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New bancassurance regulations in Indonesia

On 23 December 2010, Bank Indonesia issued a circular to all commercial banks in Indonesia entitled "Application of Risk Management in Banks Which Conduct Joint Marketing Activities With Insurance Companies (Bancassurance)."

The circular sets out a comprehensive regulatory framework for bancassurance activities. The new regulations are likely to lead to fundamental changes to existing bancassurance models in Indonesia. The regulations came into effect immediately.

Bancassurance models

The circular categorises bancassurance activities into the following three business models:

- Referral Model:

In this model, the bank's role is to refer/ recommend insurance products to customers, with the bank engaging in limited marketing.

The circular mentions two types of products being offered under the Referral Model: insurance that is linked to banking products and insurance that is not ("packaged" and "unpackaged"). In the first case, the bank will inform the customer that insurance must be purchased in conjunction with the banking product to safeguard the bank from associated risks (e.g., credit insurance for consumer loan products or other loan-related coverage).

For unpackaged insurance products, a bank can use leaflets, brochures and websites to promote insurance products but must refer customers directly to insurance companies in respect of sales.

- Joint Distribution Model:

In this model, the bank is directly involved in providing insurance advice to customers via insurance advisors, telemarketing or other media. In this case, the bank is responsible for explaining the products to customers.

- Integrated Model:

In this model, the insurance product is sold together with banking products and the bank is directly involved in marketing the insurance products to customers.

The circular goes on to state that banks are only permitted to distribute insurance products that are defined in an agreement between the insurer and the bank.

Risk management framework

Banks conducting bancassurance activities are required to review and develop their bancassurance policies and procedures in accordance with the new risk management framework. The key requirements are summarised below:

- A bank must carry out the necessary due-diligence/periodic assessments to ensure that the insurance partner has adequate financial strength, has obtained approval from the Ministry of Finance to conduct bancassurance and has met the necessary requirements to sell unit-linked business.

- A 'cooperation agreement' must be agreed between the bank and insurer for each insurance product that is being sold, setting out the responsibilities of the parties, the model being adopted, the term of the agreement and termination/settlement provisions.

- In using customer data, a bank must have regard to regulations governing the transparency of bank products and use of personal customer data. To protect customers, the bank must implement principles of transparency in line with the regulations. These include appropriate use of the bank's logo and disclosure of fees/commissions received by the bank. Moreover, for the Joint Distribution and Integrated Models, appropriate explanation/description to the customer, both orally and in writing, is required to ensure that they have fully understood the underlying risks of product, with a signature from the customer to document this.

- When selling packaged insurance under the Referral Model, a bank must offer customers a minimum choice of three insurance products, and such products can only be protection-based.

- In the case of unpackaged insurance sales under the Referral Model, the space allocated by the bank to the insurance company for in-branch sales must specifically indicate the name of the insurer. The insurance company's employees assigned to in-branch sales will not be allowed to wear the same uniform as bank employees.

- Under the Joint Distribution model, a bank must set up a dedicated bancassurance unit. The employees assigned to this unit have to meet a prescribed level of training on insurance sales. Banks can only be responsible for insurance sales, with underwriting, issuance and claims being the responsibility of the insurer. The bancassurance unit can sell protection products or unit-linked plans that are invested in money markets or fixed-income type assets (which the industry is interpreting to mean funds with less than 20% equity content).

- Similar requirements are set out for the Integrated Model with respect to the requirement to establish a dedicated bancassurance unit. Under this model, bank staff can only sell protection-related insurance, and banks are required to segregate the packaged product into its insurance and banking components and to ensure that the risk between these components can be separately identified and measured. The risks related to each component must be explained to the customer both orally and in writing.

Reporting requirements

The ongoing reporting requirements included in the regulations are as follows:

- For new and existing bancassurance arrangements, a business plan/bancassurance activity report needs to be submitted to Bank Indonesia in the format prescribed by the circular.

- Ongoing bancassurance reports are to be prepared internally on a monthly basis and reported to Bank Indonesia quarterly.

Various penalties and sanctions are stipulated for non-compliance, and companies have been given up to six months to ensure that existing bancassurance policies and practices meet the new requirements.

Reactions and possible implications

The new requirements have received a mixed reaction from the insurance industry in Indonesia.

Several companies have voiced concerns over the prevention of bank staff selling unit-linked plans that have a significant equity component, understanding the impact that this may have on bancassurance sales. Other companies have commented on the likely different interpretations of some model definitions, such as 'Referral', and hence whether certain sales practices fall under this classification. There is widespread dismay about the amount of work required to draft separate Cooperation Agreements for each product sold.

Some of the impacts of the new regulations that we foresee are:

- Reduced new business volumes for some players as they adjust to the new regulatory regime.
- Restructuring of existing bancassurance models and agreements.
- Some insurers being better placed to secure new bancassurance relationships and agreements, especially those with experience of using their own people to sell insurance.
- Increased demand for experienced in-branch insurance advisors.
- Changes to product design and the mix of business sold through banks.
- Changes to investment strategy/mix underlying unit-linked business sold through banks.
- Greater competition in protection products, with banks needing to offer choice to customers under the Referral model.
- Better point of sale advice, possibly resulting in improved persistency over time.
- Higher costs (implementation and ongoing compliance) which will impact profitability and/or premium rates/charges.

In recent years bancassurance has become a very important distribution channel in Indonesia. Many banks have proactively sought insurance providers and many insurance companies (particularly the foreign insurers) have worked with their bank partners to provide a range of product offerings to the bank customer base. At a time when the Indonesian insurance market is attracting so much attention, and when some of the larger banks are reviewing their insurance strategies (distributing or manufacturing), these changes will have a major impact on some of the strategic decisions to be taken.

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