NIGERIAN INSURANCE COMPANIES IN AN AGE OF REGULATION

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INTRODUCTION

Regulation of Nigeria’s insurance industry has become substantially intensified in the last two decades. This paper critically evaluates the philosophy and challenges of insurance regulation in the context of post-authoritarian governance and increasing economic liberalization in Africa’s potential largest insurance market. The last two decades has witnessed among others, government regulatory intervention through the establishment of a regulator and mandatory recapitalization. This study assesses the regulatory experience of the Nigerian insurance industry prior to and after the capitalization era; spanning 1999 to 2009. Temporally, the trajectory of developments in the last decade which coincides with post-authoritarian military rule in the country is significant. As a developing economy, the Nigerian insurance industry presents an example of untapped and gross under-utilization of its boundless potentials. Adopting a qualitative approach, this paper explores the factors responsible for the industry’s slow growth in comparison with its huge human and material resources and what lessons might be learnt to chart a way forward.

The first part of the paper traces the origin of insurance in the country to its colonial heritage. The second part examines the rationale for regulating insurance business. The focus then shifts to regulation of insurance in Nigeria. The paper is yet to be concluded as there are outstanding issues for analysis in on which research is still in progress.

ORIGIN OF INSURANCE IN NIGERIA- THE BRITISH CONNECTION

Nigeria, a country of more than 140 million people with a landmass of about 923,768.64sq. km and immense human and material resources is a former British colony. Hence, the country shares almost all its political and economic settings from its former colonial heritage. Before the introduction of the modern form of insurance, some form of social insurance had existed in the Nigerian society. These social schemes evolved through the existence of extended family system and social associations such as age grades and other unions (Osoka, 1992). Until 1966, Nigeria
copied British parliamentary system of government. This British system still dominates aspects of the country’s socio-economic settings. For instance, the legal practices in Nigeria still reflect its colonial heritage. Economic institutions such banks and insurance companies, in practice, copy the British style of conducting their businesses. However, the country’s progress since independence in 1960, has however been undermined by long years of military rule, political instability and systemic corruption. In 1999, a civilian government was finally elected to office after a successful political transition process.

The origins of modern insurance are intertwined with the advent of British trading companies in the region and the subsequent increased inter-regional trade. Increased trade and commerce led to increased activities in shipping and banking, and it soon became necessary for some of the foreign firms to handle some of their risks locally (Uche and Chikeleze, 2001). Trading companies were therefore subsequently granted insurance agency licences by foreign insurance companies. Such licences made it possible for such firms to issue covers and assist in claims-supervision. The first of such agency in Nigeria came into force in 1918 when the Africa and East Trade Companies introduced the Royal Exchange Assurance Agency. Other agencies included Patterson Zochonis (PZ) Liverpool, London and Globe, BEWAC’s Legal and General Assurance and the Law Union and Rock (Osoka, 1992).

There was an initial slow pace of the growth of the insurance industry in the country, particularly between 1921 and 1949. This has been traced to adverse effect of the World War II on trading activities both in United Kingdom and Nigeria. As soon as the war ended, business activities gradually picked up again, and insurance industry in Nigeria began to record remarkable improvement in growth (NICON, 1994). It was not until 1958 that the first indigenous insurance company, the African Insurance Company Limited, was established (Nigeria Re, 1993). At independence, only four of the then 25 firms in existence were indigenous. By 1976 the number of indigenous companies had far surpassed that of the foreign companies.

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\[\text{\textsuperscript{4}}\]

\[\text{\textsuperscript{2}}\] For instance, to qualify as a chartered accountant or chartered insurer, passing the British qualifying examinations offers better recognition than local qualifications.

\[\text{\textsuperscript{3}}\] Some of these agencies subsequently transformed into branch offices of their parent insurance companies. For instance, the Royal Exchange Assurance became a branch office in 1921 and Legal and General Assurance became a branch office in 1948. Other insurance companies that were subsequently introduced include: Norwich Union, Fire Insurance Society and Tobacco Insurance Company Limited, all established in 1949.

\[\text{\textsuperscript{4}}\] Of the 70 insurance companies then in existence, only 14 were foreign-owned. Forty-six were indigenously owned while ten were wholly owned by the various state governments or the Federal government (Nwankwo, 1980).
WHY REGULATE INSURANCE?

The whole world regulates insurance. Perhaps the foremost rationale for regulating insurance is its intangible nature. In almost all jurisdictions, government is closely involved in the regulation of the business of insurance. To varying degrees in different states and nations, government deploys legislative and judicial branches to regulate solvency, underwriting practices and contract structure. It likewise often distinguishes the business of insurance from other businesses regarding the extent to which separate enterprises must behave competitively rather than cooperatively (Chandler, 1999).

As the United States Supreme Court has long recognized, insurance is business coupled with a public interest (Klein, 1995). Consumers invest substantial sums in insurance coverage in advance, but the value of the insurance lays in the future performance of the various contingent obligations. Because the interests protected are so important— including an individual’s future ability to provide for dependents in case of death or injury, to retire, to obtain necessary medical treatment, to replace damaged or destroyed property—regulation of the industry furthers public welfare.

Central to regulation of insurance is its classification as a public-interest business. According to Outreville (1998: 316), there are two important reasons for classifying insurance as a public-interest business which if viewed cursorily, can be traced to the intrinsic nature of the enterprise. The first is that insurance companies sell complex promises. The complexity of insurance and consumers’ inability to obtain and understand information about insurance commends the need for regulation. The second is the high potential for discrimination and abuse against customers. Consumers are ill-equipped to assess a company’s future solvency, to compare the coverage of various policies, or to evaluate a company’s claims service.

Theoretically, government regulation of insurance eliminates these problems. Regulation can ensure solvency and the insurer’s ability to pay claims in the future, standardize policy coverage, require minimum coverage, and require fair claims processing (Randall, 2007). The primary reason for regulating insurance thus goes beyond the traditional market failure reasons. The purpose is to guarantee that contracts entered into are valid and enforceable (Kimball 1969). As

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5 There is the International Association of Insurance Supervisors (IAIS) which meets every year and develops insurance core principles. See [www.iaisweb.org](http://www.iaisweb.org) with over 200 members from different jurisdictions world-wide who meet to design frameworks for regulating members.
Outreville (1998) further suggests, solvency regulation seeks to protect society against the risk that some insurance companies will become insolvent. Market regulation on the other hand is related to the economic efficiency of the insurance market. This is can be regarded as “prudential supervision” of the sector.

In general, there are a number of objectives of insurance regulation. Three of the key ones are the need to maintain efficient and stable insurance markets, ensure a fair and safe market for profitable insurance business transactions and provision of adequate protection for policyholders. Given the socio-economic context briefly described earlier, it is clear that these three factors are central the relevance of insurance regulation in the country.

REGULATION OF INSURANCE IN NIGERIA

The Context

Nigeria has a considerable high level of high rural population, a good proportion of which are either illiterate or with very low-levels of basic education. Years of misgovernance has straddled it with poor infrastructure and poverty (Osaghae 1998). There are risks of potential abuse, low level awareness, poor market penetration, low operating capital as well as low capacity for retention and acceptance of foreign risks (Daniels 2008). In this context, regulation is perhaps can be regarded as a sine qua non for the conduct of insurance business, and certainly so, in an age of regulation even if governments cannot (and should not) regulate everything (Scott 2008:7), the context of a developing country with poor infrastructure commends the need for a strong regulatory regime for insurance business considering its high-abuse potential mentioned earlier. The challenge of course is how to ensure the institution of an appropriate and adequate system of regulation.

The enactment of the Insurance Companies Act of 1961 marked the first direct measure taken by Government to establish and organise the insurance industry. By the provisions of the Act, the office of the Registrar of Insurance was created to supervise insurance practice. Other provisions of the Act included minimum capital requirement and other conditions for registration, monitoring and control of insurance operations generally. This was followed by a series of legislations which sought to further the cause of insurance regulation in the country.\(^6\) The first

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\(^6\) These include the Insurance Companies Regulations (1968), Decree No 59 of 1976, Insurance Companies Regulations (1977), Decree No 58 of 1991, Decree No 2 of 1997, and so on.
major attempt at regulating insurance in the country was the promulgation of the Nigerian Insurance Decree 1976.

Regulation of insurance in the period under review can be considered as part of two separate but complementary processes. One is the reinvigoration and redirection of the economy after years of limited access and participation in global economy. The second germane factor is the demand for public and corporate accountability which underpins the anti-corruption campaign that has been ongoing in the country during this period (Yusuf 2010: 110-114). Both derive from the political transition from almost three decades of authoritarian military rule which has fostered high-level of corruption and at some points, shut the country out of critical global economic development. Hence, it can be said that Nigeria’s anti-corruption reforms are seen to be fundamentally geared towards improving the economy and ensuring better service delivery to the people.

The second front, the accountability initiative is of particular relevance to this study. Barely six years into its post-independence had the military taken over governance in the country and held on to it for almost three decades. Successive military regimes continually proclaimed economic rectitude as a policy objective. Rather, corruption was institutionalised by the military hegemony which came to regard the country as ‘conquered territory’ and her vast resources as ‘spoils of war’ (Synoptic Overview Oputa Panel Report: 2-3) The various military regimes attained notoriety for corruption that was unprecedented in the country moving it rapidly from one of the richest nations to one of the poorest. With the advent of civil rule, the public opinion was firmly united on the critical need to combat the malaise of corruption in the country. Government initiatives in this direction include the establishment of the Independent Corrupt Practices and Other Related Offences Commission (ICPC), and the Economic and Financial Crimes Commission (EFCC), implementation of civil service, financial and banking reforms, and the institution of the Budget Monitoring and Price Intelligence Unit (BMPIU), otherwise known as the ‘Due Process Mechanism.’ The EFCC Act of 2004 specifically mandates the Commission to combat financial and economic crimes. The Commission is empowered to prevent, investigate and prosecute economic and financial crimes. It is also charged with the responsibility of enforcing the provisions of other laws and regulations relating to economic and financial crimes including money laundering, failed banks, and advance fee fraud (EFCC ACT 2008). It has in most recent times been actively involved in the prosecution of some key financial sector players.
(specifically bank directors and management) for sundry financial crimes thus constituting it also into a regulatory force of sorts in the financial sector.

**A Prescriptive Regime**

In his analysis of regulation and accountability, May identifies three regulatory regimes. Two of these, performance-based regulation, and system-based regulation are fairly emergent in the practice of regulatory governance, sometimes supplementing or supplanting the traditional prescriptive regulatory regime. The performance and system based regimes are essentially voluntary, professional and industry-led regulatory frameworks. This distinguishes them from the rules-led government agencies model of prescriptive regulation (May 2007).

It is fairly safe to assert that in Nigeria, despite political change from military to authoritarian rule, the prescriptive model continues to dominate the regulatory environment. The situation is the same from manufacture of foods and drugs, professional services like medical practice, water and sanitation, forestry, to transport and aviation. And so it is with insurance and other constituents of the financial sector.

Under its prescriptive model of regulation, virtually all aspects of insurance business practice— from company formation, operation to liquidation— are regulated in Nigeria. The impact and operation of performance-based and system-based regulation though existent, are still very much in gestation or infancy stages with minimal, if any, impact. In this circumstance, the work of the National Insurance Commission (NAICOM), a refurbished quango, established by the penultimate military administration in the country in 1997 is important.\(^7\)

The powers of NAICOM under the prevailing legislation for the industry in the country, the Insurance Act 2003 (Insurance Act) are clearly comprehensive. Section 86 of the Insurance Act provides that subject to the provisions of the Act, NAICOM shall be responsible for administration and enforcement of the provisions of the Insurance Act. Criteria and standards for registration, policy provision, rates, expenses limitations, valuation of assets and liabilities, investment funds, and the qualifications of sales representatives are set by NAICOM. To monitor insurance practitioners’ compliance with its rules, NAICOM adopts the international standards

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Nigerian Insurance Act 2003
core principles of insurance supervision which have been entrenched in the Insurance Act 2003. The Act also serves as the benchmark for the supervision and monitoring of intermediaries (brokers, agents and loss adjusters) who must renew on annual basis after supplying their annual returns and accounts for verification.

NAICOM has also been active in releasing annual insurance policy guidelines for the underwriters and intermediaries. The release of the guidelines is brought about by the dynamics of the environment and related to a continuous review of relevant regulatory tools which are consistent with the existing laws. This is also meant to strengthen the operational standard within the insurance industry and bring about improved transparency and accountability in operations. Some of the selected areas of the annual review include filing of annual returns and accounts; renewal of licence; quarterly returns; clients’ account, opportunism (fraud) and related malpractices; corporate governance; and compliance with anti-money laundering/combating financing terrorism activities laws.

NOTABLE CHANGES IN INSURANCE REGULATORY ENVIRONMENT FROM 1999 TO 2009

Recapitalisation

In terms of regulatory policy, the recapitalisation program has had the most profound effect on the industry to date. In the post-authoritarian period under review, government turned its attention to the financial sector and introduced a recapitalisation program. The move was directed in part at flushing out operators with weak or dubious financial bases from the financial sector and to galvanize financial institutions into assuming the challenge of transforming the nation into one of the top ten world economies within the turn of a decade. The first major recapitalisation process was introduced by the Insurance Act 2003. Section 9 of the Insurance Act raised minimum capital requirements by as much as 650%. This recapitalisation exercise

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8 This is part of the so-called ‘Vision 2010’ Program.
which ended in February 2004 however still left over 107 insurance as well as reinsurance operators in the market and was perceived as not effectively achieving the aim of drastically reducing the number of players in the industry (Fatula 2007:129).

With the results of the 2003 recapitalisation making rather dismal impact on the industry and the drastic recapitalisation requirements later imposed on the banking industry, it was not surprising that even higher capital requirements would be introduced to the insurance sector sometime down the line. Indeed, Section 9 (4) of the Insurance Act provides that NAICOM may increase the amount of minimum capital requirement ‘from time to time’. What was unsettling for the operators was the timing and quantum of increase in the minimum capital requirements. The then Minister of Finance announced a new minimum capital regime in September 2005 which was to be complied with by the end of February 2007. While previous the Insurance Act 2003 only required new capital of less than N500 million (about $4m), which, as stated earlier, was raised easily by most operators, the 2005 recapitalisation directive required a minimum of N2 billion (about $15m) for life operations and N3 billion (about $23m) for non-life business. With the previous low capital requirement, the scope of operations of many of the companies was severely limited. Options for increasing the capital base like the capital market were not explored. The 2005 recapitalization changed the landscape considerably as many companies were forced to merge in compliance with the follow-up directive of NAICOM that the requirements were only to be met through mergers or acquisitions.

Following on this new requirement, many insurance executives took the view that the industry erred in not challenging the provisions of Section 9(4) of the Insurance Act. The feeling is that the industry now operates on the whims of the government. It was contended that consultation on the increase was minimal, and that the increase was ill-timed given that the industry was still recovering from the former requirements imposed in 2003. The table below shows the old and new capital base with the percentage increases:

**Table I - Old and New Capital Requirements**

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<td>Life Insurance</td>
<td>N150 million</td>
<td>N2 billion</td>
<td>1,233.0%</td>
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<td>N200 million</td>
<td>N3 billion</td>
<td>1,400.0%</td>
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<tr>
<td>General Insurance</td>
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<tr>
<td>Composite</td>
<td>N350 million</td>
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<tr>
<td>Reinsurance</td>
<td>N350 million</td>
<td>N10 billion</td>
<td>2,757.0%</td>
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REFERENCES


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