

REFORM OF THE INSURANCE INDUSTRY FOR DEVELOPMENT OF THE PRIVATE SECTOR

(TC-98-05-02-1-PR)

EXECUTIVE SUMMARY

BENEFICIARY AND EXECUTING AGENCY: Central Bank of the Republic of Paraguay (BCP) through the Superintendency of Insurance (SIS).

FINANCING: Modality: Grant - Window I

MIF:	US\$ 915,000
Local counterpart:	<u>US\$ 772,000</u>
Central Bank:	US\$ 610,000
Insurance firms:	<u>US\$ 162,000</u>
Total:	US\$1,687,000

IMPLEMENTATION SCHEDULE: Commitment period: 30 months
Disbursement period: 36 months

OBJECTIVES: The principal objective of the project is to improve the functioning of the insurance market in order to foster the rapid development of the Paraguayan private sector. To achieve this aim, the program will seek: (i) to strengthen the Superintendency of Insurance (SIS) as an institution to give it the capacity to issue modern prudential standards and to supervise the country's insurance companies effectively, and (ii) to develop efficient procedures for the regulatory agency and for insurance companies to improve solvency in the sector. The program will have the following components: (i) staff strengthening, (ii) consultancy for preparation of legislation and standards, chart of accounts, manuals, guidelines, data collection, and business accounting, (iii) establishment of risk registry and complaint system, (iv) training, (v) supply of equipment, and (vi) project coordination.

SPECIAL CONTRACTUAL CONDITIONS: Prior to the first disbursement of funds, the SIS must meet the following requirements to the Bank's satisfaction: (i) appoint a project coordinator (paragraph 3.19); (ii) have a budget allocation approved by the BCP board of directors to cover the hiring of ten staff members (paragraphs 3.3 and 3.5); and (iii) establish that the training-for-trainers component will be financed equitably with the enterprises on a *pari passu* basis (fifty-fifty) (paragraphs 3.3 and 3.20). The contract will also include conditions to ensure program monitoring and

Executive Summary

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evaluation, submission of duly audited financial statements, and use of the Bank's procedures in procuring goods and consulting services.

EXCEPTIONS TO BANK None.
POLICY OR
PROCEDURES:

I. ELIGIBILITY

A. Country eligibility

- 1.1 On September 15, 1994, the Donors' Committee of the Multilateral Investment Fund (MIF) declared the Republic of Paraguay eligible for all types of funding from the Multilateral Investment Fund.

B. Project eligibility

- 1.2 The proposed operation is compatible with the funding criteria set forth in Section 2 of the MIF's Establishing Agreement, which provides, among other things, for the use of MIF resources for governmental entities in eligible countries to support the development of their financial systems, in particular by establishing minimum prudential regulations and strengthening the institutional capacity of supervisory institutions.

II. BACKGROUND

- 2.1 The sector's legal framework is governed by the new insurance law promulgated in February 1996. This law represents a major improvement over the previous one. It defines asset requirements with respect to a company's risk assets and it delegates authority for regulation to the Superintendency of Insurance. It also establishes the requirement that different capital funds be maintained, one to cover potential property loss liabilities and another to cover personal risks, especially disability and death. The law further establishes principles for the operation of reinsurance firms as well as requirements for reinsurance contracts. Effective enforcement of the law calls for issuing appropriate standards and regulations and strengthening the supervisory agency. Both of these elements are provided for in the present operation.

III. THE PROJECT

1. Objectives

- 3.1 The principal objective of the project is to improve the functioning of the insurance market to foster the rapid development of the Paraguayan economy's private sector. To achieve this aim, the program will seek: (i) to strengthen the Superintendency of Insurance (SIS) as an institution in order to give it the capacity to issue modern prudential standards and supervise the country's insurance companies effectively, and (ii) to develop efficient procedures for the regulatory agency and for 43 insurance firms in

order to improve solvency in the sector. Appropriate oversight and compliance with respect to insurance services will give the general public confidence, making it possible to reduce claims-related risk. Also, the development of life insurance will promote long-term domestic savings, which will encourage development of the domestic capital market and the use of long-term domestic financing to fund long-maturing productive projects.

2. Cost and activities

- 3.2 The project will consolidate and deepen the Paraguayan insurance industry. The project has five components: (i) strengthening personnel; (ii) outside consulting; (iii) creation of a risk registry and a complaint system; (iv) training; (v) providing equipment; and (vi) coordination.

COST OF THE COMPONENTS AND ACTIVITIES ENVISAGED (In US dollars)				
ACTIVITIES	FIRMS	BCP	MIF	TOTAL
Subprogram I: Strengthening personnel		480,000		480,000
Strengthening personnel (10 professionals, 2 years)		480,000		
Subprogram II: Outside consultants	98,000		313,000	411,000
Drawing up legislation and standards			48,000	48,000
Chart of accounts for insurance firms			64,000	64,000
Preparation of manuals and guidelines			128,000	128,000
Manuals for evaluation of firms			48,000	48,000
Outside audit policies			16,000	16,000
MERCOSUR policies			64,000	64,000
Automated systems consulting	98,000		73,000	171,000
Automated data collection	50,000		25,000	75,000
Insurance firms' accounting	48,000		48,000	96,000
Subprogram III: Systems improvement			192,000	192,000
Creation of risk registry			96,000	96,000
Client complaint system			96,000	96,000
Subprogram IV: Training	64,000		261,000	325,000
Training of trainers	64,000		64,000	128,000
Staff training costs			197,000	197,000
Subprogram V: Computers		21,000	49,000	70,000
Equipment		21,000	49,000	70,000
Coordination		109,000	-	109,000
Contingencies		100,000		100,000
TOTAL	162,000	610,000	915,000	1,687,000
Percentages	10	36	54	100.0

- 3.3 The Central Bank of Paraguay (US\$610,000) and the insurance companies (US\$162,000) will make a commitment to provide counterpart funding as a condition of the proposed operation. The executing agency will be the same as the one presently carrying out the technical cooperation operation for supervision of banks (TC9601354) to which a coordinator will be added, with experience in the insurance market and its supervision.

SUBPROGRAM I: Strengthening of SIS Personnel (US\$480,000)

Specific Objectives

- 3.4 The specific objective of this subprogram is to ensure that there is enough qualified staff to carry out the tasks envisaged within the SIS, especially in the following areas: (i) database management; (ii) development and supervision of insurance company charts of accounts; (iii) maintaining accounting software; (iv) operation of the risk registry that is to be created; (v) preparation and updating of guidelines and manuals for company evaluation; (vi) developing policy on and dealing with outside audits of insurance companies; (vii) management of the client complaint system; and (viii) development of staff training for the insurance sector.

Activities and cost

- 3.5 Hiring ten additional staff members for SIS at a cost of US\$480,000 for the first three years. The funds for hiring this personnel will come entirely from the BCP.

SUBPROGRAM II: External consultants (US\$411,000)

Specific objectives:

- 3.6 The purpose of this subprogram is to:
- a. issue regulations for the law and the corresponding standards;
 - b. develop a new chart of accounts for insurance companies;
 - c. prepare manuals and guidelines for: (i) evaluation of firms; (ii) development and updating of policies on outside audits of insurance firms; and (iii) development of MERCOSUR-compatible policies.
 - d. improve computer systems for: (i) automatic data collection and (ii) modernization of insurance company accounting procedures.

Activities and costs

- 3.7 The main activities of the subprogram are: (i) hiring two professionals for seven months to review and issue new regulations and standards (US\$48,000) and develop insurance firm charts of accounts (US\$64,000); (ii) hiring one professional for six months

at a cost of US\$48,000 to write manuals and guidelines for evaluating insurance firms; (iii) hiring one professional for two months at a cost of US\$16,000 to develop policy for external audit management; (iv) hiring two professionals for four months at a cost of US\$64,000 to study policy regarding adaptation to MERCOSUR; and (v) hiring three professionals for eight months each as consultants on the development of computer systems for automated data capture and for insurance firms' accounting management (US\$171,000).

- 3.8 The idea is to begin reviewing legislation and drafting current standards during the first quarter of the technical-cooperation program. The chart of accounts will be ready in the second and third quarters. The manuals and guidelines will be started in the third quarter and finished by the beginning of the sixth quarter. Finally, work will start on the computer systems for automatic data capture in the second quarter, while work on accounting systems for firms will begin in the program's third quarter.

SUBPROGRAM III: Improvement of systems (US\$192,000)

Specific objectives

- 3.9 The specific objective of this subprogram will be to develop two main systems to improve competitiveness and quality in the sector: (i) a risk registry and (ii) a system for receiving and analyzing client complaints.
- 3.10 The risk registry will provide a centralized database with aggregate information on claims by region and subsector. This is essential if firms are to gradually improve their estimates of premiums on the basis of reliable information from the Paraguayan market. The client complaint system will make it possible for SIS to track, by sector, fulfillment of contracts and degree of client satisfaction with each insurance company. Both systems will be essential for improving competition in the insurance sector as companies attempt to address the needs of their clientele more effectively.

Activities and costs

The main activities of the subprogram are:

- (i) Hiring two consultants with experience in developing microcomputer programs for six months each at a cost of US\$96,000 to develop computer programs for the risk registry; and
- (ii) Hiring two consultants with experience in developing microcomputer programs for six months each at a cost of US\$96,000 to develop a computerized system for client complaints.

SUBPROGRAM IV: Training (US\$325,000)

- 3.11 This subprogram consists of two years of training for SIS professional staff in the form of short courses in which they will have the opportunity to share experiences with staff of other Latin American superintendencies. At least 22 SIS staff members are expected to receive training.

Another aim of the subprogram is to join with counterparts from insurance firms in providing some of the training and instruction for 40 private trainers who will then work on an ongoing basis to train employees in the sector on various fundamental aspects of the insurance business and to disseminate knowledge of insurance legislation.

Specific objectives

- 3.12 The first objective of this subprogram is to improve training of qualified personnel at SIS. To this end, the intention is to arrange visits to specialized institutes and other supervisory agencies in the hemisphere to enrich the staff's fund of experience. In particular, the program will seek to hone the technical skills of SIS staff in the following areas: (i) inspection and supervision of insurance firms; (ii) development and updating of standards; (iii) automated data collection by firms; (iv) analysis of contracts for new types of insurance; (v) analysis of the quality of services provided by insurance firms; and (vi) analysis of aggregate costs and risks for insurance firms based on information from the risk registry.

Activities and costs

- 3.13 The activities to be carried out under this subprogram are: (i) hiring four experts for four months at a cost of US\$128,000 to train trainers; and (ii) hiring three professionals for 12 months at a cost of US\$197,000 to train SIS personnel.

SUBPROGRAM V: Computers (US\$70,000)

- 3.14 This subprogram consists of acquiring 28 IBM-compatible micro-computers with modern features (e.g., 233-MHz Pentium CPU's, 16 MBs of memory, high-speed modems—faster than 56 KB/second-compatible with the country's telephone service, CD-ROM readers, and 10-GB hard drives for information storage).

Specific objectives

- 3.15 The objective of this subprogram is to improve SIS's operational capacity, insofar as it does not presently have machines of its own. The new equipment is expected to increase capacity for timely data capture, and for recording, reviewing, and analyzing it.

Coordination (US\$109,000)

- 3.16 This component will cover the fees of a coordinator who will act as administrative and technical chief of the project. This should be a professional with broad experience in insurance and management. The costs involved will be defrayed by the local counterpart funding. Office and secretarial expenses will be shared with the executing unit for the banking supervision technical cooperation project (TC9601354).

Organization and execution

- 3.17 The SIS, acting through the executing agency, will be responsible for implementing the program. Prior to the first disbursement of the financing, the Central Bank of Paraguay will appoint the program coordinator who will perform the following functions: (i) coordinating the programs and the operational aspects of the training subprograms with the Paraguayan Association of Insurance Companies (APSC); (ii) hiring the necessary consultants; (iii) presenting annual progress and implementation reports to the BCP and Bank authorities; and (iv) presenting the annual accounting and operating records for the program.
- 3.18 For execution of the insurance units component, SIS will sign an agreement with APCS on its participation in the program. The APCS has committed to furnishing the local counterpart funding of US\$162,000, by means of a special contribution from its affiliates of 0.10% of its production for two years. This will make it possible to collect approximately US\$100,000 annually from the insurance companies.
- 3.19 Goods and services will be procured and the audited financial statements of the program presented, in accordance with the Bank's policies and rules. Also, a revolving fund will be established in an amount of up to 10% of the total financing.

IV. RATIONALE FOR THE PROGRAM

- 4.1 The proposed program meshes well with the government's development strategy, which centers on an integrated macroeconomic adjustment program, with a long-term horizon aimed at improving the country's economic competitiveness. Furthermore, one of the areas accorded priority in the Bank's activity in Paraguay is institutional strengthening in the context of reform and modernization of the State. The Eighth Replenishment affirms the need for the Bank to support the modernization and strengthening of the financial and judicial institutions of its borrowing member countries. In view of the foregoing, the proposed operation is fully compatible with the Bank's program for the country.

V. BENEFITS AND RISKS

- 5.1 The strengthening of the regulatory system will set the stage for sustained growth in goods and services in the private sector without excessive risk. Improved prudential regulation and supervisory capacity at the SIS will win insurance firms the trust of the public and ensure the transparency of the system and its satisfactory growth. In addition, it is expected to promote the development of life insurance, which will in turn lead to the accumulation of substantial long-term private savings.
- 5.2 The main risk associated with the program has to do with procedural delays that may arise in implementation. This risk will be minimized through a commitment by the BCP to strengthen the executing unit effectively.

VI. PERFORMANCE CRITERIA AND ASSESSMENT OF RESULTS

- 6.1 The criteria for assessing the project's performance will be based strictly on the quality and timely completion of the various anticipated products that result from the activities carried out as part of the different components. A description of these results/products is included in the logical framework (Annex 1). The progress of the program and its successful outcome will be assessed on the basis of the semi-annual and final reports to be submitted by the executing agency.

VII. EXCEPTION TO POLICIES OR PROCEDURES

- 7.1 No exceptions to current policies or procedures for operations of this type is required for the present project.

VIII. ENVIRONMENTAL AND SOCIAL IMPACT FACTORS

- 8.1 The profile was sent to CESI for its information on June 19, 1998. No comments have been received.

SIMPLIFIED LOGICAL FRAMEWORK OF THE PROJECT

SIMPLIFIED LOGICAL FRAMEWORK OF THE PROJECT REFORM OF THE INSURANCE INDUSTRY FOR DEVELOPMENT OF THE PRIVATE SECTOR		
GENERAL OBJECTIVE OF THE PROJECT		
Functioning of the insurance market to foster the rapid growth of the Paraguayan private sector		
SPECIFIC OBJECTIVES OF THE PROJECT		
The issuance of standards and regulations, and improve oversight of insurance companies by the Superintendency of Insurance (SIS); and (b) develop effective practices by the Superintendency and in insurance firms.		
Subprogram	Activities to be executed	Results/Products
Level strengthening	Have enough qualified personnel to carry out the work of SIS.	Ten additional professionals hired and trained (30 months)
Employment of consultants	Hire specialized consultants to: (a) Develop regulations for the law and issue the supplementary standards.	Regulations and standards issued and introduced (12 months)
	(b) Draw up new chart of accounts for insurance companies.	Modern chart of accounts prepared and introduced (12 months)
	(c) Prepare manuals and handbooks for (i) evaluation of firms; (ii) outside audits; and (iii) adaptation to MERCOSUR.	Manuals finished and in use (30 months)
	(d) Improve systems for automated data capture and company accounting.	Systems complete and functioning
Improvement of risk registry and client complaint system	Develop risk registry and client complaint system.	Risk registry and client complaint offices in place and functioning (30 months)
Training of SIS and private sector officials	Train SIS professionals through courses, seminars, and visits to similar agencies. Train private sector professionals in order to disseminate knowledge throughout the sector.	22 SIS officials and 30 private-sector trainers trained (24 months)
Equipment	Purchase and installation of computer equipment and making it operational.	Computer system modernized and inspectors given equipment to carry out their work (18 months)
Technical administration	Technical administration of the project, as well as evaluation, reports and schedules, prepared by a coordinator.	Successful execution and supervision; completion of intermediate tasks, followed by their implementation (36 months)

PROPOSED RESOLUTION

**PARAGUAY. NON REIMBURSABLE TECHNICAL COOPERATION PROGRAM FOR
REFORM OF THE INSURANCE INDUSTRY TO PROMOTE
PRIVATE SECTOR INVESTMENT**

The Donors Committee of the Multilateral Investment Fund

RESOLVES:

1. That the President of the Inter-American Development Bank, or such representative as he shall designate, is authorized, on behalf of the Multilateral Investment Fund, to enter into such agreements as may be necessary with the Central Bank of the Republic of Paraguay and to adopt such other measures as may be pertinent for the execution of the plan of operations incorporated in the donors memorandum referred to in Document MIF/AT-_____ with respect to a technical cooperation, the purpose of which is the reform of the insurance industry to promote private sector investment.
2. That up to the amount of US\$915,000 is authorized for the purpose of this resolution, chargeable to the Technical Cooperation Facility of the Multilateral Investment Fund.
3. That the above mentioned sum is to be provided on a non-reimbursable basis.