CHAPTER-III

LIFE INSURANCE: PROFILE OF THE INDIAN INDUSTRY

EVOLUTION OF INSURANCE

The exact time of the origin of insurance cannot be easily traced. Almost 4,500 years from today, in the ancient Babylonia, merchants used to bear the risk of the caravan trade by granting loans that had to be later repaid with interest when the goods arrived safely. Around 2100 BC after two millenniums, the Code of Hammurabi granted authorization for this practice.

Some kind of Life insurance was practiced in ancient Rome, where citizens used to form burial clubs that would meet the funeral expenses of its members and also provide some financial assistance to the surviving family members.

The Code of Manu that was in force during the Reign of the Cholas in South India shows that there was the practice of marine insurance carried out by traders in India with those in Sri Lanka, Egypt and Greece.

As the European civilization progressed, welfare practices also became more refined. With the discovery of new lands, sea routes and the consequent growth in trade, medieval guilds took it upon themselves to protect their member traders from loss on account of fire, shipwrecks and the like.
Insurance is a financial tool by which losses of a small number of people are compensated out of funds (premium) collected from plenteous. More specifically, insurance is a contract wherein one party (the insurer) agrees to pay to the other party (the insured) or his beneficiary a certain sum upon a given contingency (the risk) against which insurance is required. (Bolda et al., 2003).

Insurance is “a contract for reducing losses from accidents incurred by an individual party through a distribution of the risk of such losses among a number of parties.” The definition goes on to say: “In return for a specified consideration, the insurer undertakes to pay the insured or his beneficiary some specified amount in the event that the insured suffers loss through the occurrence of a contingent event covered by the insurance contract or policy. By pooling both the financial contributions and the ‘insurable risks’ of a large number of policyholders, the insurer is typically able to absorb losses incurred over any given period much more easily than would the uninsured individual” (Encyclopaedia Britannica, Micopaedia, 1987, p.335)

Alternatively, Insurance can be defined as “A contract wherein one party (the insurer) agrees to pay another party (the insured) or his beneficiary, a certain

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2. Encyclopaedia Britannica, (1987), Micopaedia, Chicago: University of Chicago
sum upon a given contingency (the risk) against which insurance is required”.

(Bolda et al, 2003)³.

**Types of insurance**

I. Classification on the basis of nature of insurance

(a) Life insurance

(b) Fire insurance

(c) Marine insurance

(d) Social insurance

(e) Miscellaneous insurance

II. Classification from business point of view

(a) Life insurance

(b) General insurance

III. Classification from risk point of view

(a) Personal insurance

(b) Property insurance

(c) Liability insurance

(d) Fidelity guarantee insurance

**Evolution of Life Insurance**

Marine insurers were the first insurers of life; they started insuring the life of master and crew of the ship and the merchants. The early life insurance policies

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were issued for short duration and relief was given to the widows for a certain period.

**Significance of Insurance in Disaster Prone Indian Subcontinent**

The Indian subcontinent is among the world’s most disaster-prone areas. This coupled with lower per capita income individuals cannot bear the risk and insurance is very vital for the common man. (Atmanand 2003)\(^4\).

**Life Insurance Industry in India**

The insurance sector in India has come back to square one from being an open competitive market to nationalization and back to a liberalized market once again.

**A brief history of the Indian Life Insurance sector**

The business of life insurance in India in its existing form started in the year 1818 with the establishment of the Oriental Life Insurance Company in Calcutta.

Some of the important milestones in the life insurance business in India are:

1912: The Indian Life Assurance Companies Act enacted as the first statute to regulate life insurance business.

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1928: The Indian Insurance Companies Act enacted to enable the government to collect statistical information about both life and non-life insurance businesses.

1938: Earlier legislation consolidated and amended to the Insurance Act with the objective of protecting the interests of the insuring public.

1956: 245 Indian and foreign insurers and provident societies taken over by the central government and nationalised. Life Insurance Corporation formed by an Act of Parliament, viz. LIC Act, 1956, with a capital contribution of Rs. 5 crore from the Government of India.

1993: The Indian government constituted the “Malhotra Committee” to suggest reforms in the insurance industry.

1994: “Malhotra Committee” submitted its report, with recommendations for opening the insurance sector to private players, improving, service standards and extending insurance coverage to larger sections of the population.

1999: the Insurance Regulatory Development Act was passed in the Indian Parliament and the door was opened for private companies with foreign equity.

The life insurance industry in India dates back to 1818, when a British firm Oriental Life Insurance Company opened its office in Calcutta (now Kolkata), followed by Bombay Life Assurance Company in 1823. By the year 1956, 154 Indian insurers, 16 foreign insurers and 75 provident societies were carrying on
life insurance business in India. During that time the business was concentrated in urban areas and limited to upper income group people.

The president of India declared an ordinance on 19.01.1956 taking over management and control of business of Life Assurance in India including foreign business of Indian insurers and Indian business of foreign insurers and then nationalized on 01.09.1956 when the Life Insurance Corporation of India was formed by an act of parliament. More specifically, the main aims of nationalization were:

1. To spread insurance to rural areas;
2. To encourage public savings to finance the Five-Year Plans;
3. To provide complete security to policy-holder;
4. To prevent malpractices, misuse of powers and positions, etc.;
5. To avoid wasteful efforts in competition and conduct the business with utmost economy; (Bolda, B.S. et al 2003)\(^5\).

On January 19, 1956, the management of all the 245 insurance companies operating in India was taken over by the central government. Although it was a virtual monopoly since 1956–1999, there were very small players’ viz. Postal Life

The need for reforming the industry was felt in the early 1990s for providing better coverage to the Indians and to increase flow of long-term financial resources to finance the growth of infrastructure. In 1993, the Indian government constituted the “Malhotra Committee” to suggest reforms in the industry. The committee submitted its report in 1994, with recommendations for opening the insurance sector to private players, improving service standards and extending insurance coverage to larger sections of the population (Subhadra, K 2003). In 1999, the Insurance Regulatory Development Act was passed in the Indian Parliament and the door was opened for private companies with foreign equity. So far thirteen private players have been granted license to conduct life insurance business in India. The insurance sector was thrown open to private sector because of these three primary reasons (T.S. Rama Krishna Rao 2006).

1. To fund infrastructure development initiatives

2. Increase insurance penetration in the country

**List of Insurers**

Insurance industry, as on 1.4.2000, comprised mainly two players: the state insurers:

**Life Insurers**

Life Insurance Corporation of India (LIC)

**General Insurers**

General Insurance Corporation of India (GIC) (with effect from Dec'2000, a National Reinsure)

GIC had four subsidiary companies, namely (with effect from Dec 2000, these subsidiaries have been de-linked from the parent company and made as independent insurance companies).

1. The Oriental Insurance Company Limited

2. The New India Assurance Company Limited,

3. National Insurance Company Limited

4. United India Insurance Company Limited.
List of Life Insurers as on August 2006

2. Birla Sun Life Insurance Co. Ltd
3. HDFC Standard Life Insurance Co. Ltd
4. ICICI Prudential Life Insurance Co. Ltd
5. ING Vysya Life Insurance Company Pvt. Ltd.
6. Life Insurance Corporation of India
7. Max New York Life Insurance Co. Ltd
8. Met Life India Insurance Company Pvt. Ltd
9. SBI Life Insurance Co. Ltd
10. Kotak Mahindra Old Mutual Life Insurance Limited
11. Tata AIG Life Insurance Company Limited
15. Shriram Life Insurance Co, Ltd.
16. Bharti AXA Life Insurance Company Ltd.

Post Liberalisation Era

There is no looking back for private players in the life insurance industry since ICICI Prudential, the first private insurer to start operations. And there are phenomenal transformations in the life insurance sector after liberalisation. (T.S. Rama Krishna Rao 2006).
The average growth rate has increased from 10-15 per cent to 20 per cent. The new channels to sell life insurance policies like bancassurance, corporate agents, brokers and direct selling through internet have totally revolutionized the selling process in the life insurance industry. The market share of private players was 20 per cent as on December 2005. Insurance penetration has increased to 2.6 per cent from 1.5 per cent (global standard 4.7%). 70 per cent of the new policies sold are Unit Linked Insurance Plan (ULIP).

Life Insurance Corporation of India had 5 zonal offices, 33 divisional offices and 212 branch offices, apart from its corporate office in the year 1956. Today Life Insurance Corporation of India, functions with 2048 fully computerized branch offices, 100 divisional offices, 7 zonal offices and the corporate office. LIC’s Wide Area Network covers 100 divisional offices and connects all the branches through a Metro Area Network. LIC has arrangements with some Banks to offer on-line premium collection facility in selected cities.

LIC is still on top with a lion’s share of the market. LIC customers had turbulent times through the years. Though, LIC had a variety of insurance plans to cater to all categories of people and to their diverse needs, quality and quick customer service were absent throughout due to customer unfriendly attitude.

It appears as if LIC’s position is at stake, due to this slew of private life insurance companies. But it is not going to be so in the near future. The main
reasons are, it will take time for private sector companies to set up a wide
distribution network, Strong Brand equity of LIC and long gestation period for
private sector companies

While the leader LIC’s task is to retain its leadership, the new entrants want
a larger pie of the market. With the competition getting tougher, to survive
relationship marketing appears to be a promising way not just to survive but to
grow and excel. LIC of India has taken many relationship marketing initiatives.
For instance, the policy holders can know about the status of their policy, calculate
premiums and do a host of activities on LIC’s web site.

While the agents can sell policies of one life insurance company and one
non-life insurance company at a time, a broker can sell policies of several life
insurance companies and non-life insurance companies at a time (Jampala, 2005)\(^9\).

**Problems**

Almost all the private players are incurring substantial losses. Widespread
losses are common in this industry. But what is worrying is the two major sell outs
in the Indian insurance industry. The first is the sale of AMP Sanmar to Anil
Ambani’s Reliance Capital and the second is the sale of ING Vysya Life Insurance

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to Gujarat Ambuja Cements and Exide Industries. The following are the major problems that haunt private life insurers (Yassir A. Pitalwalla 2006)\(^\text{10}\)

The ceiling for Foreign Direct Investment (FDI) in the sector is only 26 per cent. Capital is very important because of the solvency margin regulation of Insurance Regulatory and Development Authority (IRDA).

To meet the IRDA norms for solvency, for every Rs.100 claim payable to the customer, the life insurance company must have assets worth Rs.150. So, the companies can sell more and more policies only if they are able to invest more and more money. The Indian shareholders are gasping for capital, while the foreign partners have huge chest of resources, the FDI cap of 26 per cent prevents them from pumping money.

The commission for first year premium paid to agents is 40 per cent and insurance companies receive only Rs.60 for every Rs.100 paid by the customer. With fast track growth on the cards, the high commission paid for first year premiums will push the break even point to a couple of years.

In a competitive market, to attract customers private life insurers are declaring bonus ranging from 4 per cent to 14 per cent. This bill has to be funded by shareholders, as there is no adequate surplus to pay bonus.

Another area of concern is the attrition rate of agents. The attrition rate is precipitous at 80 per cent and companies have to incur huge cost for training agents for the mandatory 100 hours IRDA certification.

The competition in Indian life insurance marketing is getting tough and Insurance companies are adopting strategies like Bancassurance where insurance products are sold through banks. And relationship marketing initiatives like online payment of premium, providing policy status on internet, for dissemination information kiosks are put up at prime locations in major cities, and Information Centers manned by skilled employees to provide you with information about the products, policy services, branch addresses are established.