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Towards new typologies for microinsurance intermediation

Document prepared for the FinMark Trust

7 November 2007

07/11/2007: **VERSION 2.5**

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The discussion of international typologies draws on a global scan of trends in microinsurance intermediation conducted by Enterplan as part of the broader study.

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1. INTRODUCTION

Distribution is one of the key challenges in extending microinsurance to the poor. Internationally, the bulk of microinsurance is based on compulsory sales where very little additional effort is required to include insurance on the extension of credit. In many cases the lender, rather than the borrower, is seen as the insured party and the insurable interest is the risk of non-recovery of the loan on the death of the borrower. Developmental/non-profit MFI[1] credit networks and client bases tend to be regarded as the dominant distribution mechanisms and target markets. These networks however tend to have a small reach relative to the potential market and the current reach of commercial entities (particularly if bank reach is included).

More recently, commercial insurers have started to extend distribution models beyond the limitations of MFI markets. As a result they are facing new challenges in finding efficient distribution models able to sell the complicated financial product of insurance to a market mostly unfamiliar with its value. The move towards “alternative” distribution has prompted the need to update the discourse on microinsurance to provide useful language and typologies for the analysis of the broader microinsurance intermediation issue.

This document draws on a broader study on microinsurance intermediation and its regulatory challenges in South Africa that was conducted for the FinMark Trust[2] and takes the first steps to extend intermediation typologies beyond MFIs and compulsory sales.

The next sections are set out as follows:

- Section 2 briefly notes the most prominent “traditional” international intermediation models and the typology used.
- Section 3 outlines the main features of the South African microinsurance and intermediation market as well as the current forces shaping it.
- Section 4 introduces the characteristics of the intermediary, product and sales processes used to construct the proposed new typology for the intermediation of microinsurance.
- Section **Error! Reference source not found.** applies this typology to describe the South African microinsurance intermediary market.
- Section 6 concludes with the main findings.

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[1] In this document we apply the CGAP definition of MFI, which includes all entities (extending across profit/non-profit, government/private, cooperative/joint stock) providing any financial services (not only credit) to the poor. In this case, we are referring to a specific subset of MFIs which are non-profit or developmental in nature. While these do not seek to profit they do seek to be sustainable and generate a surplus.

[2] See (Genesis, 2006b).

2. TRADITIONAL TYPOLOGY OF MICROINSURANCE INTERMEDIATION MODELS

Four categories of models are typically noted in the international discussion on microinsurance intermediation:

Partner–agent: The partner-agent model is by far the most commonly-referenced microinsurance distribution model. It consists of an insurer (the partner) using another organisation (the agent) to distribute insurance products to its (often captive) clients. In the general model agents may be for-profit or non-profit, are usually tied to one insurer and combine the sale of insurance with other financial services (notably but not exclusively microcredit). This can cover a wide variety of models. In most cases, the discussion of this model however actually does not refer to the general model, but rather specifically to the model linking commercial insurers with non-profit/developmental MFIs[3]. These MFIs are typically driven to enter into partnerships with insurers by the need to cover the risks of unsecured lending. Key features to note regarding the developmental credit partner-agent model are:

- Insurance is typically not distributed on a voluntary and/or standalone basis but embedded as a compulsory addition to a credit product. As a result, the insurance product is not "sold" on its own merit, but is driven by the demand for the credit product.
- Developmental credit models have not achieved success in distributing voluntary insurance to the broader public, as they are restricted to their member base and have focused on the sales of embedded or bundled products.
- International experience suggests that insurers are no longer guaranteed a captive distribution mechanism through developmental credit MFIs. While in the past such MFIs had few options outside of dealing with the insurer, other options are becoming available. At the least, MFIs are starting to charge for the role they play in distribution. In some cases they may even opt to become insurers themselves.

Mutual/cooperative insurer: As noted by Fischer and Qureshi (2006), there are several categories of cooperative and mutual insurance models, distinguished by the nature of the role played by the cooperative/mutual in the insurance process. However, microinsurance literature often fails to separate the role of a cooperative/mutual as underwriter from the role of a cooperative/mutual network as intermediary for insurance products. In the model where the mutual/cooperative serves as intermediary, the members, who have an ownership stake in the intermediary entity, are both the distribution agents[4] and the clients of insurance products. Most commonly this category would include credit unions and other

[3] See for example McCord (2006).

[4] In the case of TUW SKOK, the insurance is distributed by individuals that are members of the cooperatives union.

formal and informal mutual organisations that often also offer other financial services. The close link between intermediary and clients has benefited this model by shaping product design, facilitating client service and trust. This benefit is enhanced where the underwriting is also provided within the mutual/cooperative structure. In the health sector, this type of model is also sometimes referred to as a "community-based insurance model", where "the policyholders are themselves the owners and managers of the insurance program" (McCord, 2000). Examples of this model include TUW SKOK (Poland), the CARD network (Philippines)[5] and Columna (Guatemala).

Tied agent: In this model the insurer recruits and manages a direct sales force to sell and service insurance products to low-income clients. The insurer is responsible for product development and pricing, as well as sales and servicing. One of the benefits to the insurer of such an agent force is that it enables them to maintain some control over the client base. As with the partner-agent category, the category of tied agent models may include a variety of models with widely varying features. Examples of this category include Delta Life Insurance (Bangladesh), Tata-AIG (India) and CLICO (Ghana).

Broker: The broker is an independent agent that sells and services insurance products on behalf of many insurers, but does not carry any of the insurance risk. In some environments, broking licenses require significant capital outlays and special requirements in terms of staffing, training of field staff and other aspects. The greatest advantage of the independent intermediary is the choice of insurers and products offered to clients. Examples of this model include Megatop/ITC (India) and Servi Peru (Peru).

Need for a new typology. The above-mentioned models tend to overlap in features. An MFI can be considered to be a tied agent as it is typically linked to only one insurer. Independent agents may conduct individual sales or provide the link between an insurer and an MFI (or any other group). Cooperatives may act as client groups only selling insurance to their members, as agents for other cooperatives (e.g. Solidaria in Colombia) or even as agents for sales to the broader public (e.g. La Equidad in Colombia).

While these models were sufficient to describe the pioneers of microinsurance, the increasing variety of models and permutations require a more detailed breakdown, based on an analysis of the key distinguishing features of different models. This can then be used to evaluate the appropriateness of regulatory environments and assess the performance of different models in the microinsurance market.

Accordingly, this document takes the first step in identifying a more detailed set of characteristics that could be used to gain insight into the features of the various models employed in the microinsurance market. This emerging typology and its relevance will be demonstrated using examples and key features from the South African context. We used these key features to develop intermediation categories

[5] Where the underwriting is also done on a mutual basis.

that are of relevance to South Africa. These categories will not necessarily be exhaustive of all models found internationally, or be relevant to all other jurisdictions. It is therefore the *typology of features* that emerges which is more important to consider. If a clear typology is established, it can be mixed and matched to develop intermediation categories relevant for any specific jurisdiction.

3. THE SOUTH AFRICAN MICROINSURANCE CONTEXT

Before proceeding with the discussion of intermediation models, it is necessary to provide some context on the South African market and to note the current dynamics and drivers of change[6].

Large voluntary market, small MFI market. The South African microinsurance market is characterised by:

- *Small MFI market.* South Africa has a very small traditional/developmental MFI market. Microcredit is mostly provided on commercial terms by banks and microlenders. These lenders also pursue credit insurance as additional income stream and to cover their risk exposure.
- *Large voluntary funeral insurance market.* Microinsurance is dominated by funeral insurance. This market has developed on commercial terms and largely without government intervention. Funeral insurance products are sold on a voluntary basis on the back of strong demand for funeral services driven by the cultural necessity of dignified funerals. It is the only product category where regulation does not limit the commission that may be charged. It has also benefited from reduced intermediary regulation.
- *Large informal market.* 52% of the funeral cover market consists of informal cover provided by burial societies (FinScope 2006)[7]. Of those that state they have a formal product[8], 57% bought their policies from funeral parlours. Many funeral parlours are likely to self-insure their books without being authorised insurers[9].

Changing regulatory environment. Government policy and regulation has a significant impact on the microinsurance and insurance market in general. Multiple (and sometimes conflicting) policy objectives impact on government and commercial initiatives aimed at extending access to financial services to the low-income market. South Africa is faced with two specific challenges. Given the history of exclusion, the country has a large low-income population not traditionally served by the formal financial sector. This low-income group is vulnerable to abuse by unscrupulous service providers, but also needs financial services. Accordingly,

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[6] For a more detailed overview of the South African insurance market see Genesis (2006b).

[7] 52% of all people who noted that they have some form of funeral cover (formal and informal), only had cover from a burial society.

[8] I.e. the perceive their product to be a formal product although this may not be the case.

[9] See Genesis (2005) for more details on the funeral parlour market.

two policy objectives have had a particular impact on the development of the South African insurance market[10]:

- *Ensuring consumer protection.* Given the vulnerability of the poor, consumer protection is an important policy goal in South Africa. It has been the main driver behind the Financial Advisory and Intermediary Services Act, 2002 (FAIS), the main act regulating the insurance intermediaries' market. The Act prescribes who may act as an intermediary and advice-giver (e.g. setting minimum skills and experience requirements[11]) and how advice and intermediary services must be provided (e.g. requiring a financial needs analysis as basis for the advice). Although the Act does not require advice to be provided on all transactions, there is some uncertainty over what exactly constitutes advice and when is it required[12]. Under the Act, all intermediaries[13] (irrespective of whether they provide advice or not) must be registered and must adhere to certain minimum requirements in terms of education, business infrastructure and recordkeeping. This has since been relaxed by a guidance note exempting staff providing purely 'clerical' services from the bulk of the requirements (including minimum skills levels). Such staff must still be linked with a registered Financial Service Provider, who has to comply with all the conditions of the Act. These requirements have increased the regulatory risk for intermediaries and the cost of intermediation, particularly where it involves advice.
- *Extending access to the poor.* As a result of its history of exclusion, South Africa is also faced with the challenge of extending insurance products to the poor. The push to extend inclusion is most clearly captured in the Financial Sector Charter (FSC) of 2003, an agreement between government and industry on targets for broad-based black economic empowerment in the financial sector and for expanding access to financial services to the poor. The Charter commits each industry in the financial sector to reach specific targets for access. In the insurance industry, respectively 6% and 23% of LSM1-5 individuals should have effective access to non-life insurance products[14] and life assurance products[15] by 2014.

Models evolving to cope with regulatory and market challenges. Given that these regulatory changes have emerged fairly recently, intermediation models are still in the process of adjusting. To manage the need to extend financial services with the increased regulatory cost on advice-based sales, current microinsurance

[10] For a more detailed discussion of the regulatory environment in South Africa see Genesis (2006b).

[11] Under an FSB exemption, the full education requirements do not apply to intermediaries of funeral insurance until 30 September 2007 (FSB Board notice 104 of 2004), a deadline that was later extended.

[12] Advice is defined in the FAIS Act as "…any recommendation, guidance or proposal of a financial nature furnished, by any means or medium, to any client or group of clients in respect of the purchase or investment in any financial products." Requirements for what is to be included in advice are contained in the Financial Services Board (the South African non-bank financial regulator) General Code of Conduct for Authorised Financial Services Provider and their Representatives issued under Section 15 of the FAIS Act of 2002.

[13] Defined as a person providing advice or any "intermediary services" relating to the selling of a financial product, unless the services rendered are purely administrative or clerical.

[14] Referred to as "short-term" insurance products in South Africa.

[15] Referred to as "long-term" insurance in South Africa.

models mostly focus on non-advice or so-called 'tick-box'[16] sales models. These changes suggest that, in extending consumer protection requirements on advice-based sales, the regulator may have priced advice beyond the reach of the poor. While non-advice models may allow the industry to pursue its access objectives, it is not clear that it will satisfy government's consumer protection requirements and it may result in mis-selling. Furthermore, it is not clear whether these models will achieve take-up as it does not allow for active selling by sales staff of the products to new clients. The interplay between inclusion and consumer protection is likely to be the dominant driver of change over the next decade.

Cell phone technology as driver of change. In addition to the regulatory changes noted above, the emergence of cell phone technology has created new opportunities and is a driver of innovation in microinsurance intermediation. Cell phone usage extends well beyond the reach of financial services amongst lower-income households and presents opportunities to unlock new client bases.

Communication as primary function. The current application of this technology is quite simple and relies purely on the ability to communicate with consumers (payment reminders, policy activation, advice and help lines, etc.). Experience shows that significantly better payment performance can be achieved on cash premium collections by sending short message service (SMS) payment reminders, which can be generated at low cost. The ability to communicate directly and immediately via the popular SMS medium has therefore increased the viability of non-debit order premium collection (including cash premiums), thereby extending the market for insurance beyond those with bank accounts. Some cash premium models are reporting premium persistency in excess of 80%, which exceeds that of some the debit-order-based microinsurance models.

Airtime transaction models being considered. New models are also expected to increase in sophistication by using the cell phone as payment device including potentially using airtime as currency. The first versions of airtime payment models have been launched in South Africa. The primary obstacle that these models have faced is the strict regulatory regime which effectively limits the provision of such transaction services to banks.

Success of new models still limited to funeral insurance. It has to be noted that these innovations are quite recent and that to date little penetration has been achieved beyond funeral insurance in South Africa. Where insurers have tried to include non-life products, these have not been successful. Where insurers have withdrawn these products they have noted the need to "sell" non-life products as a key problem. Funeral insurance is an anomaly, as cultural demand means that it is bought not sold, thereby allowing for much easier intermediation. The main challenge going forward will be to extend the offering beyond funeral insurance.

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[16] In these models, consumers are not provided with advice and simply presented with the option of insurance (usually as part of purchasing other goods or obtaining credit). They accept the policy by simply ticking the option on a contract. Currently these models are not only provided without advice but often without any verbal disclosure and the client is left with only the disclosure provided in the sales contract.

Battle for channel control. Underlying these developments is a trend playing out in the broader insurance market. The current (mostly high-income) market is dominated by broker distribution. This happened because brokers historically presented a lower-cost channel (relative to agent models at the time) to the insurers. The increasing dominance of broker distribution has, however, meant that insurers have gradually lost control over their client base. Brokers control access to their clients and can move them away from a specific insurer if they want to. In a move to address this, insurers have started to implement new models such as call centre distribution. Not only does this potentially[17] offer lower-cost distribution than brokers and traditional agents, but it also provides insurers with more control.

Insurers are also partnering with retailer and other networks that could provide an alternative access point as well as premium collection system to address the dependency on banks and bank accounts. Interestingly, the retailer models are being rolled out first in the low-income market, where brokers were traditionally absent and, therefore, present little resistance. However, these models are likely to eventually extend into higher-income markets as well.

4. EMERGING TYPOLOGY OF MICROINSURANCE INTERMEDIATION

Although the international typology described in Section 2 provides a first step in categorising and describing intermediary models, it does so at a very high level and does not yet incorporate recent developments on the distribution front. In order to develop a more functional categorisation that can overcome these restrictions, we consider a more detailed set of features that describe and categorise the intermediary market.

The criteria used for the description may vary depending on the focus of the categorisation (e.g. for regulatory or market analysis purposes). The criteria considered here focus on the ability of the model to provide appropriate access to the poor and relate to the nature of the intermediary and the sales process. These criteria have also proved useful in understanding regulatory challenges and explaining market dynamics.

Nature of intermediary. The first set of criteria relate to the nature of the intermediary:

- *Tied/independent:* All intermediaries are either contractually tied to or independent of the insurer whose products they are selling. An independent intermediary is free to sell the products of different product providers, while a tied intermediary is limited contractually to selling the products of one insurer. A tied intermediary may be owned/employed by the insurer or be bound through

[17] There is still much debate about the actual cost of call centre models as these have proven more costly than initially expected. It is not clear that call centre models provide lower cost distribution than brokers and agents in all cases.

a vehicle such as a joint venture. Tied intermediaries do not provide independent advice on products.

- *Relationship with one or many insurers:* Even though intermediaries may not be contractually bound to an insurer, an independent agent may still opt for a relationship with only one insurer. This is relevant when considering whether an intermediary that is independent in theory is independent in practice. In some cases a de facto tied relationship may be useful despite the loss of independence. Independent member-owned intermediaries may, for example, commit to a relationship with one insurer in return for products which are tailored to suit its members. Without the commitment of such a relationship, South African insurers have been unwilling to incur the cost of customisation.
- *Control of access to client*: This considers whether the intermediary or the insurer controls access to the client base. If an intermediary controls access to the client (e.g. a cash retailer), it means that the insurer will have great difficulty accessing the client base if not dealing with the particular intermediary. An intermediary that controls access to its client base could, therefore, move to a different insurer and take the client base with it. Depending on the client base in question, this may provide the intermediary with significant negotiating power.
- *Product ownership/innovation*: This characteristic considers who leads and controls product design and development. Traditionally, the product is controlled by the insurer, but this is not always the case. In some case intermediaries may also choose to be involved in the product design process even if they do not control the product. The South African case shows that intermediaries that are closer to the clients (e.g. informal mutual insurers or union-owned intermediaries) tend to develop products that are better suited to their clients' needs. An example is the union-owned intermediary Lesaka. Given its large client base and the fact that it is owned by its clients (the union members), it has been able to negotiate customised and low-cost insurance products with various insurers.
- *Private benefit/member benefit:* Intermediaries can be either for-profit or member-owned/non-profit. In the case of for-profit intermediaries, the risk of abuse and mis-selling may be higher than, for example, cooperative intermediaries where member-governance helps to reduce (but not remove) the risk of abuse. For example: based on their mutuality and member governance, informal burial societies in South Africa are unofficially exempted from intermediary regulation as they are regarded as 'client groups' rather than intermediaries.
- *Multi-function/sole function:* Some intermediaries may exist for the sole purpose of selling insurance, while others combine the selling of insurance with other activities (e.g. the provision of funeral services, the provision of banking or other financial services, the selling of general retail products, etc.). While multi-function intermediaries benefit from sharing costs across a broader range of activities, the combination of insurance sales with other activities (such as funeral services or furniture retailing) have in some cases been found to lead to

abuse[18]. Such a combination makes it very difficult for the client to consider the cost and value of the insurance product separately from the rest of the transaction and provides a captive insurance market to for example the credit retailer.

Nature of intermediation process. In addition to the characteristics of the intermediary, the nature of the sales process and of the products distributed may have a significant impact on the cost and nature of distribution mechanisms. In the South African case, the following characteristics were found to be relevant.

- *Nature of client contact or sales platform.* Traditionally insurance sales are conducted through face-to-face contact on a one-to-one basis with brokers or agents. As this method is quite expensive, a number of new methods have emerged in order to facilitate microinsurance intermediation. These include call centres (outbound and inbound), internet sales, over-the-counter sales (e.g. in retail stores), bundling or embedding the product with other products (e.g. credit life with a credit good purchase or loan), network marketing (often combined with call centre sales) and affinity group sales (e.g. using brokers/agents, network marketers or members of the client group). As a result of the increasing cost of advice-based intermediation in South Africa, a new category of non-advice salesperson, the sales representative, has also emerged. The sales representative is not qualified or registered as either broker or agent and can only conduct the clerical components of the sale, without providing any advice.

  These models can be distinguished by whether they entail face-to-face sales or not and whether they access cash premiums or not. Various combinations of these client touch points may be used in originating and closing the sale (e.g. originate sale via network marketer and close the sale by call centre; or originate sale by roaming sales representative and close sale by broker in central office).

- *Advice-based vs tick-box sales.* The regulation of advice-based sales and the need to find lower-cost distribution mechanisms for microinsurance have resulted in the emergence of so-called “tick-box” sales techniques. In South Africa, uncertainty around what exactly constitutes advice has resulted in many of the new models not only avoiding advice, but all verbal disclosure of product features. Although these models have successfully avoided regulatory cost, the complete absence of advice and even basic verbal disclosure in a low-income market where financial literacy is low may result in mis-selling.

- *Passive vs. active sales*. A number of the low-income models that have emerged in South Africa utilise passive sales models expecting the client to ask for the product rather being actively sold the product by a salesperson. While this may work to some extent for funeral insurance (given the demand-led nature of this product noted in Section 3), it is not clear whether this sales model will work for other products. Most low-income clients are unfamiliar with

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[18] For a more detailed discussion on the market failure resulting from the close association of funeral services and insurance in South Africa, the reader is referred to Genesis (2005).

commercial insurance and are unlikely to ask for the product out of their own volition. The absence of a 'market maker' in these models is therefore potentially problematic.

- *Embedded/bundled vs. standalone products.* **Embedded** insurance products are seamlessly (and also often opaquely) integrated with other financial products or commodity sales. The most common example in low-income markets is credit life insurance on credit purchases of household goods where the client is often not even aware of having obtained (and paid for) credit life insurance as part of the credit purchase. Embedded insurance holds particular appeal to insurers as it is easy to achieve volume and to avoid anti-selection and it entails low administration cost.

  In contrast, **standalone** products are sold as financial products in their own right and do not have to be combined with the purchase of another product.

  Bundled products fall somewhere in-between these two categories, as the insurance product is closely associated with another product, but not completely embedded. From the client's perspective, there is often little difference between embedded and bundled products. Bundling can however also refer to the combination of different types of cover and benefits in one standalone insurance product. This often appeals to the low-income market, but the extent to which it is possible will depend on the demarcation regime in the particular country.

  Quite different distribution and regulatory challenges exist for these different types of product combinations. Standalone products are harder and more costly to distribute than embedded or bundled products, as volumes are not simply achieved on the back of other product sales. Clients need to be sold on the value of the product and the insurer faces the risk of anti-selection. Standalone sales are therefore also more sensitive to increases in the regulatory burden and costs on intermediation.

- *Compulsory vs. voluntary products*. Closely related to the embedded versus standalone distinction is whether a product is compulsory or voluntary. Though compulsory products are mostly embedded or bundled, it is important enough to warrant separate discussion. It may also be that a standalone product is made compulsory as a condition to the sale of another product. Internationally, the bulk of microinsurance tends to be compulsory. It has often been used to the benefit of the credit provider and insurer, rather than the consumer. In South Africa, it was found that such insurance is often sold without the knowledge of the consumer, thereby undermining the value it may have offered.

- *Product complexity.* Complex products require more costly and time consuming distribution methods. In addition, more complex products may require higher levels of consumer education and advice as the consumer often finds it difficult to obtain sufficient information and compare products. In order to facilitate microinsurance intermediation and ensure consumer protection, it is therefore necessary to also consider the complexity of the product and incentivise the development of simplified microinsurance products.

- *Servicing and sales requirements.* Asset insurance products may expect multiple claims over the duration of the insurance contract. Each claim may require some level of verification, and the benefit paid will vary depending on the level of cover and the level of damage incurred. In contrast, funeral insurance pays a fixed benefit on the death of the policyholder or covered person. The latter is, therefore, much easier to intermediate and simpler for the client to understand. Such asset insurance products will be more sensitive to increases in regulatory burden and cost on intermediation.

5. INTERMEDIARY MODELS IN SOUTH AFRICA

Applying the distinguishing characteristics discussed in the preceding section, five main categories of intermediaries with various sub-categories can be identified in the South African market. The main interest here is not in the actual categories (which may be different for other countries) but how the features identified above were used to develop categories relevant to the domestic market and the relevance of these categories from a regulatory point of view[19].

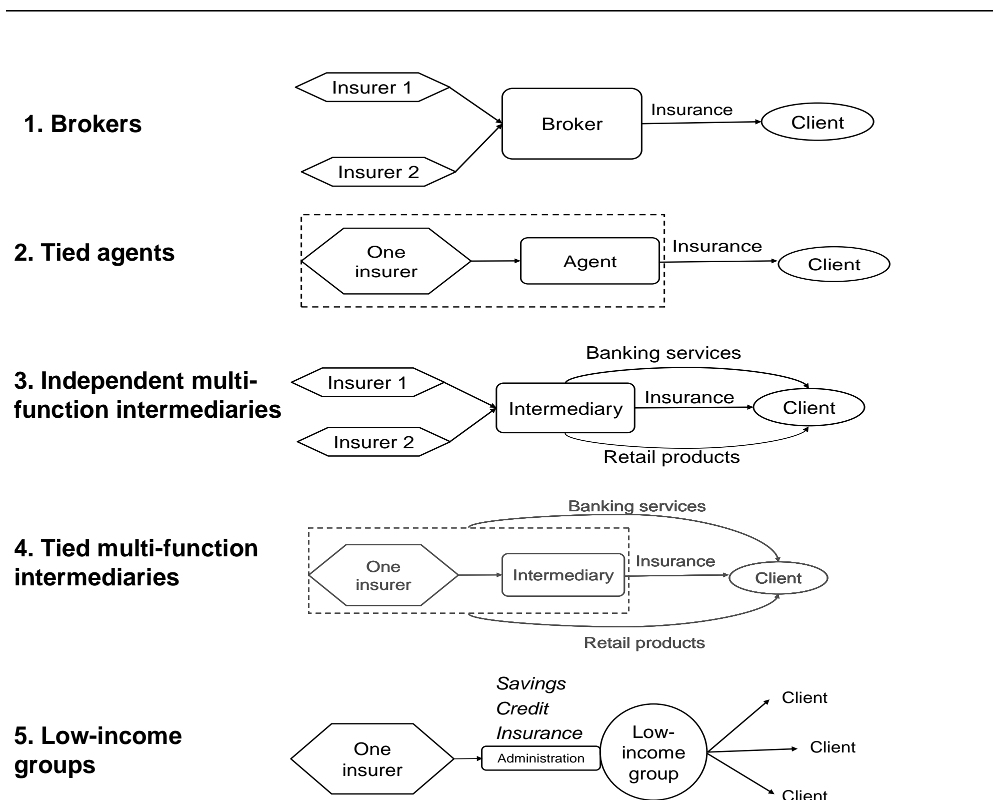

Figure 1. Models of insurance intermediation in South Africa.
Source: Genesis Analytics

[19] Also note that the focus of the discussion is on intermediary models currently or potentially serving the lower-income retail market. Accordingly, this document does not present a complete overview of the South African insurance intermediary market.

Category 1: Brokers (also referred to as independent agents) are independent intermediaries who have relationships with many insurers and whose sole function is selling insurance to clients. As an independent intermediary, a broker represents the interests of the client and advises the client on the purchase of insurance *independent of the insurer*. Access to the client is controlled by the broker, but the insurer is responsible for product development. Income is usually received in the form of commission but may also include administration fees. Given their focus on advice, brokers traditionally serve higher-income clients requiring advice on more complex products. In South Africa, brokers have a limited presence in the microinsurance market. Four types of brokers relevant to the microinsurance market can be distinguished:

- *The traditional broker*. The traditional broker serves middle- and higher-income clients on a face-to-face basis. Sales are usually done on a one-on-one basis, but could also be done on a group basis (e.g. a broker selling insurance to a group of employees). Given the economies of scale of the latter, brokers have been able to serve some lower-income groups (of which the members are mostly formally employed).
- *The emerging broker.* The emerging broker, in contrast to the traditional broker, typically derives from a lower-income community, has fewer or lower qualifications than the traditional broker and generally sells simpler products. The emerging broker can also conduct group sales but this is usually limited to smaller groups as they have difficulty competing with the more sophisticated traditional brokers and agents for the larger client groups.
- *Networked brokers.* Brokers (be they traditional or emerging) are also clustering to share in the increased regulatory compliance costs. A networked brokerage is one version where brokers by their own initiative (without insurers' involvement) cluster together to share the costs of certain compliance expenses and backroom administration activities. While member brokers are able to remain independent, they gain the benefit of consolidated bargaining power and shared costs.
- *Shared brokerage.* Whereas networked brokers are established by the brokers' initiative, a shared brokerage is established by the initiative of an insurer, who may also carry or subsidise the cost. The involvement of the insurer raises some questions on the brokers' independence. From the point of view of the insurer, supporting smaller independent brokers avoids broker consolidation, which creates larger brokerages with increased power to negotiate with the insurer.

New sales platforms and channels reduce cost. Given the vulnerability of the low-income market and their need for advice, the question has been raised whether brokers can serve the lower-income market. One way in which brokers may achieve this is by harnessing lower-cost sales platforms. Although brokers are unlikely to be able to serve a significant proportion of the low-income market in South Africa, two interesting variations have emerged: broker call centres, and the use of a number of sales representatives to attract clients which the broker then advises if required. Broker models however remain expensive, but more

importantly, advice-based sales are being crowded out of the low-income market by new non-advice based models. Whether this trend will continue depends on whether such non-advice models will prove to be successful in achieving take-up and whether the regulatory space created for these models remains.

Category 2: Tied agents have an exclusive relationship with one insurer (i.e. they are contractually bound) and their sole function is to sell insurance. The agent therefore represents the interest of the insurer and not the client and, while they could provide advice, this is limited to the set of products offered by their sponsoring insurer. The insurer is able to access the client directly[20], but generally only interacts with the client through the agent. The insurer is also responsible for product development and administration but the agent may provide limited assistance with administration. Tied agents generally receive commission on products sold, although some insurers employ agents on a salary basis. The following types of tied agents were identified in South Africa:

- *The traditional (or doorstep) agent* is similar to the traditional broker noted above and sells insurance through face-to-face interaction on an individual or group basis.
- The *call centre agent* sells policies telephonically from inbound and/or outbound call centres, with initial interaction with the prospective client often initiated over the internet. Call centre distribution tends to rely on the ability to deduct premiums from a bank account. This rules out a large proportion of the low-income market who may not have a bank account or may not want to have premiums deducted automatically (due to the difficulty of stopping such payments).
- The *franchised agency* is a new breed of agents currently emerging with the help of insurance companies. Franchised agencies receive financial support from insurance companies to either exclusively sell their policies or at least reach an insurer-specified sales target while allowed to also sell the policies of other insurers. This agent example can be considered a hybrid between an agent and a broker. Franchised agencies are more independent than traditional agents, but receive more system and compliance support from the insurer than the traditional brokerage. Franchised agencies operate from infrastructure situated outside the insurance company and mainly serve higher-income clients.
- The *tiered-agency force* has emerged in direct reaction to the increased regulatory cost on advice-based sales (similar to brokers using sales representatives as described above). An example may be where an insurer which owns a chain of funeral parlours creates a tiered-agency force consisting of agents and sales representatives to support funeral insurance sales in and outside its funeral parlours. In this model agents will be registered to provide advice, while sales representatives will not be allowed to provide advice and

[20] The insurer has full information on the client and contracts directly with the client. If the agent leaves, the relationship continues and the insurer can initiate sales of other products to the client without going through the same agent. However, in most cases, the client prefers to continue the relationship with the agent, rather than the insurer.

will simply be presenting a tick-of-the-box sales option to prospective clients and collect cash premiums.

- The *call centre-supported agency force* is another variation that has emerged to facilitate easier compliance with intermediary regulation while still giving clients access to the often preferred face-to-face sales process. In this model centralised call centre agents support traditional insurance agents on product information as well as in capturing client details. The agents initiate the sale with prospective clients and after the policy sale has been closed, the call centre is phoned to capture the client information and immediately affect policy cover. The call centre agent can also assist with more detailed product questions.

Categories 3 and 4: Multi-function intermediaries. These intermediaries are multi-functional as they also sell a range of other services or products, such as retail products (clothing, food, etc.), funeral services and banking services. The intermediary often has a recognised brand, which is used to attract clients. As a result, the client often views the intermediary as the product provider and is not aware of the underwriting insurer. The intermediary, therefore, controls access to the client but also carries the reputation risk. Although product ownership and innovation may still be handled by the insurer, multi-function intermediaries actively participate in the product design and often take initiative in suggesting products that suit their client base. Such intermediaries may be tied or independent. Four groups of multi-function intermediaries have been identified in South Africa:

Retailers. This model utilises the distribution network of clothing, food and furniture retailers to distribute insurance products. The retailer may be dependent or independent and the product may be sold on a standalone basis or bundled/embedded with the sale of another product. Three typical variations of this model were found:

- *Independent retailer, standalone insurance sales.* In this model, the intermediary is independent and the product is sold on its individual value and not attached to the sale of other products. An example is the distribution of funeral insurance through Shoprite, a low- to middle-income retailer. Funeral policies of HTG Life, a registered insurer, are sold through Money Market counters in all Shoprite stores, but without an exclusive agreement. Money Market counters provide a range of transaction services to Shoprite clients, including payment of television licenses and municipal accounts. Shoprite is responsible for the marketing, selling and premium collection associated with the policy, while HTG Life handles policy administration, claims management and payout. Premiums can be paid in cash. The take-up through this channel has been very low because sales have to be conducted by Shoprite staff who are not trained insurance agents, do not receive commission on the sales and do not actively sell the policies.
- *Tied retailer, standalone insurance sales.* The clothing retailers Pep and Edcon (through its retail chains Jet and Edgars) both have joint venture agreements with Hollard Insurance to distribute its insurance products. Pep sells "starter-

pack" insurance that provides funeral, personal accident and cell phone insurance on a cash basis off its shelves. The policy is activated at the cashier and renewed each month by paying the premium in store. The model of Edcon/Hollard is slightly different, as it limits policy holders to account holders of Edgars or Jet. Premiums are added to the customer's monthly account.

- *Tied retailer, bundled insurance sales.* This model is an almost standard feature of credit purchases of furniture and/or electronic goods in South Africa. The most important characteristic of insurance offered through this model is that the purchase of insurance is linked to the credit purchase of another product (e.g. furniture and/or appliances) and only provides cover for the duration of the repayment period. In a number of cases, the retailer owns the underwriting insurer. Although South African credit law gives consumers the freedom to choose a different insurer, the insurance is often bundled with the credit purchase in such a manner that makes it difficult for the client to opt for another insurer. In many cases, the clients are not even aware that they obtained insurance with their credit purchase (See Genesis 2006a). Because of the risk of consumer abuse, the embedded/bundled sales model is of particular interest to the regulator.

Banks sell insurance policies over the counter in bank branches (via an agent) and through separate bank brokerages. Over-the-counter sales in bank branches are targeted at the lower- to middle-income market and insurance sales to this market normally take place when a client opens a bank account or performs another transaction in the bank branch. An interesting version of this model is the agreement between Wizzit, a cell phone bank targeted specifically at previously unbanked individuals, and African Life to sell funeral insurance linked to a Wizzit account. Wizzit bank accounts are distributed through agents who also sell the funeral insurance. The bank distribution model is similar to the use of brokers and agents described above, but it is noted here because of the combination of insurance sales with other financial services. As noted for the retailer model, embedding or bundling with another financial product may complicate the sales process from the client's perspective and is, therefore, of interest to the regulator.

Funeral parlours. In South Africa, funeral parlours' extensive geographic reach (every small town is likely to have at least one funeral parlour), existing low-income client base and ability to collect premiums in cash, ideally positions them as intermediaries to the lower-income market. Funeral parlours sell only funeral insurance and tend to see themselves as selling a funeral service rather than an insurance product. They view the insurance policy as a way of prepaying (and locking in clients) for their services. For this reason, they are often not skilled or educated in financial services and will find it difficult to comply with intermediary regulation. The funeral parlour may be an independent distributor of insurance products of multiple providers, but in most cases it has a relationship (often contractually so) with one insurer. A concern to be noted is the risk that funeral parlours may also sell insurance which is not underwritten by a formal insurer.

MFIs. The non-profit microfinance sector plays a small role in the South African micro-credit market. Accordingly, this market is not of major interest to the insurers

and MFIs have struggled to find an insurance partner to offer products to their clients. The MFI SEF (small enterprise foundation) was the first to move in the insurance space at the end of 2006 with an experiment of intermediating insurance through its own operational structures. This experiment was aborted in the middle of 2007 as it proved more difficult than expected to manage the product within their own operations and they did not want to compromise their existing credit operations. Commercial microlenders (also known as payroll lenders) form a bigger market than non-profit MFIs in South Africa. Here, the same concerns regarding compulsory credit life insurance as noted above are relevant.

Category 5: Low-income affinity groups. The last intermediation model outlined in Figure 1 is the low-income affinity group, a recently emerged intermediary category in South Africa. With the exception of informal burial societies, these groups tend to exist for reasons other than the provision of insurance. Examples include: member-owned mutuals (e.g. informal savings and/or insurance cooperatives), church groups, trade unions and sports fan clubs.

These groups all represent the interest of the client and the intermediation of insurance is initiated as a collective client process rather than by an existing intermediary or insurer. As a result these groups also control access to the clients (who are members of the group). Although they normally have a relationship with only one insurer, the group is independent and can move to another insurer if the products of a specific insurer no longer meet the needs of its members. The management of the group often drives product innovation (with the help of the insurer) and products are tailored to meet the needs of the group members. The largest example is that of the Zionist Christian Church which has an insurance scheme with a number of insurers totalling in excess of 350,000 policies. The church structures are used to collect premiums and administer the policies.

It is important to note that the intermediation role of low-income groups is evolving. In some cases groups such as burial societies have moved from being informal insurers to becoming intermediaries of formal insurance products. In other cases, the low-income group can even evolve from fulfilling an intermediary role to becoming an insurer in its own right. Insurers are, therefore, no longer guaranteed of these groups as easy client aggregators.

Table 1 provides a summary of the variations on the various models found in South Africa and their potential reach[21]. An important distinction made is whether the model is advice-based, or only requires so-called “tick of the box” selling with basic disclosure. As will be apparent from the table, those models able to reach into the lower-income market have all done so on the basis of a non-advice model:

[21] These results are taken from the full Genesis report on insurance intermediation in South Africa prepared for the FinMark Trust (Genesis, 2006b). Please refer to the costing models and calculations applied in the report.

	Model	Example	Products	Bundled/ Embedded/ Standalone	Voluntary/ Compul-sory	Interm. controls access to client?	Independent/ Tied	Accept cash premiums	Advice/ Tick-box/ Disclosure	Main target market
Broker	Traditional broker		All	S	V	Y	I	N	A	High
	Emerging broker		All	S	V	Y	I	N	A	Middle, some low
	Shared brokerage	Masthead	All	S	V	Y	I	N	A	High to middle
	Networked emerging broker	Black Brokers Forum	All	S	V	Y	I	N	A	High to middle
Tied agent	Traditional agent		All	S	V	N	T	N	A	High to middle
	Direct sales (call centre only): Life	1Life	All	S	V	N	T	N	A	High to middle
	Direct sales (call centre only): Property	Outsurance	All	S	V	N	T	N	A	High
	Direct sales and network marketer: Life	Clientele	All	S	V	N	T	N	A	Full spectrum
	Franchised agency	Liberty	All	S	V	N	T	N	A	High
	Agent supported by call centre compliance and administration	Metropolitan (REI)	All	S	V	N	T	N	A	High to middle, some low
	Tiered agency force	HTG Life	Funeral	S	V	N	T	Y	T/A	Middle and low
Multi-function intermediaries	Bank counter/broker	Standard Bank	Credit life, funeral	B/E	C/V	Y	I	N	A	High to middle
	Credit retailer with own insurer	Ellerines	Credit life (with various riders)	B/E	C	Y	T	N	T	Middle, some low
	Independent funeral parlour (multi-function)	Small parlours	Funeral	B	V	Y	I	Y	T	Middle and low
	Cash retailer/OTC plus limited call centre support (independent)	HTG/Shoprite	Funeral	S	V	Y	I	Y	T	Middle and low
	Cash retailer/OTC plus call centre support (tied)	Pep/Hollard	Cell phone, Credit life, Funeral, Personal Accident	S	V	Y	T	Y	T/D	Middle and low
	MFIs	SEF	Funeral	S	V	Y	I	Y	T/D	Low
Low-income affinity groups	Union owned low-income group	Lesaka	Funeral	S	V	Y	I	N	T/D	Middle and low
	Sport fans clubs	Hollard/ Kaizer Chiefs	Funeral	B/E	V	Y	T	N	T	Middle and low
	Informal mutual societies (e.g. burial societies)		Funeral	S	V	Y	I/T	Y	A	Low to middle

Table 1: Overview of salient features of South African microinsurance intermediation models

6. CONCLUSION

The above analysis presented a more detailed approach to the categorisation of microinsurance intermediary models than that commonly found in the international literature. It then applied this typology to define a range of intermediary models in the South African market. It is interesting to note that the proposed categorisation has achieved some consistency internally and across categories. Moving down in the table above, the following trends emerge:

- There is a move from traditional models to newer models reflecting the recent entry of low-income distribution models.
- The low-income market reach increases, but this does not necessarily reflect take-up. Reach is defined from the supplier's cost point of view and, given the recent introduction of some of these models, it is too early to judge the level of take-up.
- There is a move from advice-based selling to tick-box selling where advice or disclosure is at best available on request. This is in line with the cost/reach point made in the previous bullet as models have sacrificed the level of interaction with the client (advice, etc.) in order to reduce cost.
- There is a move from active selling to mostly passive selling models relying on the brand of the intermediary to attract customers. While passive models are much less expensive to operate, it is not clear whether these will achieve take-up in the newer insurance products where more active selling may be required.
- The models start allowing cash collection and, in some cases, even irregular premiums.
- Intermediary control over client group increases. Whereas the new models provide insurers with an alternative over the bank channel, they remain dependent on the intermediary partner for access to the client base.

Furthermore it must be noted that:

- Based on the current market structure and dynamics, broker and agent models are unlikely to make a significant penetration into the lower-income market. This is not only due to the cost structure of these models, but also due to the fact that they are being crowded out by non-advice models. Whether this trend will continue will depend on the success of the new passive sales models and the continuation of the regulatory space currently available for non-advice selling.
- Active selling is likely to be required in order to develop the microinsurance market beyond funeral insurance. Passive models rely on customers taking up the product out of their own volition. While this may work to some extent for funeral insurance, the market will have to be convinced of the value of the new

products which they have to date not been exposed to. To facilitate such active selling at low cost will require clarification on the distinction between advice-based and non-advice selling. In addition, it may also require the extension of uncapped commissions to other product lines. Uncapped commission on funeral insurance have facilitated the entry of formal players into this market.

- The multi-function groups present some interesting opportunities for extending access to microinsurance markets. There is however much variation within this category and specific sub-categories are of particular concern. Potential regulatory and consumer protection concerns arise where insurance is bundled or embedded with the sale of credit or where insurance is used to create a captive market (e.g. funeral parlours). The challenge for these models will be to combine the low-cost channels with at least sufficient disclosure (if advice is not possible) to avoid mis-selling.
- The low-income affinity groups category is successful in reaching into lowest the LSM categories, but reach is restricted to their membership. None of these are intermediating insurance products to the general public. In the case of the unions this membership may, however, be significant.

The South African microinsurance market is in a state of flux which is likely to continue in the near future. The changes in regulation and the introduction of innovative business models and technologies mean that new models are entering and old models are adjusting. Although the new models are promising, they have yet to prove their success. The categorisation suggested above is, therefore, a first attempt to describe the structure of the market, but will have to evolve as the market develops.

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