

**INTER-AMERICAN DEVELOPMENT BANK
TECHNICAL COOPERATION PROFILE**

I. GENERAL INFORMATION

Project title	Assessment of the Regulatory and Legal Framework for Agricultural Insurance	
Fund	Multi-Donor Disaster Prevention Fund (MDP)	
Beneficiary country	Jamaica (Ministry of Agriculture)	
Executing Agency	Ministry of Agriculture of Jamaica	
Number of project	JA-T1040	
Team	Mark Wenner Team Leader, (ICF/CMF), Carina Cockburn (MIF/CJA), Javier Jiménez (LEG/SGO) and Virginia Franzini (LEG/SGO) and Dianela Avila (ICF/CMF)	
Date of request	August 25, 2008	
Estimated financing	IDB/ Non reimbursable	US\$60,000
	Total	US\$60,000
Execution and Payments	3 months for execution and 6 months for payments	

II. BACKGROUND AND JUSTIFICATION

- 2.1 Jamaica is an island state that is extremely vulnerable to hurricanes and rain induced flooding. It lies in the Atlantic hurricane belt; a place traversed by 8 to 24 named tropical storms each year and numerous tropical depressions. The tropical depressions and storms that pass over the island cause varying amounts of economic losses depending on the severity of the winds and flooding. For instance, in August 2007, hurricane Dean struck the island causing over \$260 million of crop losses, prompting the Ministry of Agriculture (MOA) to make payments of \$1.6 million to some of the most affected limited resource farmers. Then in August 2008, Hurricane Gustav wreaked damage to 70% of the country's banana farms, halting exports. Unfortunately, since 2006, most agriculture insurance products ceased to operate, leaving the sector highly exposed to weather risks. Currently, the entire agricultural sector, including large integrated supply chains as well as independent small farmers selling on spot markets, are absorbing most of the climate risks, without any risk transfer mechanism out of Jamaica - - neither publicly nor privately (re) insured. Most of the affected population, however, had no insurance.

- 2.2 The MOA normally makes ex-post ad-hoc transfer payments to small farmers after a disaster but would like to move towards an ex-ante explicit program for covering vulnerable producers against adverse weather events. Such ex-ante program could be financed, according to the risk layers, by a mix of own government funds, private insurance, contingent lines of credits and/or reinsurance.
- 2.3 The history of agricultural insurance in Jamaica has been a fitful one, marked by promising starts and sudden stops. Over the years, a few attempts have been made to provide multiple peril insurance for bananas, coffee, and coconuts through apex mechanisms. But they have not been long lasting or economically sustainable. For example, coffee, a competitive agricultural export commodity for Jamaica, has recently been having substantial problems with the insurance and reinsurance arrangements, to the point where today there is no coverage for climate risks. On the positive side, single peril insurance (fire) has been offered on a fairly successful basis for sugar cane.
- 2.4 The lack of sustainable and broad based agricultural insurance coverage has commonly been blamed on high catastrophic exposure and the lack of interest on the part of reinsurers as a consequence. In reality, there seems to be a combination of factors that has contributed to the checkered history of multiple peril agricultural insurance on the island: (i) the difficulty of effectively servicing small size farm holdings, (ii) the heterogeneous production conditions of the crops commonly produced in the country, (iii) technical difficulties in modeling hurricane and flood damages to agricultural crops, and (iv) a generally uninterested local private insurance market with a few exceptions.
- 2.5 Over the past three years, major strides have occurred in the development of parametric or index based insurance products at both the micro-level (individual farmer) and at the macro-level (regional or national government level). A number of index products for crops are in use or design phases in India, Nicaragua, Peru, Mexico, Ukraine, Ethiopia and Malawi. For livestock, a number of countries, Spain, Canada, and Mongolia have vegetative cover and mortality index insurance programs.
- 2.6 To date there is very limited research on windstorm or hurricane indexes. FAO in the Bahamas has initiated some work. The major exception to this is the research into the Caribbean Catastrophe Risk Insurance Facility (CCRIF), which has been designed by the World Bank at the request of CARICOM¹ and which was launched in September 2006. This facility is a macro-level earthquake and hurricane index for each country which is designed to finance post-disaster recovery. The payout system is based on the estimated impact of an earthquake or hurricane on each island, using probabilistic catastrophe risk modeling and actual exposures. As such, post-loss payouts will be immediate according to the severity of the event and index indemnity formula, and there will not be any need

¹ Caribbean Community

for damage to infrastructure, buildings and utilities to be assessed and valued. In the case of hurricane, the index is based on tracking of hurricane location and strength at the closest point of approach, and not on winds measured by meteorological stations.

- 2.7 While the CCRIF initiative provides Jamaica with a macro-level hurricane index protection for hurricanes that occur every 20 years, it is recognized that this product is intended to protect public assets, and it is not designed to protect private agricultural crops, which in fact will need a more frequent payout product structure than CCRIF. Further, CCRIF is not intended to index or measure hazard impact at a localized level. Hurricane Dean alone, caused damages estimated in US\$250 millions to agriculture, but it was not catastrophic enough to trigger CCRIF payment threshold.
- 2.8 Additionally, the Government of Jamaica (GOJ), with the support of the Commodity Boards, is developing a registry of farmers, with the intention to improve the transparency and efficiency of the public mechanisms to channel farmer support in the event of catastrophic hurricane damages. Last year, the Ministry of Agriculture (MOA) alone reported payments up to US\$1.6 million to small holder farms to compensate vulnerable farmers after hurricane Dean.
- 2.9 Agricultural parametric insurance products in the context of Jamaica will probably focus on making payouts to individual farmers based on rainfall levels, temperature, and/or sustained wind speeds. These types of insurances differ from conventional insurance in several ways and a review of the regulatory framework and supervisory practices is necessary in order to determine how best to have a facilitative and enabling environment without compromising prudential aspects.
- 2.10 The main hallmarks of parametric microinsurance are affordability, small sums insured, a high volume of transactions, transparent and simple to understand policies, few exclusions, simple claims process, payments made on observation of a predetermined variable and not on physical inspections of property, and sale and servicing of policies may depend on the use of unlicensed intermediaries and agents or the use of agents with a lower level of training and certification than is traditionally required.
- 2.11 **Added value of the Multi-Donor Disaster Prevention Fund:** This would be the first use of the Trust Fund to help design an insurance instrument targeting moderate- to low-income farmers in a country whose agricultural sector is extremely vulnerable to wind storm damage.

III. OBJECTIVES AND DESCRIPTION

- 3.1 The objective of this project is to assist the Jamaican Ministry of Agriculture and the Financial Service Commission in assessing what biases, uncertainties, or weaknesses exist in the current insurance regulatory and supervisory framework that could impede the introduction of agricultural crop insurance, especially

parametric products. The results of the study are to be used in the design of a donor financed operation to introduce an integrated climate risk management system.

3.2 **Component 1. Review of the Insurance Law and Commercial Code:** Review the insurance law in the country with aim of identifying biases and weaknesses. Specific actions to be undertaken include the following:

- a. Propose and determine how a parametric insurance product would be treated in the jurisdiction and if there is uncertainty as to whether derivatives law applies or insurance law applies, discuss the matter with the insurance commission and develop arguments for consideration as an insurance product.
- b. Barriers or restrictions on entry of foreign insurance companies
- c. Evaluate High capital requirements that may impede the establishment of regulated insurance institutions dedicated to the low-income market, since amassing the volume of small policies is required to generate a return on such an investment, this could take years or may bias an existing licensed insurance company away from focusing on the sale of small policies for the same aforementioned reason. High capital requirements protect the overall financial system but, make microinsurance unattractive.
- d. Technical reserves should be appropriate to the length of agricultural cycles and standards should not be used that are more appropriate for non-agricultural products: life, vehicles, etc. Companies offered agricultural products have a faster turnover rate in policies and should not be forced to set aside capital for periods of time longer than the actual exposure because it reduces growth potential and capability to improve market outreach.
- e. Key requirements for senior management are essential to assure competent and capable management of insurance companies but an excessive degree of credentialing can force existing companies to ignore the low-income market increased requirements are correlated with higher salaries and the need to generate more marginal revenue to cover the higher salary costs.
- f. Complex reporting requirements can make the cost of administering a large number of small valued insurance policies cumbersome and expensive thereby creating a disincentive for the introduction of microinsurance products.
- g. In the case of agricultural microinsurance and the targeting of low-income clients in general, the use of non-traditional parties such as non-governmental organizations, cooperatives, associations, and merchants may make more economical and commercial sense. Licensing requirements for agents and brokers has an impact on the distribution of insurance products. If for example, there were stringent

licensing requirements for agents and brokers that limited them to be a private person with a certain **level of education and training, then microfinance institutions or rural associations, that are closer and more accessible** to the target population could not be used. Regulatory authorities do have a legitimate interest in assuring that agents and brokers are pay appropriate fees, pass exams, and have no criminal records but a careful balancing interests may be needed in order to build more inclusive insurance markets.

- h. Training requirements for agents should be reviewed in context the need to develop functioning and effective distribution channels for microinsurance agricultural products. Training and commission rules may have to be modified and adjusted if non-traditional agents are contemplated as important by key stakeholders interested in expanding agricultural insurance and the consultants working on the technical feasibility of the product per se.
- i. Review the restrictions on the Amount of Commission, they should determine if the current rules may hinder the development of microinsurance and agricultural parametric insurance in particular. Low-income populations are expensive to serve and high commission rate structures may be necessary. If they are set too low, there will be little incentive for agents/brokers to serve this market.
- j. Clear policy wording and full disclosure is very important in promoting insurance for low-income client who many times have low levels of formal schooling. Review the language used in common contracts and suggests how they can be improved given best practices in microinsurance in other countries, especially India.
- k. Verify whether Jamaica is a jurisdiction with a tariff regime and if so, determine how this regime may hinder innovation and flexibility needed to promote microinsurance and parametric products.
- l. Review the commercial codes and related statutes and codes to determine how feasible it would be to issue a parametric contract and to enforce it.

3.3 **Component 2. Review of the Adequacy of Insurance Supervision:** Determine how insurance supervisors can have a facilitative role in making the regulatory environment more conducive to agricultural microinsurance. Review what current supervisory practices are and highlight how these practices may be adequate, neutral, or inadequate when a potentially large number of low-value policies that trigger on observable weather variables are introduced in the portfolio.

3.4 **Component 3. Consumer Education and Protection:** Determine how effective and relevant the current statutes are concerning consumer rights of insurance policy holders and suggest adaptations or actions that would be necessary is better protecting the rights of moderate- to low-income farmers.

- a. Low-income people are not very familiar with insurance policies and based on focus group interviews with potential farmer clients and discussions with other stakeholders, determine how and what will be the best way to improve understanding and inform the farmers as to their consumer rights under the law, especially in the case of disputes.
 - b. Simulated games from other countries that help the farmers better understand parametric insurance may be suggested.
 - c. Review the regulatory framework and assess how easy and low-cost it would be for an aggrieved consumer to defend his or her rights. If the procedure would be high-cost and convoluted, make suggestions as to how the process how be improved.
- 3.5 Expected results. The key expected results are a guideline for policy and regulatory authorities to follow in creating more favorable conditions for the introduction of agricultural crop insurance and a determination as to whether new parametric products can be introduced. This work will complementary a parallel feasibility study on the design of two insurance product that is being financed by the World Bank which was just awarded to a Jamaican firm on September 2, 2008.
- 3.6 Relation with the country's strategy. The main objective of the Bank's country strategy for Jamaica (GN-2422-1) approved in July 2006 is to accelerate growth by emphasizing private sector development and better management of natural disaster risks. This project is directly aligned with two of the stated goals of the Bank approved country strategy. The clarification of the regulatory framework for the introduction of an agricultural insurance product(s) will both help to diversify the portfolio of private insurance companies and mitigate natural disaster risks in a more efficient manner.
- 3.7 Relation with the loans portfolio. This technical cooperation project is complementary to the following loan and Multilateral Investment Fund operations—Enhancing Competitiveness Program (JA- L1001); Emergency Assistance in Response to Flood Damage (JA-L1015); and Expanding Access to Rural Micro Credit (JAM1010)—that were recently approved.

IV. BUDGET

- 4.1 The total cost of this non-reimbursable TC will be US\$60,000 of which the Multi-Donor Disaster Prevention Fund will finance 100%. For a detail budget plan see Annex I

V. EXECUTOR AGENCY AND STRUCTURE OF EXECUTION

- 5.1 The execution of this technical cooperation will be responsibility of the Ministry of Agriculture. The administration of this technical cooperation will be responsibility of the Bank, done through CCB/CJA and ICF/CMF. The activities financed through the Funds, as well as the selection, recruitment and supervision

of consultants, including individuals, consulting firms, hired for the purpose of providing technical assistance, will be carried out in accordance with the applicable policies and procedures of the Bank.

VI. DURATION AND IMPLEMENTATION PLAN

- 6.1 The Project will have an execution period of 3 months and a payment period of 6 months. The detail information is show the execution plan of the project and the expected results in the Annex II Duration and Implementation Plan table.

VII. SOCIAL AND ENVIRONMENTAL STRATEGY

- 7.1 The activities to be financed in this program will have no direct negative social or environmental effects. Based on the aforementioned, and according to the ESR Safeguard Classification toolkit, the operation has been classified as "C".

VIII. RISK AND MITIGATING ACTIONS

- 8.1 The main risks assorted with this operation are twofold: (1) quickly identifying and contracting an insurance regulatory expert with experience with parametric products; and (2) obtaining the buy-in of Jamaican regulatory officials and policy markets to make the recommended changes, if deemed necessary, in the regulatory framework so as to create a more favorable environment for agricultural insurance products.
- 8.2 To mitigate the identified risks the project team will begin to immediately make a short list of known legal/regulatory experts and make inquiries as to their availability without promising the assignment to any one party and to begin a dialogue with the regulatory authorities about the experiences in other countries as a means to motivate them. The recent memories of damages caused by Hurricane Gustav and Dean should also help to spur receptivity and buy-in among policy makers and regulatory authorities.

IX. CERTIFICATION

I certify that this operation was declared eligible for financing under the Multi Donor Disaster Prevention Fund (MDP) and communicated to the team leader through an email dated September 5, 2008 signed by Juliette Balabanian VPC/GCM. Also, I certify that resources from the Multi Donor Disaster Prevention Fund (MDP) are available for up to US\$60,000 in order to finance the activities described and budgeted in this document. These certification reserves resources for the referenced project for a period of ten and a half (10.5) calendar months counted from the date of signature below. If the project is not approved by the IDB within that period, the reserve of resources will be cancelled, except in the case a new certification is granted. The commitment and disbursement of these resources shall be made only by the Bank in US\$ Dollars. The same currency shall be used to stipulate the remuneration and payments to consultants, except that local consultants working in their own borrowing member country

shall have their remuneration defined and paid in the currency of that country. No resources of the Fund shall be made available to cover amounts greater than the amount certified herein above for the implementation of this Plan of Operations. Amounts greater than the certified amount may arise from commitments on contracts denominated in a currency other than the Fund currency, resulting in currency exchange rate differences, for which the Fund is not at risk.

Original Signed

Oct / 28 / 2008

Marguerite Berger
Chief
Grants and Cofinancing Management Unit

Date

X. APPROVED

Original Signed

Nov / 06 / 2008

Kurt Focke
Chief
Capital Markets and Financial Institutions

Date

ANNEX I DETAIL BUDGET

ASSESSMENT OF THE REGULATORY AND LEGAL FRAMEWORK FOR AGRICULTURAL INSURANCE (JA-T1040)

Table 1. Budget (US\$)

Components	Level of Effort (LOE)	Day Rate (US\$)	IDB/MDDPF (US\$)	Total
1. Legal Review			31,600	31,600
1.1. Diagnosis and Analysis of Insurance Law				
1.1.1 Consultant Services (Regulatory Expert)	12	600	7,200	
1.1.2 Consultant Services (Jamaica based Lawyer)	10	1,600	16,000	
1.2 Diagnosis and Analysis Commercial Law as it affects Insurance Contracts	2	600	1,200	
1.2.1 Consultant Services (Regulatory Expert)	1	1,600	1,600	
1.2.2 Consultant Services (Jamaica based lawyer)				
1.3 Findings and Recommendations				
1.3.1 Consultant Services (Regulatory Expert)	4	600	2,400	
1.3.2 Consultant Services (Jamaica based lawyer)	2	1,600	3,200	
2. Adequacy of Supervision			6,000	6,000
2.1 Review of Adequacy of Current Supervision Practices	4	600	2,400	
2.1.1 Consultant Services (Regulatory Expert)				
2.2 Extrapolation and/or Implications of Adding Agricultural Products (Single Peril, Multiple Peril, or Parametric Products)	4	600	2,400	
2.2.1 Consultant Services (Regulatory Expert)				
2.3 Findings and Recommendations	2	600	1,200	
2.3.1 Consultant services (Regulatory Expert)				
3. Review of Stipulations for Consumer Education and Protection			7,800	7,800
3.1. Review				
3.1.1 Consultant Services (Regulatory Expert)	5	600	3,000	
3.1.2 Consultant Services (Jamaica based lawyer)	3	1600	4,800	
4. Presentations of Findings to Key Stakeholders			2,800	2,800
4.1.1 Consultant Services (Regulatory Expert)	2	600	1,200	
4.1.2 Consultant Services (Jamaica based lawyer)	1	1,600	1,600	
5. Other Expenses			11,800	11,800
Travel	3	1200	3,600	
Per Diem	20	250	5,000	
Duplication Services			200	
Communications			1000	
Contingency			2,000	
TOTAL			60,000	60,000

ANNEX II DURATION AND IMPLEMENTATION PLAN TABLE
ASSESSMENT OF THE REGULATORY AND LEGAL FRAMEWORK FOR AGRICULTURAL INSURANCE
(JA-T1040)

ACTIVITY	TIME FRAME	RESULTS
1. Legal Review of Insurance Law	1 Month	<ul style="list-style-type: none"> • Selection of consultants. • Develop work plan • Interview interested parties • Finish legal review
2. Review of Commercial Codes	1 week	<ul style="list-style-type: none"> • Complete review
3. Review of Supervisory Practices	2 weeks	<ul style="list-style-type: none"> • Interview supervisors • Interview insurance companies. • Complete review
4. Review of Consumer Protection Code	1 week	<ul style="list-style-type: none"> • Interview interested parties (esp. aggrieved consumers to see how system worked or failed to work) • Finish review
5. Draft Write-up	2 weeks	<ul style="list-style-type: none"> • Complete first draft and submit for quality review
6. Presentation of Findings	1-2 days	<ul style="list-style-type: none"> • Make presentations to MOA, insurance companies, FSC, and donor staff
7. Revisions and Submission of Final Draft	2 weeks	<ul style="list-style-type: none"> • Submit revised final report