



Intervention of Reinsurance in Claims Payment: A Review of Nigeria Non-Life Insurance Industry to Educate Nigerian Insuring Public

¹ Olowoyo, Banji Jacob · ²Ariyo, Clement Olugbenga & ³Oluwaleye, Taiwo Olarinre &

¹Department of Accounting, Banking and Finance, Oduduwa University, Ipetumodu, Ile-Ife, Nigeria.

²Department of Finance (Insurance Unit), Ekiti State University, Ado Ekiti, Nigeria

³Department of Finance (Insurance Unit), Ekiti State University, Ado Ekiti, Nigeria

Emails: ¹taiwo.oluwaleye@eksu.edu.ng; ²banjiolowoyo@gmail.com; ³olugbenga.ariyo@eksu.edu.ng

¹Phone: + 2348036544424

ABSTRACT

Many Nigerian insuring public are always skeptical about the operation of insurance, in view of the huge value of the property they presents and the premium charged, many thought that operation of insurance is a mystery. This research work therefore made use of reinsurance in a lucid form to explain the spread of risk the insured presents and how reinsurance provides a shock absorber in time of claims payment. Secondary data covering the period of 1986 to 2018 of Nigerian Insurance Industry activities, specifically reinsurance and claims of non-life insurance business were used and ordinal regression model was used to analyze predictive behaviors of reinsurance and claims that cushion the effects of problems that insuring publics envisaged on claims payment. From the results of the statistical analysis, the essence of reinsurance in providing confidence to direct insurer has been vindicated. It is recommended that The Nigerian Insurance Industry should always inform the insuring public of the supportive activities of reinsurance that aids the spread of the risk they cover to the entire world and Government should rely on the support of reinsurance in their policy on insurance.

Keywords: Reinsurance Concept, Mystery Belief, Insuring Public.

Journal Reference Format:

Olowoyo, B.J., Ariyo, C.O. & Oluwaleye, T.O. (2022): Intervention of Reinsurance in Claims Payment: A Review of Nigeria Non-Life Insurance Industry to Educate Nigerian Insuring Public. *Humanities, Management, Arts, Education & the Social Sciences Journal*. Vol. 10. No. 3, Pp 77-86. [dx.doi.org/10.22624/AIMS/HUMANITIES/V10N3P6](https://doi.org/10.22624/AIMS/HUMANITIES/V10N3P6)
Available online at www.isteams.net/humanitiesjournal

1. INTRODUCTION

In marketing of insurance products, by direct insurer to the insuring public, the insurer hardly mentioned to insuring public how their risks will be effectively insured or covered. Many policy holders are not convinced that the premium they paid for huge value of their properties will be enough to provide compensation if there are losses. They therefore see operation of insurance as a mystery and many are skeptical at insuring their properties in Nigeria. For thorough understanding, the relationship between the sum insured, the value of the property, and the premium charged, the amount paid for transferring risk by the insured to insurer will be made clear.



In the process, the logical insurance operation that allays fear or cushions the effect of payment of claims when it happens, which in the insurance parlance is termed re-insurance will be discussed lucidly. Re-insurance is the bedrock for the operation of insurance. The relationship between direct insurer and reinsurance is an arrangement that helps the spread of risks. Direct insurers are insurance companies that accept risks from insuring public, when they accept risks, they also need a cover to reduce the risks they accepts. This cover is provided by Reinsurance Company, who will rateably share the risks accepted by direct insurance in an agreed ratio (Igbal and Reman, 2014).

The relationship is highly expedient because the direct insurer, based increase in its underwriting capacity on reinsurance (Acharya et al, 2010). Risk management approach varies from one insurance company to another, in line with the businesses they transacts. Mikes (2011) remarked that approach of individual insurance can be revealed by their financial transaction. Tufano and Berger (2001) referred to the importance of financial and non-financial risk as a right approach to management of risk. Arena, Amabodi and Azzone (2010) said that some organization use to police risk management to make sure that risk management policies are strictly followed. Power, Ashby, and Palermo, (2013) referred that functional management can help the organization to know external environment and its associated risks.

Froot (2007) remarked that one of the ways by which insurers can manage risk is by diversifying portfolios of debt securities and by trading credit risk derivative instruments. Cummis, Phillips, & Smith (2001) opined that derivatives can be used to manage risk. Staking and Babbel (1995) assert that one of the management techniques an insurer used to manage its financial risk exposure such as interest rate risk is variability in value, which is being borne by interest bearing assets, such as loan or bond. Mocklow, Decaro, & McKenna (2002) stress that insurers can manage underwriting risk through innovative financial instrument such as catastrophe bonds and options. Culp (2002) mentions that reinsurance is the most important tool for managing insurance risk so as to optimize performance.

This research is bordered on how the insuring public can be convinced on the operation of insurance and how to create trust or more trust in insurance. This is done by establishing relationship between reinsurance and claims payment in Nigerian insurance industry. In order to throw more light into the activities to repose the confidence of insuring public on insurance contract.

2. LITERATURE REVIEW

Reasons why insurance companies need to manage the risk that are entrusted in their hands. Meulbrock (2002) opined that insurance companies need to manage risk entrusted to their hands in order to enhance value maximization for their corporate goals, value creation and uncertainty that are associated with the business. Leaucier (2007) said management of risk helps in securing financial flexibility that support growth. Nacco (2006) management of risk by insurance helps insurance companies to take strategic decisions, such as expansion of their businesses. Doherty (2000) emphasized that management of risk received is a fundamental concept to the success of insurance companies. Smithson and Welford (1989) applaud the various way of identifying risks and the use of various instruments to tackle them in which reinsurance by insurance can be referred to as one of them.



Skipper and Kwon (2007) inferred that management of risk will help to reduce risk exposure in a business concern such as insurance business. Santomero and Babbel (1997) remarked that the risks a firm assume must be managed efficiently. McDonnell (2002) refers to financial loss warranties as one of the factors that is affecting the contract of reinsurance. In non-life business insurance, the management of risk can be done in two main ways (Etti, 2004). The first, is through underwriting process, this involves the assessment of risk that they accept by applying insurance principles such as, utmost good faith, insurable interest, proximate cause, indemnity, subrogation, contribution and reinsurance. When this is done the risk is accepted at market value as at the time of accepting it. The market value signifies the sum insured which is a maximum liability of the insurer to the insured in the event of total loss.

If the losses are total, it cannot be affected by interest rates risk, exchange rate risk and inflation risk, this financial risks factors will affect the liability of the insurer to the insured if the loss is partial. With partial loss the insurer needs to take into account the effects of financial risk factors in the management of risk as the second approach. By the use of underwriting technique, an insurance firm can manage risk through reinsurance. This is a way of sharing the risk it's accepted with other contemporary insurers or ceding i.e., transfer certain percentage of the risks it accepted to a registered reinsurance, in form of a treaty (contractual agreement). Reinsurance alleviates volatility in financial statements of an insurance company and enhance sustainability of shoulder value on their investment. This is as a result of the insurer's expertise knowledge in the field of risk management.

Mayers and Smith (1990) inferred that re-insurance expertise is providing information and advice to direct insurance companies on pricing and claims adjustment services in various classes of insurance. Pitselis (2008) says that reinsurance is a tool in the hand of insurance firm which can be used to reduce or remove losses. SWIS (2004) commends the important service reinsurance renders to direct insurance in the assessment of risk. Radler, A T (2022) refer to direct insurer (insurance companies) as a client of re-insurers. This is as a result of re-insurers' technical knowledge of how risk can be spread and hedge all over the world. Guerdouh, D, Khelfallah, N., & Vives, J. (2022) emphasized that direct insurers are in the business to protect the insured. To do this effectively if claims eventuate, they must have had contractual agreement with re-insurer company that will reimburse it at the instance of settling claims.

Colaneri, K, Eisenburg, J, & Salterini, B. (2022): They stated that insurance companies as a business concern is established to boost its business to satisfy the owners (shareholders). He went further to say that one of the strategies of optimization of insurance companies is the strategy of reinsurance because it provides the normal distribution of terminal surplus that enhance increase in business participation and ameliorate payment of claims. Avanzi, B, Lau, H, & Steffensen, M. (2022): It was stated that risk exposure can be controlled downwards by the use of re-insurance, although in trade-off manner that is the payment of re-insurance premium to ceded risks. This single out on the part of direct insurance is done to enhance sustainability and stability in insurance business transactions. Zhang, J, Wang, J, Chen, S, Tang, S, & Zhao, W. (2022): They emphasized that reinsurance companies through their dealings with direct insurers, provide statistical records that helps the stake holders in risk management such as government, research institute, disaster management to lay their hands on database that they can use to proffer solution to disaster and economic problems.



Liu, L, & Yan, R (2022): They remarked the importance of collaboration of the insurance companies and reinsurance in tackling aggregated claims. Pimentel, R.C. (2022): The persistence earning and market position of insurance companies can be realized through the support of reinsurance, when they share their risks to stabilize claim payment. Vojinovic, Z, Milutinovic, S, Sertic, D, & Lekovic, B. (2022) stated that the factors that can lead to loss of profit as loss ratio, leverage and earning volatility. Also, firm size, the risk in question, age of, and level of capitalization are factors that underline the degree leading capacity from direct insurer to reinsurance. Garayeta, A, J Inaki De La, P, & Trigo, E. (2022): They mentioned that reinsurance is statutory and is one of the factors that is relevant in the assessment of insurance company solvency. Jarzabkowski, P, Spee, A. P., & Smets M. (2013) looked at the scientific approach by which insurance managers are using reinsurance to appraise the economic well-being of their companies.

2.1 Theoretical Review

Theories are set of ideas or principles on which an activity is based. Therefore, the basis for risk management in a corporate institution will be made vivid by the following related theories.

Stakeholder Theory

Freeman, (1984) made use of stakeholder theory to explain the interest of owners of business in line with corporate policy. He emphasized that corporate management of an organization, should consider the interest of the stakeholders. He gave examples of stakeholders as insurance firm, shareholders, policy holders, employee, debtors government etc.

Reputation Risk and Reputation Risk Management Theory

Various reasons are attached to why reputation risk needs to be managed and the reasons range from economic to strategic importance. It can be linked with the society's expectation from the firm (Scott and Wcolshman, 2005). It results from the strategic approach of presenting the firms tangible benefits such as: premium prices for products reduction in the cost of factors of production such as labour and capital, enhancing the loyalty of the employee and is being used for decision making by the managers (Little and Little 2000). Reputation can be seen as an approach by which a firm can manage the risk associated with quality of product and services (Scheizer and Wijnberg, 1999). With good reputation a firm can take good decisions and also withstand shock of corporate image risk (Fombrum and Van-riel, 1997). The above cited authorities are proof that outcome of identifying reputation risks and proffering appropriate risk management approach may edify a firm through financial performance, quality of management, social and environmental responsibility performance, employee quality and the quality of goods and services provided.

3. RESEARCH METHOD

This study used time series, covering the activities of Nigerian Insurance Industry between 1986 and 2018, with macro-economic data such as summary of reinsurance cession and claim in the period. The data for the study were sourced from CBN statistical Bulletin, and NIA statistical reports of various edition from 1986-2018.



TABLE 1:

To verify the shock provided by reinsurance on claims paid.

Regression Statistics

| | |
|-------------------|--------|
| | 0.4728 |
| Multiple R | 41733 |
| | 0.2235 |
| R Square | 79305 |
| | 0.1976 |
| Adjusted R Square | 98615 |
| | 452291 |
| Standard Error | 87.54 |
| Observations | 32 |

SOURCE:AUTHOR'S
 COMPUTATION 2023

ANOVA

| | <i>df</i> | <i>SS</i> | <i>MS</i> | <i>F</i> | <i>Significance F</i> |
|------------|-----------|-----------|-----------|----------|-----------------------|
| Regression | 1 | 1.77E+16 | 1.77E+16 | 8.638846 | 0.006277 |
| Residual | 30 | 6.14E+15 | 2.05E+15 | | |
| Total | 31 | 7.9E+16 | | | |

| | <i>Coefficients</i> | <i>Standard Error</i> | <i>t Stat</i> | <i>P-value</i> | <i>Lower 95%</i> | <i>Upper 95%</i> | <i>Lower 95.0%</i> | <i>Upper 95.0%</i> |
|--------------|---------------------|-----------------------|---------------|----------------|------------------|------------------|--------------------|--------------------|
| Intercept | 603812.4862 | 952830.0 | 6.337043 | 5.46E-07 | 40921.863 | 7984.0634 | 40921.863 | 7984.0634 |
| RE-INSURANCE | 0.002454246 | 0.000835 | 2.93919 | 0.006277 | 0.00416 | 0.00075 | 0.00416 | 0.00075 |

SOURCE:

Authors computation 2019

The *Model Summary* table gives the R, R-square and adjusted-R values, which are measures of predictability of the model, using all the predictors simultaneously R = .473, and the adjusted R-Square value is .197, meaning that 20% of changes in the claims paid can be attributed to re-insurance. The *Coefficients* table supplies the significance coefficient of each of the factors considered in the model. From this table the *Beta* coefficient gives a rank value of significance from factor to the other. Also, the reported p-value is 0.006277 which is less than the significance value (0.05). We can therefore reject the null hypothesis and conclude that re-insurance provided shock on claims paid.



4. DISCUSSION

From the results of the statistical analysis, the essence of reinsurance in providing confidence to direct insurer has been vindicated. Some insuring public in Nigeria that were skeptical about the activities of insurance, that look like a magic wand can now alleviate their doubt and breathe a sigh of relief over insurance, by taking a step of good faith and take property insurance cover to protect their properties.

5. RECOMMENDATION:

This study analyzed the supportive relationship offered by reinsurance to direct insurance 1986-2018. Reinsurance in the risk provided by the direct insurance and offer shock to insurance claims. This therefore provided stability in insurance market in Nigeria. In view of the findings of the study, the following recommendations are made to the insurance regulation authority in Nigeria.

1. The Nigerian Insurance Industry should always inform the insuring public of the supportive activities of reinsurance that aids the spread of the risk they cover to the entire world.
2. Government should rely on the support of reinsurance in their policy on insurance, such as local content policy on insurance, so that they can prevent the huge amount of premium that are usually lost to other countries, most especially in oil and energy insurance.



APPENDIX 1
SUMMARY OF RE-INSURANCE CESSION (1986-2017) IN MILLIONS

| YEAR | RE-INSURANCE | CLAIMS PAID AND ADMINISTRATIVE EXPENSES |
|------|----------------|---|
| 1986 | 479,965,228 | 577,380 |
| 1987 | 826,360,490 | 685,123 |
| 1988 | 947,163,465 | 957,774 |
| 1989 | 1,391,966,881 | 1,771,515 |
| 1990 | 2,122,923,442 | 5,975,734 |
| 1991 | 2,112,358,349 | 3,798,880 |
| 1992 | 3,489,932,977 | 5,365,060 |
| 1993 | 6,091,577,392 | 5,975,734 |
| 1994 | 7,578,131,953 | 3,798,800 |
| 1995 | 16,453,387,204 | 5,365,060 |
| 1996 | 19,204,099,829 | 5,916,139 |
| 1997 | 18,143,488,220 | 6,499,399 |
| 1998 | 16,276,537,991 | 7,174,281 |
| 1999 | 16,772,221,019 | 8,013,670 |
| 2000 | 22,517,144,479 | 8,379,630 |
| 2001 | 26,702,467,340 | 9,587,800 |
| 2002 | 36,231,624,597 | 12,195,580 |
| 2003 | 45,814,180 | 24,751,291 |
| 2004 | 52,213,017 | 30,671,371 |
| 2005 | 63,383,777 | 33,806,449 |
| 2006 | 69,546,442 | 119,762,269 |
| 2007 | 84,836,396 | 123,566,488 |
| 2008 | 128,931,883 | 126,182,084 |
| 2009 | 144,660,899 | 64,174,271 |
| 2010 | 145,969,093 | 65,727,348 |
| 2011 | 163,193,857 | 71,488,823 |
| 2012 | 182,372,874 | 94,346,216 |
| 2013 | 187,419,363 | 107,236,506 |
| 2014 | 184,967,767 | 103,186,363 |
| 2015 | 178,487,081 | 108,479,773 |
| 2016 | 189,279,623 | 139,151,399 |
| 2017 | 200,389,635 | 140,161,567 |



REFERENCES

1. Arena, M. M., Amaboldi, and Azzone, G. (2010). The organization dynamics of enterprise risk management. *Accounting Organizations and Society*. 35 (7), 659-675.
2. Acharya, Viral. V. Pedersen, Lasse Heje and Philipppo. (2010). Measuring Management Systematic Risk AFA 2011 Denver Meetings Paper. SSRN: <https://dx.doi.org/10.2139/ssrn.1573171>.
3. Avanzi, B., Lau, H., & Steffensen, M. (2022). *Optimal reinsurance under terminal value constraints*. Ithaca: Cornell University Library, arXiv.org. Retrieved from <https://www.proquest.com/working-papers/optimal-reinsurance-under-terminal-value/docview/2645690129/se-2>.
4. Cornell. B, and Sharpiro, A. C. (1987). Corporate Stakeholders and Corporate Finance. *Financial Management*. 16, 5 – 14. available from
5. Colaneri, K., Eisenberg, J., & Salterini, B. (2022). *Some optimisation problems in insurance with a terminal distribution constraint*. St. Louis: Federal Reserve Bank of St Louis. Retrieved from <https://www.proquest.com/working-papers/some-optimisation-problems-insurance-with/docview/2678230319/se-2>
6. Doherty, N. A. (2000). *Integrated Risk Management-Technologies and Strategies for Managing Corporate Risk*. New York, NY: Mc Graw hill.
7. Fombrum C. and Van-Riel, C. (1997), “The reputational landscape”, *Corporate Reputation Review*, 1 (1 – 2) 5 – 13.
8. Freeman, R. E. (1984). *Strategic Management: A Stakeholder approach*, N.J Prentice hall Engle Wood Cliffs.
9. Froot, K. (2007). Risk Management, Capital Budgeting and Capital Structure Policy for Insurers and Reinsurers. *Journal of Risk and Insurance* 74(2), 273-299.
10. Guerdouh, D., Khelfallah, N., & Vives, J. (2022). Optimal control strategies for the premium policy of an insurance firm with jump diffusion assets and stochastic interest rate. *Journal of Risk and Financial Management*, 15(3), 143. doi:<https://doi.org/10.3390/jrfm15030143>
11. Garayeta, A., J Iñaki De la, P., & Trigo, E. (2022). Towards a global solvency model in the insurance market: A qualitative analysis. *Sustainability*, 14(11), 6465. doi:<https://doi.org/10.3390/su14>
12. Jarzabkowski, P., Spee, A. P., & Smets, M. (2013). Material artefacts: Practices for doing strategy with stuff. *European Management Journal*, 31(1) 41-54. <https://doi.org/10.1016/i.emi.2012.09.001>
13. Igbal M. J. and Shah, S. Z. A. (2011). Determinants of Systematic risk in Italian Banking. *The Journal of Commerce* 4 (1), 47-56.
14. Klimezak, K. M. (2005). *Corporate Risk Management from Stakeholders Perspective*. Poland, Trans’ 05, SGH, Warszawa, 371 – 380.
15. Leaucler, T.C. (2007) *Corporate Risk Management for value creation A guide to real-life application* (London Risk Books).



16. Little P.L. and Little, B.L. (2000), "Do Perceptions of Corporate Social responsibility contribute to explaining differences in corporate Price-earning ratios? A research note", *Corporate Reputation Review*, 3 (2) 137 - 142.
17. Liu, L., & Yan, R. (2022). Orderings of extreme claim amounts from heterogeneous and dependent weibull-G insurance portfolios. *Journal of Mathematics*, 2022 doi:<https://doi.org/10.1155/2022/27>
18. Mayer D. and Smith, (Jr). C. W. (1982). Corporate Demand for Insurance. *Journal of Business* 55(2), 281-296.
19. McDonnell, E, (2002), Industry Loss Warranties. Alternative Risk Strategies London: Risk Books. In Mortonlane, ed.
20. Meulbroek. L. K. (2002). A Senior Managers Guide to Integrated Risk Management. *Journal of Applied Corporate Finance* 6 (3) 16 -32.
21. Mikes, A. (2011). From Counting Risk to Making Risk Count. *Boundary-work in Risk Management Organization and Society* 36(2), 226-245.
22. Nacco, B.W. and Saulz, R.M. (2006), "Enterprise Risk Management. Theory and Practice" *Journal of Applied Corporate Finance*. 18(4), 8-20.
23. Pimentel, R. C. (2022). Earnings persistence and market reaction to earnings in the international insurance industry. *Revista De Administração Contemporânea*, 26(3), 1-18. doi:<https://doi.org/10.1590/1982-7849rac2022200404.en>
24. Power, M., Ashby. S. and Palemo, T. (2013). Risk Culture in Financial Organisations. London, U.K. *Research Report for London School of Economics, Centre for the Analysis of Risk and Regulation*.
25. Rädler, A.,T. (2022). Invited perspectives: How does climate change affect the risk of natural hazards? challenges and step changes from the reinsurance perspective. *Natural Hazards and Earth System Sciences*, 22(2), 659-664. doi:<https://doi.org/10.5194/nhess-22-659-2022>
26. Robert and Dowling (2002). Corporate Reputation and sustained superior financial performance strategic management journal/volume 23. Issue 12 Page 1077
27. Schweizer, T.S. and Wijnberg, N.M. (1999), "Transferring reputation to corporation in different Cultures: Individuals, Collective System and Strategic Management of Corporate reputation," *Corporate Reputation Review* 2 (3) 249 - 266.
28. Scott, S.V. and Walsham, G. (2005), "Reconceptualising and managing reputations risk in the knowledge economy: towards reputable action". *Organizational Science*, 16 (3) 308 - 22.
29. Smith, C. W., Smithson, C. W. and Wilford, D. S. (1989). Managing Finance Risk. *Journal of Applied Corporate Finance* 1 (4), 27 - 48.
30. Skipper H. D. and Kwon W.J (2007). Risk Management and Insurance: Perspective in a Global Economy. Baston : John Willey - Blackwel Publishing.
31. Staking, K. B. and Babbel D. F. (1995). The Relation Between Capital Structure, Interest Rate Sensitivity, and Market Value in the Property-Liability Insurance Industry. *Journal of Risk and Insurance* 62, 690 - 718



32. Vojinović, Ž., Milutinović, S., Sertić, D., & Leković, B. (2022). Determinants of sustainable profitability of the serbian insurance industry: Panel data investigation. *Sustainability*, 14(9), 5190. doi:<https://doi.org/10.3390/su14095190>
33. Zhang, J., Wang, J., Chen, S., Tang, S., & Zhao, W. (2022). Multi-hazard meteorological disaster risk assessment for agriculture based on historical disaster data in jilin province, china. *Sustainability*, 14(12), 7482. doi:<https://doi.org/10.3390/su14>.