ALMAO and YASIRU

Sri Lanka

CGAP Working Group on Microinsurance
Good and Bad Practices
Case Study No. 21

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Good and Bad Practices in Microinsurance

This paper was commissioned by the "Good and Bad Practices in Microinsurance" project. Managed by the ILO's Social Finance Programme for the CGAP Working Group on Microinsurance, this project is jointly funded by SIDA, DFID, GTZ, and the ILO. The major outputs of this project are:

1. A **series of case studies** to identify good and bad practices in microinsurance
2. A **synthesis document** of good and bad practices in microinsurance for practitioners based on an analysis of the case studies. The major lessons from the case studies will also be published in a series of **two-page briefing notes** for easy access by practitioners.
3. **Donor guidelines** for funding microinsurance.

The CGAP Working Group on Microinsurance

The CGAP Microinsurance Working Group includes donors, insurers, and other interested parties. The Working Group coordinates donor activities as they pertain to the development and proliferation of insurance services to low-income households in developing countries. The main activities of the working group include:

1. Developing donor guidelines for supporting microinsurance
2. Document case studies of insurance products and delivery models
3. Commission research on key issues such as the regulatory environment for microinsurance
4. Supporting innovations that will expand the availability of appropriate microinsurance products
5. Publishing a quarterly newsletter on microinsurance
6. Managing the content of the Microinsurance Focus website: www.microfinancegateway.org/section/resourcecenters/microinsurance

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Acknowledgements

The authors would like to thank ALMAO and Yasiru for their friendly and open participation in this study. In particular we appreciate that the Board of ALMAO and all the local organisations of both ALMAO and Yasiru took their time to meet us and answer all our questions.

Without the assistance of Mr Ramesh Weerasingham, who was kindly appointed by the CEO of ALMAO, Mr L.B Abeysinghe, and the driver Mr. Kushan Gurugamage, we would not have been able to carry out the study and learn so much about microinsurance in Sri Lanka.

We also owe a lot to Mr Sunil Silva, Chairman and CEO of Yasiru for being so open in our discussions and also for appointing Mr W.M Leelasena and Mr Wansa Abayawickrama to assist us.

We would like to thank Dr. P.A Kiriwandeniya, Chairman of the Sanasa Movement, for giving us the background and strategies for insurance services within the movement.

Thanks also to Mr Upali Herat, Managing Director of the Co-operative Insurance Company Ltd for the interesting discussions concerning the insurance industry in Sri Lanka pre and post the tsunami.

Special thanks to Mr Gerard Pierik and Mr Frank Bakx for their contributions to this report.

Finally we would like to recognize representatives from the Insurance Board of Sri Lanka and ILO of Colombo for assistance and interesting discussions.

Sven Enarsson, Swedish Cooperative Centre
Kjell Wirén, Folksam

Acronyms

ACCDC	All Ceylon Community Development Council
AGM	Annual General Meeting
ALMAO	All Lanka Mutual Assurance Organization
CBO	Community-based Organisation
CUNA	Credit Union National Association
DFID	Department for International Development
FAS	Funeral Aid Societies
GDP	Gross domestic production
GTZ	Gesellschaft für Technische Zusammenarbeit
HQ	Headquarters
IASL	Insurance Association of Sri Lanka
IBSL	The Insurance Board of Sri Lanka
ICMIF	International Cooperative and Mutual Insurance Federation
ILO	International Labour Office
LKR	Sri Lankan Rupees
MFI	Microfinance Institutions
NGO	Non-Governmental Organisation
PMU	Programme Management Unit
PPP	Purchasing power parity
Sanasa	Sakasuruwam Haa Nayaganudenu Pilibanda Samupakara Samithiya (society for thrift and credit)
SEEDS	Sarvodaya Economic Development Services
SIDA	Swedish International Development Agency
SLIC	Sri Lanka Insurance Corporation
TB	Treasury Bills
US$	United States Dollars

Executive Summary

This study covers two microinsurance schemes in Sri Lanka, ALMAO and Yasiru. Both operate through local organisations that manage all fieldwork. The local partners recruit clients/members, collect premiums and administer claims. The main target group for both ALMAO and Yasiru is the rural poor.

ALMAO has operated through the Sanasa (Sakasuruwam Haa Nayaganudenu Pilibanda Samupakara Samithiya) movement, a comprehensive, nationwide network of savings and credit cooperatives. This cooperation has been a great asset for ALMAO, but it has received no other external support. Since its start in 1991, ALMAO has experienced rapid development. Registered as a separate society in 1993, it reached its peak in 2004 when it served just under 50 000 members and had accumulated an equity of almost LKR 50 million ($500,000).

ALMAO's scheme offered coverage for disability, hospitalisation, death and maturity. Its premium structure was well adapted to the target group, with monthly payments ranging from LKR 10 to 100 ($0.2 to $2). The sums insured varied from LKR 3000 ($60) to LKR 50 000 ($1,000). ALMAO also offered the Sanasa societies services like loan protection, life savings, property and health insurance for employees. In 1998, it started a brokering subsidiary through which it serviced the movement with all types of insurance available in the Sri Lanka market, in particular motor insurance for three-wheelers.

With the support of the Sanasa movement, ALMAO was registered as a formal life insurance company in 2002, and in 2005, also as a general insurer. The scheme has become a fully-fledged commercial insurance company. The old society and its products are in run-off, but the ALMAO insurance company is facing problems to market its new products with a minimum premium of LKR 3000 (US$30) per year. The organisation is in the process of developing additional products adapted for people with low incomes and more suited to the customers of the Sanasa societies. It is of decisive importance for ALMAO to succeed with this effort. It has a huge immediate market of 8500 Sanasa societies servicing some 2 million members and non-members. ALMAO has to overcome the problem of developing products that are sound in accordance with insurance regulations while meeting the needs of poorer people with affordable coverage.

Yasiru started in the middle of the 1990s as an in-house insurance service in a federation of NGOs called All Ceylon Community Development Council (ACCDC). In 2000, Yasiru was registered as a special society and ACCDC became its partner for the implementation of the insurance scheme. After a couple of years, Yasiru started partnering with other local NGOs and today it has eight active partners with some 60 000 members. Yasiru is providing insurance to over 9 000 members through its partners. It has accumulated equity and reserves of almost LKR 5 million ($50,000). The product covers death, disability and hospitalisation and has a typical low-income profile. The monthly premiums vary from LKR 10 to 150 ($0.1 to $1.5) and the benefits range from LKR 3000 to 120 000 ($30 to $1,200).

Since its start, Yasiru has been supported by the Rabobank Group and its reinsurance company, Interpolis N. V., through which Yasiru has received funding, technical assistance and a very favourable reinsurance arrangement. Rabobank's contributions to Yasiru's head office, the Programme Management Unit (PMU) will cease in 2005. As in other cases of development cooperation, Yasiru will face problems when the donor support is reduced. Unless Yasiru succeeds to substantially reduce its costs, it needs to increase its annual premium sales by some 60% to fully compensate for the reduced financial support to the PMU. A vital factor is to increase the number of reliable partners.

Yasiru's legal status is unclear. It is registered as a society, but without doubt it provides insurance services even if the word "insurance" is excluded from Yasiru's constitution and operations. A couple of years ago, Yasiru approached the Registrar of Societies and argued that it was allowed to provide its services to members on a mutual basis. The Registrar has so far not responded to the approach. The Insurance Board of Sri Lanka (IBSL) insists that it has no knowledge of Yasiru's operations. Since the organization is not registered as an insurer, the product, pricing and reserves are not formally and publicly analysed and controlled by external insurance professionals. In this situation, Yasiru's cooperation with Interpolis N. V. is of utmost importance.

Lessons Learnt

In the opinion of ALMAO and Yasiru, the following are the most important lessons learnt from their operations:

- Make a careful analysis of the general conditions and the environment and identify needs through consultations with the target group
- Build a system with democratic control and a mutual basis for the service
- Cooperate with established partners in the field
- Collaborate with an established insurance company and act as agent for them, which avoids high capital requirements, but will facilitate access to professional knowledge
- Offer simple, affordable products that can be easily understood by the target group
- Build equity and reserves, especially if the intention is to become a formal insurer
- Minimise maturity but cover death

Conclusions and Observations

1. Both ALMAO and Yasiru are needed in Sri Lanka. The Government does not have resources to offer sufficient social security to the citizens and the penetration of the commercial insurance industry is too limited. There is a huge need for risk management, not only among poor people but also in the middle and lower income classes. Through microinsurance, the private sector can cover up for shortcomings in the existing public and commercial sectors. Successful microinsurance interventions will meet important needs and will also build additional and much needed long-term capital.

2. If ALMAO and Yasiru fail to expand their distribution capacity, they may not survive. ALMAO must reach out to many more Sanasa societies and their customers. It needs to develop attractive products. Yasiru has to increase its network of good partners substantially.

Both organisations need to reach their potential clients/members with insurance knowledge, awareness, marketing and sales.

3. Yasiru's strategy of excluding middle-income groups is questionable. In fact, the viability of the scheme may substantially increase if such people are also targeted. Other measures can be taken to make sure that the original target of reaching rural poor people is not blurred.

4. Most microinsurance schemes will need support in the initial stages. In some cases, the start-up period will cover several years. It is natural that the administrative costs and commissions are high in the beginning, but there should be a realistic, future model of the scheme, illustrating a cost level that is low enough to provide clients with beneficial insurance services. Using existing organisations for distribution of the service is a likely way of running the service efficiently.

5. Donor support for microinsurance needs to be well planned, including a plan for the withdrawal of support. Realistic, long-term budgets should be prepared illustrating how self-sustainability will be achieved. Continual follow up of the cooperation is needed to secure a smooth withdrawal. Products, fees, the building of reserves, etc. have to be carefully analysed by actuaries at the start of the cooperation.

6. Developing countries all over the world have knowingly accepted that MFIs have received deposits from customers without the legally required registration as banks (savings and credit coops are an exception since they are normally allowed to receive deposits from their members). Similarly, informal microinsurance schemes seem to be allowed to give clients/members insurance services even though they lack the necessary license from the government's insurance board. The original ALMAO scheme and the present Yasiru scheme illustrate this awkward situation. A difficult question is how potential donors should act in these situations. Well-designed microinsurance schemes may be of great importance for poor people, but there is no legal framework for them.

7. The transformation of a microinsurance scheme into a registered commercial insurance company needs to be studied further. Can service and products be maintained and/or developed so that they fit both the legal rules and regulations and the needs of poorer sectors in a country?

8. Great care should be taken in all microinsurance schemes to avoid high levels of dropouts.

9. Many governments, like in Sri Lanka, do very little to facilitate development of insurance services for poor people. There is no development of alternative legislation to make it easier to implement microinsurance schemes. There are reasons to believe that many governments lack awareness and knowledge of how microinsurance services may fit into their development plans. The donor community and representatives of developing countries should organise meetings and conferences to spread awareness and knowledge. Models of suitable systems and facilitating legislation should urgently be developed to assist countries in which there is interest in microinsurance.

1. The Context

Table 1.1 Sri Lanka 2004

Macro Measure	Value
GDP ($ Billions)	20.1
Population (millions)	19.5
Population density per km^2	310
GDP/Capita ($)	1031
GDP Growth Rate	5.4
Inflation, annual rate	12 - 14
Exchange Rate (current, X Currency per $1)[1] Average rate 2004	101
Infant Mortality (per 1000 live births)	11.1
Maternal Mortality (per 100,000 live births)	0.2
Access to safe water (% of population)	70
Health Expenditure as % of GDP (public/private/total)	1.69/1.41/3.1
Health Expenditure per capita (US$)	17
Doctors per thousand people	0.5
Hospital beds per thousand people (urban/rural)	3.1
Literacy rate	92.5

1.1 Role of the State in Insurance

The Sri Lankan insurance industry is regulated and supervised on the basis of the Regulation of Insurance Industry Act No. 43 of 2000. The supervisory authority is The Insurance Board of Sri Lanka (IBSL), which has been established under the Insurance Act.

Microinsurance is not covered in the present legislation and there are no plans to accommodate it legislatively. The main current issue as far as legislation is concerned is to increase the capital requirements to LKR 100 million ($1 million) for a life license or general license from 25 million ($250,000) and 50 million ($500,000) respectively.

The IBSL has the power to grant licenses for life and general insurance. During 2004, IBSL registered two companies for general insurance, Allianz and ALMAO. In total, 14 companies are licensed: 11 composite companies with licenses for both life and general insurance; 2 are licensed for life insurance only; and one for general insurance only.

Some key provisions of the Act are:

- Mutual companies are not allowed
- There must be a professional insurer possessing the qualification of Associate of the Chartered Insurance Institute at the managerial level
- Minimum solvency margin in long term business is 5% of the actuarial value of liabilities and 10% of gross premium in general business
- Rating formulas in life insurance are approved by the IBSL
- Tariffs in general insurance do not need to be approved by the IBSL

[1] This exchange rate will be used in all calculations of current figures in this paper.

- Funds in life insurance must be evaluated by a qualified actuary
- Brokers must register annually
- Maximum commission rates in life and general decided by the IBSL

Since there is no provision for microinsurance services in the Act or in any other legislative or administrative regulation, the terms and conditions of the Act shall formally be applied to all insurance activities in Sri Lanka, including microinsurance services. The strict terms of the Act makes it very difficult to operate microinsurance services legally. The lack of provisions for mutuals also reduces the possibilities to establish such services and the plans to increase the capital requirements for insurance companies will, of course, substantially reduce the possibilities further.

Table 1.2 Insurance Industry Basics

Issues	Observations
Name of Regulatory Body	The Insurance Board of Sri Lanka (IBSL)
Key responsibilities of the regulatory authority	Mission: “To ensure that insurance business in Sri Lanka is carried on with integrity and in a professional and prudent manner with a view to safeguarding the interests of the policy-holders and potential policy-holders” Major tasks: *Licensing insurers, registering brokers, testing agents *Solvency margin rules *Policyholders protection fund *Maximum commissions *Instructions for investments * On-site inspections
Minimum capital requirements for insurance license	LKR 25 million ($250,000) for Life Insurance LKR 50 million ($500,000) for General Insurance. The minimum capital requirements for a licence for Life and General insurance will be increased to LKR 100 million (US$1 million) each.
Other key requirements	Only Limited companies can receive a license. Mutuals are not allowed.
On-going capital requirements	Solvency margin of 10% of gross premium in general insurance and 5% of actuarial value of liabilities in Long Term business.
Other key requirements for regulatory.	According to the Act the insurer must appoint at managerial level a person who at least has the qualifications of Associate of the Chartered Insurance Institute. Another requirement is that the IBSL has the power to review all reinsurance contracts
Number and value of regulated private insurers	Total of 14: 11 composite companies, 2 Life and 1 General; Total Premiums LKR 29.6 billion ($295 million).
Number of public insurers	Not existent
Other regulated insurance organizations	45 Insurance Brokers
Number of re-insurers	Nil
Unregulated organizations that offer insurance	Old ALMAO, Yasiru, SEEDS, Women Development Fund in Hambantota.
Certification requirements for agents	Only private persons can be appointed as agents. An insurer or a broker can appoint agents, who must pass tests supplied by the Board before doing long-term business.

1.2 The Role of the State in Social Protection

There is a well-established tradition of providing social protection within the community in Sri Lanka. In an informal manner, the family, the extended family and the local community provide basic social security. The form and coverage of these traditional social services have changed over time but they still exist to a large extent. During the last decades, the traditional systems have been complemented with new NGOs or community-based organisations (CBOs), many of which are supported by donors. The ILO in Sri Lanka has carried out thorough studies of social security services in the country, including those provided by the informal sector. The information in this part of the report is largely based on the ILO studies.[2]

More than 7000 CBOs that deal with an aspect of social security have been identified on district level, including 2100 funeral aid societies, 1300 social development organisations and 1000 welfare organisations. The register of CBOs is not complete and the numbers are likely to be substantially higher, especially for funeral societies. The pattern of informal and formal local organisations is complemented by some 50 international organisations involved in promotion of social services in Sri Lanka.

Although quite extensive, the social protection provided by the adjusted traditional systems and the many CBOs/NGOs has great shortcomings, especially with respect to old-age pension and access to complementary health services.

Social Protection Schemes

The Ministry of Samhurdi and Poverty Alleviation provides a variety of different schemes to assist the poorest families in Sri Lanka. The most extensive scheme is its Subsidy Programme. Families with an income of less than $15 per month qualify to receive monthly Allowance Cards. In 2004, 1.9 million families received this subsidy. The value of the cards varies with the size of the family. The vast majority receive $1.5 to $6 per month. The value of the support is only 5% of the generally used poverty line of $1 per day, but its outreach is significant; some 35% of the population get the subsidy. The study team was not in a position to properly judge the fairness and the effectiveness of the scheme. However, it is commonly accepted that there are significant difficulties in administering high volumes of low value transactions.

Another scheme run by the Samhurdi Ministry is the Social Security Programme. The beneficiaries, classified as poor people, get US$30 when they marry and when a child of a beneficiary marries, they get $10 for the wedding, and $20 for the first child and $10 for the second child. They also get $0.5 per day in hospital for a maximum of 30 days per year and the dependents get $50 at the death of a beneficiary. This programme has paid out over half a million claims since its inception in 1997. Some beneficiaries have of course received more than one benefit.

The Ministry of Samhurdi and Poverty Alleviation manages a number of other schemes although they are not as wide-reaching as these two. Other schemes cover a variety of areas

[2] Diagnostic Report on the Social Security Situation in Sri Lanka, ILO Colombo, 2004; Mapping of the Informal Sector Social Security Schemes in Sri Lanka, ILO, Colombo, 2004

like self-employment, infrastructure, village empowerment, banking and credit services, marketing, nutrition and agricultural development.

The Government of Sri Lanka also promotes a number of programmes to establish old age pension schemes for different categories of people. The target group is the working age population (18 – 65 years). With the exception of employees in public service, most schemes require voluntary contributions by the eligible people. More than half of the working age population is eligible to participate in at least one of these formal schemes, but only 26% to 28% have chosen to enrol.

Health care is free of charge in principal, but the health facilities are insufficient. Even though the Government's Samhurdi Social Security Programme covers 30 days hospitalisation per year, during the assessment surveys, the need to get assistance during hospitalisation was also identified as urgent. It is likely that the greatest need is to cover the loss of income when a bread-earner is hospitalised.

Overall, the State offers a great variety of ambitious security schemes, but these schemes offer inadequate benefits and are fragmented. This is particularly the case with pension schemes. There is a great need of additional risk management and with increasing income levels it is likely that the demand for private insurance services will increase to compensate for the insufficiencies in the public social security network. Currently, the penetration of commercial insurance service is extremely low and only 6% of the population have private life insurance.

State Role in Controlling or Promoting Microinsurance

The insurance act stipulates that no person can use the word "insurance" or any derivate or similar word to describe its service other than registered insurers or brokers. It is, however, not the duty of the Insurance Board of Sri Lanka (IBSL) to police the private sector and make sure that no on-going activity is providing insurance services without proper registration. In fact, IBSL showed no interest in microinsurance when the team met with the Board.

One of the institutions the team has looked at, Yasiru, is registered as a society under the Societies Ordinance. Two years ago, Yasiru asked a lawyer to analyse whether a society could offer mutual benefit services to its members. These services are in fact microinsurance, but they are not called insurance. The opinion of the lawyer was forwarded to the Registrar of Societies and so far there has been no response. This can be interpreted as indifference by the State regarding initiatives to provide poor people with risk management services. It is not known if the Registrar of Societies has been in contact with the IBSL on this matter, but it would be strange if there has been no communication between the two authorities. Indirectly, the reluctance to interfere with ongoing microinsurance programmes is possibly an indication of a facilitating attitude.

The IBSL has appointed a committee to look into the possibilities of facilitating insurance services for poor people. The committee has made no proposals so far. Instead, the IBSL is in the process of trebling the minimum capital requirement for life insurance while doubling it for non-life insurance in the near future. ISBL does seem to be concerned about the possible negative effects of this change on efforts promoting risk management for poor people.

Box 1.1 The Insurance Ombudsman Sri Lanka

The new office of the Insurance Ombudsman Sri Lanka was opened on February 1, 2005. The positive experiences from The Financial Ombudsman Scheme in Sri Lanka led to the establishment of this new office. The objective of the Insurance Ombudsman Scheme is the satisfactory settlement and resolution of complaints/disputes by policyholders of insurance institutions covered by the Scheme. The Ombudsman has the power to make monetary awards that are binding for the participating insurance institutions. Apart from the primary function of attending complaints, the Ombudsman engages in efforts to create greater awareness about insurance among people in Sri Lanka.

The Ombudsman is appointed by the Insurance Association of Sri Lanka (IASL) in concurrence with the IBSL. The initial costs for the office are provided by the members of the IASL, but eventually the costs will be allocated proportionately to insurance institutions in accordance with the number of settled complaints.

1.3 Brief Profile of Microinsurance in Sri Lanka

There are three main carriers of microinsurance in Sri Lanka. ALMAO covers a large part of Sri Lanka with 18 districts and over 50 000 clients. Yasiru operates in 6 districts and has just under 10,000 members. Apart from Yasiru and ALMAO**,** there is also another scheme called SEEDS (Sarvodaya Economic Development Services Ltd) that has been operating for seven years. This microfinance organization comprises of around 3,000 village societies with 300,000 savers and 150,000 borrowers. SEEDS offers loan protection upon the death of a borrower, it pays the remaining debt to the Society. It additionally pays an amount equal to what the borrower already has repaid to the deceased's family/beneficiaries. In addition there is a Women Development Fund in Hambantota district that provides microinsurance services for its members.

The key trend is to operate through partner organisations and both ALMAO and Yasiru have the ambition grow within their respective markets. The schemes need to increase their distribution capacity quite substantially. For ALMAO, this means increasing the number of agents and insurance desks within the Sanasa movement; for Yasiru, this means entering into agreements with a number of new NGOs/CBOs.

In 2002, the ALMAO scheme was licensed as a life insurance company and is regulated like all other insurers in Sri Lanka. The Insurance Board of Sri Lanka, however, officially has no knowledge of the Yasiru scheme. Although the IBSL is aware that life insurance only covers 6% of the total population, there are no plans to make life insurance services more accessible for poor people in rural areas. The fact that the capital requirements will be increased to LKR 100 million ($1 million) will not contribute to the promotion of legal microinsurance projects.

The newly established Office of the Insurance Ombudsman (see Box 1.1) states that there is a "woeful need to create a greater awareness about insurance among our people". But nothing that could facilitate insurance services among poor people in rural areas can be expected from the Government or the IBSL in the near future. It is fair to say that there is no state assistance for the development of microinsurance in Sri Lanka.

2. The Institutions

2.1 History of the Institutions

ALMAO

A survey in 1989 showed that the funeral aid societies (FAS) were the most appreciated CBOs among poor people in Sri Lanka. On this basis, ideas were formed about providing poor people with coverage for a wider range of risks. In 1991, an insurance scheme was started by seven cooperating FASs; one hundred and eighty two people joined the scheme, which provided coverage for death as well as disability caused by accidents, falling from trees, poisoning, fire and lightning, floods and snake bites. These risks were identified by the participating villagers.

In 1993, the informal scheme became All Lanka Mutual Assurance Organisation was registered under the Society Ordinance as an apex body of the partner organisations. ALMAO was closely related to the Sakasuruwam Haa Nayaganudenu Pilibanda Samupakara Samithiya, Sanasa, (see Box 2.1), a wide-reaching and well-established movement based on savings and credit cooperative societies.

Box 2.1 The Sanasa Movement

The basis of the Sanasa movement is cooperative savings and credit societies. Most of these societies are located in rural areas and provide members with simple savings and loan services. They are small organisations, normally run by a few local people and guided by a board that is elected by the members. The development of the movement started in 1906 and it is the oldest branch of the cooperative movement in Sri Lanka. The number of societies and members increased during the first three decades but between 1937 and 1978 the movement stagnated. There were around 1,200 rather weak societies by that time. In 1978, the movement was inspired by a new leader, Dr P.A. Kiriwandeniya. During his leadership, the movement grew rapidly and now has around 8500 societies with more than 800 000 members. The total savings accumulated in 2004 was LKR 3,730 million (US$36 million). The total amount of outstanding loans was LKR 2,778 million ($27 million).

In 1997, the movement started its own bank, the Sanasa Development Bank. It is registered as a development bank according to the bank regulation in Sri Lanka. In 2004, the bank had share capital of LKR 216 million (US$2.1 million), customers' deposits of LKR 2,310 million (US$23 million), and an outstanding portfolio of LKR 2,028 million (US$20 million).

ALMAO did not receive assistance from any outside sources except for a contribution of LKR 80,000 (US$800) from the Forum of Development, an apex NGO. Until 1996, ALMAO's operation was managed by voluntary workers, normally engaged by a Sanasa society. The rapid growth afterwards, however, required specific salaried staff. In 1996, ALMAO also merged with the insurance section of the Sanasa Federation. At this time, ALMAO intensified its cooperation with the Sanasa societies and provided a wider range of services: loan protection, life savings and property insurance.

In 1998, ALMAO established a brokering subsidiary of to service the Sanasa societies as well as provide members and non-members with motor insurance and other non-life insurance. During 1997 and 1998, three more types of life insurance policies were introduced.

In 2002, the movement mobilised capital and a commercial life insurance company was registered under the name of Sanasa Almao Insurance Company. In 2005, the company was also granted a licence to provide general insurance. ALMAO is now a fully-fledged composite commercial insurance company. The activities of the original ALMAO society are phased out. However, the dropout rate is rapidly increasing and is expected to be around 40% during 2005. The effect of non-renewals on the emerging microinsurance market is probably negative and will be further elaborated in Chapter 7. In this report, the activities of the original ALMAO society will be referred to as the "old" and the activities of the ALMAO insurance company as the "new". For the last couple of years they have overlapped. During 2004, substantial assets from the old scheme were transferred to the new company. In the factual description of ALMAO, in particular in the tables, the figures for the period 2000 to 2003 are from the old scheme. Figures for new insurance company are shown for 2004.

The target group of ALMAO was initially people between 16 and 65 years old who were members of Sanasa societies, funeral aid societies, or other types of CBOs. Other people could become members of ALMAO through contacts with the local Sanasa Society or a FAS. Most clients were small-scale farmers or self-employed people in rural areas. Only members were covered and their family members had to join as individual policyholders to enter the scheme. To emphasize its focus on the poor, the scheme excluded persons who were employed in the public or private sectors.

The old scheme covered disability, hospitalisation, death and life savings**.** The premiums were paid monthly and ranged from LKR10 to 100 $0.1 to $1) in the beginning, and from LKR 25 to 250 (US$0.2 to 2) since 2001.

The insurance services provided by ALMAO have been developed progressively. Before the registration of the Sanasa ALMAO Insurance Company, the ALMAO Society offered a variety of services to its members and to the members of Sanasa savings and credit cooperative societies as well as to non-members. The services of the old scheme, including the services offered through the brokering subsidiary, were as follows:

- Four life insurance schemes, covering disability, hospitalisation, death, loss of house, maturity and funeral expenses. In 2002, 46,980 members had policies, representing a steady growth since 1996 when only 6,430 members were covered.
- Loan protection services to the members of 773 Sanasa societies
- Life savings to the members of 161 Sanasa societies
- Property insurance to 388 Sanasa societies
- Health insurance to employees of the Sanasa societies
- Funeral aid insurance
- General insurance to members and non-members through the brokering company

The growth of ALMAO's services was rapid, but still it covered less than 10% of the Sanasa societies. The 8,500 societies, with some 800,000 members, represent a great potential for further development. Considering that most Sanasa societies also give simple services to non-members, who actually seem to outnumber the members, this distribution channel indirectly reaches almost half the population of Sri Lanka if 4 to 5 dependents are added for each member/non-member.

In 2002, the premiums for life insurances amounted to LKR 15 million ($150,000). The total annual premium for the non-life insurances was LKR 10.7 million ($111,000).

The Sanasa Federation, which provided loan protection, etc. to the Sanasa societies, transferred its loan protection programme to ALMAO in 1996. Since 1992, Sanasa had an arrangement for reinsurance with the CUNA Mutual. This passed on to ALMAO as well, but it ceased in 1997 when a change in CUNA Mutual's strategy led to its withdrawal from a number of developing countries. ALMAO instead reached an agreement with the Sri Lanka Insurance Corporation, SLIC, which at that time was a state company and had around half of the insurance market in the country (SLIC was privatised in May 2003)**.** The agreement covered non-life and half the premiums were paid to SLIC for reinsurance on a 50–50 quota-share basis. In 2002, when ALMAO was registered as commercial company most of the business was reinsured with NTUC Income of Singapore and since January 2005, all of ALMAO's formal insurance is reinsured with NTUC.

Table 2.1 The Old ALMAO – Trends

	2003	2002	2001	2000
Total assets ($)	597 000	511 000	362 000	302 000
Annual budget ($)	255 000	186 000	154 000	140 000
Equity ($)	504 000	462 000	326 000	277 000
Number of branches	4	4	3	2
Total number of all clients	37 154	46 980	36 754	32 403
Total number of microinsurance policyholders	37 154	46 980	36 754	32 403
Total number of microinsurance insured lives	n/a	n/a	n/a	n/a
Number of microinsurance staff, HQ – branches, life only, excluding staff in Sanasa societies	35 - 30	32 - 25	30 - 20	28 - 16
Staff turnover (%), management estimate	10	10	10	10
Number of policyholders / microinsurance staff	572	824	735	736
Microinsurance marketing costs	n/a	n/a	n/a	n/a

Table 2.2 Insurance Organisation Basics - The new ALMAO

Issues	Observations
Legal structure	Limited Insurance Company
Registration status	Licensed as Sanasa Almao Insurance Company Ltd for long term and general insurance
Regulation status	Regulated by the IBSL
Start of corporate operations	Long-term operations started in 2002; general insurance in 2005.
Start of microinsurance operations	1991
Core business	Long term
Target market – core business	Low-income people
Geographic area of operation	All of Sri Lanka except northern and eastern part
Partnership with other institutions	Cooperation with the Sanasa Movement.
Reinsurance provider, type	NTUC Income in Singapore, Quota share

YASIRU

The All Ceylon Community Development Council, ACCDC, also called SLPSM in Sinhala, was started in 1987 as a federation of CBOs. It covers seven Districts, mainly in southern Sri Lanka, and supports a range of CBOs like savings and credit societies, farmers' societies and funeral aid societies among others. The close cooperation with funeral aid societies convinced ACCDC that risk management was a high priority among poor people in rural areas. In the mid-1990s, the ACCDC had developed an insurance package as a complementary service to what the funeral aid societies were providing. The package included coverage for death and disability caused by accidents, and it also covered fire and lightening damage as well as crop failure. The premiums varied from LKR 10 to 50 per month ($0.1 to $0.5), and the benefits varied correspondingly. Although the scheme was not recognised by the insurance board, the state-owned insurance company, SLIC, provided reinsurance for the death coverage in the scheme (but not for the other parts of the package). The package was designed without insurance expertise and ACCDC soon realised it would not be possible to reimburse all the claims. Paid premiums were refunded and the scheme was simplified and re-launched. The fee range remained the same, but the coverage was limited to:

- Total or partial permanent disability caused by accident
- Death caused by accident
- Natural death
- Hospitalisation of member

The maximum limit of cover was LKR 20,000 ($200) and the service was offered to the poor strata of villagers. A monthly earning of LKR 3,000 ($30) or above per family member disqualified one from membership. Even though the scheme was not publicly registered as an insurance service, the state insurance company, SLIC, gave technical assistance in the form of training.

In December 2000, the scheme was registered as a separate entity under the name of the Yasiru Mutual Provident Fund (generally called Yasiru). It was registered as a special society under the Society Ordinance. During the first couple of years, Yasiru only worked through ACCDC and offered its services to the members of affiliated CBOs. It later started cooperation with other NGOs and today it has eight partners with almost 60,000 members. Yasiru's membership is 9,100.

The covered risks have remained the same, but the monthly fee range has been adjusted to LKR 10 to 150 ($0.1 to $1.5). The greatest change is that children and other adults in the family can be included under the same policy.

In connection with the registration in 2000, Yasiru started to cooperate with the Rabobank Group of the Netherlands. The Rabobank Group was involved earlier in ACCDC's insurance services and was actually instrumental in setting up Yasiru as a separate entity. Interpolis N.V., a reinsurer connected to Rabobank, signed an agreement to provide long-term reinsurance for Yasiru as well as technical.

The central management and administration of the Yasiru scheme is called the Programme Management Unit (PMU) and is operationally, although not legally, a separate unit. In practice, the PMU functions as the head office of the Yasiru society. This study team has treated the provident society and the PMU, as one unit.

Table 2.3 Insurance Organisation Basics – Yasiru

Issues	Observations
Legal structure	Registered Society
Registration status	Registered in 2000 under Societies Ordinance No. 16 of 1891.
Regulation status	Regulated by the Registrar of Societies
Start of corporate operations	2000
Start of microinsurance operations	2000 (under ACCDC since 1997)
Core business	Micro insurance
Target market – core business	Low income and poor members of NGOs or CBOs
Target market – insurance business	Low income and poor members of NGOs or CBOs
Geographic area of operation	Southern part and middle part of Sri Lanka
Partnership with other institutions	Agreement with seven NGOs/CBOs.
Reinsurance provider, type	AV Interpolis of Holland, Quota share

Table 2.4 Yasiru - Trends

	2004	2003	2002	2001
Total assets (US$)	58500	42100	23800	12900
Annual budget (US$)	18200	11600	13500	9600
Total equity (US$)	48900	39600	14900	12700
Number of partners	8	6	1	1
Total number of all clients	9090	6265	3780	2698
Total number of microinsurance policyholders	9090	6265	3780	2698
Total number of microinsurance insured lives	23780	22609	9472	8151
Number of microinsurance staff, PMU + partners Partners' staff is not always on full time	7 + 48	7 +36	5 + 6	5 + 6
Staff turnover (%), head office only	15%	20%	20%	20%
Number of policyholders / microinsurance staff (%)	190	145	345	245
Microinsurance marketing costs ($) Training and field work not included	140	100	20	20

2.2 Organisational Development

ALMAO

ALMAO has continually changed since it started offering simple insurance services in 1991. It registered as a society in 1993, merged with the insurance section of Sanasa Federation in 1996, established a brokering subsidiary in 1998, registered as a commercial life insurer in 2001, and then as a composite insurance company in 2005. During the first five years of operations, the services were run by voluntary workers. In recent years, ALMAO has been managed by professional insurers in accordance with the insurance regulations of Sri Lanka.

The shareholders' annual meeting elects a board of 11 people, mostly from Sanasa societies. The Chief Executive Officer is a qualified insurer and is, in accordance with the regulation of the insurance act, responsible for the viability and reliability of the insurance company. A General Manager manages the operations of ALMAO. The organisation has four main departments: Life insurance, General insurance, Accounts and Finance, and Marketing and Training. There are 5 branch offices organised under the Marketing and Training department.

There are 60 employees in Head Office, including some officers who mainly operate in the field, and 35 employees in the branches. Top management has significant experience in the insurance industry. Many of the other officers also have previous experience of insurance, including work with ALMAO's brokering company. Practically all employees have passed A-levels as their basic education (roughly 13 years schooling) and about a quarter have diplomas (for instance in management or insurance).

ALMAO has about 300 agents who carry out the field marketing and premium collection and are involved in settlement of claims. Ninety percent of the agents are from Sanasa Societies and 10% are independent. The officers in the Sanasa societies who work as agents are normally employed by the Society and the commission is usually collected in full by the society. Some of these officers work full-time on ALMAO's services and some also do other work for the Sanasa society. A number of societies have opened separate ALMAO desks. It has not been possible to properly analyse whether the commission received by the societies covers the costs of the services provided. However, the societies visited seemed satisfied with the arrangement and indicated that it was profitable for them.

The minimum education level required for agents is O-levels (11 years' schooling). The agents are supervised and supported by Sales Promotion Officers who are employed by ALMAO. Nowadays, agents must pass a test organised by the IBSL to sell long-term products.

Throughout its existence, ALMAO has developed and indeed deepened its cooperation with the Sanasa movement. There is also no doubt that in the near future, ALMAO's expansion will take place within Sanasa. Currently, ALMAO's services cover only 10% of the societies. Another 7,500 societies, with around 800,000 members, have not yet been involved in the insurance scheme.

Yasiru

The Yasiru microinsurance scheme started as an in-house service of the ACCDC, managed by its staff. After a couple of years (in 2000), Yasiru was registered as a separate entity, with a 5-person staff that constitutes of the Programme Management Unit. For another two years, it only served members of organisations associated with the ACCDC. Today, the PMU of Yasiru shares its office with ACCDC, but it provides services to another 8 partner organisations. It now has 8 staff including a secretary, manager and an accountant. The chairman of Yasiru, Dr Sunil Silva, is responsible for the overall operations of Yasiru, and acts as the General Manager of the society. The small Head Office is divided into four departments: Finance and Administration, Research and Development, Planning and Networking, and Mutual Administration.

The main difference between Yasiru and ALMAO is that the latter has evolved into a professional insurance company, whereas Yasiru is a peoples' development organisation providing insurance services. No staff in Yasiru have any professional experience in insurance. The general education level of the staff is A-levels or O-levels.

Yasiru’s partners play a crucial role in the operation of the services. The partners are all local NGOs with field operations. They have different structures and objectives; but they all deal with the poorer strata of the rural population. They are expected to set up a microinsurance unit with one coordinator, four field officers and one accountant. The partner organisation carries out the recruitment of members/clients, the underwriting and the claim procedure in the field. For recruitment, the partners engage animators, who also collect the premiums and participate in the processing of claims. The partners share the commission with the animators but the division of the commission differs from one partner to another. The partners visited by the research team were satisfied with the financial outcome of the arrangements, but there were no specific accounts available to calculate profits or losses.

The members of the Yasiru society are the policyholders. Members in each of the 9 partners’ operational areas meet to elect 7 representatives for the Annual General Meeting (AGM). They elect 7 representatives irrespective of how many clients/members the partner has recruited. Currently ACCDC has recruited 5,100 clients and the smallest partner has recruited only 290. The AGM elects the Board of Yasiru and of course considers the Annual Report for approval. The chairman and the treasurer of the Board are also part of the leadership in Yasiru’s Programme Management Unit (PMU), which manages the Yasiru’s operations.

The partners are represented in Yasiru’s structure. There is a Central Committee that meets quarterly to review the progress of Yasiru and makes recommendations to the Board. All the partners are represented in the Central Committee.

Training

The Sanasa movement has a large training campus near Kegalle, 70 kilometres northeast of Colombo. The campus has four colleges; one for the commercial Sanasa bank, one for the Sanasa savings and credit societies, one for ALMAO, and one for women. The latter college trains women in self-employment and certain women and child related activities.

Insurance is integrated in all training at the campus. The goal is to make the Sanasa movement knowledgeable about insurance so that the members understand insurance and that staff and board members can provide the membership with ALMAO’s services.

The ALMAO college provides training for targeted groups like marketing officers, board members, and selected agents. The college is also involved in training at the District-level, and, in particular, in the training of agents. All agents recruited from 2003 onwards will have to pass IBSL’s test to be allowed to deal with long-term insurance.

Most agents have received 2 to 3-days of training locally, but some received training at the college. District Marketing Officers get provisional employment for three months during which they receive 2-days training at local level and 3 days at the college. It should be pointed out that there is no standardised training programme implemented. There are variations in training between different areas.

Yasiru is a much smaller organisation and cannot organise a standardised training system for its limited staff. Animators normally get one-day of training in the partner's locality. More advanced, 2 to 3-day follow-up courses are organised intermittently for animators by several partners. Women animators, though, have difficulty travelling for external courses. Other training, for staff of a new partner, is organised in accordance with need and is often carried out by the head office staff.

2.3 Resources

Although they are very different in size, the main resource for both ALMAO and Yasiru are their partners. ALMAO has the required share capital of LKR 75 million ($750,000) to operate both life and general insurance services and has a staff of nearly a hundred employees. Still, the resources available in the Sanasa movement to assist in the provision of the services are much greater. The thousands of employees, the 800,000 members and even a greater number of non-member customers, represent a giant resource and market for ALMAO.

ALMAO's professional staff and its reasonably well qualified general staff is comparatively good in the implementation of microinsurance services. The ALMAO college is another important resource in this respect.

Yasiru, with its small head office of 8 employees, builds its operation through participation of its partners. The strength of Yasiru is its genuine inclination towards the development of poor people, but embedded in it is the risk to underestimate the financial requirements such as profitability and long-term viability**.** The partners visited by the study team were satisfied with the financial terms and conditions of their participation. If this is correct, then there is potential for Yasiru to engage more partners and expand the services to more members. This will certainly increase its long-term viability and there are numerous development organisations in Sri Lanka that could be potential partners.

2.4 External Assistance

Besides a token grant of US$1,600 from a local NGO apex, the ALMAO scheme has not received any formal external assistance. In particular, no foreign donors have been involved in ALMAO's development. However, the support to ALMAO from the Sanasa movement and its leadership cannot be underestimated. Without its close cooperation with Sanasa, ALMAO's rapid development, from a small microinsurance scheme to a fully-fledged insurance company, would not have been possible.

The cooperation with CUNA Mutual, and later SLIC, on reinsurance cannot be termed assistance since it mainly was done on a business basis. ALMAO recently became a member of ICMIF, the International Cooperative and Mutual Insurance Federation.

Yasiru was started as an in-house service to the members of ACCDC partners. It was supported by SLIC in the area of reinsurance and training. ACCDC had earlier cooperated with the Dutch Rabobank Group. When Yasiru was registered as a special society in 2000, formal links were established with Rabobank, which agreed to support Yasiru. A development cooperation agreement was signed that included a long-term re-insurance arrangement with Interpolis N.V., the group's re-insurance provider. Interpolis N.V. has also provided technical assistance to Yasiru. The PMU of Yasiru received substantial financial support until the end of 2004.

The re-insurance arrangement with Interpolis N.V., which has been very favourable for Yasiru, is still in force, but the conditions are under adjustment to become more business like.

2.5 Risk Management Products

Since ALMAO received its insurance licence, it changed its portfolio of products quite drastically. From providing products with monthly premiums starting at LKR 10 per month, it now offers four different life products with a minimum annual premium of LKR 3,000 ($30).

The products offered by ALMAO cover death risks, but also include endowment policies. On the basis of its long cooperation with funeral assistance societies, ALMAO has seen the need for substantial capital if the insured dies prematurely. Its product, "Pilisarana" where 2 to 2.5 times of the sum insured and bonus is payable upon policyholder's early death demonstrates this. The maturity amount, on the other hand, is reduced to 60% of the sum insured. This shows ALMAO's intention of providing insurance in order to help low-income people when they really need assistance and not only as a form of capital investment, like most life insurers do in Sri Lanka.

The products offered by Yasiru can be regarded as more typical microinsurance products. They offer cover for death, permanent disability and hospitalization. Yasiru offers products that are affordable for the members and give reasonable compensation in case of death, permanent disability or hospitalization. The members are classified in four classes according to their family situation. In each class, members can choose among 4 monthly premiums. The member, with the advice of an animator, decides how much he is willing to pay per month. Monthly premiums start at LKR 10 ($0.1) and the maximum premium is LKR 150 ($1.5) per month. The benefits increase in relation to the size of the premium.

There is no actual maturity payment in the scheme, but there is a mechanism for profit sharing. Yasiru opens an account for each member. When a member reaches the age of 75, or terminates the membership, he/she will receive the credit balance of the account if the membership has lasted for more than five years. Forty percent of the scheme's profit is credited to members' accounts.

2.6 Profit Allocation, Distribution and Investment Policies

Yasiru has a very clear policy on profit allocation. Half is allocated to a Risk Fund to build up reserves for future claims, etc. Forty percent is allocated to the members' individual accounts, which, upon termination of membership after 5 years, will be paid to the member. Ten percent is contributed to a Welfare Fund that finances certain extra, health-related benefits to members outside the normal benefit package. Examples of such extra benefits are contributions to eyeglasses or wheelchairs.

ALMAO's policy on life insurance is that at least 90% of the profit shall benefit the policyholders. Normally, the surplus will be allocated to Life Funds for later payment to clients. The current policy on general insurance is to use part of the profit for no claim bonuses to policyholders. Historically, though, the old ALMAO scheme used surplus to increase its own capital, which grew from LKR 10.3 million ($103,000) in 1998 to LKR 44.5 million ($445,000) in 2002. The recently registered commercial insurance company will have a similar need to build up its own capital.

The investment policy of both Yasiru and ALMAO is conservative. ALMAO aims at keeping 30% of its investments in Treasury Bills (TB) and the remaining as fixed deposits. Yasiru keeps all of its investment capital in fixed deposit accounts, normally with government banks. The return of both TBs and fixed deposits is around 9%, compared with an inflation rate of around 13%.

2.7 Reinsurance

Both ALMAO and Yasiru have managed to obtain reinsurance with credible reinsurers. ALMAO has an agreement with NTUC Singapore for its new life business. Claims in excess of LKR 100,000 ($1,000) are paid by NTUC. The premium is 50 % of the risk premium. For the Funeral Assistance insurance, ALMAO had an agreement with SLIC up to the end of 2004, but now it is reinsured with NTUC on a quota share basis.

Since its operations started, Yasiru has been reinsured with Interpolis as part of its development support. The favourable terms would not be available in the open market. Yasiru lacks reinsurance coverage for hospitalization claims. Since the number of claims, as well as cost for hospitalization, is increasing, it is desirable that the service is reinsured, but it is difficult and expensive to reinsure health services.

3. The Members

Table 3.1 Client Information Table

Issues	Observations ALMAO	Observations Yasiru
Intended target groups/clients	Old scheme: Poorer sections and disadvantaged groups New: Villages and low income communities	Rural poor without permanent employment.
Actual clients and reasons if deviation from intended market	Most of ALMAO's clients are members of the Sanasa societies. Many are middle and low income earners and do not consider themselves among the poorest strata	Small-scale farmers, estate workers and rural people with low income. A formal upper income limit of LKR 3000 ($30) per household member per month is not strictly applied. Animators avoid "rich" people.
Exclusions of specific groups	Old scheme: -People with permanent employment -People under 18 and over 65 -Disabled people In practice permanent employment has not been a hindrance New: Underwriting rules differ for each type of insurance. No group exclusions	Membership can only be started after 18 years of age and before 60. Children between 3 months and 18 years and persons between 18 and 75 years may be covered. Government employees were earlier excluded. Now the guideline is to exclude households with an income of LKR 3000 per household member per month. (see under "Actual Clients" above)
General economic situation of clients	Middle and low income earners with bank accounts in the Sanasa movement	Small-scale farmers and people from the informal sector.
Key economic activities of clients	Employment and self-employed, traders and taxi drivers (three-wheelers)	Farming, estate workers, casual labourers, informal sector activities
% of clients in the informal economy	Estimate: 5-10 %	Estimate 15 – 30%, most other clients are farmers
Social characteristics of clients	Mainly rural and semi-urban families with stable but low or middle incomes. A majority are women.	Farmers and people from the informal sector in rural areas. Low income. 64% are women.
Geographic characteristics	Covers 18 Districts with 90% of the country's population, excluding the north and north-eastern areas (Tamil areas). Main operations in small towns and rural areas.	Operates in the rural areas of 6 Districts in central and southern Sri Lanka.
Nature of membership	Old: members of the ALMAO society New: clients of the commercial ALMAO company	Clients are registered members of the Yasiru society.
Methods of recruitment of clients	Through field agents employed by Sanasa societies	8 partners organise animators to do direct recruitment among their members and others

3.1 Socioeconomic Conditions

Since ALMAO operates in almost all of Sri Lanka, with the exception of Tamil-dominated districts in the north and northeast, the general conditions of the country are also ALMAO's conditions. Sixteen of the 18 Districts are in rural areas and 69% of the population is rural. Agriculture is the main source of livelihood. Rice, vegetables, fruits, tea, coconut and rubber are the major agricultural crops. Some 17 million people live in the Districts and 1.4 million of them stay in commercial plantation areas. The population density is high, between 200 and 600 hundred people per square kilometre, in most of ALMAO's operational area. Sri Lanka defines poor people as those in the lowest four deciles of the average per capita expenditure who spend more than 50% of household expenditure on food. The percentage of poor people in the 18 Districts varies from 48% to 9% (Colombo). In Kegalle District, which is the heart of ALMAO's operations, 36% of people are classified as poor. The average number of hospital beds per 1000 people in Sri Lanka is 3.6. In half of the Districts where ALMAO operates, this figure is between 2 and 2.8. The average household size is 4.2 to 4.6 members per household.

Yasiru operates through its partners in 6 rural Districts with a total population of 4 million. Seventy-eight percent live in rural areas. The population density varies from 72 people per square kilometre to 673. Agriculture is the main economic activity and common crops are rice, vegetables, fruits, tea, coconut and rubber. The average household income in these Districts is lower than the country average. The provision of health facilities is also below the average for the country.

3.2 Major Risks, Vulnerabilities

Both ALMAO and Yasiru have involved the intended target group in identifying the risks faced by the group. Based on this, the insurance coverage of the two schemes is similar; in particular there were great similarities between the old ALMAO scheme and Yasiru. Death, accidents and disability, hospitalisation and funeral costs are the risks that worry the target group.

Other risks that are of concern are loss of crop caused by floods or elephants, loss of household assets (for instance due to floods or mudslides), and the risk of being unable to pay for the education of children. For a short period in the mid-90s, ACCDC actually tested an insurance scheme that had a broad coverage including crop insurance. It quickly realised that this was unrealistic and premiums were repaid to the members. This experience and contacts with commercial insurers (SLIC, CUNA Mutual and Interpolis N.V.) helped the ACCDC and Yasiru in limiting the schemes to risks that could be viably insured.

Thefts, robberies or fires are not risks that cause considerable concern among the target group. After its registration in 2005 as a general insurance company, ALMAO is in a position to offer property insurance, but so far coverage for property has not been included in what ALMAO considers to be its microinsurance services.

The common risk coping strategy for low-income people, both in urban and rural areas, has been membership in funeral aid societies or similar informal groups. In Sri Lanka, these groups often consist of 60 to 100 households and it seems that the groups help out in different types of emergencies (see Box 3.1).

Box 3.1 Funeral Aid Societies

The societies in Sri Lanka have deep traditions in providing basic informal social security in different forms. In times of great difficulties, assistance has been provided by immediate family, other relatives, neighbours, cheettu groups (rotating savings and credit groups) and Funeral Aid societies.

Most of the local communities have some sort of organised cooperation to provide funeral assistance to their members. The role of the Funeral Aid societies and also of the other parts of the local social security net varies from one area to another. What is typical for a Funeral Aid society is obvious from its name; it provides assistance in case of death. Very often the assistance is given not only for the death of the member of the Funeral Aid society, but also when the spouse or children of the member die. There is no standard for the type of assistance given by a society. In one of the reports from ILO[3] reference is made to a sand-miners' village, Diyagma, where the Funeral Aid society pays LKR 3,500 ($35) if a members dies and LKR 3,000 if other family members die. It seems that most Funeral Aid societies raise the money when the need arises but some societies administer small amounts of accumulated capital. In one Funeral Aid society, it was suggested that capital should be raised to give assistance to the elderly and disabled persons. It is likely that a number of Funeral Aid societies give assistance for purposes other than the occurrence of death, but the knowledge about the functions of the societies is incomplete.

The Funeral Aid societies and other parts of the local social security net can only provide a very basic social security. The protection is still important for the most vulnerable in the local community. According to the quoted ILO report, this traditional fallback mechanism has weakened with time and made the vulnerable even more vulnerable. The tendency seems to be that when better off people get an improved formal security, their support to the traditional social security net is reduced.

However, both Government Organisations and NGOs are showing interest in cooperating with and supporting the existing social security CBOs, not least the Funeral Aid societies.

The numerous funeral aid societies and other informal social services in the community, together with ALMAO's and Yasiru's services, provide an improved basic risk management for the target group under the prevailing circumstances. The members seem to have sufficient knowledge about the complementary insurance schemes to be able to utilise the services.

[3] Mapping of the Informal Sector Social Security Schemes in Sri Lanka, ILO, Colombo

4. The Product

Table 4.1 Product Details – The New ALMAO Products

	Product Features and Policies
Microinsurance type	Long term, Life, Accident and Loan Protection
Group or individual product	Individual; Group insurance for funeral assistance
Term	Annual
Eligibility requirements	Not below 18 years and not above 65. Each application is subject to strict underwriting rules
Renewal requirements	Premium payment not in arrears
Rejection rate	Very few, 1– 2% only.
Voluntary or compulsory	Voluntary
Product coverage	• Sum insured + bonus paid upon accident, disability or death of policyholder/covered persons • Daily, monthly amount during time of hospitalization • On maturity: whole or part of sum insured + bonus
Key exclusions	Suicide during first 12 months
Pricing – premiums	Minimum premium LKR 3,000 (US$30) annually Funeral cover LKR 172,50 (US$1.7) annually
Pricing – co-payments and deductibles	No deductibles or co-payments
Pricing – other fees	No other fees

Table 4.2 Product Details - Yasiru

	Product Features and Policies
Microinsurance Type	Life, Accident, Hospitalization
Group or individual product	Individual
Term	Annual
Eligibility requirements	Members above 18 years but not older than 65. No families with an income of more than LKR 3000 (US$30) per family member (the rule is not strictly applied in the field)
Renewal requirements	Premium payment not in arrears
Rejection rate	No rejections
Voluntary or compulsory	Voluntary
Product coverage	• Sum insured paid upon accident, disability or death of policyholder/covered persons • Daily or monthly amount during time of hospitalization • On termination of membership after at least 5 years; the amount on the member’s account
Key exclusions	Suicide and contagious diseases
Pricing – premiums	Monthly premiums from LKR 10 (US$0,1) to LKR 100 (US$1.0)
Pricing – co-payments and deductibles	No deductibles or co-payments
Pricing – other fees	No other fees

4.1 Partners

ALMAO

Since inception, ALMAO has been closely integrated with the Sanasa movement. Through Sanasa, ALMAO distributes its products, collects premiums and processes claims. The chairman of the Sanasa Development Bank is also the chairman of the Board of ALMAO Assurance Company Limited.

In the initial stages, ALMAO had reinsurance cooperation with CUNA Mutual. CUNA Mutual withdrew from Sri Lanka and most other developing countries in 1997. At that time, ALMAO established a reinsurance contract with SLIC. When ALMAO was licensed for life insurance in 2002, NTUC Income from Singapore became its reinsurance partner. Besides the reinsurance partners, no donors or other organisations have supported ALMAO financially or technically. It is the Sanasa movement that has facilitated ALMAO's development.

Yasiru

When ACCDC started its insurance service as a forerunner to Yasiru, it cooperated with SLIC. SLIC provided reinsurance and some technical assistance. When Yasiru was established as a separate entity, it established cooperation with Rabobank and Interpolis N.V. and has been supported by them throughout its operations. Rabobank has offered various types of support, which covers technical know-how, computer hard- and software, and financial contributions. Interpolis N.V. has implemented the technical support and provided the reinsurance facility.

ACCDC was Yasiru's predecessor's partner and the only implementing partner for a couple of years after Yasiru's inception. During the last three years, the number of partners has increased to 8 with a total of 60,000 members, and discussions are going on with other potential partners. So far the field partners have been NGOs, but Yasiru is also discussing with the Samhurdi Ministry, the cooperative movement and World Bank financed projects.

4.2 Distribution Channels

ALMAO

The basis for the distribution of ALMAO's insurance service is the Sanasa movement. Less than 4% of the 8,500 societies are so far operating as ALMAO agents, and so there is a great potential for expansion. Some 10% of the societies use ALMAO's general insurance services. ALMAO was not in a position to explain why the penetration of the insurance services was low. Neither could they describe the distinction between the societies that have joined the ALMAO operations and those who have decided not to join.

ALMAO has 5 branch offices to promote and follow up its operations. It has about 300 agents selling insurance and servicing the policyholders, of whom some 30 are outside the Sanasa movement. Some of the Sanasa societies have set up insurance desks where they receive clients and inform them about the insurance products that they can provide. Besides life insurance, the staff at the insurance desks can sell general insurance such as motor and home insurance. There are 7 Sales Promotion Officers who monitor and support the agents.

Yasiru

Yasiru's distribution network consists of eight NGOs that have signed an Agency Agreement with Yasiru. The NGOs have offices in rural areas and appoint "animators" who carry out the recruitment of clients and sales of policies in the field. Normally the NGO, at its normal meetings or at specially organised meetings, inform the membership of the insurance scheme and about the animator. The animators then visit the members, and others, in their homes for recruitment.

Their Effectiveness

One challenge facing both organizations is the vastness of their markets. Only 6% of the Sri Lankan population is covered by some kind of life insurance. Within the Sanasa Movement, there are 800 000 members and around one million non-members who are served by the Sanasa societies, but ALMAO has only 2,000 policyholders in its new product portfolio. This may be an indication that the new products are not attractive for the Sanasa members or that they are too complicated to understand.

Yasiru's current partners have some 60,000 members out of which just above 9,000 are members of the Yasiru scheme. But there is also a great potential to partner with qualified organizations in CBO-rich Sri Lanka.

Rejections

There are very few rejections within either system. The Yasiru program has simple rules on exclusions. It is open to its partners' members, but also to other people in the local community above the age of 18 and below 65 who earn less than LKR 3000 ($30) per family member per month. The income rule is not rigorously applied by the animators. Rejections are made locally by the animator and/or the Society. It is very exceptional for the PMU to reject an applicant.

In the case of ALMAO, which now operates as a licensed life insurance company, an underwriting policy, originating from Swiss Re underwriting manual, has been adopted. All applicants fill in a personal form, including their health history. The head office screens the forms before acceptance of the application. They have the possibility of asking for medical exams if the sum insured is above LKR 750,000 ($7500) and the customer is more than 50 years old. Furthermore they have the possibility of charging higher premiums or reduce insured sums for individual applications if required by the underwriting rules.

This system has only been in operation since 2004 and so far the number of rejected applications is very low.

Underwriting

The client's role for underwriting is similar in both programs. An application form has to be filled out and signed by the applicant. The application form for Yasiru contains only one question about the health of the applicant or covered persons; the applicant must write down any "ailments". The application form for ALMAO products contains a full health declaration to be filled out and signed by the applicant. Filling out the form is always done with the help of an “animator” (Yasiru) or an agent or insurance staff (ALMAO). In both cases, the client has to pay the premium when the application is signed. In most cases a monthly premium is paid but if the client so wishes he/she can pay for a longer period in advance.

4.3 Benefits

ALMAO

When ALMAO was granted the license for life insurance, its old book of business was put in run-off. Its present product portfolio in life insurance contains four life insurance products and a funeral assistance product.

Box 4.1 New ALMAO’s Products

“Pilisarana” – This life product is a Whole Life product with a limited premium payment period. The premium is paid up to the age of 60. Minimum premium LKR 3,000 ($30) annually. The sum insured is payable with accrued bonuses either during the premium payment term or thereafter.

“Sithumina” – Premiums paid for a fixed term, minimum LKR 3,000 ($30) annually. The term can vary from 10 to 25 years. Maximum age when the cover ceases should not exceed 70 years. The sum insured is payable together with accrued bonuses if the insured survives up to the end of the term. In case of death during the term, the sum insured x 10 plus accrued bonuses will be paid to the beneficiaries.

“Senehasa” – This product is a children’s policy. The plan gives benefits to the children of the insured if he/she dies during the term of the policy. Twenty percent of the sum insured is payable on death and thereafter 20% of the sum insured continues to be paid on each subsequent death anniversary till the end of the term. Minimum premium for this policy is LKR 5,000 ($49.50) annually.

“Jenamithuru” – A Whole Life product with a minimum premium of LKR 1,000 ($10) and maximum of LKR 5,000 (US$49.50). The client can pay LKR 1.000 ($10) and then stop payments. The sum insured is then LKR 6,000 ($59) and is payable upon death whenever it occurs. Further premium payments can be added later and the sum insured will be increased. This product requires careful underwriting.

Funeral Assistance – A benefit of LKR 10,000 ($100) is payable upon death of any of the covered persons. Up to 9 persons can be covered by the same policy. Member, spouse, parents, children and in-laws can be covered. Benefits are only paid for two deaths per year. The premium is LKR 172.50 (US$1.70) per year independent of the number of covered persons.

This last product is a popular complement to the assistance provided by the funeral aid societies. ALMAO’s objective is to continue to use this product as an introduction to insurance services to the Sanasa members. The premiums do not cover the operational costs and the claims. Previously, a favourable reinsurance agreement with SLIC actually subsidised the scheme, but as from January 2005, the insurance is reinsured with NTUC on a quota share basis

Unlike the old products, the new products contain an element of savings (see Box 4.1). This demands higher skills from the sales force in order to explain what life insurance is and the importance of maintaining it. This may be difficult for the clients of ALMAO to understand and that is why the information to the client is of utmost importance when the policy is sold.

Another complication is that the savings element has also meant a substantial rise in the premiums. Difficulties to sell the new products may indicate that the price is too high for ALMAO's target group. It may also mean that they do not appreciate the savings element or think that they cannot afford it.

Yasiru

The original terms and conditions of the Yasiru scheme were developed in dialogue with the intended membership. This dialogue has continued and the coverage and structure has continually been adjusted. It seems that Yasiru's good communication with the members secures that the benefits reflect what the members want reasonably well. Today the members are divided into four categories depending on their household situation. The categories show that small households are given lower premiums and that additional adults in a household can be covered on an individual basis. Within each category, the member can choose between five different levels of monthly premiums. The categories and the premium levels are summarized in Tables 4.3 and 4.4.

Table 4.3 Membership Fees for Covered Persons (Premium)

Covered Persons	Membership Fees
1 Household with no children	LKR 10, 20, 30, 50 or 100 ($0.1 – 1.0)
2 One parent with children	LKR 10, 20, 30, 50 or 100 ($0.1 – 1.0)
3 Household with children	LKR 15, 30, 45, 75 or 150 ($0.15 – 1.5)
4 Other adult > 18 years	LKR 5, 10, 15, 25 or 50 ($0.05 – 0.5)

Table 4.4[4] Different Benefit Classes for Minimum/Maximum Premiums

Benefit class	Monthly Premiums	
	Minimum LKR 5 – 15	Maximum LKR 50 – 150
1. Death after the age of 18 and before 65 due to an accident	6000	60 000
2. Permanent disability after three months before the age of 65 due to an accident	12 000	120 000
3. Death after the age of 18 and before 65 due to natural causes	3 000	30 000
4 a. Sudden death before reaching the age of 18	3 000	3 000
4 b. Sudden death between the age of 65 and 75	3 000	6 000
5 a. Hospitalization cost per day for a maximum of 15 days	30	300
5 b. Traditional or similar treatment cost per day for a maximum of 15 days	15	150

Role of Insurance in Meeting Institutional and Client Needs

ALMAO and Yasiru were started in rural areas to serve poor people. Both consulted with the target group to determine the need for insurance services. Partly through trial and error, and partly through collaboration with insurance professionals, the two schemes have narrowed down to what is both needed and possible to offer. In the study team's discussions with members, there were a few risks mentioned that are not currently covered. The risk of crop failures is one example but Yasiru's main partner, ACCDC, tried crop insurance and realised it was not manageable. The members accepted that the risk of crop failure could not be insured at present. Generally, members were satisfied with the on-going service and had few

[4] The full premium and benefit schedule is shown in Annex 1.

proposals for improvements. Insurance cover for death, disability, sickness and accidents seems to be a relevant mixture for the target group in Sri Lanka. This is what Yasiru offers and what the old ALMAO offered.

For the new ALMAO, it is worrying that professionally designed (but a bit more complicated) life products have so far attracted few clients in the Sanasa movement. After almost two years, only about 2000 members have signed up for one of the new products. It is important for ALMAO to design more products that appeal to the Sanasa members. The Funeral Assistance insurance has a profile that suits poor people, but it should be seen as part of ALMAO's promotion efforts since it is clearly unprofitable.

ALMAO's current problem may have been caused by ALMAO's new role as a commercial and professional company that has developed modern insurance products. The intention was to continue to serve the Sanasa members and the poorer sectors of the society, but the products have not been very attractive to the target group. There is no doubt, though, that the members of the Sanasa movement are people with reasonable incomes and they consider themselves to belong to the middle or low-income groups. A clear majority are not among the poorest strata of the population. The pricing of the new ALMAO life products should, in principle, suit Sanasa members. More marketing and awareness campaigns may help overcome the problem. Development of additional products in cooperation with the target group may be another solution.

It is very likely that Yasiru's members have lower incomes than the Sanasa members and ALMAO's clients. There is, practically speaking, no competition between the schemes and the commercial insurance companies are preoccupied with richer people.

Changes to Benefits

The main change to the ALMAO scheme was in 2002 when it was granted a license for life insurance. The old products were then abandoned and the new life insurance products were presented to the market.

As far as Yasiru is concerned, there have been gradual changes of the coverage and benefits since 2001. The changes have been motivated by requests from the clients, by need for simplicity and efficient administration, and by the need for improving the economic sustainability of the program.

Three of the more important changes are:

- In 2002, a maximum of two dependants per policy was introduced. Before that a policyholder could insure as many people as he/she wished. This change improved the financial viability of the scheme. But at the same time, the waiting period for eligibility for natural death benefits was reduced from ten to two years of membership.
- A new definition of a "covered person" was introduced in 2004. The change had the effect that all persons on one policy are covered in exactly the same way, which was not the case before. Furthermore the change meant that more people could be covered on the same policy but for a premium for each person.

- Before 2004, coverage was only given for funeral assistance up to the age of 65. Members wanted this limit be to increased to 75. This was decided by the Annual General Meeting in 2004. At the same time, hospitalization caused by maternal complications was included.

Special Needs of Women and Children

The members of both ALMAO and Yasiru are predominantly women. Sixty-four percent of Yasiru members are women and there is a similar percentage among ALMAO members. Most Sanasa societies have special programmes and services for women and children. One of the four major life schemes that ALMAO offers is specifically designed for children. The funeral aid scheme also covers dependents, including children. Yasiru' also specifies the coverage for husband/wife and children.

Yasiru has made efforts to involve the target group in the design and development of their services. In this way, women have had an opportunity to influence its services. The team has noted, though, that like in many other countries, women generally play a background role in meetings.

4.4 Premium Calculation

The Yasiru scheme was designed to be as simple as possible. The fixed premiums and fixed sums insured are easy to understand for both animators and clients. Fifty percent of the premium paid by the policyholder is set aside to cover claims and to build up reserves for future payments. The other 50% is used to cover commission and administration costs. There has been no actuarial calculation of the premiums or evaluation of the reserves and the capital adequacy.

The new products sold by ALMAO are modern life insurance products. The tariffs are based on mortality assumptions, interest rates and estimated costs for administration and commission. The tariffs are reviewed annually and filed with the IBSL for approval. The CEO of the company, who is an Associate of the Chartered Insurance Institute, is responsible for the tariffs. The calculations of the tariffs, the funds and solvency margins are made by an actuarial and management firm.

Operations Costs

When ALMAO started operating as a life insurance company in 2003, the old life business was transferred to the new company. Even as a new company, it has very high operational costs. During the first year of operations of the new company, the administrative costs were 74% of the premium and commissions were 38% of the premium. The Board of Directors is well aware of the financial problems during start-up, which are faced by all new life insurance companies during their first years of operation.

Half of the premiums in the Yasiru scheme are split between commission and the costs of the head office. Twenty-five percent stay with the partner and animators as commission and 25% are used to contribute to the costs of Yasiru's PMU. Yasiru's development partner, the Rabobank Foundation, has until 2004 made substantial contributions to cover the costs for the PMU. In the budget discussions for 2005, Yasiru has agreed that the PMU expenses should be financed by the operations of the scheme. It will be a difficult task for Yasiru to meet the agreed targets for premiums and membership. After a decrease in 2004, the Rabobank contribution still covered 60% of the total operating costs of the PMU. This covered also extraordinary investments and training expenses. The remaining 40% was covered from the premium. Effective actions need to be taken to roughly double the premium income and to reduce costs. One problem to solve is to improve the collection of premium arrears. This is also necessary to keep the dropout rate at the budgeted 10 %.

Commissions

In the Yasiru scheme, a commission of 25% of the premium is paid. The common rule is that the animator receives 15% and the remaining 10% goes to the partner organisation. The partners have, in some cases, changed these proportions. The commission is not reduced after some time. It stays the same throughout the life-span of the policy.

ALMAO uses the official and by IBSL approved commission structure for Long Term insurance, as illustrated in Table 4.5.

Table 4.5 IBSL-approved Commissions

Policy Year	Maximum Commission Payable
1	30%
2	20%
3	15%
4	10%
5	5%
6-10	5%
11-	0%

There is a great danger that in a country like Sri Lanka where banking or postal payment systems are not widely used, the retention rate will go down drastically when the agent's commission is reduced. The system is based on premium collection by the agents, which is most often in the house of the client. When the agent earns 3 to 6 times more by contracting a new client, it is much more attractive to recruit new clients than to collect premiums from the old. Unless ALMAO implements more effective systems for premium payments, like standing orders to withdraw the amount from the member's savings account, one can expect a high dropout rate, which is very bad for the future of microinsurance.

Reinsurance

Ever since the launch of its program, Yasiru has been supported by Interpolis. The present cover offered by Interpolis is a 100% quota-share with a maximum of LKR 120,000 ($1200) per risk. The premium to Interpolis N.V. for the annual contract is 20% of the gross premium, but 95% of the reinsurance premium is retained by Yasiru as a no-claim commission. This means that only 1% of the premium is payable for reinsurance. This kind of favourable reinsurance agreement will be very hard for Yasiru to find elsewhere in the market. In 2005, the partners have started to adjust the reinsurance agreement towards more market-based terms but the arrangement will still be favourable for Yasiru.

Thus far, the reinsurance agreement has not led to any cash transfers between the partners. According to the management of Yasiru, there has been no balance in favour of any of the two parties. The reinsurance cost is not specified in the annual report of Yasiru.

The benefits for hospitalization are not covered under the reinsurance agreement. But Yasiru is looking into different possibilities to find a reasonable solution to find reinsurance cover.

The new life insurance business of ALMAO is reinsured with NTUC Income of Singapore. ALMAO covers LKR 50,000 ($500) of each claim; benefits above that limit are covered by the reinsurer. The premium for the reinsurance cover is 9.5% of the gross premium.

For the funeral assistance product, ALMAO has, up to the end of 2004, had an old contract with SLIC, which was very favourable as the agreement covered up to 100% on a quota-share basis excluding commissions. Since January 2005, the funeral assistance is reinsured on a quota share basis with NTUC Income. ALMAO retains two thirds of the business and NTUC Income covers the rest. According to the management of ALMAO, the product is used as a "door-opener" for wider insurance services and for this reason they are prepared to accept losses for the product.

Subsidies and Grants

Apart from the implicit contribution from SLIC, ALMAO is running its business without any subsidies or grants. It has not received any technical assistance since it started the Life Insurance Company in 2003. When an insurer obtains the licence, it must appoint a Chartered Insurer as CEO of the insurance business. The CEO is also a member of the Board.

Since the start of Yasiru's operations, it has received funding and technical support from Rabobank and from Interpolis. The funding of the PMU by Rabobank ended in 2004. The arrangement with Interpolis N.V. for the reinsurance contract is another important support to Yasiru.

Summary and Issues

Pricing. In the old ALMAO scheme, the highest annual premium was LKR 3,000 ($30) per year and the lowest was LKR 240 ($2.40) per year. The pricing of the products was obviously adjusted to be affordable for poorer people. Three of the four life insurances offered by the new licensed ALMAO insurance company have a minimum annual premium of LKR 3,000 or above. The price increase is justified by the fact that the new products contain an element of savings, but a problem may be that the original target group cannot afford this improved product. The Board of ALMAO insists that their primary target group remains the same and are concerned about the low outreach of the new products.

This illustrates the difficulty for duly registered, controlled and professionally-run insurance companies to offer appropriate services for poor people. It is difficult to both follow the legal regulations with actuarially sound products and to service the poorer segments of the population. In the case of ALMAO, the study team believes that since only 6% of the potential market is currently exploited, there is great need of products similar to what ALMAO is offering (for instance for middle-income people who are not covered by the commercial insurance companies). So even if the products do not reach the poorest of the poor, it is still highly justified to offer good products for other segments of the population.

The premiums for Yasiru's products vary from LKR 120 ($1.2) to LKR 1,800 ($18) per year and there is no doubt that Yasiru is a development organisation with the objective to offer insurance services to poor people on a mutual benefit basis. It should also be pointed out that Yasiru's premiums and benefits are not based on proper actuarial analysis. Furthermore, the services have, so far, depended on external support.

Inflation. In Sri Lanka, inflation is generally a threat to insurance operations. The great problem is that returns on safe investments in line with the insurance regulations do not match inflation. The return on Treasury Bills is between 9% and 10% whereas the inflation runs at 13%-14%. ALMAO and Yasiru are of course affected by this situation, just like the whole insurance industry.

However, the two organisations suffer also in other ways from inflation. Neither of them has implemented an index system to adjust premiums and benefits to the effects of inflation. As a result, premiums remain the same while most of the operational costs increase in line with the inflation. Since these increased costs cannot be offset by rationalisations, it means that more premiums will have to be used to meet costs. Less will remain to meet death and hospitalisation claims and returns to the clients. Another effect of the current inflation rate is that if no adjustments are made, the real value of the benefits will be almost halved after only 5 years and reduced to less than one third after 10 years. This will be a bitter first experience of insurance services for the clients. Members who are aware of the effects of inflation can to some extent reduce the effect of inflation by opting for a higher premium level.

4.5 Premium Collection

One of the most important tasks for the animators in the Yasiru scheme is to collect premiums from the policyholders monthly. Out of the collected premiums, the animator normally keeps 15%. If a policyholder cannot afford to pay the premium one month, the animator will return next month to collect two payments. If the policyholder cannot pay after three months, the policy will lapse.

The agents of ALMAO have the same task as the animators of Yasiru when it comes to premium collection. They visit the policyholders within their geographic area to collect the premium monthly. For ALMAO's new business the premium should, in principle, be paid annually. The tariff is based on annual payments.

The main method for premium collection for both the old ALMAO and Yasiru is through visits to the policyholder's home. In both cases, the members/clients are offered the possibility to pay the premium at the partner's office. Some societies have convinced clients to pay the premium through standing orders from his/her bank account. This payment method should naturally be promoted in the Sanasa movement where almost all ALMAO's customers operate savings accounts. Yasiru too has this option since most of its partners operate savings and credit services for their members. If both organisations could extend this possibility to all their customers, it would reduce their operational costs substantially. It would also reduce the commission payable. In addition, it would significantly improve the retention rates, which are too low for both organisations. The team was not given any reasonable explanation why the standing order procedure is not generally implemented. A hidden reason may be that a great number of people, also within the organisations, would lose their commission if standing orders become common.

The new products offered by ALMAO, where the minimum premium is LKR 3,000 ($30) annually, cannot bear costs for monthly premium collections. Still, there is a growing tendency among the clients to ask for monthly premium payments. This is accepted in most cases, but it increases the administrative costs and reduces the viability of the products.

The commission system affects the retention rate. Yasiru does not reduce commission over time, which makes it attractive for the animators to collect the premium from the established customers. ALMAO follows the recommendation by the IBSL, and has a scale for reduced commission. It goes down from 30% of the premium the first year to 5 % in the fifth year and no commission after 10 years. This will certainly reduce the retention rate in long-term business. This is especially true for newly started operations. When there are plenty of new potential clients, the agents will be eager to attract new business instead of servicing old customers, which is less rewarding.

Problems

Both programs, and in particular the old ALMAO, suffer from low retention rates. In the long run, this will seriously damage the trust in the schemes among the customers/policyholders and among the potential, new clients. Many people in the local society will have paid insurance premiums without receiving any benefits and when they drop out of the scheme, they will see no advantage in being insured. In a local society, the experience and disappointment will be quickly spread. The system of commission rates dropping down to 5% after four years, in combination with collection of premiums in the client’s home, put even more pressure on the already low retention rates.

The problem is even more serious if you take into consideration the risk that a great number of people will develop a negative attitude towards insurance. They were pioneers in their local area and their experience is that they have had no use of the insurance and therefore they have become disappointed. Few of the dropouts will understand fully that although they have received no benefit, they were actually insured while they paid the premiums. As pointed our earlier, it is likely that many of the clients who terminate the insurance will tell their neighbours that they have paid for several years but received nothing. If a great proportion of the pioneers do this, there is a risk that it will be very difficult to implement future microinsurance services aimed at increased social security for poorer people. Great and expensive measures may be needed to explain the nature and benefits of insurance to rebuild trust in microinsurance services (see Box 4.2)

Box 4.2 Response to Social Insurance Schemes

The authors of one of the ILO[5] reports have made the following observation: low-income respondents "did not have a clear idea about micro insurance but mentioned that there are a very small number of persons who had taken insurance policies from private companies. The aim was to insure some form of security for their children in the future. It was also revealed that even the small number of policyholders, after defaulting the payments and instalments, had given up their interest in insurance. In such cases, insecurity of earning income from work of a seasonal nature has caused difficulties in paying instalments of insurance policies.

This experience had created apprehension and doubts in their minds on the use of insurance for purposes of ensuring protection. On further explanation of the features of the social insurance scheme and microinsurance facilities, they expressed interest in such schemes, provided there was high government participation, and better control and transparency in such arrangements."

4.6 Claims Management

There are many similarities between the two schemes in the claims settlement process (see Table 4.6). In both cases, it is the animator/agent who helps the policyholder or the beneficiary to fill out the claims form. The animator/agent also collects all the necessary documents. The documents needed are doctor's certificate, death certificates, and in some cases police reports.

Table 4.6 Claims Settlement Details, ALMAO and Yasiru[6]

Issues	Observation
Parties involved in claims settlement	Beneficiaries, animators/agents, Head Office In ALMAO also branch office in some areas
Documents are required for claims submission	Claims form, medical documents, death certificate and when necessary for accidents police report
Claims payment method	Cheque or cash
Time from insured event to claim submission	One to three weeks
Time to pass through any intermediaries	One week
Time from submission to payment	Two weeks
Claims rejection rate	Less than 5 %

The opinions among animators/agents and societies vary a lot regarding how long it takes to get all the necessary documents. To get a doctor's certificate or a death certificate, it can take from one week to more than one month. When the documents and the claims form have been collected, the file is sent to the head office where the final decision and payment is made. Sometimes, for example in cases of hospitalization, the society can make direct payments to the policyholder after informing the head office by fax or telephone. Trusted and experienced partners even make pre-payments in safe and obvious cases. Payments are usually made by cheques or cash.

[5] Mapping of the Informal Sector Social Security Schemes in Sri Lanka, ILO, Colombo.
[6] The procedures are so similar that they can be described in the same table.

The most common reason for delay is connected with problems securing the necessary documents. Delays with death certificates were often mentioned. Both organisations have very few rejections. The only reason that was mentioned for rejections was policies that had lapsed due to non-payment of premiums.

4.7 Risk Management and Controls

Both schemes are subject to very low risk when it comes to moral hazard and fraud. The cover is limited to payments upon death, disability and hospitalisation, and risks regarding fraud and moral hazard are easily manageable. Claims must be supported by legal documents, such as death certificate, doctors' certificates and hospital statements. No organisation reported any problems with fraudulent claims.

Since both ALMAO and Yasiru recruit clients who already have joined their partner organisations as members, the risk of adverse selection is heavily reduced. In addition, the health declaration and the underwriting rules used by ALMAO are adequate and will reduce a possible problem of adverse selection.

As for waiting periods, applicants to the Yasiru scheme will not be granted payments for hospitalisation until the membership has lasted for six months. Full payment of death benefits requires that membership fees have been paid for at least two consecutive years. If the fees have been paid for less than two years, a proportionate amount, depending on the number of months of fee payment, will be awarded.

There is the problem of fixed premiums and costs that are subject to inflation. In ten years' time, hospitalisation is likely to be more than three times as expensive as today if the inflation rate remains the same. The real value of benefits for member is quickly eroding.

4.8 Marketing

ALMAO does not have a specific marketing plan or budget allocations for marketing. The completely dominating marketing activity is the field recruitment of clients that is carried out by the agents. Normally this takes place through discussions with the Sanasa members when they visit the society or during visits to their homes. A general introduction to ALMAO's services is often done in different types of meetings of the Sanasa society.

The most important marketing activity of the Head Office is to train the agents and enhance their skills. For this purpose, ALMAO operates a mobile training van and uses the ALMAO college at the Sanasa Training Campus. The mobile van is manned by professional trainers and equipped with training material and facilities. Through the mobile van, the training can be brought to the clients and agents instead of bringing them to training centres. ALMAO also prints simple leaflets and is in the process of planning a national marketing campaign. The management estimates that in 2004, ALMAO spent about LKR 3 million ($30,000) for marketing activities.

The only marketing activity of Yasiru is to give each partner 1000 copies of its brochure free of charge. Each brochure costs about 20 US cents to produce. Similar to ALMAO though, the most important marketing is carried out by the animators who are engaged by Yasiru's partners. In this sense, effective training of the partners and their animators is an important marketing activity.

Neither organisation has tried to assess its marketing strategy. It may be necessary to visit homes to convince poor, rural people to join the schemes. It may be difficult to establish confidence in an office or through other contacts. ALMAO’s main target group, the members of the Sanasa societies, should be a bit different in this respect. They are used to the Sanasa offices and should have full confidence in staff working there. A substantial share of ALMAO’s underwriting takes place at the Sanasa offices, which is less costly and possibly more effective than home visits, but no proper assessment has been made.

The monthly collection of premiums in the client’s home must be a very expensive and uncertain method, in particular when the agent’s commission (as in the ALMAO case) goes down to 5% after 4 years. It is unclear why more emphasis has not been placed on standing orders to recover the premiums from the client’s savings account with the Sanasa society.

4.9 Customer Satisfaction

As the new ALMAO scheme has been in operation for a very short time, there are no figures on renewal rates. The old scheme, however, had very low renewal rates. Renewals are offered, but the collection of premiums is not as intensive. According to management, the dropout rate was almost 40% in 2005, which means that very few old policies will be in force after some years. This is a serious development for ALMAO. The sales of the new products develop very slowly, and in 2004, 80% of the premiums came from the old scheme. If that dominating income is quickly evaporating, ALMAO will face great problems. Its plans to develop new products that are attractive to the members of the Sanasa societies are of great strategic value in this light. But ALMAO also needs to retain premiums from the old scheme.

Since the start of Yasiru’s operations some 2,000 members have chosen not to renew their membership. The renewal rate, according to management, is around 80%. The main reason for not renewing is the failure to pay the fee/premium. When the animators collect the fees/premiums, members can postpone the payment for a maximum of three months. If not paid after three months, the membership is closed.

Neither organisation has conducted customer surveys to find out if members are satisfied or not. The local presence of the partner organisations ought to facilitate surveys to monitor customer satisfaction.

5. The Results

5.1 Management Information

The management information used to monitor the schemes seems to be adequate. There are monthly reports from branches and partners regarding sales and premiums collected, new business and renewals. Claims are also monitored on a monthly basis. The claims data contain all the necessary information to monitor their development. These figures are discussed during monthly meetings with the management committees. The financial results are monitored on a quarterly basis and reported to the boards.

In view of the lack of formal, external control of Yasiru's insurance services, its regular reporting to Interpolis N.V. is an important complement to the internal information system.

5.2 Operational and Financial Results

In the analysis of the results of the two organisations, it is important to bear in mind that they now operate under very different rules. One is a regulated insurance company and the other is a society subject to a different legal regulation, that of the Societies' Act.

ALMAO

In Table 5.1, the development of old ALMAO is shown up to 2003. The results for 2004 are shown only for the new ALMAO. The old organisation is formally only handling general business during this year. All people with knowledge of the insurance sector know that new life insurance companies face tough challenges during the first years in breaking even. The new ALMAO accounts for a small profit due to the transfer of the life business from the old organisation, which accounted for 80% of the premium income. The business with new products generated a loss of LKR 4,650,000 ($46,000).

The slow development of the sales of the new products is worrying. The renewal rate is comparatively high at 92%, according to management, but the products are not popular to the general membership of the Sanasa societies. The new ALMAO is in the process of developing new products that are hopefully more attractive to the members of the Sanasa movement. Until such new products have become successful, the new ALMAO should take good care of its old clients even though the old policies are no longer sold.

It has not been possible to get separate accounting reports and results for the agency activities in the Sanasa societies. All societies the team has discussed with are, however, satisfied with the arrangement. The applied commission is satisfactory in their opinion.

Table 5.1 Key Results - ALMAO, old

	2003	2002	2001	2000
Net income (net of donor contributions) $	247 300	179 000	139 900	111 100
Total premiums (value) $	224 600	149 800	120 200	97 100
Growth in premium value	+ 50 %	+ 25 %	+ 23 %	+ 33 %
Claims / total premiums (%)	10 %	9 %	12 %	11 %
Administrative costs / premiums (%)	50 %	55 %	48 %	46 %
Commissions / Premiums (%)	31 %	33 %	30 %	27 %
Reinsurance / Premiums (%)	0	0	0	0
Reserves added for the period / Premiums (%)	8 %	22 %	27 %	30 %
Net income for the period / Premiums (%)	30 %	20 %	19 %	25 %
Claims cost / total number insured $	0.6	0.3	0.4	0.3
Growth in number of insured (%)	- 26 %	+ 28 %	+ 13 %	+ 20 %
Income earned from investment of premiums	22700	29300	19700	14000
Percentage of profit distributed	0	0	0	0
Renewal rate (%)	70%	80 %	80 %	80 %

Table 5.2 Key Results - ALMAO, new

	2004	2003	2002	2001
Net income (net of donor contributions) $	312200			
Total premiums (value) $	263400			
Growth in premium value	0			
Claims / total premiums (%)	10 %			
Administrative costs / premiums (%)	74 %			
Commissions / Premiums (%)	38 %			
Reinsurance / Premiums (%)	2 % (9.5% of new prem.)			
Reserves added for the period / Premiums (%)	4 %			
Net income added for the period / Premiums (%)	0 %			
Claims cost / total number insured $	0.6			
Growth in number of insured (%)	First year			
Income earned from investment of premiums	48800			
Percentage of profit distributed	0 %			
Renewal rate (%)	New business			

YASIRU

The Yasiru operations are managed by the PMU. Formally, the PMU is not a separate entity, but an integrated part of the Yasiru Mutual Provident Society. In practice, the PMU functions as the implementing head office of the Yasiru operations, but it maintains its own set of accounts. The PMU receives 25% of the premiums, and the Mutual Provident Society Limited is allocated 50% of the premiums. Another 25% stays with the local partner and the animators to cover their expenses and commission. The PMU manages and administers the scheme including approval of member applications and handling of claims. The Provident Society has no staff but legally bears the costs for benefit payments and is the owner of the Welfare Fund, the Risk Fund and the Members’ accounts.

So far the Provident Society has shown good profits. Claims ratios are low but increasing. To make a safe estimate of the operational results, it is vital to make an actuarial analysis of the scheme and an estimate of the strength of the reserves.

Yasiru's financial situation is, of course, positively influenced by the support it has received from the Rabobank, which has allowed Yasiru to build up reserves quickly. Besides direct financial contributions, the support has comprised of subsidies of staff training, awareness campaigns and insurance literacy for members, member recruitment and investments in office and communication equipment. Financially, the reinsurance agreement with Interpolis N.V. has been of great importance.

Yasiru and Rabobank were in agreement already at the start of the cooperation that the support should be reduced over time. Yasiru is now facing a tough period during which it should build up its independence and viability. The support to the PMU was reduced in 2004, but it still represented almost 60% of the unit's expenses, including some extraordinary investments and training activities. In 2005, this support has ceased. In 2006, the reinsurance agreement will become more business like. To overcome the reduced support and to continue to build up necessary reserves, Yasiru should in the nearest couple of years preferably double its premium income and at the same time cut costs and increase efficiency.

Yasiru's partners do not keep separate accounts for their involvement in the scheme. It is therefore not possible to analyse the profitability of their cooperation with Yasiru. The partners the study team visited were very satisfied with the arrangement.

Table 5.3 Key Results – Yasiru

	2004	2003	2002	2001
Net income (net of donor contributions) $	38000	27600	9400	6400
Total premiums (value) $	36900	27200	8800	6700
Growth in premium value	+ 36 %	+309 %	31 %	+ 60 %
Claims / total premiums (%)	22 %	19 %	15 %	5 %
Administrative costs / premiums (%)	69 %	43 %	177 %	161 %
Commissions / Premiums (%)	25 %	25 %	25 %	25 %
Reinsurance / Premiums (%)	1 %	1 %	1 %	1 %
Reserves added for the period / Premiums (%)	26 %	37 %	105 %	76 %
Net income added for the period / Premiums (%)	28 %	67 %	34 %	36 %
Claims cost / total number insured, $	0,9	0,6	0.1	0,07
Growth in number of insured (%)	5 %	39 %	16 %	n/a
Income earned from investment of premiums $	1 025	390	520	210
Percentage of profit distributed	0	0	0	0
Renewal rate (%)	80 %	80 %	80 %	n/a
Donor contributions to the PMU, $	14 300	19 400	8 700	8 300

The high administrative costs for both these organizations will be further discussed in Section 7.2.

5.3 Reserves

During the decade when old ALMAO was active, it built equity capital and reserves amounting to LKR 49 million ($490,000), mainly from its own surplus, but also through increased shareholding by the owners, the Sanasa societies. Most reserves were transferred to the new ALMAO in the form of equity capital, so that roughly half of the equity capital in the new ALMAO comes from the old organisation. At the time of registration, the Sanasa movement only had to mobilise less than LKR 40 million ($400,000) to meet the minimum requirements of the IBSL. With the new minimum requirements of LKR 100 million ($1 million) each for life and general insurance licenses around the corner, one wonders how the movement will manage to put in another LKR 125 million ($1.25 million) as equity capital.

Yasiru is a much smaller organisation and in that light, it has been successful in accumulating reserves. During four years, Yasiru has accumulated almost $50,000 in reserves. The funding, the technical assistance and the favourable reinsurance agreement, from Rabobank and Interpolis respectively, have strongly contributed to Yasiru's ability to accumulate reserves.

5.4 Impact on Social Protection Policy

As it has been pointed out earlier, the penetration of life insurance services is limited to about 6% of Sri Lanka's population. There is no doubt that the country would need policies and regulations that would facilitate for common people to manage different types of risks in their lives. One would think that microinsurance schemes like ALMAO and Yasiru would attract attention and encourage the state to take action in this direction. It does not appear that the state, in particular the IBSL, has any serious intention to support the development of an insurance sector with a substantially increased outreach.

Both ALMAO and Yasiru are aware of the situation, but have not taken any decisive steps to convince the government that private microinsurance schemes constitute an excellent, and actually necessary, complementary service to the government's own social service programmes. Indeed, Yasiru avoids the government instead of trying to influence its policies. The Societies' Act gives great powers to the government to intervene in the societies' affairs, which is why societies tend to avoid involvement of the government. In the case of Yasiru, one can also add the fact that its insurance operation has not been officially accepted by the Registrar of Societies. Nevertheless, Yasiru is prepared to establish cooperation with government organisations in the field to get a greater outreach for its services (for instance with the Ministry of Samhurdi).

The state in Sri Lanka has implemented numerous social security systems (see Section 1.3) to assist the poorer segments of its population. The systems do not adequately reduce risks for poor people, but evidently there is an ambition to offer social security. Since this study is on microinsurance, it should be pointed out that the global insurance industry and the donor community have not developed any effective models for how the state should facilitate the development of microinsurance. Neither have they succeeded in making governments aware of the potential of microinsurance. The government in Sri Lanka needs both a higher level of awareness and concrete models for what it can do.

6. Microinsurance Product Development

The main objective of both organisations is to offer good and affordable products to their target groups (low-income people). As mentioned above, the current ALMAO portfolio is very young and will need some more years to mature and improve financially. The management of ALMAO is aware that its new products cannot address the needs of the poorest sector of the population since the minimum premium is as high as LKR 3,000 ($30) per year. Sixty-five percent of the comparatively few that have signed up for the new products have opted for the minimum premiums.

According to the management of ALMAO, the present products were developed to address 85% of the market, i.e. the people who could not afford the products offered by the other insurance companies. An “endowment culture” had developed in the commercial market where the aim was to offer insurance with benefits for the client while he/she was still alive. Most weight was put on financial performance for maximum payment on maturity. In its design of the new products, ALMAO followed this trend, but gave a higher priority to a good benefit also upon death. The reason for this is that death of the wage earner in ALMAO’s target families is a loss that must be compensated.

The new products were developed by insurance professionals and based on the commercial market. Adjustments, like higher death benefits, were made to meet the assumed demand in the target group. However, there was limited involvement of the target group itself. A greater involvement of the Sanasa members, who constitute the prime target group, would most likely have resulted in products with lower prices and, as a consequence, also lower benefits.

Discussions are going on within the organisation to add more products to the portfolio. New products will have to be more adapted to the needs of the Sanasa members who, so far, have been reluctant to subscribe to the current products. The leadership of Sanasa and ALMAO is aware of the importance in succeeding in this respect. Further research is needed before launching new products. The process for development will involve the Sanasa movement, ALMAO and external actuaries. When new products are ready to be put on the market, the management will start with different types of test sales before a wider launching. The challenge for ALMAO is to design products that are actuarially correct and in line with the IBSL regulation and, at the same time, easy to understand and attractive and affordable for Sanasa members. One great problem to overcome is the comparatively high costs compared to what premiums the target group can pay. The regulations about financially viable products complicate this matter further.

Since the Yasiru operations started, adjustments to the product have been made almost every year. The proposals for changes have come from the field through animators, field officers and coordinators. Members have also suggested changes at the annual general meetings and during other meetings of their organisations. The PMU has also suggested changes based on its experiences of running the scheme.

The most important factors in deciding whether changes are required are:

- client needs
- more effective and less costly administration
- enhancing renewals
- improving the financial sustainability

The number of requested changes to the present scheme and new products has been quite high. This shows that the NGOs and their members are interested in the scheme and their suggestions form a good basis to improve services. Through their representation in the Board of Yasiru, they take part in the decision making of the scheme. For examples of recent changes decided by the Board, see Section 4.3.

7. Conclusions

In 2003, ALMAO adjusted its products to the requirements of the formal insurance industry. The increase of the minimum premiums to LKR 3,000 ($30) for three of the four new products evidently made it difficult for the majority of the Sanasa members to buy the insurance products. The rather complex nature of the products was possibly confusing to low-income people. Indirectly, the change in the portfolio reflected a change in the main strategy of the company. The ten-fold increase of the minimum charges for most products automatically changed the focus to people with higher income. There is no simple explanation to the change. As a newly registered insurance company, ALMAO may have been under pressure to introduce products that were similar to what the commercial companies were offering. The greater influence by professional insurers has also affected the design as well as the rules on viability.

The Board and the management of ALMAO have realised the change in focus as a consequence of the new product mix. The chairman now even labels the new products as "macro" insurance products. Discussions have started to develop new products that are affordable for the low-income members of the Sanasa movement. For ALMAO, it is of vital importance to offer products that can reach a high penetration rate. The management of ALMAO expressed the opinion that profits generated in the general insurance sector might be used to support the implementation of new microinsurance products. Since the old products with a low-income profile are no longer marketed, the success of such products is very important for ALMAO’s future.

The study team is a bit puzzled by the difficulties in selling the new products. Members of the Sanasa societies are not extremely poor. Rather, they represent middle-class and low-income people who can afford insurance protection more easily than the rural poor. Also taking into consideration the very low penetration by the commercial insurance companies, there is a giant market in Sri Lanka among the middle-class and the upper poor. There is no shame in providing insurance service to this population, even if the products that are designed for them do not fit the needs of poorer people. If ALMAO succeeds with this market, it may actually help it to develop and sustain its service to the declared priority target group: poor people.

The main reason for the slow progress of the new products may, of course, be lack of awareness campaigns and intensive and strategic marketing.

The main issue within the Yasiru is that there are no new products. The products offered by Yasiru have been changed stepwise in order to meet needs and demands from the clients and to improve the financial sustainability of the scheme. At present, the challenge is to attract new, qualified partners to the program and to expand the membership through them. A wider base for its operations is a question of survival for Yasiru.

These new partners may not necessarily be NGOs or CBOs. Instead government organisations, like Samurdhi, the cooperative movement or World Bank projects, could be new partners. This process has been started and management is carefully screening possible new partners.

7.1 Key Issues Summary

Major Breakthroughs, Challenges and Lessons Learned

One of the most remarkable changes in the Sri Lankan microinsurance market is the Sanasa movement's transformation of its microinsurance operations into a commercial life insurance company. This led to a shift of market, which probably was unintended. The old products have been phased out and the new, modern products are not designed to suit the poorest members. The lesson learnt so far is that it has been very difficult to reach out with the new products and that ALMAO needs to develop new products to reach the poor.

The management is well aware of the challenge in running a profitable life insurance operation. Well-educated and experienced insurance professionals have been hired to develop and monitor the new business. An important lesson is to involve insurance professionals at an early stage of development of new products to secure financial viability of the program.

The market facing the new company is huge. The Sanasa Movement comprises more than 800,000 members in 8,500 societies, out of which only around 10% offer insurance services. Attracting new societies and educating staff within these societies is one of the major challenges for the new company. Other studies in the series of "Good and Bad Practices in Microinsurance" have indicated the difficulties for MFIs in handling insurance as a side business. The slow recruitment of more agents and establishment of ALMAO desks in the Sanasa societies may be another sign of this complication.

The main strategy for Yasiru is to cooperate with partners and to have insurance agency business incorporated into their ongoing operations. All partners offer microfinance products and are therefore well equipped to extend their services to include microinsurance. The penetration rate of the Yasiru scheme needs to be increased among the 60,000 members of its current partners. This will demand resources for marketing and for further training of staff within the partner organisations.

A major challenge for Yasiru in the years to come will be to adapt to a new financial situation with reduced external support. Yasiru has to secure the financial viability of its products. Actuarial skills must be brought into the organisation to establish whether the funds/reserves are adequate and that the premiums are sufficient to cover commissions, administrative costs, reserves and a reasonable profit. An operational surplus is necessary for investments in new partners and for marketing among members of existing partners. An intermediate action could be to identify a new donor (or donors).

Yasiru's legal status is unclear. Although officially unknown to the IBSL, Yasiru is recognized by the Registrar of Societies, which has no capacity to control insurance operations. This situation makes it even more important for Yasiru to have professional control of its services. Although Yasiru has been, and still is, fortunate to get technical and financial support, it will, in the long run, be important to have the funds and premiums evaluated by local, and preferably independent, actuaries. Such skills available in Sri Lanka and ought to be affordable for Yasiru.

Other lessons learnt by the management are to distribute standardised and simple products in dialogue with the target group. Yasiru already encounters demands from partners and its members, as they did when operations were started, for new products (crops, livestock and assets insurance). But the main focus for the next few years is on the financial viability of the present scheme. Adventures with new products such as crop insurance proved to be too difficult and distracting.

Best Advice for Others

In a pamphlet about the development of ALMAO, the leadership has presented the following lessons learnt for others to note:

- Newly set-up microinsurers should offer simple insurance products with terms and conditions that could be easily understood by ordinary persons and the benefit package must be affordable.
- At the start, a microinsurer should operate its business through an agency of an established insurance company to avoid the need for adequate capital, expertise in underwriting, adhering to actuarial constraints and constraints from the regulatory authorities.
- It is advisable to minimise the provision of maturity benefits and to concentrate more on providing death cover (see Section 6).
- Insurance is a capital-intensive industry and if the intention is to establish a full-fledged insurance company, it is essential to accumulate adequate equity capital. This need could be achieved through selling shares among member societies.

The Chairman of Yasiru, Dr Sunil Silva, identified the following points for other microinsurers:

- On strategy: Identify partner organisations very carefully. Cooperate with established organisations. In dialogue with the partners, reach an agreement to assist them in widening their service to their members and include microinsurance.
- Make a careful analysis of the environment and other conditions in which the scheme is going to work. It is a great advantage if factors contributing to failure or success can be identified at an early stage.
- Carry out a careful analysis of the target group’s needs. The services have to be demand-driven.
- Build a system with democratic control. The basis should be a mutual relationship between the target group/members and the service organisation.
- Take care to involve people; their participation will help the insurance provider to avoid many problems along the way.

7.2 Outstanding Questions

Beware of a High Dropout Rate

For a couple of decades starting in the late 1960s, numerous developing countries, supported by willing donors, wanted to provide small-scale farmers with credit to develop their production. Very few were aware of the difficulties in supplying a great number of very small loans to poor farmers in societies that lacked structure and organisation. Farmers soon realised that if they did not repay the loans, nobody would have the capacity to force them to pay. Often it also meant that they avoided the established agricultural marketing channels because loan repayments were often administered through these channels. Many agricultural marketing cooperatives lost their business in this way. A long-lasting problem was the attitude towards loans that was created through poorly designed credit schemes. In particular, if government or donor funds were involved, farmers had learnt that they did not have to repay loans. It took a long time before MFIs could change this mindset and start operating successfully. Nevertheless, few MFIs extend credit to small-scale farmers.

There is a risk that poorly designed and implemented microinsurance schemes will have a similar effect on poor peoples' attitude toward insurance. If the dropout rate is 20% to 40% or higher, a substantial share of the recruited, poor people will pay premiums for years without seeing any tangible benefit before they drop out. It is very likely that this will be a bitter experience for clients and many will become reluctant to pay for insurance services in the future. Some will also warn their friends and neighbours that insurance coverage is of no use. A high dropout rate may create a negative attitude towards insurance, which may substantially hinder implementation of future microinsurance services.

It is a challenge for microinsurance promoters to include measures that reduce the dropout rate. Agents and animators should perhaps get the same commission for collection of premium from old clients as they get for new client. That would stimulate the agents to maintain all clients. A negative consequence of this method is that it increases the cost level in the long run. This negative effect is reduced if the initial commission is lowered to 10% to 15% from 25% to 30%. Whether a commission on this lower level will provide sufficient incentive for the partners and agents remains to be seen.

Another method to reduce dropouts is to use part of the microinsurance premiums to build up a member's personal account, which is forfeited if the member drops out. Yasiru has implemented this mechanism. A certain part of the surplus is allocated to individual member's accounts. Perhaps there should be benefits for the clients intermittently even if there is no claim occurrence. An example is that if members' personal accounts are accumulated, the members could be allowed to withdraw half the amount every fifth year.

Administration Costs

The administrative costs for ALMAO and Yasiru are two to three times too high to provide worthwhile insurance coverage for the clients. When 70% to 90 % of the premium income is spent on administrative costs and commission, the clients will, without external subsidies, get very low risk coverage for the premiums they pay. It is normal that new insurance operations have high costs at the start and that efficiency improves over time. There is no obvious trend in this direction for Yasiru or ALMAO. ALMAO's development is further blurred by the recent transformation into a registered insurance company.

To provide microinsurance services with good value for money, both organisations will have to increase their turnover without increasing their costs. Without substantial reductions of the cost ratio, one can raise doubt about the organisations' ability to provide beneficial insurance services to the poor.

Anyone who has been involved in microinsurance is aware of the problem of profitability with many small insurance policies in an environment with a low level of insurance knowledge and rudimentary banking and postal services, among other shortcomings. One way to reduce the difficulties is to use existing organisations for the distribution of the insurance service. The method will be particularly effective if the organisation already has a system for money transactions with its clients/members. Both ALMAO and Yasiru use this arrangement but they still face problems with their cost levels. It is likely, though, that if they had set up their own, separate field organisations to provide the service, the cost situation would have been even worse. If ALMAO can fully utilise the great Sanasa movement for its distribution and Yasiru succeed to engage more partners, the two organisations may turn the current problems into success.

The study of ALMAO and Yasiru and their ongoing struggle also illustrates the need for microinsurance organisations to get substantial support during the start-up period, and that microinsurance schemes may need a long period of support to become sustainable. ALMAO got its support from the Sanasa movement, which for many years carried out most of the administrative work without charges. Yasiru still gets support from Rabobank and Interpolis N.V. The study team believes that it in most cases it will be difficult to build up microinsurance services without support during a rather long initial period.

Effective Premium Collection

It is argued that poor people prefer to pay a small premium every month. They find it difficult to pay higher premiums quarterly or yearly. Dialogue with the target group has confirmed that they prefer frequent, small payments. Yet the team wonders if this is really applicable to small-scale farmers who normally have a long period of no income when they do ploughing, planting, weeding etc. There is a rather short period, the harvest period, when they get income and when they may prefer to pay a premium. Whatever the case, both ALMAO and Yasiru collect premiums on a monthly basis from their members/clients.

As long as the frequency of premium payments in the microinsurance schemes is high, it is of crucial importance that the collection mechanism is highly effective. Like ALMAO and Yasiru, many microinsurance schemes work in partnership with MFIs, peoples' banks or savings and credit cooperatives. For ALMAO and Yasiru, it is strange that so few of the clients sign a standing order to withdraw the premium payment from their savings account, which would be a more cost-effective payment method. If that occurred, agents would lose commission. Perhaps standing orders are not promoted because as long as the penetration of the partners' membership is very low, there is a great potential for the agents to recruit more clients instead of collecting premium payments from old clients. To overcome this obstacle, a good bonus could be paid to agents who convince clients to sign a standing order. Such a system should lead to an increase in number of clients and reduced dropouts, thereby contributing to the viability of the scheme. If fees are correctly set, there is normally a strong relation between increasing number of clients and viability.

In all microinsurance schemes with a connection to banking organisations, careful analysis should be made of the possibilities to use standing orders as a common premium payment method. The development of good promotion material for standing orders could be a suitable objective for a donor contribution.

Target Group and Viability

The original ALMAO scheme and Yasiru worked through informal exclusions of groups of people like those with permanent employment, those employed by government or who had an income of more than $30 per month per household member. These exclusions were not implemented with great discipline or formality, and field agents sometimes interpreted the rule to mean exclusion of rich people. The fee structure and the benefits were adjusted for poor people.

When ALMAO was registered as a commercial insurance company, the products offered changed substantially. The cheapest product became 25 times as expensive as the cheapest in the Yasiru scheme. The old, informal exclusions were also scrapped. Still, the main target group were the members of the Sanasa movement and they, generally speaking, represent the lower or middle-income classes. The company is in the process of developing a product for poorer people.

Yasiru maintains its product profile, which is designed for poor people. The income limit of $30 per household member per month is still a formal exclusion, but it is not strictly observed.

The insurance industry in Sri Lanka has a penetration of 6% for life insurance. It is a bit difficult to understand why microinsurance schemes should exclude people with a normal income. Their need to manage risk is also high and they are not served by commercial insurers. People with low or middle-income could become very good clients. The costs for premium collection could be reduced and it is also likely that they would subscribe for higher benefits and pay higher premiums. It is very likely that a great number of clients from these classes would make the scheme more profitable. The inclusion of these groups could actually turn a non-viable service into a viable one.

The old ALMAO scheme and Yasiru implemented unnecessary limitations that may jeopardize their viability. The noble intention of reaching only poor people may in fact mean that the poor people get no service in the long run or that they get poor and unviable service.

It may be justified to exclude certain groups, for instance government officers, because of fear that if they are allowed to become members, they will grab power and take over the organisation. The question is whether this fear is reason enough to exclude people who need the services and who would become good clients and contribute to the schemes' viability. One should also remember that the scale of benefits would not normally attract rich and powerful people. Bylaws, clear and powerful objectives, and management systems can, of course, also facilitate the original target of reaching poor people.

Adjustment for Inflation

In countries where there is great need of microinsurance services, the economy is often not under strict control and inflation figures tend to be on the higher side. If high inflation, as the case is in Sri Lanka, is combined with low returns on safe investments, the conditions for insurance services are generally bad. Registered and controlled insurance companies will have to reduce benefits, in real terms, for the clients if such conditions prevail over a long period. Microinsurance schemes suffer in the same way.

Neither ALMAO nor Yasiru have included any systematic adjustment for inflation in their schemes. When the inflation rate is 12% to 14% per year, the real value of premiums and benefits erode very quickly. The real value is halved in less than 6 years. The operational costs, however, will basically follow inflation and as a consequence, after deducting for the escalating costs, there will be little left for reserves and claims. There is also a great risk that the clients will be disappointed by the real value of their benefits.

The problem of low returns on safe investments, which does not match the inflation rate, is difficult for any insurer to overcome. This is a question of financial and economical policy of the country. The lesson learnt from Sri Lanka is that in the planning stage, microinsurance schemes will have to analyse the general economic conditions in the country and look into projections for the future. If inflation and/or other imbalances can be foreseen, systematic adjustments for the effects of such circumstances should be built-in at the start of the schemes. Although, difficult to explain to the target group, it may be necessary to include some system of continual index adjustments of premiums and benefits.

Role of Donors

The old ALMAO microinsurance scheme was developed without any support from donors, except some minimal input at the start of the scheme. Instead, its development has been supported by a well-established, local savings and credit cooperative network.

Yasiru, on the other hand, has had a longstanding development cooperation agreement with the Rabobank Group. Rabobank’s subsidiary, the Interpolis N.V, a reinsurance company, provided support in form of technical assistance, capital support and reinsurance. Yasiru has considered this mixture of support to have been very satisfactory.

The future, however, is worrying. The subsidy of operating expenses in the PMU has ceased in 2005. The preferential reinsurance agreement will be replaced by a less favourable agreement in 2006. The Yasiru benefit scheme has been developed on a trial and error basis. Since its inception claims have been much lower than anticipated. Yet, because of the lack of actuarial analysis, Yasiru is not sure if the service is viable in the long run. Donor cooperation, in particular in the case of organisations providing services on a business basis, should contain a plan of how support will be withdrawn and how the activity will become self-supported and viable. According to Rabobank, such a plan exists, but it has been negatively affected by the non-fulfilment of targets and expectations. In discussions with the study team, Yasiru is not fully aware of the exit plan. The withdrawal of the donor support, as in so many other cases, is a vulnerable phase. Yasiru is not fully prepared for this important stage in its development. This is a serious problem since insurance services that cover life are of a long-term nature. They must not cease when the donor support ceases. Hopefully, Yasiru will, with the continued assistance by Rabobank and Interpolis N.V., overcome the future challenges.

Based on the situation in Sri Lanka, there are two other observations concerning the role of donors. It is obvious that, although the Sri Lankan government has the political intention to develop the poorer sectors in the country, it is not aware of the role of microinsurance in this respect. The lack of awareness and limited interest of the Insurance Board speaks for itself. There is, however, no basis to blame the government for this state of affairs. The knowledge about microinsurance and its importance in reducing of poor peoples' risks is limited. Donors involved in microinsurance can play a big role in spreading awareness and knowledge of its importance to developing countries and to other donors. Development of education and promotion material on microinsurance and organisation of conferences and seminars on the subject are simple examples of what can be done.

Lessons from microfinance are relevant in this regard. In the case of MFIs, the regulations in most countries were a great obstacle for the implementation of effective and independent MFIs. One objective of the Banking Act is to protect savings by the public and therefore substantial capital is required by banks to be registered. A large equity creates a secure basis for the savings they receive from customers. As a consequence, most MFIs were not allowed to receive savings from their customers. The MFIs normally depended on donor funding for their operations. An exception was the savings and credit cooperatives, which were allowed to receive deposits from their members. It took decades to promote and develop special legislation for MFIs that made it easier for them to receive savings and to base their lending on accumulation of local capital instead of donor or government funding. Still today, only a few countries have implemented a special legislation for MFIs. The main reason is that it is difficult to balance a more liberal regulation against the need to safeguard the customers' savings. Sri Lanka is in the process of enacting a law on MFIs.

Similarly, insurance regulations are there mainly to protect policyholders from organisations that do not have the financial or managerial capacity to fulfil the commitments they have underwritten. The case of ALMAO indicates clearly that if a microinsurance operation is turned into a commercial, registered insurance company, it will be difficult to maintain the objective of servicing the poorer strata of the population. If microinsurance services are an important development tool, the possibility of creating special legislation for such services should be explored. This will be a difficult and sensitive task. The need of an insurance service for low-income people will have to be weighed against the state's responsibility to make sure that organisations are able to fulfil their obligations. Donors, together with developing countries, should appoint a commission to develop a model of appropriate legislation or a special set of rules for microinsurance. Such guidance would be of great value for any country that would like to include microinsurance in its development programme. Currently there is an awkward situation where microinsurance organisations are operating without proper registration and public control. Very often the unregulated microinsurance service continues even though the state is fully aware of the activity.

There is one more aspect of the role of microinsurance that is often overlooked. All development economists today recognise that if a country is going to have stable development, the whole population will have to take part. In a country like Sri Lanka, where a great part of the population is poor or has low income, there is a great need for different programmes to stimulate these segments of the population to take a more active part in the economic activities in the country. Microinsurance is an important tool for these people to manage different types of risks, but can also make an important contribution to overcome a major shortcoming in most developing countries: the availability of long term capital. Even if poor people cannot afford high premiums, many small contributions can quickly grow into a large amount of capital for investment. ALMAO illustrates the potential quite well. In just over a decade some 40 to 50 000 people have built up a long-term capital of about LKR 50 million ($500,000). If microinsurance schemes could mobilise 50% of Sri Lanka's population with a development similar to what ALMAO has achieved, this could mean around US$20 million as long term capital building up over a decade for useful investments. That would not be a bad, additional resource for a country like Sri Lanka.

Annex 1

EXTRACT FROM YASIRU'S BROCHURE ON RULES AND BENEFITS
"Membership fee for covered persons and benefit awards

Monthly fee (LKR)	I	II	III	IV	V
1. Household no children	10	20	30	50	100
2. One parent w children	10	20	30	50	100
3. Household w children	15	30	45	75	150
4. Other adult >18 years	5	10	15	25	50

1. **Death of a covered person after the age of 18 and before reaching the age of 65 due to an accident.**

Benefit	6000	12000	18000	30000	60000

Preceding benefits or advance payments because of permanent disability as mentioned in clause no. 14 due to the same accident shall be deducted thereof with a maximum of the benefit awards for death.

2. **Permanent disability of a covered person after 3 months before reaching the age of 65 due to an accident.**

Benefit	12000	24000	36000	60000	120000

In case of 100 % disability of the member, the agreement ceases with the benefit payment for the member.
In case of partial disability the agreement can be continued if the membership fees are paid regularly.

3. **Death of a covered person after the age of 18 and before reaching the age of 65 due to natural causes:**

Benefit	3000	6000	9000	15000	30000

If the membership fees have been paid for 2 or more consecutive years, full payment will be paid. If the period is less than 2 years, a proportionate amount depending on the number of months paid by the member after obtaining the membership number, will be awarded.

4A. Sudden death of a covered person before reaching the age of 18

Benefit	3000	3000	3000	3000	3000

4B. Sudden death of a covered person between the age of 65 and 75:

Benefit	3000	6000	6000	6000	6000

In case of natural death:
If the membership fees have been paid for 2 or more consecutive years, full benefits will be awarded.
If the period is less than two years, a proportionate amount dependent on the number of months paid by the member after obtaining the membership number, will be awarded.

5A. Hospitalization of a covered person:

Benefit	30	60	90	150	300

Benefit is awarded once in 12 consecutive months only for one event subject to a maximum delay of 15 days per covered person.
Repeat benefit claims for the same illness will be entertained once in two years.
Hospitalization claims can be made only after completing 6 months of membership.

5B. Auryedic or similar treatments of a covered person:

Benefit	15	30	45	75	150

If hospitalization conditions are not being met, benefit is awarded once in 12 consecutive months only for one event subject to a maximum of 10 days per covered person. Repeat benefit claims for the same illness will be entertained once in two years. Ayurvedic or similar treatment claims can be made only after completing 6 months of membership.”