Defining informality

- Not regulated for the purposes of providing financial services
- **Definition of insurance**
  - Guaranteed vs non-guaranteed benefits
  - Excluding benefits-in-kind
  - Excluding particular provider or product (e.g. labour unions, funeral parlours, etc)
  - Gaps in definitions (e.g. health insurance)

- Informal insurance market not necessarily illegal

- **Roles**
  - Underwriting/risk management
  - Intermediation

- **Informal insurance**
  - Regulation exists but is not applied
  - Supervisory forbearance
    - Non-compliance
    - Explicit exemption
    - Regulatory forbearance
Examples

- **Uganda & Zambia**: Health insurance provided by unregulated players (HMOs, Hospitals)
- **India (20%*)**: Health schemes by NGOs and cooperatives not regulated by IRDA
- **Philippines (41%*)**: Cooperatives self-insuring
- **Ethiopia**: Iddir and self-insuring MFIs
- **Brazil (60%*)/**Colombia (52%*): In-kind benefits by funeral parlours excluded from insurance definition
- **Kenya**: Insurance definition excludes benefits-in-kind (including funerals), benefits by labour unions, employee associations and friendly societies
- **South Africa (46%*)**: Burial societies and self-insuring funeral parlours

* estimated percentage of microinsurance provided by informal providers (number of policyholders)
South African microinsurance market

- 40.1% (7.2m) have funeral cover
- 2.1% (375,000) have life cover (excl. funeral insurance**)
- 0.41% (74,000) have credit life insurance.
- 2.1% (382,000) have a retail hire purchase account
- 1.5% (262,000) have short term insurance

Informal cover: 60.9% (4.4m) have burial society membership only

Formal cover: 39.1% (2.8m) have a form of formal funeral cover

39.9% (1.1m) have cover through a funeral parlour/undertaker

Key features:

- Large voluntary MI market dominated by funeral insurance (40% of LSM 1-5)
- Large informal (61%) market
- Potentially large illegal funeral insurance market (40%)

Source: Eighty20 calculations based on FinScope 2007 (using weightings derived from the Census 2001)*
* The definition of LSM used is according to the 2005 algorithm
** Does not imply that respondents in this segment do not have funeral insurance, but that they have a formal life policy
Hierarchy of formality

Degree of formalisation

- Public company registered as insurer
- Mutual with dedicated act
- Friendly Society
- Registration as Friendly Society
- Registered for company, health, tax but not insurance
- Not registered for any regulation
- Registration as co-op allows provision of non-guaranteed benefits
- No registration
Policy perspectives on formalisation

- **Insurance supervisor**
  - Consumer protection: Risk of abuse and failure
  - Industry reputation
  - Financial inclusion and existing needs being met
  - Increased competition

- **Insurance industry**
  - Unlevel playing field
  - Access to aggregators if formalised
  - Reinventing insurance for bulk of market

- **Revenue services**
  - Tax revenue

- **Health/local authorities**
  - Public health risks

- **Trade and industry**
  - SME development
  - Local economic empowerment

- **Fiscal policy**
  - Reduce state burden – growing private welfare provision
Should I formalise?

- What is the risk to consumers?
- Do I have the capacity to supervise?
- Are there strong political imperatives?
- Will continued informality undermine development of the market?
Formalisation options

“you cannot bludgeon people into the formal economy, you have to entice them”
Formalisation options

- **Accommodate**: creating space for different institutional types
- **Exemption**: E.g. for specific types of institutions (requires monitoring)
- **Tiering**: proportional regulation
- **Graduation**: Grow into regulatory requirement. Could utilise mechanisms such as cell captives.
- **Fix gaps**: close down regulatory loopholes
- **Formalise the clients**: Encouraging clients to use formal services
Formalisation process

- Understand the market and the scope of the problem
- Define the timescale
- Create clear evolution path to get from informal to formal
- Carrots & sticks
  - amnesties
  - iconic prosecutions
- Compliance support
- Political support
Formalisation process

Illustration:

- Now
- MI Act commencement
- Yr 1: Nominal registration
- Yr 3: Provisional licence
- Yr 5: Full compliance

- Phase-in:
  - Compliance
  - Tax
  - Capital

- Awareness & support campaign

- Consolidation, transformation
Leverage the market

- **Delegated supervision** - making regulated institutions partially responsible for oversight of new players, especially in intermediation

- **Market mechanisms** to incentivise formalisation (such as microfinance rating agencies) can play a supportive role
Leverage the state

Essential to coordinate with other public players:
- Revenue authorities
- Central bank – payment systems
- Health authorities
- Trade and industry
- Law enforcement
- Telecoms regulator
- Utilities regulator
Thank you!

Doubell Chamberlain (doubell@cenfri.org)
Hennie Bester (hennie@cenfri.org)
The Centre for Financial Regulation and Inclusion
+27 21 918 4390