Summary

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बीमा विनियामक और विकास प्राधिकरण
INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY

Plenary 3 – Group vs. individual

Ellis Wohlner, Consultant to SIDA, Sweden
Overriding issues

Insurance and the poor

In comparison with better-off persons, the poor have

- lower premium-paying capacity
- greater difficulty in satisfying more urgent basic needs for food, shelter, and clothing.

Most people, especially in less-developed countries, have little knowledge or understanding of insurance. Like everyone else, the poor need the protection that insurance provides. But due to their lack of resources, they have a particular need of protection from bad insurance – from overpriced and ill-designed products that provide little or no value and which may even lead to personal tragedies by inducing a false sense of security.

These factors must be taken into account when designing insurance programmes for the poor. A fundamental question is how their needs can best be served, by group or by individual plans, and how the poor themselves can be involved in designing or selecting the coverage.

Group insurance

Insurance is, by its very nature, a collective enterprise. No insurance company can assume the risk of insuring only one person, object, or eventuality (accident, fire, etc). There must be a sufficiently large pool of lives, objects or eventualities so that the “law of large numbers”, “spread of risk”, and reduction of “anti-selection” can come into play. Large pools can more easily be achieved thru group policies than thru individual policies.

Group insurance is available only to groups that have been formed for purposes other than insurance protection. Examples include co-operatives, self-help groups, labour unions, professional societies, religious congregations, sports clubs, etc. Any group formed soley for the purpose of obtaining insurance coverage would be very likely to include a disproportionate number of bad risks.

That problem is minimized in groups that alreay exist for other purposes. In addition, they will usually have membership records and sometimes even individual membership accounts that may greatly facilitate the

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provision of voluntary group insurance to members. Hopefully, the group and its elected leadership will also enjoy its members' confidence and thereby be able to bargain and obtain appropriate insurance cover at reasonable prices for its members.

"Individual insurance" is actually a bit of a contradiction, and the acceptance of individual risks in an insurance pool introduces numerous complications, including many or all of the following:

- need for costly marketing and sales activities (inc. commissions)
- more differentiated tariffs
- less comprehensive coverage
- expensive underwriting to minimize adverse selection
- exclusion of some risks
- more costly administration
- more complicated claims handling
- more difficulty and expense to inform the insureds
- less consumer influence.

In short, individual insurance is vastly more expensive and less advantageous than group insurance for the same risks. A significant number of risks that would be rejected by an insurer on an individual basis can be covered in group schemes, thereby improving access to suitable insurance. This aspect alone is very important from the standpoint of social policy.

Main types of group insurance

- compulsory for everyone in a group, with a single payer
- "automatic affiliation" - coverage applies to each and every member unless expressly declined
- completely voluntary participation.

Compulsory plans obviously provide the maximum spread of risks and are the most cost-efficient. Automatic affiliation plans allow for those who do not want coverage to decline it. Completely voluntary plans eliminate the possiblity of including individuals who do not want to participate, but some who do want coverage may (for various reasons) miss the opportunity to sign up. Such plans have the lowest participation rates, are exposed to adverse selection, and have the highest costs.
Whatever the type, group insurance plans usually require a minimum number of members and a minimum participation rate.

Limitations of group insurance

Only a "pre-existing" group formed for some other purpose can be eligible for insurance.

Even some pre-existing groups may not be able to obtain insurance coverage if the group represents a concentration of bad risks.

Many people and/or risks in need of coverage do not qualify for any sort of group insurance.

The generalized provisons of group coverage may at times be inappropriate for the individual needs of members.

Group insurance coverage is not always available. (However, there is room for creativity on the part of both insurers and groups seeking coverage. In Sweden, for example, unemployment was a risk long considered to be "uninsurable". Attempts at individual insurance were not particularly successful. It wasn't until trade unions began taking out obligatory group policies for their members that this particular line of insurance became a lasting feature of the Swedish insurance market.)

Three excellent examples of group insurance

Loan Protection Insurance

Developed in the mid 1930s for credit unions, this microinsurance product provides automatic coverage of all eligible loans (nearly 100% qualify), with the premium being paid by the credit union from its general revenues. The insurer requires no individual records until a death or a total and permanent disability occurs. Total costs are only a fraction of those for individual credit life insurance; all marketing, sales commissions, and underwriting costs are eliminated; and both administration and claims procedures are greatly simplified. Claims ratios are usually well over 80 per cent of premiums and costs are well under 10 per cent of premiums.

Family Group Life Insurance (FGL)

This voluntary group life insurance product was developed and launched by League Life Insurance Company in Michigan in 1963 for members of credit unions and their immediate dependents.

A fantastically successful microinsurance plan, FGL provided USD 2,000 of term life coverage on each credit union member up to age 65, USD 1,000 on his/her spouse up to age 65, and USD 1,000 on every dependent child in the member's household up to age 19 (23 if still studying) - all for a premium of 50 cents per week, automatically deducted every quarter from the member's savings account (USD 6.50 for thirteen

weeks). Unmarried members with no dependents were eligible for coverage on themselves for a premium of 30 cents a week (USD 3.90 per quarter).

League Life Insurance Company was wholly owned by the Michigan Credit Union League, the state association of about 1,000 credit unions. All marketing was by direct mail and no sales commissions were paid. When an individual credit union decided that it wanted to offer coverage to its members, the presidents of the credit union and of League Life sent a joint letter to all members of the credit union, describing the coverage on offer.

“Experts” in the field of direct marketing said that sales to 1 or 2 per cent of eligible members would constitute a success. Actual sales levels were as high as 50 per cent! Prior to the launching of FGL, the Michigan association of life insurance agents made strenuous efforts to stop it. They feared a loss of business and spoke of “unfair competition”. But they failed in their efforts to stop the plan – to their own good fortune. For as it turned out, their sales greatly increased due to increased insurance awareness among the 500,000 of Michigan’s two million families (total population about 9 million) that chose to participate in FGL. For many, it was their first life insurance unconnected with the work place.

Each credit union received a quarterly computer printout of all covered members and an invoice for the total premium to be paid to League Life. The credit union checked to see whether any members had closed their accounts or lacked sufficient funds (very rare occurrences), and added members who had recently joined the plan.

Total costs for the scheme amounted only to some 12 per cent of premiums. Over 80 per cent of premiums were paid out in claims.

Group householders insurance

Despite a high level of insurance consciousness in the Nordic countries, up to 20 per cent of trade unionists dwelling in rented apartments lacked householder’s insurance coverage before it was made available in group form. The Norwegian Trade Union Confederation (“LO”), and the co-operative/trade union insurance company, Samvirke, introduced group householders insurance in Norway in the late 1960s. Borrowing the Norwegian innovation, a similar plan was adopted in the late 1970s by the corresponding institutions in Sweden, LO and Folksam insurance company.
This pioneering and highly successful example of group non-life insurance was bitterly opposed by other insurance companies in both countries. Masking their (quite correct) fears of reduced market shares with arguments about the proper role of trade unions, about “forced participation”, etc, some companies even resorted to obstructive legal

action. However, the courts ultimately rejected such arguments and ruled that helping their members to obtain low-cost householders insurance was a legitimate activity of trade unions. Today, Folksam has 50 per cent of the householder insurance market in Sweden, nearly three-fourths of it via group plans.

Of the 1.3 million households with such coverage from Folksam, approximately one million have “compulsory” coverage, where the insurance is a benefit included with membership in a trade union. The average premium level is slightly over 50 per cent lower than for comparable individual insurance. “Automatic affiliation” plans account for only a small portion of insureds, while most of the remaining 300,000 households are covered by voluntary group plans, where the average premium level is 33 per cent lower than for comparable individual coverage.

For all forms of Folksam group householders’ insurance, roughly 75 per cent of premiums are used for paying claims. Premium levels are so low that costs account for 20 per cent of the premiums. But in absolute terms, total costs are only half of those for individual insurances).

The basic package of householder’s insurance includes: coverage for property losses due to fire, storm, water damages, burglery, etc; civil liability protection; and a number of other benefits associated with the Nordic market, such as coverage for holiday travel and for legal fees. In contrast to comparable individual insurance plans, it is not necessary to specify a monetary value for household contents; full coverage is automatically guaranteed. For those who own their homes, a separate insurance policy is required on the building.

Due to the absence of most marketing, sales, underwriting and some administrative costs, premiums could be drastically reduced. Participating trade unions have been able to materially assist their members, who have received more adequate coverage (not having to “guesstimate” the value of their household contents) for premiums that are 33-50 per cent lower than would otherwise be the case. The societies of Sweden and Norway have benefited from the consequently fewer cases of uninsured persons requiring social assistance as a result of fire and other calamities.

The insurance companies involved have obtained much larger market shares and a better spread of risks. They have also gained a market potential for selling supplementary individual coverages, especially for the buildings 0f house owners.

Two bad examples; one group and one individual

A group personal accident insurance plan

This plan was featured in one of the case studies and was referred to as a "success story". It is esentially a compulsory insurance plan but with a claims ratio of only 16 percent. The premium share consumed by costs was about 4 times greater than that for claims! If instead the plan had a claims ratio of 80 per cent, as in the two group life plans described above, the premiums would need to be reduced by 80 per cent.

An individual endowment insurance plan

This plan was featured in another case study, and was also described in very glowing terms. The claims ratio was less than 8 per cent. Costs as a share of premium were about 6 times greater. If the plan had a claims ratio comparable to the three plans described above, the premiums would need to be reduced 90 per cent. It should also be noted that lapse rates were 55 per cent and that 15 per cent of all claims were rejected. (An important separate issue not considered here is whether endowment insurance in any form should be sold to the poor.)

In conclusion

All insurance is not, per se, good insurance. And, contrary to what some people here may believe, all microinsurance is not, per se, good microinsurance. Even some group plans (see bad example above) are not good plans.

To repeat: The poor not only need protection through insurance, but even protection from insurance; i.e., not being lured into buying overpriced and ill-designed products that provide little value for money. Clearly, neither of the two plans described in the section above can reasonably be described as providing value for money.

The unmet insurance needs of the poor are so great, and their premium-paying capacity so limited that the first priority of microinsurance promoters and providers should be well-designed and reasonably priced group plans for the poor that provide optimal value for money.