

In Focus: Risk-based Supervision

Promoting Insurance in Ghana - PromIGH

Subject

The role of insurance supervision is to promote the maintenance of a fair, safe and stable insurance sector for the benefit and protection of policyholders.¹ Insurance supervisors worldwide are currently – and in line with the international insurance standards described by the International Association of Insurance Supervisors (IAIS) – moving from a compliance-based towards a risk-based approach to perform this role more efficiently.

Through the approach of risk-based supervision (RBS), the supervisory authority identifies and assesses various risk categories and their severity that insurers are exposed to, as well as their ability to manage those risks (using both off-site monitoring and on-site inspections). Based on this assessment, supervisors can allocate their limited resources accordingly (i.e. place greater supervisory efforts on insurers with the greatest risk and impact on the sector). Moreover, capital requirements are set commensurate with the insurer's risk (risk-based minimum capital requirements).

In Ghana, where insurance regulation and supervision is still predominantly compliance-based, capital allocations and solvency requirements are not yet risk-based and have rarely been enforced. Arguably, the potential of insurers bearing unnoticed significant risks and finally becoming insolvent puts policyholders at risk of losing their benefits.

Therefore, the National Insurance Commission (NIC) in Ghana has proposed a new legal and regulatory framework (including provisions for RBS) to approximate the insurance industry to the international standards. This framework is currently in the legislative process. However, the NIC has already started to move towards a risk-based approach to fulfill its supervisory tasks.

¹ IAIS Insurance Core Principle 1.3

Project name	Promoting Insurance in Ghana (PromIGH)
Programme name	Programme for Sustainable Economic Development (PSED)
Project region	Ghana
Name of component activity	Risk-based Supervision
Duration	2009 – 2019; current commission: April 2016 – March 2019
Cooperation and local partner	National Insurance Commission (NIC)
Target group	Direct: insurance sector Indirect: policyholders (among them low-income households)
Documentation	www.nicgh.org/live/en/
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Challenges

For the supervisor

- Successful implementation of RBS requires NIC to build up capacity and properly train and manage staff. This is due to the fact that with RBS supervisors will be making a transition from objective rules-based compliance assessments to more subjective risk assessments which require higher levels of technical expertise.



RBS is forward-looking and abreast of the dynamic context insurers are operating in. Rather than concentrating on institutions which have broken certain rules (compliance-based approach), RBS aims at identifying the possible risks supervised entities will be facing in the future. In this way, RBS increases the probability that significant problems will be spotted and remedied in a timely fashion.

- RBS is time and resource-consuming because it entails a process of continuously updating risk assessments through on-site inspections and off-site monitoring.
- The process of data analysis associated with the implementation of RBS is complex and voluminous. It requires NIC to analyze the data provided by all registered insurance companies using specific software, called VIZOR.
- RBS is not yet implemented in and promoted by adequate national regulation because the draft legal and regulatory framework is currently still in the legislative process.

For the industry

- RBS requires insurance companies to put adequate risk management systems and capable control functions in place (risk-based management). Currently, most insurers in Ghana lack actuaries, dealing with the financial impact of risk and uncertainty, and adequate risk management functions to fulfill this task.

Solution

Enabling the supervisory body to implement RBS

- Two on-site inspections were carried out as training exercises for all NIC technical staff in 2013 and blueprint inspection reports were produced. Follow-up round table discussions were carried out to discuss issues which had arisen during inspections. International advisors accompanied NIC during the implementation of on-site inspections.
- To enable NIC to perform off-site monitoring, the purchase and installation of the monitoring software VIZOR was supported. RBS off-site monitoring using VIZOR systems commenced in 2013; NIC staff members attended a VIZOR Building Training Program. This enables the team to refine and extend the 12 Supervisory Departments Returns for the important regular data collection from insurance companies.
- Continuous long-term capacity building and technical advisory services to NIC are supported by an internationally credentialed actuary working as an integrated expert.

Promoting support and compliance by the industry

- The NIC organized industry workshops on the benefits of risk-based management and drafted requirements for in-house actuaries. Moreover, joint policy papers were developed to promote consensus and support concerning the implementation of RBS among insurers.
- The promotion of risk-based management in insurance companies is complemented by activities to build up actuarial capacity in Ghana.

Lessons learnt

- The transition to risk-based supervision in jurisdictions that previously followed simple compliance-based supervision often leads to higher capital requirement and compliance costs (e.g. staff and capacities for risk management functions) with the insurers. Therefore, it is imperative to have the insurance industry backing the policy process. The development of joint policy papers is a first step on consensus-building to effectively pursue necessary changes. Regular industry workshops on drafted legislation, regulation, market conduct rules, instruments and incentive policies are suggested to follow.
- Especially in the early days of RBS-implementation supervisors often have to decide on the software and technology to be used in the immediate future. Since there are only a few very specific providers, supervisors are advised to shop around well for the best suitable providers in order to avoid high maintenance costs, e.g. through necessary adjustment of software, purchase of further software modules, sending staff for international trainings, etc. Inquiring for expertise with other jurisdictions' regulators is strongly suggested.
- Risk-based supervision requires high levels of actuarial expertise by the supervisor. In countries with emerging insurance sectors such capacities are rarely to be found. Hence, regulators have to decide early on domestic strategies to sustainably develop actuarial capacities within the insurance industry.

Published by Deutsche Gesellschaft für
Internationale Zusammenarbeit (GIZ) GmbH
Registered offices Bonn and Eschborn, Germany

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Cooperation and Development (BMZ)

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As at September 2015

GIZ is responsible for the content of this publication.

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