Regulation of e-distribution Channel

Insurance Context

Introduction

E-commerce, which refers to electronic buying and selling of goods and services over a public network, is emerging as the most important distribution tool in recent times. In fact, it has the potential of altering the very way business is conducted.

The potential of e-commerce is mind-boggling. It is expected that worldwide online sale would exceed a trillion dollar within a year or two. It is also estimated that by the year 2003, there would be in excess of 500 million Internet users in the world. The rate at which this technology is being embraced can be gauged from the fact that Internet has taken only 4 years to reach 50 million mark, worldwide, where as the same magic figure took 38 years for Radio, 13 for TV and 16 for PC.

E-Commerce in Insurance

Insurers are not far behind in exploiting the potential of electronic commerce. Forrester research estimates that by the year 2001, global on-line insurance sale would exceed US $ 2.1 Billion. A visit to any global insurance company's website would reveal as to how seriously insurers have begun to use worldwide web to offer services to prospects and customers. Then there are web brokers like Insweb.com, Quotessmith. Com, quicken.com etc. offering quotation and simple products in life and non-life segments.

In its 1996 research paper titled 'Global insurance in the 21st century', International Intelligence unit, New York has compiled a survey done on 3500 senior executives in 9 countries over North America, Europe, Australia, New Zealand and Japan. According to the paper, the respondents believe that by the beginning of the millennium, over 40% consumers would prefer e-channel to human channel to purchase less complex instruments. The insurers have broad agreement on following services desired by customers online

- Receive quotation over web (70% concurrence)
- Pay premium on line using secured lines (65%)
- Obtain product information (63%)
- Comparison shop across providers (61%)
- Query update policy information (58%)
- Link to human insurance financial service experts (55%)
- Query claim status (54%)

Indian Context

In the Indian context, importance of e-business is significant for insurers. In order to compete against the incumbents, given their massive geographical reach, brick and mortar infrastructure and market presence, e-distribution would be a critical supplementary channel for new players. GIC and LIC would definitely not be far behind. The current rapid pace of computerization would logically lead to empowering the ultimate consumer through offering value-added services over the internet.

However, the legal framework and infrastructural availability would be the decisive factor for making full use of the power of e-business. Insurance contracts have their own specialty and follow principle of indemnity and utmost good faith placing the onus of disclosure of material fact on the proposer. Unlike on-line retailing of consumer goods, e-distribution of insurance is complex due to the procedural rigours and application of various statutes such as Contracts Act, Insurance Act etc.

In this paper we seek to understand the concerns relating to e-distribution of insurance products. As technology would be the enabler to sound regulation and to instill confidence among online buyers, technological imperatives would be the focus. For the sake of comprehensiveness, the cyber laws and international practices are also touched upon.

Exploiting the web

Industry, and companies within an industry, embrace Information technology to different extent based on their outlook and comfort. In the context of insurance industry, this could cover

- *Brochureware-* Information about company, its offerings and services are offered to prospects over the web
- *Enquiry over web-* This would score higher in terms of interactivity than brochureware and could include policy and claim enquiry facility for the customers and answer to the queries from prospects. Linkage to dedicated call centre could be possible over the web
- *Transaction using dedicated lines-* This has been the most widely exploited part of IT where field staff and agents of insurers solicit business and transfer data to the insurance company over the public or private network for further processing.
- *Sale of product over the web-* This would include facility to place order and buy insurance over the web. Concepts like shopping cart, on-line payment using innovative means add to the shopping experience. Sale of product is emerging as the most important component of e-commerce and promises to offer great value in terms of cost reduction, rapid access to markets, superior service and most importantly, customer convenience.
- *Sale of customized product over the web-* Taking user empowerment a step further, this could encourage buyers to configure the products through mix and match. Assistance based on customer profile and demographics would add value to the service. In the foreseeable future, it is believed, success of e-strategy of insurers would hinge on their ability to empower the customer.

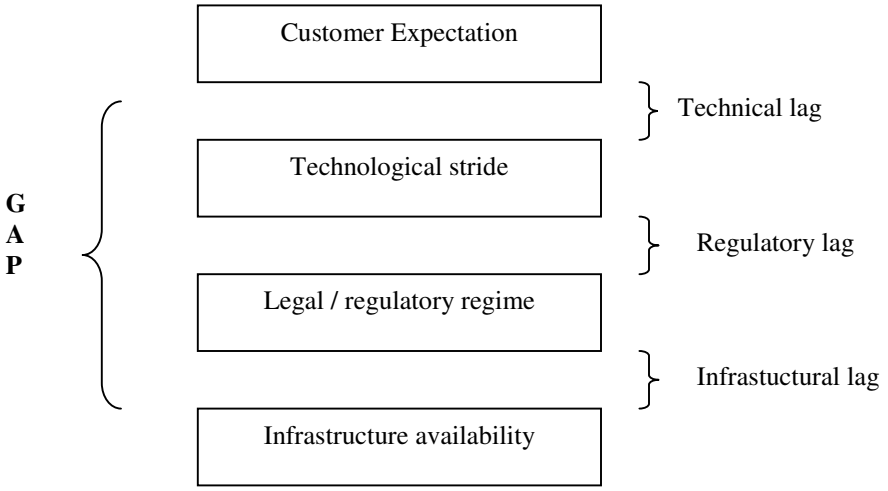
At another level, the insurers could differ in their level of comfort integration of web with their host system. At the extreme end of automation, an online request for quote from a proposer could trigger off a series of actions in the insurers host system leading to issue of policy and intimation of policy number to the customer on-line. Specialized software would collect necessary underwriting information, assess the risk and quote rates, payment mechanism would be activated, and policy would be generated, ready to be

dispatched. In most cases, however, there would be elements of manual intervention, once quotation is provided on line. These interventions could be the need for physical signature on the proposal form, review of proposal by underwriter before confirmation of transaction on the host system etc.

The practice adopted in a market would closely follow the available IT Infrastructure and the legal / regulatory framework in existence. As of now, even in the advanced markets, simple products in the personal lines and low-end commercial lines are being sold most often over the web. It is only when the more complex products are sought to be sold on line that the insurers would experience the real challenge within the legal, technical, regulatory and marketing framework in place.

The Gap

If we were to look carefully, there would always exist a gap between what is desired and what is deliverable.



want faster access than is possible with existing bandwidth, more convenience than is possible technically and higher protection against fraud in e-commerce than ever existed in paper form.

The legal system should be expected to assimilate the technological stride in a cautious, conservative and reactive manner.

Lack of infrastructure such as reliable network, sophisticated electronic payment systems and trained manpower could lead to compromise in service levels.

Issues

E-distribution brings, in its wake, following issues to the fore. Regulation of e-distribution channel would require consideration of these issues. It may be observed that many of the issues have technological solutions in place. However, constant innovation is

underway to keep ahead of those trying to undermine the power of the e-business. This is the cost for winning and retaining the faith of on-line shoppers. In addition, even the legal system would also depend on the technological means, particularly with respect to establishing authenticity of electronic documents

1. Security over the web

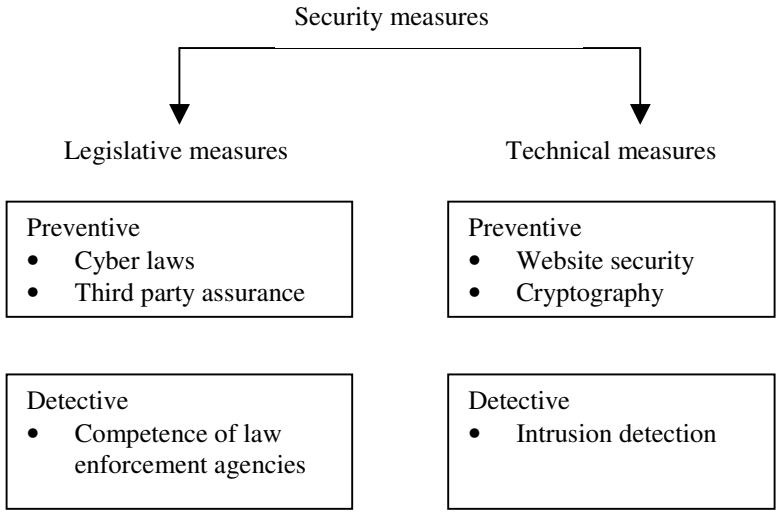
Issue of security is paramount in e-commerce. A paper based trading is firmly ingrained in our psyche as paper based order cannot be modified easily without leaving trace. Electronic documents can however, be modified without leaving any trace. It is therefore necessary that manual and technical controls are exercised to make e-commerce a reliable means of doing business and regulatory and commercial practices encourage secure way of doing business.

Internationally, there appears to be concern about buying online. A recent survey indicated that of the total online accessors, only 43% actually buy online! A study by Arthur D. Little and Giga Group indicated that the biggest barriers to adoption of e-commerce were security and privacy concerns.

In India also, as in other nations, there is great reluctance to part with credit card number online. It is understood that during online purchase, payment using VPP and fax is preferred to authorizing payment with credit card number.

Security of transaction covers not only transaction details during the transit but also the subsequent utilization and storage of information. In the context of insurance, the security concerns are paramount, as insurers are privy to substantial information as regards, financial status, demography, health details etc. of the proposer.

Security concerns are addressed through legislative and technical measures. These are again divided into preventive and detective measures- preventive is believed to be more effective.



The security issue is made of several strands and each one is important to usher in a viable, secure and reliable e-distribution.

- *Confidentiality*- This refers to protection of information from unauthorized users and hackers during transmission and storage.
- *Integrity*- The information should appear to the recipient in exactly the same form as was dispatched by originator. Any modification en-route should generate an alert. Further, information should not be replayable using the authorization features of the original message.
- *Availability*- Information should be stored and available whenever required.
- *Authenticity*- Reliable identification of the originator and recipient of data need to be established to be reasonably sure and to verify, if required, the source of the message.
- *Non-repudiation*- This refers to binding the messages and acknowledgement with the originator so that, at a later date, they are not able to deny it.
- *Auditability*- Auditing of data to ensure integrity and confidentiality requirement

Security solutions

The above requirements are met through cryptographic technique which involves encryption of data before it is transmitted and then decryption at the receiver end using secret keys.

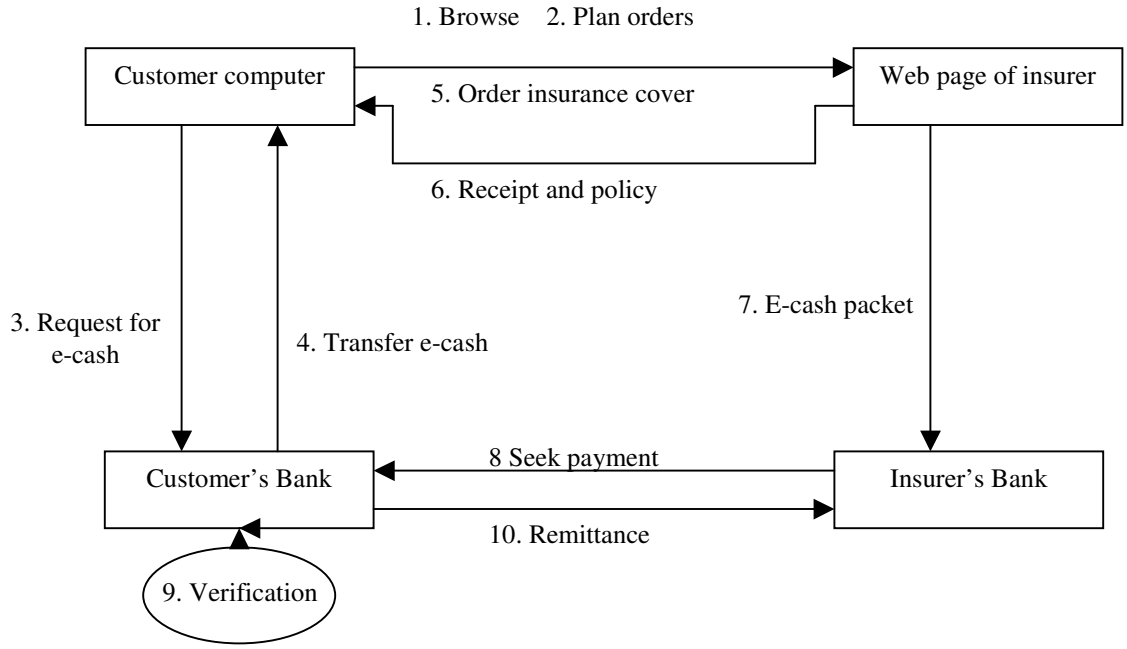
Cryptographic systems are either symmetric or asymmetric.

2. Payment over web

One of the concerns would be electronic payment. Under the existing Insurance Act, Sec 64 VB, cash before cover is the rule. How would the statute evolve to take care of requirement in case of e-distribution? In case of on-line payment instruction, will the transaction be settled fairly and efficiently and in case of installment payments, how would the installment be paid?

Technology exists to make payment on-line, but the infrastructure for this is not in place with most financial intermediaries as of now. Given reluctance to even part with credit card number over the web on the part of users, innovative means need to be adopted such as automatic clearance house etc. to make e-commerce a reality in insurance industry in India.

One of the technical possibilities is discussed below
Electronic cash over internet- E-cash, is one of the method of paying on-line



Here, after finalizing buying plans, the customer requests his banks for e-cash in encrypted form. The bank transfers e-cash, after verification which is stored in the hard disk of the user into the "electronic wallet". Th customer may place orders and transfer the e-cash to the insurer. The insurer, through its bankers, would seek remittance from the customer's bank. Based on customer's public key and the e-cash pack, the customer's bank remits the fund. In case customer misplaces e-cash, he has to provide full details such as serial number etc. to the bank to refund cash.

In this entire transaction, security is provided through encryption, digital signature and password.

It is clear that financial intermediaries, such as banks and credit card companies need to provide the necessary infrastructure to make on-line transaction possible in a secured manner. In the developed world there are host of financial and technical intermediaries. A partial list is

- Checkfree corporation- Bill payment services and on line disbursement
- Commercenet- Consortium of ISP's and online sale organizations
- Cybercash- Internet payment service for business to consumer electronic wallet and business to business fund transfer
- Digicash- Provides payment mechanism using e-cash
- First visual – Provides virtualPIN, using which customer can buy on-line but recovery from credit card is made only after e-mail confirmation from the customer.

3. Procedural rigour

Use of electronic documents, messaging system and electronic transaction is a paradigm shift. Not only the trading partners should be comfortable in placing its trust on e-transmission and storage, but the legal infrastructure need to evolve to provide for admissibility of electronic evidence. IT bill 1999 addresses some of these issues.

The paper-based system is also liable to be misused, as we witness sometimes around us. However, a procedural rigour and protocol that has been built around it lends it an authenticity. Writing, signature (legal and ritualistic symbol of finality, assent and authenticity) and notarizing lends an aura to a paper based document.

In the USA, notarizing function for non-repudiation is sought to be carried out through Trusted Third Parties (TTP's) service. TTP holds the public key of all users and users hold the public keys of TTP's they are connected to. In case of dispute, TTP would certify the origin of the message. Indian IT Bill is silent on TTP.

Similar to a protocol in the paper world (for example, shipping documents), there is a need for *interchange agreement* in the EDI world to supplement the cyber laws in areas where the legal position is not clear. United Nations has adopted a Model Interchange Agreement for International commercial use of EDI and is applicable to interchange of data. This model underlines the need for uniformity of agreements and deals with roles, responsibility of trading partners while transmitting, receiving and storing electronic messages. In particular, it lays down communication message standard (UN / EDIFACT) system operations, changes in system, security procedures and record storage. Receipt, acknowledgement, validation, enforcement, confidentiality and liability are also delineated in the model.

4. Enforceability of clickthrough contract over the web

A contract is established when an offer is communicated by the offeror and its acceptance is received from the acceptor. Offer may be made over the Internet and accepted using the e-mail or by clicking the "I Agree" button, after reading the terms and conditions.

The issue relates to the eligibility and authority of the party entering into contract. Is a contract entered into when the visitor clicks "I Agree" button, even if he may be a minor? What would be the legal position, if the customer wishes to buy a certain insurance plan and clicks "I Agree" button, but due to electronic hiccup, different plan is underwritten and despatched.

The implication of these in the insurance contract would be felt. For example, a person may seek insurance cover for a certain amount and effects payment on line and then clicks "I Agree". Is the risk transferred to the insurer? Would he be indemnified, if the life or property is lost before policy document reaches him and has chance to review the policy.

In the USA, Article 2B of Uniform Commercial Code (under review by the National Conference of Commissioners on Uniform State Laws- NCCUS) is seeking to bring

sanity in this maze of confusion as regards legal electronic contract, albeit in the context of software sale- The considerations are well applicable for service industry too.

As regards " I Agree" Article provides for concept of "Manifestation of Assent" by which necessary steps are taken to let customer realize that contract is being made. If a customer has reasons to know that a particular action will form an agreement, then he is bound by the action. An example would be

" BY CLICKING ON THE 'I AGREE' BUTTON, YOU AGREE TO PURCHASE THE POLICY AT THE PRICE AND TERMS QUOTED ABOVE"

The Article says that restrictions and terms and conditions should be made known before order is placed and payment effected, otherwise refund must be provided. The sentiments are similar under FTC regulations and European Distance Contracts Directive, both under consideration in the USA.

Article 2B also encourages the vendor to provide the customers a reasonable chance to check orders and make necessary corrections before placing order.

The implication for insurance contract would be (insurance is not covered under Article 2B) that if fine prints are not displayed beforehand, the customer may seek refund and cost of return, if contract terms were not acceptable once reviewed

5. Privacy

Insurance contracts generally require disclosure of confidential information by the proposer who would not like this to be used by the insurer or their agents for any other purpose. However, given the fact that many on-line traders have been known to be selling customer information, customers may be wary of sharing personal details unless assured of confidentiality. Indian IT Bill is silent on this aspect.

Government and trade bodies in the USA are trying to come up with solutions to protect the privacy of the information provided by the visitors on the website. In particular, Consumer Interest Privacy Protection Act, 1997 prohibits disclosure of personally identified information without prior informed consent and users are allowed to change their mind and revoke consent. Data Privacy Act 1997 provides for industry working group to establish voluntary guidelines for

- Limiting the collection and use of personal information for commercial marketing
- Distribution of unsolicited commercial mails
- Prohibition of use of health and medical information without prior consent of the person.

A new initiative is privacy branding. Entrust, Cybertrust and TRUSTe etc. offer privacy branding in the USA.

TRUSTe, founded by Electronic Frontiers Foundation and CommerceNet has created a branding programme that provides privacy labeling system to inform online users about

the end use of information to help them make informed decision. The trust marks created by TRUSTe are

- *No exchange*- If the site bears this mark, anonymity of user is assured. No personal data is being collected using 'cookies' etc
- *1 to 1 exchange*- Organization would hold the information for dealing with the visitor on one to one basis but would not be shared this information with anybody else.
- *3rd party exchange*- Site may share personal information collected from the visitor or pass it on commercially.

In the context of insurance, customer information may be passed on to the medical practitioners of the insurers, claim assessors, reinsurers etc. It needs to be reviewed, if the insurers should disclose this explicitly on their web page, as the information may be going out of their sphere of influence.

6. Fraud

In the USA and also European Union, Internet fraud is emerging as a concern. Taking advantage of the venerability of many websites due to inadequate security measures as well as poor regulatory framework, fraudsters have struck more than once. At least in one example, a fraud involving insurance business was perpetrated when Finance advisors of terminally ill patients were sold some 15000 policies, siphoning off US $ 100 million. Now SEC and FTC in the USA and FSA in UK are trying to come up with measures to combat cyber crime.

We, in India, are beginning to experience the e-commerce revolution and it would be worthwhile making efforts to minimize the fraud and win confidence of the consumers. Preventive action, such as security of websites and databases from hackers and detective actions such as installation of detective tools by the providers are necessary to start with.

7. Consumer protection and redressal

A guideline has been issued by Organization for Economic co-operation and Development (OECD) and Consumer International are seeking for consumers the same level of protection over e-commerce as is available in any other method of shopping. Consumer International has issued a guideline seeking

- Privacy and security of personal data
- Security of payment systems
- Protection against aggressive advertisement and junk e-mails
- Quality, range and accuracy of promotional information, especially full disclosure as regards charges, taxes, delivery mechanism, customer's liability, terms and conditions for use etc.
- Redressal mechanism for resolution of disputes

In Indian context also, a redressal mechanism need to be explored to handle deficiency in service and other disputes as regards e-commerce. Internationally, the emphasis is on

self-regulation with US administration also favouring it as per the e-commerce framework issued by the White House.

Conclusion

Electronic commerce and distribution is a nascent area even in the developed west. The regulations are in its incipiency and only time would tell if the self-regulation in practice is sufficient or needs to be supplemented with the authority of the state. A transparent and predictable legal environment recognizing the uniqueness of Internet as a media is still emerging. The matter is compounded enormously as the Internet transcends national boundary in its reach and brings to the fore issues such as tariff regime, jurisdiction, Intellectual property rights etc. In order to sustain this revolution, infrastructure- physical, legal as well as financial, need to be strengthened, without being oblivious to the new challenges and risks it poses before us.

Regulation of e-distribution of insurance requires a careful and cautious approach. It requires full utilisation of the available technology to lay down the procedures which will instill confidence in the minds of the consumers about the security and reliability of the system. The road ahead is e-xciting !