



# Agricultural Index Insurance Kenyan Experience: Regulation and Supervision



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## Introduction



Agricultural index insurance in Kenya

### Regulatory framework

- Kenyan Draft Index-based Insurance Regulations discussed in the stakeholder workshop in 2017
- IAIS currently is currently working on an issues paper on IBI

### Supervisory approach and consumer protection

- Product approval: faster product approval process
- On-going monitoring

### Other supporting activities

- Consumer awareness/ education campaigns
- Facilitating PPPs – government and private insurance sector
- Advise the government on how to improve subsidised schemes (KLIP & KCIP)

### Facilitation of pilots

- Products used on a pilot basis have been given regulatory exemptions
  - Helps encourage market development of the product
  - Gives understanding of what works and what does not
- Pilot products may need to be redesigned once the formal regulations and product approval guidelines come into force. However most features of the current product would comply with these requirements

## Question for Discussion



What are the challenges supervising agricultural or agricultural index insurance in your country?

## Regulatory Issues/ Challenges



- Position on insurable interest for an index based insurance contract – when should it be determined?
- Is it insurance or derivative?
- What if it is a derivative and not insurance – how should it be regulated?
  
- Creating a separate class of business called IBI & commission caps
- Allow for a separate method of calculating the technical reserves
- Specify index based insurance specific capital requirements
- Delay in enacting regulations to set the legal framework
- Data on pilot schemes – lack of statistical information on volumes covered, premiums collected and claims paid
- Lack of formal distribution channels

## Key Regulatory Considerations



- The product must offer fixed-sum instead of indemnity insurance
  - Allows for consequential losses and mitigation costs
  - The index can only serve as a proxy for the actual loss
  - The policy must not promise indemnity payment and IBI products must not be sold as indemnity contracts
- Insurable interest exists if there is prospect of adverse impact on the insured should the insured risk occur
  - Contract must state the risk against which insurance is provided. This is intended to distinguish under insurance from basis risk

## Key Aspects to Consider for Index-based Insurance Schemes



- Targeted customers and covered crops/ livestock and perils insured
- Product features and terms and conditions: manage risk and fair terms and conditions
- Index: credibility of index and basis risk
- Underwriting and pricing: pricing should be viable, affordable and ensure client value, consider the level of subsidies or financing support
- Distribution and aggregation: roles of the different parties, manage conflicts of interest and ensure fair treatment of customers, longer-term sustainability of the model
- Customer awareness and marketing
- Operational processes: exchange of information between different parties
- Claims processes: timely, adequate and transparent claims process
- Reinsurance and risk management: Appropriate and sufficient reinsurance and allowance for investment in infrastructure if necessary

## Proposed Product Approval Guidelines



Agricultural index insurance in Kenya

### 1. Key Product Features:

- IBI products cannot be sold as indemnity insurance, and should be considered as a form of “fixed sum” or “agreed value” insurance
- Maximum size of the possible total pay-out should be specified in the contract
- No waiting / grace period or cancellation to be allowed for IBI products
- Sales & Cover windows , any exclusions, index to be used to calculate the pay-out and expected frequency of payouts must be clearly specified
- Must specify the data sources and back-up sources or method to be used to approximate lost/inaccurate data
- Explain design features included to **minimize basis risk** in an **actuarial report**

Agriculture Index Insurance

## Proposed Product Approval Guidelines



Agricultural index insurance in Kenya

### 2. Contract requirements (Index)

In order to ensure that the contract minimizes basis risk and maximises policyholder value, the index used to determine the pay-out should have the following features:

- Easily observable and measurable-specify how the data used to calculate the index will be observed and how the index values and resulting benefits will be determined
- Transparent, objective and independently verifiable
- A good predictor of the risk covered- the index should not trigger a payout unless the insured risk occurs
- Predictive variable -allow the index to be based on a predictive variable

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## Proposed Product Approval Guidelines



### 3. Claims/ Consumer Protection requirements

Marketing material should explain product and risks:

- Explain that pay-out depends on the value of the index and not the actual loss
- Explain which risks are covered and which will not be; what index is used to calculate the pay-out and expected frequency of payouts
- State eligibility criteria – determining insurable interest
- Insurer must specify a complaints resolution process prior to product launch
- Interested 3<sup>rd</sup> party/policyholder be allowed to receive data and calculate the pay-out themselves

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## Proposed Product Approval Guidelines



### 3. Claims/ Consumer Protection requirements;

- Policyholders do not need to lodge a claim – insurer must provide a notice
- Pay-outs must be verified, communicated and paid within 30 days
- If an independent data validator is to be engaged, a SLA is needed with the independent body indicating:
  - how to resolve conflicts over the data, index values and benefits
  - the penalties the independent body is liable for if it makes mistakes

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## Proposed Product Approval Guidelines



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### 4. Distribution

#### 1. Use of Aggregator

- Insurers allowed to use aggregators to distribute the insurance to individual policyholders
- Insurer to submit the SLA with the aggregator to the Authority before it can start selling the product

#### 2. Group Cover and Master policyholder

- Insurers providing index-based insurance products allowed to underwrite & sell policies on an individual or group basis

#### 3. Portfolio cover

- Insurers allowed to sell index-based insurance to organisations that use the policy to protect themselves against losses from the risk event as measured by the index, adversely impacting their clients or their business interests

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## Proposed Product Approval Guidelines



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### 5. Reinsurance

- Index-based insurance products expose insurers to catastrophic risks
- Adequate reinsurance coverage required before product approval
- Expertise of reinsurer with index insurance products and sharing of technical knowledge
- Type of reinsurance and rationale for the choice used
- Reinsurance contract certainty and clarity (terms, conditions, clauses etc.)
- FSR for the reinsurer(s) and the rating agency used

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## Valuation Requirements and Reporting



### Method of calculating technical liabilities

- Unearned premium reserves:
  - assume risk only expires at the end of the insured period; or
  - assume risk expired proportionally over the cover window of the policy
- Calculation of the outstanding claims incurred reserves
  - appointed actuary to use any method but describe method used in valuation report

### Calculation of the capital requirements

- Still needs to be specified

### Reporting

- Monitoring performance monitoring to ensure value for money and financial viability
- Insurer to report index values vs. actual payments to ensure correct payouts

## Questions for Discussion



1. Describe the regulatory and supervisory approach to agricultural insurance in your country
2. What information should be gathered or included in supervisory reporting requirements for agricultural or agricultural index insurance? What indicators would be useful in monitoring the performance of agricultural or agricultural index insurance?



# Thank you

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