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October 1999 – Issue No. 20

Ley 100 (Law 100) in Colombia
continued from page 9

serve as EPSs and potentially as a TPA providing services to EPS organizations. However, the traditional insurance company can also seize an opportunity by providing excess coverage to those who would prefer a degree of care beyond that provided by the POS plan design. It is already the case that EPS's are working with insurance carriers in an effort to efficiently coordinate the claim adjudication function when excess coverage is provided. First, the insurance carrier processes the claim as though the coordination with the EPS did not exist. The insured is reimbursed this total amount and the EPS then reimburses the carrier for the portion of the claim that they were responsible for as the primary insurer. A potential drawback is that this higher level of coverage in a contributory plan could never be made to be mandatory by an employer for all of its employees, which could create the age-old problem of anti-selection.

Another control that the government has in place is a type of guarantee fund, which takes 15% of contributions earmarked for the EPSs. This money serves the purpose of re-distributing funds to EPSs that have had adverse experience in an attempt to maintain equality among the various entities.

Since the entire population is not obliged to be part of the POS until the year 2001, the actual size of a potential higher tier market is difficult to measure. But, given Colombia's population of some 38 million (3rd largest in Latin America behind Brazil and Mexico), this could represent a substantial opportunity in the region. This will certainly be a sizeable opportunity should the nation's somewhat turbulent political past improve.

Rod Mangrum, ASA, is an assistant actuary with Pan-American Life Insurance Company in New Orleans, Louisiana. His responsibilities include actuarial pricing and product development for group insurance portfolios in seven Latin American countries.

Life in China: Part One

by Cao Qing Yang, FLMI

Editor's Note: Executives who attended LOMA's 1998 Strategic Issues Conference were given up-to-the-minute briefings on a number of emerging insurance markets in the Asia-Pacific region. Here's what one expert had to say about the People's Republic of China.

This article is reprinted from LOMA Resource *with permission. The second half of the article will appear in the next edition of* International Section News.

This year, mainland China's life insurance industry is half a century old. It has been a very interesting 50 years—especially the most recent 15, which have been characterized by industry reform, open markets and economic development.

Launched in 1949, the life industry thrived in the People's Republic of China (PRC) until 1958, when all operations were suspended. In 1982, they resumed, although life insurance premium income was very low at RMB¥ 1.59 million (approximately US$ .19 million) and the state-owned People's Insurance Company of China (PICC) dominated the market with a 90% + share of business.

Since then, dramatic change has occurred in the PRC's life insurance industry, the evolution of which has occurred in three distinct phases. The result? During the past 10 years, life premium income has grown, on average, 40% per year; in 1997, it grew 82% to RMB¥ 60 billion (US$ 7.3 billion). In addition, more and more Chinese have begun to recognize the importance of life insurance and the industry has become a popular career choice among the young.

The emergence of the PRC's individual life insurance market can be attributed largely to the establishment of Beijing-based PICC in 1949. At that time, PICC's life insurance department was in charge of the company's life operations. In July 1996, PICC was organized, becoming PICC (Group), with RMB¥ 20 billion registered capital, RMB¥ 102.9 billion total assets, and three wholly-owned subsidiaries: PICC (Life), PICC (Property), and PICC (Reinsurance). At the time of the reorganization, PICC (Life) had RMB¥ 1.5 billion registered capital and RMB¥ 74 billion total assets.

PICC (Life) currently has 1,561 branches at or above the county level, an 851-person business department, 40,000 regular employees and 180,000 agents. Its contributions to mainland China's life insurance industry are immense—among them, launching the country's life insurance market, training managerial per- sonnel for the life industry, providing the industry with examples of basic contract provisions, and formulating mainland China's first life insurance mortality table (1990-1993) on the basis of its experience data in 1995.

Another important driver behind the rapid development of the PRC's individual life market has been the agency system for product distribution—a system all domestic life insurance companies have adopted. In 1996, there were only 140,000 life insurance agents, and they generated RMB¥ 5.5 billion of premium income (16.7% of the country's total premium income). The following year, the number of life insurance agents skyrocketed to 350,000 and they generated RMB¥ 21 billion of premium in- come (35% of the PRC's total premium income).

Major Players

At the moment, there are 22 domestic insurance companies in mainland China, of which seven are life insurance companies. The only state-owned life insurer, PICC (Life) operates nationally, as do the shareholding companies Ping An, Pacific, New China, and Tai Kang. AIA, the only foreign company, operates regionally, as does Zhong Hong, which is funded jointly by Chinese and foreign investors. While Ping An has enjoyed the highest growth rate of any life insurance company, PICC (Life) still holds the largest market share with a 65% stake in 1997. Last year both Ping An and Pacific completed business restructuring in order to separate their life and property operations.

New shareholding companies and joint-venture companies will continue to enter mainland China's market; in fact, the People's Bank of China actually encourages foreign companies to enter the life sector by joint venturing with Chinese companies.

Products & Distribution

Today, there are hundreds of life insurance products in the PRC. These fall into three major categories: individual, group, and riders.

Individual life products include juvenile insurance, which basically provides the policyholder with an educational fund and typically has a supplementary option like a deferred annuity; critical illness insurance, in the form of whole life and term life, which covers eight to ten serious illnesses and provides a total permanent disability benefit; whole life insurance, which typically has a premium refund benefit; endowments, which are the most popular products and offer a living payment every three or five years; and deferred annuities, most of which cover death and total permanent disability.

Group life products include group endowment, group accidental and dismemberment, group annuity, industrial insurance, and group medical expense insurance.

Life riders include medical expense insurance, which has a one-year term, a coinsurance provision, and a relatively low face amount (about RMB¥ 20,000); special disease insurance, which has a one-year term and covers specific diseases such as cancer or cardiovascular disease; and hospitalization insurance, which offers a maximum daily benefit of about RMB¥ 100 for a maximum of 90 days.

How have customers responded to these products? First, products with a savings component have been well received and currently hold the largest market share. The traditional products promise a higher rate of interest than that of the banks and all of them are non-participating. Because they lack flexibility, however, these products have not fared as well in the marketplace. With only a critical illness plan and some medical riders available in mainland China, the range of health insurance products is too limited to meet market demands. Most of the products available in the country offer extensive protection against death and total permanent disability as well as a maturity payment; nonetheless, they have not been designed to meet market needs.

"Agents distribution consists of life agents, part-time agencies and career agencies. Life agents are captive—that is, they can sell only one company's products."

Agents, employees, branches, brokers and others sell life products in the PRC.

Agent distribution consists of life agents, part-time agencies and career agencies. Life agents are captive—that is, they can sell only one company's products. AIA introduced life agents to mainland China in 1992; since then, all Chinese companies have adopted this sales channel. There are more than 350,000 life agents in the country today and they are concentrated in major cities and coastal areas such as Beijing, Shanghai, Guangdong and Jiangsu. With 180,000, 100,000 and 48,000 life agents respectively, PICC (Life), Ping An, and Pacific control 93% of the life agents in mainland China. Part-time agencies—which are affiliated with several companies and generate more than one-third of the country's group business and career agencies, which are few in number and focus primarily on property insurance are two additional agent distribution systems employed in the PRC.

Brokers are another sales channel in mainland China. There are very few brokers and they mainly handle property insurance. Most are located in big cities; there are 20 in Shenzhen and three in Beijing, for example. In February 1998, the People's Bank of China issued the "Regulations of Insurance Broker (trial)," which is a sign that the insurance brokerage market will be opened up in the future.

Insurance company employees also sell insurance in the PRC. In each life company, about 5% of the employees are responsible for selling group products; often, they generate two-thirds of a company's group business.

Until 1993, life company branch offices were an important component of PICC distribution. These branches sold group products such as group accidental insurance and annuities. Today, there are more than 1,000 PICC branches throughout the country. However, they are gradually evolving from sales channels to business management centers.

Other distribution channels in mainland China include banks, which sell group and individual annuity products; post offices—which sell accident products; and automated policy sales machines which offer flight accident insurance to airline passengers. These alternative sales channels generate less than 1% percent of the PRC's total business volume.

The 350,000 life agents have become the country's primary distribution channel. Since 1998, prospective agents have been required by the country's regulatory body to sit for the "National Examination for Agent Certificate." Those who pass

(continued on page 12, column 1)

Life in China: Part One
continued from page 11

the exam then take a short training course about the company to which he/she is applying for work. Upon completion of this course, the individual becomes a qualified insurance agent.

In 1997, the number of agents increased rapidly, as did the numbers of regulatory violations. To address this negative trend—and to enhance agent quality and ethics—the People's Bank of China strengthened regulation in 1998. A life agent's commission for 20-year payment products can not exceed 40% of the annual premium and he/she can receive a commission on the product for up to five years. And, insurers now model life agent administration on the methods that prevail in Taiwan and Hong Kong.

Management Issues

Mainland China is facing a grave shortage of insurance professionals, and our training facilities are insufficient to meet the growth of the industry. Although the functions of underwriting, claim administration and customer service have been established and are functioning in the industry, the limited application of computer systems has hampered the standardization of business management.

Companies have established their own underwriting systems by drawing on foreign experience. Because of the country's existing healthcare system, few individuals have complete medical records. Patients' health files are kept only in the hospitals where they have been treated. As a result, they are not available to life insurance underwriters, which greatly affects the accuracy of underwriting decisions. The only insured health information the underwriter can get is the medical checkup results in the hospital designated by the insurance company. Some insurance companies have even set up their own checkup centers. Another underwriting challenge is that Chinese insurers currently do not require smokers to pay higher premiums than non-smokers. Because there are no tax records or accurate income records for most people, another problem is verifying the accuracy of the information supplied by individuals applying for large amounts of coverage.

Most underwriting personnel are doctors who are short on insurance vocational training. In addition, there is a great shortage of experienced underwriting personnel here. Because most life insurance products are endowments or annuities requiring a premium payment of less than RMB¥ 100,000, the shortage and importance of experienced underwriters is felt acutely.

The claim administration situation also is far from perfect. Due to the difficulty insurers have in collecting the necessary data to process a claim, they often overpay. In addition, claimant misstatements and fraud are fairly common. Customers have concerns, as well. According to a 1997 survey of the Beijing insurance market, many policyholders are dissatisfied with life insurance companies, primarily because of their claim settlement decisions.

In life insurance companies here, actuaries are mainly responsible for product design and reserve calculations. We have approximately 20 ASAs in mainland China, though neither the actuarial system nor its examination system are in place. In 1995, the Japanese life table that Chinese in-surers had been using was finally replaced by the PICC-stipulated China life mortality table. We still have no morbidity table, however, and have not acquired enough experience data, which, of course, is critical for health insurance operations. Compared with foreign markets, Chinese life insurers are somewhat more conservative in pricing. Among themselves, there are only negligible differences in premium rates, expense rates and agent commissions.

In 1997, many life insurance companies set up customer service centers. Several factors compelled them to do so, among them a rapid growth in business and inefficient and ineffective business management. Another important reason is problems with the agent distribution channel. Misrepresentation of policy terms and conditions is on the rise. In addition, the agent retention rate is quite low (more than 4% of agents quit during their first year of employment), which has led to an increase in orphan policies. When you combine these distribution problems with customers who are learning about insurance contracts for the first time, customer service becomes increasingly important for insurers wishing to grow their business.

At present, customer service centers typically are responsible for policy renewal, consulting, litigation, and orphan policy management. Because of the limited application of technology and the insufficient training of service staff, however, they are far from perfect. I believe the customer service function will become the focal point of companies looking for a competitive advantage in mainland China's insurance markets.

Another management challenge in the PRC is technology. The systems currently in place simply are unable to accommodate insurers' rapidly expanding business. As a result, most companies are giving high priority to improving their technology infrastructure. Nonetheless, most companies have not yet been able to centralize their functional operations via technology. As a result, head offices frequently can not handle underwriting, reinsurance or claim administration either directly or efficiently.

What's more, the country's banking

system does not accommodate depositing and withdrawing funds at different locations and most people do not use credit cards. The result? Policyholders can make premium payments only in the city in which they originally applied for insurance. This is also true for benefit or claims payments.

During the past two years, the Internet has garnered much public interest, especially in big cities where access has become quite fashionable. Analysts predict that the number of Internet users in mainland China will reach one million in the near future.

This new development has already attracted the interest of life insurance companies. Most of them have established home pages on the Internet, through which they are introducing life insurance products and recruiting agents. In 1997, the China Insurance Information Net—a window through which people can learn more about the insurance industry—was launched. No insurer sells insurance over the Internet, however, because of the constraints of the country's banking system.

Cao Qing Yang, FLMI, is deputy manager, Business Department, at The People's Insurance (Life) Company of China.

A Social Security System for the 21st Century: Part II

by Chiu-Cheng Chang & Geraldine Chen

Editor's Note: The first half of this article was published in the last issue of International Section News. *The list of 21st century trends immediately below summarizes key points included in the first portion of the paper.*

II. 11 The Trends of the 21st Century: A Summary

1) The population will be aging.
2) The spread of technology and information will engender a world that will be increasingly interdependent. Future technology will be so efficient that most of the time, it will be taken for granted. The indications are already there—for example the increasing use of the "Smart card"—of the move from technological complexity to technological transparency.
3) Politics will take a back seat to economics. The global corporation will become the agent of international economic integration and the catalyst for social and political change in developing countries, taking over some of the roles of governments and international organizations. Decision-making will be increasingly decentralized.
4) The consumer will be sovereign. Firms will seek ways of adapting their operations and management styles to maximize their responsiveness to consumer tastes that will evolve over time and differ across cultures. People and knowledge, brainpower and innovation will be the driving forces of the 21st century and access to markets will be the critical factor determining business success. Countries have responded by carving out their "markets of influence," most visibly through the formation of trade blocs.
5) Employees with innovative drive and the ability to harness and exploit information will expect and demand better remuneration, benefits and pension packages. However, with greater international labor mobility, the traditional pay-as-you-go social security systems will be increasingly anachronistic.
6) The availability of information, multinational production, trade and foreign investment will nurture a new global lifestyle. Present cultural and societal barriers to certain types of behavior and lifestyle patterns will break down.
7) Individuals will become accustomed to looking after themselves and taking responsibility for their actions and their lives.

The next two sections will outline the inadequacies and drawbacks of pay-as-you-go social security systems in the light of these trends and, using the Singapore pension system as an example, develop the essential characteristics of the social security system of the 21st century.

III. The Pay-as-you-go System

The pay-as-you-go defined-benefit system is the norm in the industrialized countries. Workers pay pensions, usually financed through payroll taxes or general revenues, to retirees today, with the expectation that their pensions will be paid by the next generation of workers. A pay-as-you-go pension plan's current revenues are just adequate to cover its current obligations. There is no stock of assets to pay future pensions.

(continued on page 14, column 1)