), constituted a Joint Working Group (JWG) to serve as a global dialogue platform for identifying issues, undertaking studies and sharing knowledge on micro insurance. This culminated in the launch of the Access to Insurance Initiative (A2II)7 in 2010. The purpose of the Initiative is to strengthen the capacity of policymakers, regulators, and supervisors seeking to advance insurance market access by promoting sound, effective and proportionate regulation and supervision of insurance markets that facilitate the growth in availability of insurance products appropriate for the low income consumers.

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7 The Access to Insurance Initiative is a global partnership between the IAIS, the German Ministry of Economic Cooperation and Development (BMZ) together with the German Technical Cooperation (GTZ) who acts on its behalf (and who hosts the Secretariat of the Initiative), the CGAP, the International Labour Organisation (ILO) and the South Africa-based FinMark Trust. ([www.access-to-insurance.org](http://www.access-to-insurance.org))
The JWG developed a guidance paper whose purpose is to provide guidance to insurance supervisors with the aspects or principles of regulation and supervision that are specifically relevant to enhancing inclusive insurance markets, while protecting policyholders, and contributing to the global financial stability.

The Kenya Insurance Industry is characterized by a small market focused on corporate and asset markets which gives rise to stiff competition. Insurers have not focused on widespread growth in the untapped market. A different concept of insurance is therefore necessary to facilitate the required growth by tapping into the potential existing in the informal sector.

It is increasingly being recognized that the Microinsurance agenda is inevitable as a form of financial inclusion and avenue for increasing insurance penetration. Microinsurance aims at improving financial access by the low income and economically vulnerable households in line with the Government’s financial sector policy objectives as outlined in the Vision 2030.

In Kenya, there are many smallholder farmers, small traders and manufacturers and people generating livelihoods on a small and generally vulnerable scale and constitute the base of the untapped micro insurance market. Although the banking sector has been active in tapping into this market through micro finance institutions and savings and credit co-operatives sectors, the insurance industry is only recently venturing into this market.

International experience has shown that insurance can play an important role in helping the poor manage their risks by protecting the assets and incomes of low-income households when financial losses occur. This can help prevent them from falling further into poverty in the first place, or falling deeper into poverty, as a result of having to take children out of school to work, utilise
savings, sell hard-earned assets, or obtain credit or other expensive means of post-event risk-management available to them. (CENFRI report 2010).

1.3 MI Steering Committee

It is in recognition of the foregoing that towards the end of 2010 the Insurance Regulatory Authority formed a Steering Committee to drive the Microinsurance agenda with responsibility to:-

i) Identify issues that affect Microinsurance penetration, articulate the same through research and propose solutions in form of a policy framework paper to be submitted to the government

ii) Facilitate participation of relevant stakeholders in the Steering Committee

iii) Support the development of the steering committee’s vision, goals, objectives, strategies and priorities in support of Microinsurance initiatives

iv) Agree on the work-plan and budget linked to agreed priorities, as developed by the Steering Committee

v) Undertake monitoring and evaluation and impact analysis of the Microinsurance

vi) Feed the results of projects and initiatives undertaken into the National Strategy for long term sustainability of Microinsurance in Kenya

vii) Disseminate Microinsurance information to the relevant stakeholders

viii) Advise on a strategy for Microinsurance

ix) Develop a strategic implementation framework

x) Any other assignment as directed by the appointing authority
1.4 Definition of Microinsurance

Microinsurance refers to insurance that is accessed or accessible to the low-income population (also known as the mass market), provided by a variety of different providers and managed in accordance with generally accepted insurance practice. It does not operate in isolation but forms part of the broader insurance market, distinguished by its particular market segment focus on the low-income market, which translates into distinct means of product design and distribution. This definition should simultaneously achieve two goals:

i) Reflect the features of products demanded by the low-income market;

ii) Generate sufficiently low prudential risk so that Microinsurance products can safely be provided by a wide range of Microinsurers distributing it in a straightforward manner.

These factors combined merit simplified regulatory requirements.

1.5 Microinsurance products features and standards

In order to qualify as Microinsurance, products should comply with the following product features and standards:

i) Risk only; it is proposed that risk benefits with no surrender value be included in the Microinsurance product category.

ii) Benefits provided on a sum assured basis: All Microinsurance policy benefits should be defined on a first loss or sum assured basis. First loss insurance refers to insurance that provides a defined benefit upon a defined event as opposed to indemnity insurance that indemnifies losses, i.e. pays benefits according to the actual value of the
loss suffered. This restriction is considered necessary since the loss adjustment process required for indemnity insurance is generally too costly for Microinsurance. However, should the market develop cost-effective ways to provide indemnity insurance to low-income households, the need for this provision will be reviewed. A consequence of this restriction is that asset Microinsurance policies, liability policies and accident and health policies must disclose how many claims (and the monetary limit thereof) may be made within the contract period.

The need for a dedicated Microinsurance regulatory framework dates back to concerns about the risk of consumers being exposed to the unregulated products which target the most vulnerable strata of the population pyramid. This has hindered efforts in developing the Microinsurance market despite its apparent need and potential.

A Microinsurance landscape survey carried out by Cenfri in the year 2010 identified that lack of appropriate regulation is a key barrier to Microinsurance development since it does not provide an enabling environment.
2.0 SITUATIONAL ANALYSIS

2.1 Regulation poses barriers
Currently, Microinsurance is regulated under miscellaneous class of insurance business in the Act. Although piecemeal amendments have been done over the years, the legal framework does not conform to international best practices with regard to development of micro insurance.

In view of the foregoing, the conventional insurance regulation is applied to Microinsurance despite its unique nature. The Law is currently under review and is expected to address in totality the subject of Microinsurance.

2.2 Perception of Insurance
A study carried out by Cenfri (A. Smith, et al, 2011) identifies several factors as contributing to the current state of perception of insurance and low penetration of insurance services especially among the low end market:

i) Lack of trust of insurance companies – this is characterized by non-payment of claims or lengthy and tiresome processes before a claim is paid.
ii) Low engagement and low awareness of insurance companies – the informal market is largely oblivious of insurance and regards the same as a preserve of the rich.
iii) Low understanding and lack of relevant insurance products – most of the information in the market is incomplete and of little value in helping the customer to make valuable risk management decisions. There is also a pronounced lack of appropriate products for the low-income market.
iv) The government has not adequately supported insurance uptake by allowing tax exemptions and providing conducive fiscal measures.
2.3 Research and Development

Due to the unique nature of the population at the bottom of the pyramid, a research and development strategy that addresses the various needs of this market segment is necessary. To serve this market, supply side players need to think differently about customer’s needs and expectations.

Microinsurance must be affordable to the poor otherwise they will not take up insurance and will not benefit from the coverage. Microinsurance providers need to make informed decisions based on a systematic situational analysis of issues in this continuum.

2.4 Claims settlement

Poor claims settlement has created a negative perception of insurance hence the slow uptake. The main causes of poor claims settlement are:

   a) Misselling: clients are not aware of what is covered or not.
   b) Inefficient claims settlement processes
   c) Poor and inconsistent claims monitoring

2.5 Enabling environment

One of the primary functions of insurance regulators and supervisors is to develop insurance markets by improving market efficiency and including persons who currently have no access to or are unable to afford insurance through appropriate product design and delivery mechanisms.

Although improving market efficiency by correcting market imperfections is a classic task for supervisors, an analysis of the International Association of Insurance Supervisors (IAIS) database on national insurance regulations reveals that few member countries have an official developmental mandate.
However, regulators increasingly realize that an enabling regulatory environment and better appreciation of the dynamics of the insurance market could help remove the perceived obstacles that normally discourage insurers from serving the low-income markets. They need to commit to supporting the growth of Microinsurance by adapting their regulations.

3.0 CURRENT STATUS OF MICROINSURANCE

3.1 Demand Side

The features of the low-income and currently uninsured market were captured in the findings of the 2009 FinAccess survey. Subsequently, Centre for Financial Regulation and Inclusion (Cenfri) analysed the low-income market’s experience of risk, as well as their perceptions of and demand for insurance products. Differences between the insured and uninsured from FinAccess survey showed that the insured are more affluent than their uninsured counterparts.

Risk experience and perceptions

According to the FinAccess report of 2009 loss of main wage-earner, followed by drought and/or famine have been underlined as major risks. Sickness and accidents, loss of property, were also enlisted as major risks.

Microfinance institutions clients face all the risks associated with owning running and financing a business which are different from those faced by farmers, artisans and traders for example. Price fluctuations also impact on the levels and stability of their income.

These different risks imply different levels of impact and financial implications which, in turn, determine the type of coping mechanism used. Competing needs for the low income earners including food, shelter and education also take priority over insurance premium.
Consumer education and awareness

This far, a few attempts have been made to start consumer education campaigns but none has been specific for the low-income market. Currently Insurance Regulatory Authority is running a public campaign to educate the masses on insurance.

The Association of Kenya Insurers (AKI), with the support of International Labour Organization (ILO) and in partnership with Microfinance Opportunities (MFO) has implemented a consumer education campaign. Other efforts are found with Non-Governmental Organizations (NGOs) and MFIs targeting their customers only.

The Financial Sector Deepening (FSD), through its Financial Education and Consumer Protection Partnership (FEPP), has also been promoting financial education amongst Kenyans. The FEPP is a public-private sector partnership driving the development of a comprehensive national financial education strategy for Kenya.

Together, the partnership aims to build a strategy that finds effective ways to improve the nation’s knowledge and understanding of personal finances. However, this has been limited to a few projects but focus has been on general financial awareness leaving out awareness on insurance.

3.2 Supply Side

The current situation regarding supply of Microinsurance is as follows:

i) There is lack of reliable IT Solutions to facilitate successful real time transmission of information and cost effective operational processes to manage large volumes of small policies.

ii) Underwriters lack necessary capacity to develop products, underwriting and claims processes to accommodate the unique features of this market.
iii) There seems to be little reinsurance processes to provide umbrella protection to the primary underwriting market.

iv) Challenges of keeping the transaction and administrative cost low.

v) Lack of effective promotion and marketing programmes that gain consumers’ trust.

vi) Generally poor perception of insurance, high insurance illiteracy levels and poor understanding by low-income consumers.

vii) The bulk of potential Microinsurance target market is employed in the informal sector with staggered incomes and therefore cannot sustain consistent premium payments.

viii) The predominant focus of insurance companies has been the provision of services to corporate bodies and to the formally employed.

ix) Currently, there exists an informal risk mitigation mechanism which makes low income households hesitant to embrace insurance as a suitable risk transfer measure.

x) There is lack of a collaborative approach involving the government, insurers and communities to overcome challenges associated with development and distribution of Microinsurance products. There is no focus on understanding customers’ needs and the market trends to push products to consumers.

xi) There is lack of adequate, complete and reliable historical data to enable insurers and reinsurers have a clear understanding of the risk exposure which would assist them in proper underwriting.

xii) Some cultural and religious beliefs discourage people from taking insurance covers.

3.3 Enabling Environment

Regulatory obstacles to the development of Microinsurance in Kenya were identified as:
a) There is no consistent industry or regulatory definition of Microinsurance in Kenya. This framework has defined it in our opening pages.

b) Regulatory hurdles affecting the development of Microinsurance products include:

   i) Capitalization levels, management and reporting requirements
   ii) Stringent licensing requirements for agents and brokers, and restrictions on the amount of commission and management expenses
   iii) Complexity of policies and unsuitable products – use of legal is a challenge due to low literacy levels

c) There is no model for sharing the costs and profits with distributors due to regulatory restrictions hence mass aggregators see little potential in terms of revenues from Microinsurance.

4.0 PURPOSE OF THE PAPER

This policy paper sets the framework for the development of micro insurance in Kenya. It covers demand side, supply side and enabling environment sets out required obligations and support structures for growing micro insurance.

This is based on recognition that in the recent past, stakeholders from the public and private sectors in Kenya have begun to include microinsurance into their agendas recognizing its relevance for poverty-alleviation and social and economic well-being as well as its potential to deliver an important pro low-income financial service, particularly when used together with other microfinance services such as savings, lending and cashless payment systems. An increasing number of private insurers and intermediaries such as Microfinance Institutions are pioneers in providing microinsurance products.

The IRA has recognized the importance of providing an appropriate legal and regulatory framework for microinsurance and has become a key driver in the
process of pushing the microinsurance agenda forward whilst at the same time integrating microinsurance into the mainstream insurance sector.

This Paper proposes a policy blue print for a legal and regulatory framework for microinsurance integrated into the wider legal and regulatory framework for insurance. By means of specific provisions, the new framework will encourage and facilitate the provision of low cost, but high value insurance products that are appropriate to the needs of low-income households and micro and small enterprises and that will enable them to effectively manage their risks. This Paper is designed to set out the high level policy framework.

5.0 OBJECTIVES OF THE PAPER

This policy framework paper is intended to achieve the following objectives:

5.1 Broad objective:

“The policy paper aims at providing a framework for entrenching Microinsurance as a tool for socio-economic empowerment and risk management for low income households in Kenyans”.

5.2 Specific objectives

i) Create awareness initiatives to stakeholders and protect the interests of customers by requiring transparency with respect to product offering and servicing and by requiring insurers and intermediaries to treat their customers fairly (CONSUMER PROTECTION),

ii) Facilitate effective supervision aimed at ensuring the integrity of the insurance market as a whole and require microinsurance providers to act in a prudently sound manner (STABILITY)

iii) Ensure that providers are able to meet claims (SOUND CLAIMS MANAGEMENT)
iv) Encourage private sector engagement in risk protection for the low-income segment, and the development of the microinsurance market in a sustainable manner, including motivating consumers to buy insurance (MARKET DEVELOPMENT).

v) Relax barriers to entry. This should encourage broader participation, promote competition amongst providers and further support poverty alleviation through economic growth and job creation (APPROPRIATE REGULATION)

6.0 OPPORTUNITIES AVAILABLE

Focusing on anchor risks can help overcome distrust in the insurance industry.

The public has been willing to take up insurance when:

a) A particular risk is viewed as having a high mitigation priority; and

b) A risk is attached, or has the potential to be attached, to a type of service delivery or tangible product associated with the risk. The clearest anchor risks in Kenya are health risks, life risks (in particular, funeral) and the risks associated with agricultural production. Consideration of these anchor risks needs to inform product design for the low-income market.

Health risk has been the growth and innovation point for Microinsurance in Kenya.

Health insurance products are generally viewed as complex products to manage for the low-income market, due to the difficulty of claims management and high levels of administration expenses. High demand for these products (particularly by MFIs and their clients) as well as insurers’ willingness to experiment with the product has resulted in to design and distribution of health products.
Funeral expense as anchor life risk offers distinct opportunities for insurance companies and community-based organizations.

The general population attaches much cultural significance to funerals whenever death occurs in a family. This often translates into a financial burden for the family of the deceased with at times wiping out savings thereby pushing families deeper into cycles of poverty.

As a result, families have to cope with the loss of income where a breadwinner passes on. Although there are many coping mechanisms for example welfare group and Harambees, this informal coping mechanisms have become unsustainable due to the frequency of occurrence of risk events a result of rise in cost of living. This creates potential for Microinsurance agenda to be adopted in order to provide the market with appropriate products and services.

Agriculture offers Microinsurance opportunities around value chains and networks.

Agriculture is a main source of income for many Kenyans. FinAccess 2009 shows that agriculture-related activities are a source of income for 87% of the Kenyan adult population.

The agricultural sector therefore presents two opportunities for Microinsurers:

a) An opportunity to develop Microinsurance products to cover agricultural risk.

b) Use of agricultural value chains to distribute not only agricultural insurance but also other relevant life, health asset products.
Banks and emerging networks of payment system offer potential distribution channels.

Premium collection in Kenya can further be enhanced by engaging financial institutions and the payment system networks e.g. Banks, MFIs, M-PESA and SACCOs. This would entail amending the relevant laws to enable registered financial institutions and payment system networks to distribute Microinsurance products.

In order to achieve the desired growth, stakeholders will have to follow a collaborative process to address the collective obstacles to market development.

**Consumer education and awareness can increase demand for Microinsurance products**

Consumer education has been identified as one of the key drivers for insurance penetration especially for the low-income market (creating demand for insurance).

To complement this policy framework paper, FSD and ILO in partnership with IRA, are carrying out an in-depth study focussing on life and health Microinsurance to further inform the appropriate regulation. In a different project, FSD is working on Agricultural Microinsurance as an anchor risk. The findings of this ongoing work which focuses on demand, supply and regulation of Microinsurance, will further information the development of the policy and regulatory framework for Microinsurance.

### 7.0 CONCLUSION

As noted in the situational analysis, the Kenyan insurance industry has mainly focused on corporate and property markets despite majority of the Kenyan working population being in the informal sector. It is not surprising
therefore that the rate of penetration into the insurance market is below 3% of GDP covering only about 7% of the population.

A number of insurance providers are increasingly partnering with the informal sector to design and distribute Microinsurance products. However, the providers have been facing challenges related to design, distribution and administration of products customized to meet the needs of the low income market. Extensive Research and Development will enable insurance providers to develop relevant and appropriate insurance solutions for the low income market.

Despite the efforts to reach the low income market with appropriate insurance products, poor perception of the insurance industry by the public has hindered market development. This has been compounded by the collapse of previously reputable insurance companies.

Consumer awareness and education complemented by consumer protection policies could help restore consumer confidence and build the market.

In the current insurance Act Cap 487, Microinsurance is regulated under miscellaneous class of business. This means that Microinsurance is regulated under the conventional insurance law which does not adequately provide for the insurance needs of the low income households.

This policy framework summarizes the challenges faced in the design, distribution and administration of Microinsurance products. It also makes policy recommendations to enable the development of an appropriate regulatory framework to facilitate growth of Microinsurance.
The proposed regulatory framework for Microinsurance in Kenya is to be incorporated through amendment of the existing insurance legislation.

8.0 WAYFORWARD

Dedicated focus for Microinsurance education and awareness

This will be achieved through:-

a) Standardized Microinsurance product features
b) Tax relief and incentives for education and awareness campaigns
c) National Microinsurance champions and Incorporation of insurance in the formal Education curriculum
d) Adopt-a-school campaign and introduction of Insurance clubs in schools
e) Fundraising and resources mobilization for consumer education
f) Capacity building for Microinsurance agenda drivers through exposure visits and participation in regional and global Microinsurance conferences among other avenues.

Product Development

The development of Microinsurance products should address the following key factors:

a) Address as many risks as possible in one package (product bundling): This means that in one package, a low income person should be able to address a portfolio of risks such as: credit life, funeral expense cover and health cover. This will ensure that costs of delivery of products to the market are minimized.
b) Product simplicity: This ensures the products can conveniently be sold, distributed and be easily understood by the low-income market. Simple products also minimize the risk of misselling.
c) Minimize underwriting costs: This is in the best interest of Microinsurers as the low income market ought to be exempted from stringent underwriting standards.

d) Minimize the policy exclusions: This will ease policy administration and ensure that policyholders enjoy a wider range of benefits under the same policy.

e) Streamline products to meet customers’ expectations in relation to costs, premium payment and claims management.

To ensure effective monitoring, it is important that IRA be aware of all product features both at the time of registration and on an ongoing basis.

**Distribution channels**

The key attributes of a good model of Microinsurance distribution include but are not limited to:

i) Easy and efficient access to market

ii) Simple premium payment mechanism and claims settlement

iii) Must fit the client’s lifestyle

iv) 

**Information Communication and Technology (ICT)**

Although ICT is not fully embraced in the insurance industry, it has been successfully used by other financial institutions like banks with significant success rates leading to deepening of financial access. Tax waivers could be considered to attract investment in progressive ICT solutions for effective handling of voluminous business.
**Strategic Partnerships**

Microinsurance players need to partner with different business sectors and donors if they are to increase the level of penetration of insurance. Strategic partnerships provide avenues for distribution, risk-sharing, consumer education, funding among other benefits. This calls for different partnership models such as:

a) Public-Private Partnerships  
b) Collaborations with Donors and International Partners

**Corporate governance**

Corporate governance requirements are essential to ensure adequate oversight, including risk management and compliance. As Microinsurance will cut across different institutional forms, it is important that common corporate governance principles be set to which all Microinsurers should adhere. All Microinsurers will be required to adhere to at least the following corporate governance requirements:

(a) Transparency:

(b) Skilled supervision of management:

**Role of actuarial assessment**

Actuaries will be involved in pricing which will in turn determine reserving. It is therefore proposed that Microinsurers secure actuarial sign-off on the total premium for all new products, as well as any changes in pricing.

The Actuarial Society will be requested to develop criteria for actuarial skills needed to sign off on Microinsurance premiums, and to issue corresponding certificates to qualifying individuals to authorize them to do so.
Reinsurance

The underwriting and pricing policies of traditional insurers selling microinsurance products is likely to be based on its experience in the line of business being insured or driven by the reinsurance market. On the other hand exclusive microinsurers often do not have reserves/technical provisions commensurate to the risk in their portfolio. The government/supervisor may choose to put in place institutional arrangements or regulations for residual risks in case there is lack of reinsurance support.

The following provisions shall apply with regard to the reinsurance of Microinsurance:

a) Reinsurance will not be compulsory for Microinsurers although it will be highly recommended. As long as pricing is signed off by an Actuary, reserving should be adequate and risk accounted for.

b) Registered insurers may underwrite part of the risk of Microinsurers, but will be required to acquire a Microinsurance license as a separate legal entity for this purpose. Isolating Microinsurance reinsurance into the Microinsurance license also allows Microinsurance reinsurance to be managed and reported on separately.

c) Registered Microinsurers will be allowed to underwrite part of the risk of other Microinsurers, but subject to such licensing conditions with regard to the provision of reinsurance as may be imposed. This provision is primarily intended to allow full insurers with a Microinsurance license to act as reinsurance partners to smaller Microinsurers and is not intended to allow small entities into the reinsurance space who are not deemed competent to provide reinsurance.

d) In line with international developments, the introduction of a
policyholders’ protection fund could be considered as has been emphasized by the International Association of Insurance Supervisors (IAIS).

**Enabling environment**

To encourage the development, a supportive legal and regulatory framework is required to address the following:

i) The legal approach  
ii) Regulation of distribution channels  
iii) Regulation of products  
iv) Acquisition and management expenses  
v) Composite Services  
vi) Returns

For the purpose of providing an enabling environment for the growth and development of Microinsurance, it is proposed to:

a) Encourage participation of reinsurers in the Microinsurance space.  
b) Encourage the creation of a flexible and low-cost intermediation regime that would entail enabling the distribution of insurance by financial and other institutions, including banks, MFIs, SACCOS, informal businesses and community based organizations.  
c) Amendment of the Insurance Act, Cap 487, to include a definition of Microinsurance followed by the development and implementation of Microinsurance Regulations. These regulations will address, amongst other issues:  
   i) Product development and design for Microinsurance – which may be approved by the Insurance Regulatory Authority and which may comprise of a combination of life and general business lines.
ii) Intermediation for Microinsurance products – the regime relating to appointment of Microinsurance agents and other relevant intermediaries and or service providers.

d) Acquisition costs and management expenses – setting out a remuneration structure that allows for the appropriate remuneration for the distribution channels taking cognizance of the need to keep the costs as minimal as possible.

e) Amendment of Section 150 of the Insurance Act to relax registration requirements for Microinsurance intermediaries. Insurers should take responsibility for the appointment and control of Microinsurance intermediaries under the agent/principal model and in accordance with Codes of Conduct approved and Guidelines issued by the Insurance Regulatory Authority.

The Microinsurance policy framework shall be enforced by IRA upon adoption by issuing guidelines to insurers to encourage a flexible intermediation and distribution regime for Microinsurance and in consequence approve appropriate codes of conduct. Concurrently, the Authority should champion industry-wide consumer education programmes on Microinsurance.