CHAPTER-1

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1.1 INTRODUCTION

The financial sector is growing enormously in terms of size, innovations, diversity, complexity and sophistication in the world. The financial services sector industry today is carrying out a host of actives like intermediation, agency services, real estate, consumer durable financing and like. The financial sector reforms initiated in 1988 had wide ranging ramifications. Within the financial services sector the insurance companies constitute an important segment as they are mobilizing large sum of money from policy holders and supplying it to invest in socially desirable sectors in the economy.

Marketing starts with human needs and wants. The concept of marketing is that the customer buys a benefit to satisfy a particular need. Marketing is the process of identification of unmet needs of the target customer segment, understanding their buying behavior and preferences to develop suitable products and services and utilization of the elements of marketing mix like product, price, place, promotion, people, process and physical evidence. Marketing helps in maximizing customer satisfaction with the overall profit requirement of business concern. Marketing is different from selling. In marketing, the customer need is the prime determinant for product and services development. Product is the focus of selling.

The marketing approach involves anticipating, identifying, reciprocating and satisfying the customers' needs and wants effectively and profitably. Application of marketing techniques in a financial organization implies use of product, price, promotion and distribution policies for customer satisfaction. The marketing concept in insurance industry emerged in late fifties in the form of “advertising and promotion”. Marketing is broadly recognized as an important activity in insurance company. Most of the insurance companies consider marketing as essentially an advertising and public relations job. Insurance is a personalized service-oriented industry and hence should provide services
which satisfy the customers’ needs. The need of each group of customers’ is different from that of the others. It is therefore, necessary of the insurer to indentify different groups of customers, find out their needs, design the schemes/policies to suit their needs and deliver these schemes/policies in the best possible manner.

1.2 THE CONCEPT OF LIFE INSURANCE

Life is full of risks, being a social animal and risk averse, man always tries to reduce risk. An age –old method of sharing of risk through economic cooperation led to the development of the concept of ‘insurance’.

Insurance may be described as a social device to reduce or eliminate risk of loss to life and property. Insurance is a collective bearing of risk. Insurance spreads the risks and losses of few people among a large number of people as people prefer small fixed liability instead of big uncertain and changing liability. Insurance is a scheme of economic cooperation by which members of the community share the unavoidable risks. The risks that can be insured against include fire, the perils of sea, death, accidents and burglary. The members of the community subscribe to a common pool or fund, which is collected by the insurer to indemnify the losses arising out of risks. Insurance cannot prevent the occurrence of risk but it provides for the losses of risk. It is a scheme that covers large risks by paying small amount of capital. Insurance is also a means of savings and investment.

Insurance and mutual funds are fundamentally different in their objective. The objective of insurance is to cover the eventuality of death and therefore, is more long – term in its outlook while, mutual funds are purely investment gain vehicles.

Insurance can be defined as a legal contract between two parties whereby one party called the insurer undertakes to pay a fixed amount of money on the happening of a particular event, which may be certain or uncertain. The other party called the insured pays in exchange a fixed sum known as premium. The insurer and the insured are also known as assurer, or underwriter, and assured, respectively. The document, which embodies the contract, is called the policy.
An insurance policy is a special type of contract. It is synallagmatic and aleatory in character. A synallagmatic contract is one by which each of the contracting parties binds himself to the other. It is aleatory because the insurer's obligation to pay a loss (claims) is distant and often uncertain, while the insured must pay a fixed premium during the policy period. Thus while the sacrifice (premium) is certain and immediate, the benefits (claims) are distant and contingent for the insured. This makes it a unique financial product, requiring a broad understanding of pure and speculative risks to which an individual or enterprise is exposed, in order to take an informed buying decision.

The insurance companies are distinct financial institutions (intermediaries) in the financial system.

1. Insurers collect insurance premiums by issuing insurance policies which are debt instruments (claims) and invest these premium in financial assets and markets to generate cash flows to pay future claims. Thus, insurers are liability-driven financial intermediaries.

2. Unlike other intermediaries, insurers have to hold risk capital or solvency capital to ensure their obligations to the insured. Insurers demonstrate their financial strength to the insured by holding risk capital, which provides a cushion against unexpected losses. Another unique feature of the industry is the distinct principles such as uberrima fidei, indemnity, subrogation, causa proxima and insurable interest of which underwriters (insurers) are more aware of than the insured.

3. In addition, insurance pricing differs from the pricing of other products. In case of other products, the producer knows the costs of production and the profit he wants to earn. Insurance is a different activity from most other kinds of business activities. Insurers are in the business of risk. It is very difficult to price risk. In case of insurance, the actual cost of risk coverage can be known only at the expiry of the contract or when the event occurs whereas the premium rate is determined at the beginning of the contract. The determination of premium rate involves many statistics, use of probability theories and study of demographic trends and market trends.
Marketing of insurance product is a challenging task. Insurance is sold, never bought. The seller (agent) should possess expert knowledge of the insurance products. Have the skill in making people listen carefully and strive to establish a long-term relationship with the clients to get repeat business. Only those who are open to new ideas, able to plan their activity well and willing to face challenges can succeed in marketing insurance products.

1.2.1 Meaning of Life Insurance:

According to sec. (2) (11) of the insurance Act, Life Insurance business means “the business of effective contracts upon human life. It includes:

(a) Any contract whereby the payment of money is assured upon death or the happening of any contingency dependent on human Life.

(b) Any contract which is subject to the payment of premiums for a term dependent or human Life.

(c) Any contract which include the granting of disability and double or triple indemnity, accident benefits, the granting of annuities upon human Life, and the granting of superannuation allowance.”

1.2.2 Definition of insurance:

Insurance is one of the primary risk management devices available to the people. The term ‘insurance’ stands for a mechanism to protect against risks, hazards or dangers to life and property. By insurance, a person is able to shift the risk and for this purpose, he has to part with a sum called as ‘premium’. The person who takes out insurance policy is the ‘insured’ and the company that provides the insurance cover is the ‘insurer’. The insurer is also called as ‘underwriter’ in insurance terminology. The subject matter of insurance is the life of a person in the case of life insurance and non-life insurance covers the risks of fire, perils of the sea, burglary, etc. non-life insurance is also called as general insurance.
Vaghan and Vaghan define insurance from two points of view. From an individual point of view, 'insurance is an economic device whereby the individual substitutes a small certain cost for a large uncertain financial loss that would exist if it were not for the insurance.

Second, from the society point of view, 'insurance is an economic device for reducing and eliminating risk through the process of combining a sufficient number of homogeneous exposures in to a group to make the losses predictable for the group as a whole.

The definition of insurance can also be made from two points (i) Functional definition and (ii) Contractual definition.

Functional Definition

Insurance is a co-operative device to spread the loss caused by a particular risk over a number of persons, who are exposed to it and who agree to insure themselves against the risk. Thus the insurance is (a) co-operative device to spread the risk; (b) the system to spread the risk over a number of persons who are insured against the risk; (c) the principle to share the loss of each member of the society on the basis of probability of loss to their risk and (d) the method to provide security against losses to the insured.

Similarly another definition can be given. Insurance is a co-operative device of distributing losses, falling on an individual or his family over a large number of persons, each bearing a nominal expenditure and feeling secure against heavy loss.

Contractual Definition

Insurance has been defined to be that in which a sum of money as a premium is paid in consideration of the insurer's incurring the risk of paying a large sum upon a given contingency. The insurance, thus, is a contract whereby (a) certain sum, called premium, is charged in consideration, (b) against the said consideration, a large sum is guaranteed to be paid by the insurer who received the premium, (c) the payment will be made in a certain definite sum, i.e., the loss or the policy amount whichever may be and
(d) the payment is made upon a contingency. More specific definition can be given as follows-Insurance may be defined as a “consisting one party (the Insurer) agrees to pay the other party (the insured) on his beneficiary, a certain sum upon a given contingency (the risk) against which insurance is sought”.

1.2.3 Benefits of Life Insurance

1. **Risk cover:** Life insurance gives full protection against the risk of death of policyholder. In the event of death of the holder, the insurance money along with bonuses accrued is paid the family.

2. **Savings habit:** Life insurance encourages the habit of savings or thrift amount the public. Premiums can be paid in installments. For instance, the monthly deduction from salary on account of premium under the salary savings scheme is a convenient means of savings for the individuals.

3. **Liquidity:** Life insurance policy can serve as a security to avail the loans. Even for other commercial loans, the insurance policy is as a security. The main benefit is that it results in immediate liquidity to the holder.

4. **Tax benefits:** Insurance is one of the common methods adapted to savings in income tax. The premiums paid on life insurance policies are allowed as a deduction in computing the taxable income of the individuals. Because of the tax relief available, the effective cost of the premiums paid by the holder of the policy will be less.

5. **Earmarking:** Life insurance policies are sometimes taken with a specific goal in mind. Children’s education, marriage and retirement are some of the specific goals with the policy are introduced.

1.2.4 Functions of Insurance

Insurers provide insurance policies, which are legally binding contracts for which the policyholder pays insurance premium. Under an insurance contract, insurance companies promise to pay specified sub contingent on the occurrence of future events. Based upon this, the functions of insurance may be discussed as follows.
Certainty: Insurance provides certainty of payment for the risk of loss. There are different types of uncertainty in a risk. The risk will occur or not, when will occur, how much loss will be there? In other words, there are uncertainty of happening of time and amount of loss. Insurance removes all these uncertainty and the assured is given certainty of payment of loss. The insurer charges premium for providing the said certainty.

Protection: The main function of the insurance is to provide protection against the probable chances of loss. The insurance guarantees the payment of loss and thus protects the assured from sufferings. The insurance cannot check the happening of the event but can compensate for losses arising at the happening of the risk event.

Risk Sharing: when risk takes place, all the persons who are exposed to the risk share the loss. The share is obtained from each insured in the shape of premium without which the insurer does not guarantee protection.

Assists in capital formation: The insurance provides capital to the society. The accumulated funds are invested in productive channel. The scarcity of capital of the society is minimized to a greater extent with the help of investment of insurance.

Prevention of Loss: The insurance companies assist financially to the health organization, Fire Bridge, education institutions and other organization, which are engaged in preventing the losses of the masses from death or damage. The insurance joins hands with these institutions in preventing the losses of the society because the reduction in loss causes lesser payment to the assured and so more saving is possible which will assist in reducing the premium. Lesser premium invites more business and more business cause lesser share to the assured. The reduced premium will stimulate more business and more protection to the masses.

The primary function of insurance is to act as a risk transfer mechanism. Under this function of insurance, an individual can exchange his uncertainty for certainty. In return for a definite loss, which is the premium, he is relieved from the uncertainty of a potentially much larger loss. The risks themselves are not removed, but the financial
consequences of some are now known with greater certainty and he can budget accordingly.

In the early days of marine insurance, the various merchants who were having goods carried on a ship would agree to make contributions to those who may have suffered a loss during the voyage, after the loss had taken place. This certainly removed the risk of a total loss from any one merchant, because each one knew that his loss would be shared. What it did not do was to give the merchant any idea of what his loss would be; he knew this only after a voyage. If there has been no losses then he would have nothing to pay, he had agreed to share in any losses which had taken place and the exact amount of these could be determined only after the event.

It can be seen that the assessment of risk is extremely important. The insurer has to ensure that a fair premium is charged, which reflects the hazard and the value which the person or company brings to the pool. This is a complex enough process, but in addition the premium must also be competitive. There is not just one insurer in the marketplace and hence competition enters into the calculation. If an insurer charges a premium, which greatly exceeds that, quoted by other insurers, then it will probably lose the business. Charging too little also has its dangers: the contributors to the pool would be less than required and a loss would be made. This loss would have to be re-coped at some stage, possibly making the premiums uncompetitive at that time.

Based on discussion made above, it can be conclude that the primary function of insurance is the creation of the counter balance for risk, which is security. Insurance does not eliminate or decrease the uncertainty for the individual as to whether or not the event will occur, nor does it alter the possibility of occurrence, but it does reduce the extent of financial loss connected with the event. From the individual's point of view, the purchase of an adequate amount of insurance on a house reduces the financial loss in the event of the house catching fire.

A number of times one might think that he has wasted his money in purchasing insurance policy if loss does not occur and consequently, no financial return are received. Some even feel that if they have not had a loss during the policy term, their premium
should be returned. Both viewpoints constitute the inadequate understanding of the insurance concept. Relative to the first, it is already known that the insurance contract provides a valuable feature in the relief from the burden of uncertainty. Even if a loss is not sustained during the policy term, the insured has received something for the premium in the form of freedom from the worry of financial loss. With respect to the second, one must appreciate the fact that the operation of insurance principle is based on the contributions of the many paying the losses of the unfortunate few. If the premiums were returned to the many who did not have losses, there would be no funds available to pay for the losses of the few who did. Basically, then, the insurance device is a method of loss distribution. What would be devastating loss to an individual is spread in an equitable manner to all members of the group, and it is on this basis that insurance can exist. In other words, insurance meets the social commitment every member of the society has to provide relief to those who necessitate it.

1.2.5 Principles of Insurance

Insurance is basically a contract between the insured and the insurer. These contracts are based on certain basic principles. These principles apply to all types of insurance excepting the principle of indemnity which does not apply to life insurance. Here, a discussion on the principles is provided.

1. Principle of uberrimae fidei: Insurance is a contract uberrimae fidei meaning that it is a contract based on utmost good faith of the parties involved. As insurance involves transfer of risk from one party to another, it is essential that there must be utmost good faith between the insured and the insurer, information about the subject matter of insurance must be fully disclosed so that the insurer can assess the extent of risk and charge accordingly. Withholding of any relevant information may result in declaring the contract as void by the insurer once he discovers it. This principle applies to all types of insurance.

2. Insurable Interest: The principle of insurable interest in a contract of insurance distinguishes it from a wagering contract. A person is said to have insurable interest if he derives benefits from its existence and loss from its destruction. The insured
must have a pecuniary interest in the subject matter of insurance; either he must own part or whole of it, or he must be in such a position that any injury to it would affect him adversely. An owner of a ship, for example, runs the risk of losing his ship and the owner of the cargo runs the risk of losing his cargo in the event of a sea peril. Both the owner of the ship and the owner of cargo have an insurable interest in the subject matter of insurance.

3. Principle of Indemnity: Indemnity principle implies that the loss incurred by the insured is made good by the insurer. This is embodied in a contract of insurance except the life insurance contract. In a life insurance contract, it ceases to be a contract of indemnity because a fixed sum is payable on the happening of the event insured. Indemnity principle requires that the insurer pay the actual loss suffered by the insured due to the happening of the event. An insured cannot make a profit out of the loss through insurance.

4. Mitigation of Loss: The principle of mitigation of loss demands that in the event of a mishap, the insured shall act as though he were uninsured. He must take all reasonable efforts that a prudent person will do to prevent the insured property being damaged by the event or the peril. He should do everything in his power to minimize the loss and to save the property.

5. Causa Proxima: The principle of causa proxima states that the insurer is liable for a loss if such a loss must have been proximately by the peril insured against. It is the proximate or the nearest cause that must be looked into where there has been a succession of causes. If the cause of the loss is a peril insured against, then the insured can recover the amount.

6. Subrogation: The essential feature of an insurance contract is the principle of indemnity which we have described earlier. Now, the principle of subrogation enables the preservation of indemnity principle. We have stated that the insurer has to indemnify the loss to the insured. If the insured gets his loss fully indemnified from the insurer, and then he gets compensation for the same loss from third parties, he would be more than fully indemnified. This negates the principle of indemnity. At this juncture, the principle of
subrogation operates. Subrogation is the substitution of one person in place of another with regard to the claim, its rights, remedies or securities. The principle applies to fire and marine insurance. Once the claim of the insured is settled, the insurer stands in his (insured's) place; insurers are subrogated to all the rights of the insured. If the insured receives any compensation for the same loss from some other person, he has to pass on that amount to the insurers. The insured cannot make a profit out of the loss.

7. Contribution: Contribution is the right of the insurer to claim from others some payment towards the loss. Contribution arises in the cases of double insurance. It is possible that there is more than one contract with regard to the same subject matter and the total amount of insurance policy exceeds the total value of the loss suffered. Under such circumstances, the principle of contribution is applied. The insurer is entitled to contribution where he has paid the insured. The amount of the contribution is the amount in excess of the ratable proportion of loss. Ratable proportion of loss is such a proportion of loss as the amount of the policy bears to the total amount of insurance. In essence, according to the contribution principle, the insurer, after having paid the insured, recovers the amount that the has paid in excess of his share from other insurers.

1.2.6 Role of insurance in Economic Growth:

With the growth of a country's economy, there is an economy; there is an increase in the facilitating role played by the financial services sector. Financial services play a supportive role in the basic activity of production. Insurance frees industries from the worries of unforeseen losses and uncertainties from the worries of unforeseen losses and uncertainties. Insurance helps the country's growth in various ways.

i. Insurance covers many economic risks. It protects entrepreneurs against the risk of damage to or loss of the goods and other assets, which they employ in manufacturing, marketing, transport and other related activities. This protection offers a kind of stability to business.

ii. With the cover of insurance on their assets, businessmen and industrialists are able to take old decisions in enlarging their field of activity, and take financial risks
which the y cannot otherwise take. Hence, insurance plays a promotional role in nation building and increasing the number of jobs for the people.

iii. Again, there is life insurance, which plays the most useful role in the lives of individuals. Life insurance offers economic safety at reasonable cost to millions of families in the country. In a way, this helps the government also as it lightens the government’s burden of providing social welfare to affected families.

iv. Insurance companies collect premium from policyholders and invest this money in government bonds, corporate securities and other approved channels of investment. In this way, insurance companies are helpful in providing capital for new ventures or expansion of old units. Moreover, these funds are also used for financing the infrastructure projects with long gestation period. In addition, this lending of funds for infrastructure and other development favorably influences the decision-making process in the government.

Thus insurance aids in the growth of modern economy. By promoting safety against personal losses, it not only improves the individual’s quality of life but also provides smoothness in the working of the affairs of business and industry.

1.3 HISTORY OF INSURANCE IN INDIA

The story of insurance is probably as old as the story of mankind. The same instinct that prompts modern businesspersons today to secure themselves against loss and disaster existed in primitive men also. They too sought to avert the evil consequences of fire and flood and loss of life and were willing to make some sort of sacrifice in order to achieve security. Though the concept of insurance is largely a development of the recent past, particularly after the industrial era – past few centuries – yet its beginnings date back almost 6000 years.

In India, insurance has a deep-rooted history. It finds mention in the writings of Manu (Manu Smriti), Yagnavalkya (Dharmasastra) and Kautilya (Arthasastra). The
writings talk in terms of pooling of resources that could be re-distributed in times of calamities such as fire, floods, epidemics and famine. This was probably a pre-cursor to modern day insurance. Ancient Indian history has preserved the earliest traces of insurance in the form of marine trade loans and carriers' contracts. Insurance in India has evolved over time heavily drawing from other countries, England in particular.

1818 saw the advent of life insurance business in India with the establishment of the Oriental Life Insurance Company in Calcutta. This Company however failed in 1834. In 1829, the Madras Equitable had begun transacting life insurance business in the Madras Presidency. 1870 saw the enactment of the British Insurance Act and in the last three decades of the nineteenth century, the Bombay Mutual (1871), Oriental (1874) and Empire of India (1897) were started in the Bombay Residency. This era, however, was dominated by foreign insurance offices, which did good business in India, namely Albert Life Assurance, Royal Insurance, Liverpool and London Globe Insurance and the Indian offices were up for hard competition from the foreign companies.

In 1914, the Government of India started publishing returns of Insurance Companies in India. The Indian Life Assurance Companies Act, 1912 was the first statutory measure to regulate life business. In 1928, the Indian Insurance Companies Act was enacted to enable the Government to collect statistical information about both life and non-life business transacted in India by Indian and foreign insurers including provident insurance societies. In 1938, with a view to protecting the interest of the Insurance public, the earlier legislation was consolidated and amended by the Insurance Act, 1938 with comprehensive provisions for effective control over the activities of insurers.

The Insurance Amendment Act of 1950 abolished Principal Agencies. However, there were a large number of insurance companies and the level of competition was high. There were also allegations of unfair trade practices. The Government of India, therefore, decided to nationalize insurance business. An Ordinance was issued on 19th January, 1956 nationalizing the Life Insurance sector and Life Insurance Corporation of India came into existence in the same year. The LIC absorbed 154 Indian, 16 non-Indian
insurers as also 75 provident societies—245 Indian and foreign insurers in all. The LIC had monopoly until the late 90s when the Insurance sector was reopened to the private sector.

The history of general insurance dates back to the Industrial Revolution in the west and the consequent growth of sea-faring trade and commerce in the 17th century. It came to India as a legacy of British occupation. General Insurance in India has its roots in the establishment of Triton Insurance Company Ltd., in the year 1850 in Calcutta by the British. In 1907, the Indian Mercantile Insurance Ltd was set up. This was the first company to transact all classes of general insurance business.

1957 saw the formation of the General Insurance Council, a wing of the Insurance Association of India. The General Insurance Council framed a code of conduct for ensuring fair conduct and sound business practices.

In 1968, the Insurance Act was amended to regulate investments and set minimum solvency margins. The Tariff Advisory Committee was also set up then in 1972 with the passing of the General Insurance Business (Nationalization) Act; general insurance business was nationalized with effect from 1st January, 1973. 107 insurers were amalgamated and grouped into four companies, namely National Insurance Company Ltd., the New India Assurance Company Ltd., the Oriental Insurance Company Ltd and the United India Insurance Company Ltd. The General Insurance Corporation of India was incorporated as a company in 1971 and it commence business on January 1st 1973.

This millennium has seen insurance come a full circle in a journey extending to nearly 200 years. The process of re-opening of the sector had begun in the early 1990s and the last decade and more has seen it been opened up substantially. In 1993, the Government set up a committee under the chair of R N Malhotra, former Governor of RBI, to propose recommendations for reforms in the insurance sector. The objective was to complement the reforms initiated in the financial sector. The committee submitted its report in 1994 where in, among other things, it recommended that the private sector be permitted to enter the insurance industry. They stated that foreign companies are allowed to enter by floating Indian companies, preferably a joint venture with Indian partners.
Following the recommendations of the Malhotra Committee report, in 1999, the Insurance Regulatory and Development Authority (IRDA) was constituted as an autonomous body to regulate and develop the insurance industry. The IRDA was incorporated as a statutory body in April 2000. The key objectives of the IRDA include promotion of competition to enhance customer satisfaction through increased consumer choice and lower premiums, while ensuring the financial security of the insurance market.

The IRDA opened up the market in August 2000 with the invitation for application for registrations. Foreign companies were allowed ownership of up to 26%. The Authority has the power to frame regulations under Section 114A of the Insurance Act, 1938 and has from 2000 onwards framed various regulations ranging from registration of companies for carrying on insurance business to protection of policyholders’ interests.

In December 2000, the subsidiaries of the General Insurance Corporation of India were restructured as independent companies and at the same time, GIC was converted into a national re-insurer. Parliament passed a bill de-linking the four subsidiaries from GIC in July 2002.

Today there are 24 general insurance companies including the ECGC and Agriculture Insurance Corporation of India and 23 life insurance companies operating in the country.

The insurance sector is a colossal one and is growing at a speedy rate of 15-20%. Together with banking services, insurance services add about 7% to the country's GDP. A well-developed and evolved insurance sector is a boon for economic development as it provides long-term funds for infrastructure development at the same time strengthening the risk taking ability of the country.
1.3.1 A brief history of insurance industry in India:

It began in the year 1818.

In the year, 1818 The British introduced life insurance in India with the establishment of the Original Life Insurance Company in Calcutta.

In 1850 Non life insurance debuts, with Triton Insurance Company.

In 1870, Bombay Mutual life assurance society is the first India-owned life insurer.

In 1907, India Mercantile Insurance is the first India non-life insurer.

In 1912, the Indian life assurance companies’ act enacted to regulate the life insurance Business.

In 1938 the insurance Act was passed, which forms the basis for most current insurance laws, replaces earlier Act.

In 1956 the life insurance had been nationalized and LIC of India was set up

In 1973 GIC was set up with 4 subsidiaries to carry the general insurance business.

In 1993 Malhotra Committee, headed by former RBI governor R.N Malhotra set up to draw up a blue print for insurance sector reforms.

In 1994 Malhotra committee recommended re-entry of private players, autonomy to PSU insurers.

In 1997, insurance regulator, IRDA (insurance Regulatory and Development Authority) was set up.

In 2000, IRDA started giving licenses to private insurers; ICICI prudential and HDFC Standard life first private life insurance to sell a policy.

In 2001 Royal Sundaram Alliance first non-life insurance to sell a policy.
In 2002 Banks allowed selling insurance plans.

1.3.2 An Aggregate View of Indian Insurance:

One can divide the history of the existence and working of insurance organizations in India in the following three phases.

<table>
<thead>
<tr>
<th>Phase I</th>
<th>1818 to 1956: (About 138 Yrs.)</th>
<th>Many (245) private sector companies only; competitive market.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Life Insurance:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(b) General Insurance:</td>
<td>1850 to 1972: (About 122 Yrs.)</td>
<td>Many (107) private sector companies only; competitive market.</td>
</tr>
</tbody>
</table>

<table>
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<tr>
<th>Phase II</th>
<th>1956 to 2000: (About 44 Yrs.)</th>
<th>Nationalization, public sector or State monopoly; only one company.</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) Life Insurance:</td>
<td></td>
<td>Nationalization, public sector or State monopoly; one company with its 4 subsidiaries.</td>
</tr>
<tr>
<td>(b) General Insurance:</td>
<td>1972 to 2000: (About 28 Yrs.)</td>
<td></td>
</tr>
</tbody>
</table>

| Phase III     | Life Insurance & General Insurance After 2000: | Opened to the entry of private domestic and foreign companies: mixed sector of public and private sector units; oligopoly of public sector companies (24 life insurance and 24 general insurance companies). |

These three phases are briefly elaborated upon in the following

The life insurance services have been in existence in India since 1818 when the first life insurance company namely, Oriental Life Insurance Company was established in Calcutta. The general insurance service has been available since 1850 when the first Tritan Insurance Company was established, again, in Calcutta. Since the respective years mentioned above and till 1956/1972, the life and general insurance services industry has grown in terms of the number of companies providing those services, the volume of
premium, investible resources, and so on. Till 1956/1972 there were a large number of insurance companies (total 352 comprising 245 life and 107 general insurance companies), and all of them were in the private sector. Both the general and life insurance industries were truly competitive. The insurance business was regulated through the Insurance Act, 1938, which itself had evolved through passing certain statutes at various points of time.

This picture changed after the Independence. In 1956, 245 Indian and foreign life insurers and provident societies were nationalized, and a new single entity namely, Life Insurance Corporation (LIC) was established by passing the LIC Act. Similarly, in 1972, 107 general insurers were nationalized through the passing of General Insurance Business (Nationalization) Act, 1972. The then existing 107 insurers were amalgamated and grouped into five companies, viz., National Insurance Company (NIC), New India Assurance Company (NIAC), Oriental Insurance Company (OIC), and United India Insurance Company (UIIC), and General Insurance Corporation (GIC). Thus, in 1956 and 1972, the competitive, private insurance industry was transformed into monopolistic and oligopolistic state or public sector insurance industry in India.

1.4 WORLD INSURANCE SCENARIO

As per World Insurance Report published by reinsurance major Swiss Re, the global insurance premium for the calendar year 2010 was USD 4339 billion, which is 2.7 per cent (inflation-adjusted) higher than USD 4109 billion reported during the previous calendar year 2009.

The share of life insurance business was 58 percent in total premium collection. While life insurance business collected USD 2520 billion as premium, the same for non-life business was USD 1818 billion. During 2010, the premium in world life insurance business increased by 3.2 per cent on the back of double digit growth (i.e. 13 per cent) in life insurance premium collection in emerging markets.

During 2010, the global non-life insurance premiums rose by 2.1 per cent. In emerging Asia and newly industrialized countries in the region, the strong economic
rebound pushed up non-life premium growth, while soft pricing continued to slow growth in Europe and the US, except in a few countries in selected lines of business. Consequently, underwriting results deteriorated further in 2010, despite average natural catastrophe losses and continuing reserve releases. Overall profitability remained low, as capital gains on invested assets only partially offset low investment yields.

Stock markets around the world continued to recover in 2010. As a result, the capital positions and investment return of insurers improved. Demand for the Unit-linked life insurance products strengthened. However, volatility remained high due to concerns about the strength of the economic recovery and the sovereign debt for the peripheral European countries. Improved sales, lower lapses and higher capital gains on financial assets supported operating margins. However, profitability continued to remain low due to adverse interest rates.

In 2011, the economic recovery is expected to continue, supporting premium growth in life and non-life insurance in the industrialised countries and emerging markets. Profitability in both sectors will continue to be low, as interest rates are expected to rise slowly. The devastating earthquakes in Japan and New Zealand are likely to result in higher prices in those countries and help to stop the trend of softening rates worldwide.

Overall, the insurance industry has recovered well from the crisis. Demand for insurance in the emerging markets is expected to continue to grow strongly in the coming years. Ageing societies will provide ample opportunities for life insurers. However, insurers face a number of challenges ahead such as derailment of economic recovery which may be caused by an escalation of the European sovereign debt crisis or an oil price shock. Introduction of regulatory reforms like Solvency II may lead to overly stringent capital requirements which would undermine profitability and ultimately may pose a challenge before the insurers. Escalation of public debt crisis may wear away the assets of insurers in view of the fact that insurers hold sovereign debt and bonds issued by banks. Broadly, it is expected that profitability will remain below pre-crisis levels for some time.
1.5 APPRAISAL OF INDIAN LIFE INSURANCE MARKET

1.5.1 Indian Insurance in the Global Scenario

In life insurance business, India ranked 9th among the 156 countries, for which data are published by Swiss Re. During 2010-11, the estimated life insurance premium in India grew by 4.2 per cent (inflation adjusted). However, during the same period, the global life insurance premium expanded by 3.2 per cent. The share of Indian life insurance sector in global market was 2.69 per cent during 2010, as against 2.45 per cent in 2009.

The non-life insurance sector witnessed significant growth of 8.1 per cent during 2010. Its performance is far better when compared to global non-life premium, which expanded by 2.1 per cent during the same period. The share of Indian non-life insurance premium in global non-life insurance premium increased slightly to 0.58 per cent, thereby improvising its global ranking to 19th in comparison to 26th in last year.

1.5.2 Insurance penetration & density in India

The measure of insurance penetration and density reflects the level of development of insurance sector in a country. While insurance penetration is measured as the percentage of insurance premium to GDP, insurance density is calculated as the ratio of premium to population (per capita premium). Since opening up of Indian insurance sector for private participation, India has reported increase in insurance density. However, the insurance penetration, which surged consistently till 2009, slipped for the first time in 2010 on account of slower rate of growth in the life insurance premium as compared to the rate of growth of the Indian economy.

The insurance density of life insurance sector had gone up from USD 9.1 in 2001 to USD 55.7 in 2010. Similarly, insurance penetration had gone up from 2.15 per cent in 2001 to 4.60 in 2009, before slipping to 4.40 per cent in 2010.
1.5.3 Appraisal of Indian Life Insurance Market

a) Registered Insurers in India

At end-September 2011, there are forty-nine insurance companies operating in India; of which twenty-four are in the life insurance business and another twenty-four are in general insurance business. In addition, GIC is the sole national re-insurer.

Of the forty-nine companies presently in operations, eight are in the public sector: two specialized insurers, namely ECGC and AIC, one in life insurance, four in general insurance and one re-insurance. The remaining forty-one companies are in the private sector.

b) Premium

Life insurance industry recorded a premium income of `2,91,605 crore during 2010-11 as against `2,65,447 crore in the previous financial year, registering a growth of 9.85 per cent. While private sector insurers posted 11.04 per cent growth (23.06 per cent in previous year) in their premium income, LIC recorded 9.35 per cent growth (18.30 per cent in previous year). While renewal premium accounted for 56.66 per cent (58.60 per cent in 2009-10) of the total premium received by the life insurers, first year premium contributed the remaining 43.34 per cent (41.40 per cent in 2009-10). During 2010-11, the growth in renewal premium was 6.22 per cent (15.69 per cent in 2009-10). By comparison, the growth in first year premium was higher at 15.00 per cent during 2010-11 but there is significant decline in growth in comparison to the previous year figure (25.84 per cent in 2009-10).

Further bifurcation of the first year premium indicates that single premium income received by the life insurers recorded 26.99 per cent growth during 2010-11 (31.05 per cent in 2009-10). Single premium products continue to play a major role for LIC as they contributed 24.94 per cent of LIC's total premium income (24.36 per cent in 2009-10). In comparison, the contribution of single premium income in total premium income has surged to 13.28 per cent for private insurance companies during 2010-11 (4.84 per cent in 2009-10).
The growth of the regular premium stood only at 5.30 per cent in 2010-11, against 21.91 per cent growth in 2009-10 with the private insurers witnessing negative growth (-19.88 per cent). The LIC continued with high growth in the regular premium. The same stood at 38.50 per cent in 2010-11 (36.80 per cent in 2009-10).

Unit-linked products (ULIPs) witnessed 5.64 per cent decline in premium income from 1,15,521 crore in 2009-10 to 1,09,002 crore in 2010-11. On the other hand, the growth in premium income of traditional products was at 21.80 per cent, with premium income increasing to 1,82,603 crore as against 1,49,926 crore in 2009-10. Accordingly, the share of unit-linked products in total premium considerably declined to 37.38 per cent in 2010-11 as against 43.52 per cent in 2009-10 (Statement No.11).

e) Market Share

On the basis of total premium income, the market share of LIC declined marginally from 70.10 per cent in 2009-10 to 69.78 per cent in 2010-11. Accordingly, the market share of private insurers has gone up marginally from 29.90 per cent in 2009-10 to 30.22 per cent in 2010-11.

The market share of private insurers in first year premium was 31.15 per cent in 2010-11 (34.92 per cent in 2009-10). The same for LIC was 68.85 per cent (65.08 per cent in 2009-10). However, in renewal premium, LIC had a higher share of 70.49 per cent (73.64 per cent in 2009-10) when compared to 29.51 per cent (26.36 per cent in 2009-10) share of private insurers.

d) New Policies

During 2010-11, life insurers issued 482 lakh new policies, out of which, LIC issued 370 lakh policies (76.91 per cent of total policies issued) and the private-life insurers issued 111 lakh policies (23.09 per cent). While LIC suffered a decline of 4.70 per cent (8.21 per cent increase in 2009-10) in the number of new policies issued against the previous year, the private sector insurers reported a significant decline of 22.61 per cent (4.32 per cent decline in 2009-10) in the number of new policies issued. Overall, the
industry witnessed a 9.53 per cent decline (4.52 per cent increase in 2009-10) in the number of new policies issued.

e) Expenses of life insurers

As per section 40B of the Insurance Act, 1938 no life insurer can spend as expenses of management in any year an amount in excess of the limits prescribed under Rule 17D of the Insurance Rules, 1939. Rule 17D takes into consideration the size and age of the insurer, while laying down the limits of such expenses. The IRDA on the recommendation of the Life Insurance Council constituted under Section 64F of the Insurance Act may enhance the limits in any year. Expenses of management refer to all charges incurred either directly or indirectly and include commission payments of all kinds, operating expenses and expenditure capitalized.

f) Paid-up capital

The total capital of the life insurance companies as on 31st March, 2011 was ₹23,662 crore. During 2010-11, an additional capital of ₹2.642 crore was brought in by the industry. The incremental capital during 2010-11 was brought in by the private sector insurers as there was no addition in the capital of LIC, the public sector insurance company.

g) Commission expenses of life insurers

The increase in expenses was lower than the increase in the gross premium collected by the insurers in 2010-11. As such, the commission expenses ratio (commission expenses as a percentage of premiums) declined marginally to 6.29 per cent in 2010-11 from 6.81 per cent of 2009-10. Overall, while the commission expenses increased in the case of regular premium, there has been a fall in the commission paid towards both single and renewal premium products. However, there is some variation in the position when compared between the private insurers and LIC, as reflected in Table 1.9, providing bifurcations of the commission ratios for both private and public sector life insurers.
The operating expenses of the life insurers increased by 14.04 per cent in 2010-11 (11.84 per cent in 2009-10). The operating expenses towards life insurance business were `32,942 crore in 2010-11 as against `28,888 crore in 2009-10.

Operating expenses, as a per cent of gross premium underwritten, increased for LIC from 6.58 per cent in 2009-10 to 8.34 per cent in 2010-11. However, the same declined marginally for private insurers from 20.97 per cent in 2009-10 to 18.11 per cent in 2010-11. For the industry as a whole, the operating expenses ratio increased slightly from 10.88 per cent in 2009-10 to 11.30 per cent in 2010-11.

1.6 INSURANCE SECTOR REFORMS AND REGULATORY FRAMEWORK

Reference was already made to the opening up of the insurance sector to foreign and private enterprise for breaking the monopoly of the public sector in this business. The insurance business can now be undertaken by corporates with foreign participation of 26% of total equity and another 26% to be left to private enterprise leaving the rest for public participation. The main objective of these reforms is to widen the base of public participation in this sector, as recommended by Malhotra Committee.

The IRDA Act was passed in 1999, and immediately thereafter, the Insurance Regulatory and Development Authority of India was set up to oversee the Insurance sector as to promote and regulate it in the public interests. The Banks' and NFBC's entry into the insurance sector is regulated by the RBI guidelines of January and June 2000 and further amendments effected to them from time to time, in the policy announcements of the RBI.

In 1993, Molhotra committee, headed former Finance Minister and RBI Governor R.N.Molhotra was formed to evaluate the Indian Insurance Industry and recommend its future direction. The committee was set up with an objective of complementing the reforms in the Indian Financial Sector. The reforms were aimed at "creating a more efficient and competitive financial system suitable for the requirement of the economy keeping in mind the structural changes currently underway and recognizing that
insurance is an important part of the overall financial system where it was necessary to address the need for similar reforms.”

1.6.1 Malhotra committee –Recommendations:

In 1994, the committee submitted the and gave the following recommendation

Structure
- LIC should be registered as a company under the companies Act and its paid up capital raised from Rs. 5 crores to Rs. 200 crores with Government holding only 50% and the rest by the Public at large. Government stake in the insurance companies to be brought down to 50%.
- Government should take over the holdings of GIC and its subsidiaries so that these subsidiaries can act as Independent Corporation.
- All the insurance companies should be given greater freedom to operate.

Competition
- Private companies with a minimum paid up capital of Rs.1 billion should be allowed to enter the industry.
- No company should deal in both Life insurance and General insurance through a single entity.
- Foreign companies may be allowed to enter the industry in collaboration with the domestic companies.
- Postal Life insurance should be allowed to operate in the rural market.
- Only one State level Life Insurance Company should be allowed to operate each state.
- The Insurance Act Should be changed.
- In Insurance Regulatory, body should be set up.
- Controller of Insurance(currently apart from the Finance Ministry ) should be made independent
Investments

- Mandatory Investment of LIC Life Fund in government securities to be reduced from 75% to 50%.
- GIC and its subsidiaries are not to hold more than 5% in any company (This current holdings to brought down to this level over a period).
- GIC paid up should be raised to Rs. 200 crores of which 50% should be held by the Government and the rest is privatized.

Customer Services

- LIC should pay interest on delays in payments beyond 30 day.
- Insurance companies must be encouraged to set up Unit Linked Pension Plans.
- Computerization of operation and updating of technology to be carried out in the insurance industry.
- The institution of ombudsman should be set up to settle disputes on personal claims up to Rs. 5 lakhs more quickly and reduce litigations.

Overall, committee strongly felt that in order to improve the customer services and increase the coverage of the insurance industry should be opened up to competition. But at the same time, the committee felt the need to exercise caution as any failure on the part of new players could ruin the public confidence in the industry.

1.6.2 RBI and Insurance Reforms:

With the passage of IRDA Act in 1999, and the setting up of Insurance Regulatory and Development Authority of India in 1999, there began a foray into this sector by banks and NBFCs.

RBI has laid down guidelines for FIs and banks to enter into insurance sector in January 2000. These guidelines are broadly set out below:

1. FIs and banks are barred to run insurance business due to high risks involved, either departmentally or through subsidiaries. They could however stake upto 50% in these ventures, along with the Indian partners and foreign investors.
2. Such entrants need to have a net worth of Rs. 500 crores or more and a reasonable level of NPAs, below the industry average.
3. Their CRAR should not be less than 10% of assets.
4. Their subsidiaries should have a satisfactory track record and continuous profitability over the last 3 years.
5. Their share in equity participation in joint ventures of insurance business should not exceed 10% of their net worth or Rs. 50 crores whichever is less.
6. Their participation in Joint Ventures should not exceed 30% of the paid-up capital of the Insurance company, with an important provision, that the total amount invested in all subsidiaries and joint ventures should not exceed 20% of the bank’s or FIs’ networth.
7. Banking business should be kept separate and not contaminated by inducting insurance business into the former due to high risk nature of insurance business.
8. RBI being controller of Foreign exchange has along with the government fixed ceiling of 26% of FDI in insurance sector. More recently in 2005, the Government proposed to raise it to 49%.

The RBI guidelines for NBFCs’ entry into insurance business were released in June 9, 2000. The following are the major highlights of these guidelines:

1. NBFCs’ need a minimum net worth of Rs. 500 crore for entry into insurance joint venture.
2. The maximum stake in insurance Joint Venture is 50% of the paid-up capital of Joint Venture.
3. NBFCs with net owned funds of Rs. 2 crores and above can only act as agents.
4. The minimum CAR is pegged at 15%, if the NBFCs are in loan and investment business with public deposits. Other should have at least 12% CAR, irrespective of whether they accept public deposit or not.
5. Ineligible NBFCs can make investments up to 10% of the owned fund or Rs. 50 crores, whichever is lower, in the insurance company.
6. Those NBFCs qualifying for entry into insurance business will have to apply to RBI for permission. The RBI guidelines for banks were already referred to earlier.

The above guidelines apply only to main insurance business and not to insurance broking, agency or surveying etc. The guidelines for them as also reinsurance business are the responsibility of IRDA.
1.7 INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY (IRDA)

The Insurance Regulatory and Development Authority of India (IRDA) was constituted as an autonomous body to regulate and develop the business of insurance and reinsurance in India. The authority was constituted on April 19th 2000 vide Government of India’s notification no. 277.

The Insurance Regulatory and Development Authority Act-1999, was enacted by parliament in the fiftieth year of the Republic of India to provide for the establishment of an authority to protect the interests of holders of insurance policies, to regulate, promote and ensure orderly growth of the insurance industry and for matters connected there with or incidental there to and further to amend the Insurance Act-1938, the Life Insurance Corporation Act-1956 and General Insurance Business(Nationalization) Act-1972. The act was approved in the parliament in December 1999 and the insurance sector was thrown open for private licenses on august 15th, 2000. IRDA was constituted in terms of the Insurance Regulatory and Development Authority Act-1999, as the regulator of the Indian insurance industry.

IRDA was set up in 1996 but it was formally constituted as a regulator of the insurance industry in April 2000.

1.7.1 Mission of IRDA

The mission statement of the IRDA contains the objectives with which it has been setup. IRDA was established.

1. To protect the interest of and secure fair treatment to policyholders.
2. To bring about speedy and orderly growth of the insurance industry (including annuity and superannuation payments), for the benefit of the common man, and to provide long-term funds for accelerating growth of the economy.
3. To set, promote, monitor and enforce high standards of integrity, financial soundness, fair dealing and competence of those it regulates.
4. To ensure that insurance customers receive precise, clear and correct information about products and services and make them aware of responsibilities and duties in this regard.

5. To ensure speedy settlement of genuine claims, to prevent insurance frauds and other malpractices and put in place effective grievance redressal machinery.

6. To promote fairness, transparency and orderly conduct in financial markets dealing with insurance and build a reliable management information system to enforce high standards of financial soundness among market players.

7. To take action where such standards are inadequate or ineffective enforced.

8. To bring about optimum amount of self-regulation in day-to-day working of industry consistent with the requirements of prudential regulation.

1.7.2 Composition of IRDA

The IRDA would consist of a chairperson and not more than nine members of whom not more than five would be full-time members to be appointed by the government from amongst persons of ability, integrity and standing who have knowledge/experience of life insurance/ general insurance/ actuarial service, finance/ economics/ law/ accountancy/ administration/ any other discipline which in the opinion of the government would be useful to it. Between the chairperson and the full-time directors, at least one person each is required to have knowledge/experience of life, general insurance or actuarial science respectively

1.7.3 Duties/Powers/Functions of IRDA

The duty of the IRDA is to regulate, promote and ensure orderly growth of the insurance and reinsurance business.

Powers and Functions: The powers and functions of the IRDA, inter-alia, are stated below;

a) Issue to the applicant a certificate of registration; to renew, modify, withdraw, suspend or cancel such registration, preference in registration to be given to companies providing with health insurance.
b) Protection of the interests of policyholders in matters concerning assigning of policy, nomination by policy-holders, insurable interest, settlement of insurance claim, surrender value of policy, and other terms and conditions of contracts of insurance.

c) Specifying requisite qualifications and practical training for insurance intermediaries and agents.

d) Specifying the code of conduct for surveyors and loss assessors.

e) Promoting efficiency in the conduct of insurance business.

f) Promoting and regulating professional organizations connected with the insurance and reinsurance business, levying fees and other charges for carrying out the purposes of the IRDA Act.

g) Calling for information from, undertaking inspection of conducting enquiries and investigations, including audit of insurers, insurance, intermediaries and other organizations connected with the insurance business.

h) Control and regulation of the rates, terms and conditions that may be offered by insurers in respect of general insurance business not so controlled and regulated by the Tariff Advisory Committee under section 64U of the insurance Act, 1938(i) Specifying the form and manner in which books of account would be maintained and statement of accounts rendered by insurers and insurance intermediaries.

i) Regulating investment of funds by insurance companies, regulating maintenance of margin of solvency.

j) Adjudication of disputes between insurers and intermediaries or insurance intermediaries.

k) Supervising the functioning of the Tariff Advisory Committee.

l) Specifying the percentage of premium income of the insurer to finance schemes for promoting and regulating professional organizations referred to above.
m) Specifying the percentage of life insurance and general insurance business to be undertaken by the insurer in the rural or social sector.

n) Exercising such other powers as may be prescribed.

The powers and functions mentioned above would enable the IRDA to perform the role of an effective watchdog and regulator for the insurance sector in India.

**Issue of Directions:** The IRDA would be bound by the directors of Government on questions of policy, other than those relating to technical and administrative matters, in writing form time to time. The decision of the Government, whether a question is one of policy or not, would be final.

**Supersession:** The government may, by notification and for specified reasons supersede the IRDA for a period not exceeding six months in circumstances specified below and during the period of supersession appoint a person to act as the controller of insurance (COI) under the insurance Act, 1938.

i. On account of circumstances beyond its control, the IRDA is unable to discharge its functions/perform its duties.

ii. Persistent default by it in complying with any direction given by the government under the IRDA Act or in discharge of functions/performances of duties imposed on it by/under the provisions of IRDA Act and as a result of such default the financial position of the IRDA has suffered.

iii. Circumstances exist which render it necessary in public interest to do so.

**1.7.4 Insurance Advisory Committee:**

The IRDA may constitute a 25-member Insurance Advisory Committee (IAC) to represent the interest of commerce, industry, transport, agriculture, consumer fora, surveyors, agents, intermediaries, including brokers, consultants and loss assessors, organizations engaged in safety and loss prevention, research bodies and employees.
associations in the insurance sector, to advise it on matters relating to making regulations by it and on such other matters as may be prescribed.

1.7.5 Amendment of LIC Act, 1956: According to this amendment, the exclusive privilege (monopoly) of the LIC ceases so as to enable other Indian insurance companies to do life insurance business. An Indian insurance company is a company registered under the companies Act, (i) in which the aggregate equity holdings of a foreign company as defined in Section 2(23-A) of Income Tax Act, 1961, by itself or through subsidiaries/nominees does not exceed 26 per cent of the paid-up capital, and (ii) whose sole purpose is to carry on general/life business.

1.7.6 Amendment of General Insurance Business (Nationalization) Act, 1972: The amendment provides that the exclusive privilege (monopoly) of the GIC and its four subsidiaries would cease and the other Indian insurance companies can carry on non-life insurance business.

1.7.7 Amendment to Insurance Act, 1938: To update certain outdated provisions and for an efficient and smooth regulation of the opened up insurance sector, consequential amendments have been introduced in the Insurance Act. The main provisions relating to these amendments are listed below.

Transfer of Powers: All the powers of the erstwhile COI under the IRDA Act are transferred to and are now vested with the IRDA.

Delegation of Powers: The powers of the central government relating to the under mentioned activities/operations of insurance companies have been delegated to the IRDA.

* Investment of assets including additional provisions (Sections 27, 27-A and 27-B).
* Maintaining the assets of insurers (Sections 31)
* Prohibition of common officers and requirements as to whole-time officers (Section 32)
* Limitation of expenditure on commission (Section 40-A).
* Provisions regarding directors (Section 48-B).
• Executive committees of the life insurance/general insurance councils (Section 64-F), resignation and filling of casual vacancies (64-G), powers of executive committees of the Life Insurance Council to hold examinations of insurance agents (64-I), functions of executive committees of Life Insurance Council(64-J), functions of the executive committee of the General insurance advisory committees to regulate rates, advantage, terms and conditions (64-UC), and licensing of surveyors and loss assessors (64-UM).
• Acquisitions of surrender values by policyholders (section 113).
• Alteration of forms (section 115).

Other Provisions/Amendments

In addition to the above, some important amendments in the Insurance Act provide for the following.

Section 2-C (Prohibition of Transaction of Insurance Business) On or after the commencement of the IRDA, only Indian insurance companies can carry out any class of insurance business in India.

Section 3 (Registration)

i. Every application for registration to carry on insurance business should be made in such manner as may be determined by regulations made by the IRDA; preference in registration would be given to companies providing health insurance.

ii. The registration fee would be determined by the IRDA regulations not exceeding Rs 50,000 for each class of business.

iii. Registration can be cancelled if the insurer default in complying with or acts in contravention of any requirement of (a) the Insurance Act or any rule/regulation/order made or any directions issued under it; (b) the companies Act, LIC Act, General Insurance Business (Nationalization) Act and Foreign Exchange Regulation (Management) Act, and (c) directions made/issued by the IRDA under the IRDA Act.
iv. The cancelled registration can be revived if the IRA is satisfied, Inter alia, that the insurer has complied with any requirement of the Insurance Act or the IRDA Act or of any rule/regulations/order made or directions issued under these Act.

v. The IRDA may suspend/cancel any registration in such manner as may be determined by the regulations made by it.

vi. The IRDA may, on payment of fee not exceeding Rs. 5,000 as may be determined by the regulations, issue a duplicate certificate of registration to replace a certificate lost/destroyed/mutilated or in any other case where the IRDA is of the opinion that the issue of duplicate certificate is necessary.

Section 3-A (Renewal of Registration) An insurer, who has been granted a certificate of registration, should have the registration renewed annually with each year ending on March 31 after the commencement of the IRDA Act. The application for renewal should be accompanied by a fee as determined by IRDA regulations, not exceeding one-fourth of one per cent of the total gross premium income in India in the preceding year or Rs 5 crore or whichever is less, but not less than Rs. 50,000,000 for each class of business.

Section 6 (Requirements as to Capital) The minimum paid-up equity capital (excluding required deposits with the RBI and any preliminary expenses in the formation/registration of the company) requirement of an insurer would be Rs 100 crore to carry on life/general insurance business and Rs 200 crore to exclusively do reinsurance business.

Section 6-A (Requirements as to Capital Structure/Voting Rights/Registers of Beneficial Owners) Prior approval of the IRDA is must in the case of transfer of shares, where after transfer, the total paid-up holding of the transferee in the shares of the company is likely to exceed 5 per cent of its paid-up capital and 2.5 per cent if the transferee is a banking/investment company. The IRDA's okay is also essential where the nominal value of the shares to be transferred by any individual/firm/group/constituents of a group/body corporate under the same management jointly or severally exceeds 1 per cent of paid-up capital of the insurer.
Section 6-AA (Divesting of Excess Shareholding) A promoter cannot hold more than 26 per cent or such other percentage as may be prescribed of the paid-up capital in an Indian insurance company. If, however, the promoters hold more than 26 per cent of the paid-up capital where an Indian company starts insurance business, they would have to divest the excess in a phased manner after the government may prescribe a period of 10 years from the date of commencement of business or within such period as. The manner and procedure for divesting the excess share capital would be specified by IRDA regulations. However, if the promoters are a foreign company, FIIIs, NRIs/OBCs they will not be allowed to hold more than 26 per cent under any circumstances.

Section 7 (Deposits) Every insurer in India has to keep a deposit in respect of the insurance business with the RBI for and on behalf of the government in cash/approved securities estimated at the market value on the day of deposit. This is 1 per cent and 3 per cent of his total gross premium written in India in any financial year but not exceeding Rs 10 crore in case of life insurance business, the deposit requirements is Rs 20 crore.

Section 27-D (Investment of Funds outside India): The funds of policy holders cannot be invested by insurers outside India.

Section 27-C (Investment of Funds outside India): The funds of policy-holders cannot be invested by insurers outside India.

Section 27-D (Manner and Conditions of Investment): In addition to the requirement of Section 27, 27-A and 27-B, the IRDA may, in the interest of the policy-holders, specify the time, manner and other conditions of investment of assets held by an insurer for the purpose of the Insurance Act. Taking into account the nature of business and to protect the interest of the policyholders, the IRDA may also issue directions to insurers relating to the time, manner and other conditions of investment of assets held by them.

Section 31-B (Power to Restrict Payment of Excessive Remuneration): The IRDA may issue appropriate direction to insurers who are paying remuneration by way of commission or otherwise on a scale disproportionate to normal standards prevailing in insurance business resources of the insurer. The insurer has to comply with these
directions within six months. Every insurers should, before the close of the month following every year, submit to it a statement in the form as specified by the IRDA in its regulations of remuneration paid to any person in excess of Rs.5,000 in that year.

**Section 32-B (Insurance Business in Rural/Social Sector):** After the commencement of the IRDA Act, 1999, every insurer would have to undertake such percentage of life/general insurance business in the rural/social sector as may be specified by the IRDA in this behalf. It is mandatory for the new companies to meet the obligations relating to the rural and unorganized sector.

**Section 33 (Power to Investigation/Inspection):** The IRDA may, at any time, order in writing a person as investigating authority to investigate the affairs of any insurer and report to it.

**Section 40-A (Limitation of Expenditure of Commission):** No person can pay to an insurance agent remuneration by way of commission an amount exceeding 15 per cent of the premium payable on the policy relating to fire/marine/miscellaneous insurance.

**Section 102 (Penalty for Default):** If any person required under the Insurance Act/rules/regulations fails to (i) furnish and document/statement/account/return/report to the IRDA, (ii) comply with its directions (iii) maintain solvency margin, (iv) comply with directions on the insurance treaties would be liable to a penalty of up to Rs 25 lakhs for each such failure and punishable with fine.

**Section 103 (False Statement):** If a person makes a false statement/furnishes any false document, statement, account, return or report knowingly or does not believe to be true, he would be (i) liable to a penalty up to Rs 25 lakh for each such failure; and (ii) punishable with imprisonment which may extend to three years or with fine for each such failure.

**Section 104 (Penalty for Non-compliance):** The penalty for non-compliance of the provisions of the Insurance Act relating to investment of assets is Rs.25 lakh for each failure.
Section 105 (Wrongly Obtaining/Withholding Property): The penalty for each failure by any director/managing director/Manager/other officer(s)/employee(s) of an insurer wrongfully obtaining possession of any property or applying to any purpose of the Insurance Act would be up to Rs.25 lakh.

Section 105-B (Failure to Comply): If an insurer fails to comply with the provisions of Section 32-B relating to insurance business in the rural/social sector, he would be liable to a penalty up to a maximum of Rs 25 lakh for each such failure. He would also be punishable with imprisonment up to three years or with fine.

Section 114-A (Power to Make Regulations): The IRDA may make regulations consistent with the Insurance Act/rules/regulations to carry out its provisions to provide, in particular, for all or any of the following.

i. Matters relating to registration of insurers.
ii. The manner of suspension or cancellation of registration.
iii. Such fee, not exceeding Rs.5, 000, as may be determined by the regulations for the issue of a duplicate certificate of registration.
iv. Matters relating to renewal of registration.
v. The manner and procedure for divesting excess share capital
vi. Preparation of the balance sheet, profit and loss account and a separate account of receipt and payments and revenue account.

vii. The manner in which an abstract of the report of the actuary is to be specified.

viii. The form and the manner in which the statement of business in force should be appended.

ix. The time, manner and the other conditions of investment of assets held by an insurer.

x. The minimum information to be maintained by an insurer in their books, the manner in which such information should be maintained, the checks and other verification to be adopted by insurers in that connection and all other matters incidental thereto.
xi. The manner of making an application, the manner and the fee for issuing a licence
to act as an insurance agent.

xii. The fee and the additional fee to be determined for renewal of licence of an
insurance agent.

xiii. The requisite qualifications and practical training to act as an insurance agent.

xiv. The passing of examination to act as an insurance agent.

xv. The code of conduct of an insurance agent.

xvi. The fee not exceeding Rs 50 for the issue of a duplicate licence.

xvii. The manner and the fees for the issue of a license to any intermediary or an
insurance intermediary.

xviii. The fee and the additional fee to be determined for the renewal of license of
intermediaries or insurance intermediaries.

xix. The requisite qualifications and practical training of intermediaries or insurance
intermediaries.

xx. The fee and the additional fee to be determined for the renewal of license of
intermediaries or insurance intermediaries.

xxi. The code of conduct for an intermediary/insurance intermediary.

xxii. The fee for the issue of a duplicate license.

xxiii. Matters as relating to the Tariff Advisory Committee.

xxiv. Matters relating to the licensing of surveyors and loss assessors, their duties,
responsibilities and other professional requirements.

xxv. Such other asset or assets as may be specified for evaluating the purposes of
ascertaining sufficiency or assets.

xxvi. The valuation of assets and liabilities.

xxvii. Matters relating to the sufficiency of assets.

xxviii. Matters relating to reinsurance.

xxix. Matters relating to the redressal of grievances of policyholders to protect their
interest and to regulate promote and ensure orderly growth of the insurance industry.

xxx. Any other matter which is to be, specified by the IRDA regulations or in respect
of which provisions are to be made or may be made by the regulations.
1.7.8 IRDA REGULATIONS

The IRDA regulations covered in this section are:

i. Rural/Social sector obligations
ii. Insurance advertisement and disclosures
iii. Licensing of insurance agents
iv. General insurance –reinsurance
v. Appointed actuary
vi. Asset, liabilities and solvency margins
vii. Registration of Indian insurance companies.
viii. Investment norms
ix. Preparation of financial statements and auditors reports
x. Third party administrators
xi. Protection of policyholders’ interest.
 xii. Corporate/Composite corporate agents
 xiii. Insurance brokers
xiv. Distribution of surplus funds
 xv. Life insurance –reinsurance
 xvi. Insurance surveyors and loss assessor and micro-Insurance.

1.7.9 RURAL/SOCIAL SECTOR OBLIGATIONS:

The rural and social sector obligations of (1) new and (2) existing insurers and discussed below.

A) New Insurers:

Every new insurer, for the purposes of Sections 32-B and 32-C of the Insurance Act, has to undertake during the first five financial years the following obligations pertaining to persons in (a) rural and (b) social sectors.
**Rural Sector:** The rural sector means the places/areas classified as rural by the population census of India. The percentages in respect of a life insurer and general insurer in the rural sector are specified below.

**Life Insurer:** of the total policies written in that year, (i) first financial year, 7 per cent (ii) Second financial year, 9 per cent (iii) third financial year 12 per cent (iv) fourth financial year, 14 per cent (v) fifth financial year, 16 per cent., and (vi) sixth year, 18 per cent.

**General Insurer:** The percentage share in the first two financial year should be 2 and 3 per cent respectively and thereafter 5 per cent of total gross premium income written direct in that year.

**Social Sector:** The Social sector includes unorganized sector, informal sector and social sector

Economically vulnerable or backward classes (i.e. persons below the poverty Line) and other categories of persons(i.e. persons with disability as defined in the Persons with Disabilities (Equal opportunities, Protection of Rights and Full Participation) Act and who may not be gainfully employed and also includes Guardians who need insurance to protect spastic persons/persons with disability.)

The unorganized sector includes self-employed workers such as agricultural laborers, bid workers, brick-kiln workers, carpenters, cobbler, construction workers, fishermen, hamals, handicraft artisans, handloom and khadi workers, lady tailors, leather and tannery workers, papad makers, power loom workers, physically disabled self-employed persons, primary milk products, rickshaw pullers, safari karamcharis, salt growers, sericulture workers, sugarcane cutters, tendu leaf collectors, toddy tappers, vegetables vendors, washerwomen, working women in the hills or such other categories. Included in the informal sector are small scale, self-employed workers typically at low level of organization and technology, with the primary objective of generating employment and income with heterogeneous activities like retail trade, transport, repairs and maintenance, construction, personal and domestic services, and manufacturing with
the work mostly labour-intensive having often unwritten and informal employee-employer relationship. All categories of insurers are obliged to insure 5, 7, 10, 15, 20 and 25 thousand lives in the first 6 financial years respectively. However, where an insurance company is in operation for more than 6 months in a financial year, no rural/social sector obligations would be applicable and the annual obligations would be reckoned from the next financial year (i.e. the first full year of operation). Where an insurance company commences cooperation in the first half of the financial year, the applicable obligations for the first year would be 50 per cent of the annual obligation. However, in the case of general insurers, these obligations would also include crop insurance.

Every new issuer should ensure that he undertakes the following obligations during the sixth financial year of operations: (i) in respect of life insurers, 18 per cent of the total policies written direct would be in the rural sector, (ii) in case of non-life insurance, 5 per cent total gross premium income written direct should be in the rural sector, and (iii) 25,000 new lives should covered in the social sector in respect of all insurers.

Obligations After The Sixth Financial Year: (a) Rural Sector: (i) in respect of life insurer, of the total written direct in that year, 18 per cent, 19 per cent and 20 per cent in the 7th, 8th, 9th and 10th year and beyond respectively, (ii) in respect of general insurer, of the total gross premium income written direct in that year, 5 per cent, 6 per cent and 7 per cent in the 7th, 8th and 9th and 10th financial years and beyond respectively; (b) Social Sector: in respect of all insurers, 25,000, 35,000, 45,000 and 55,000 lines in 7th, 8th, 9th, and 10th financial year and beyond respectively.

B) Existing Insurers:

The obligations of existing insurers (i.e the LiC and GIC) would be decide by the IRDA in consultation with them but the quantum of insurance business to be done pertaining to rural and social sectors would not be less than what has been recorded by them for the accounting year ended March 31, 2002. The IRDA would review the quantum periodically and give directions to them for achieving the specified targets.
The obligations towards the rural/social sectors from the financial year 2007-08 to 2009-10 and beyond are as follows.

(a) **LIC**: The rural Sector obligations are 24 per cent (2004-08) and 2009-10 and beyond, of the total policies written in that year. The social sector obligations are 20 lakh lives in the financial year 2007-08 and beyond.

(b) **General Insurers**: (a) **Rural Sector**: 6 per cent and 7 per cent of the total gross premium income written direct in that year respectively in 2007-08 and 2008-09 and beyond; (b) **Social Sector**: For the financial years 2008-09 and 2009-10 and beyond, the obligations would increase by 10 per cent over the previous year (s).

The term 'lives' refer to human lives insured as at the end of each financial year. The re-insurance premium should not be included while calculating the obligations of the insurers in respect of the rural and social sectors. The IRDA may prescribe/revise these obligations from time to time. The compliance with these obligations towards the rural/social sectors should be based on the sale of product in a way that the stipulations as to the minimum amount of cover as laid down in the IRDA Micro-Insurance Regulations. Every insurer should submit a return to the IRDA disclosing the level of compliance during the year in respect of these obligations.

### 1.8 PROTECTION OF POLICYHOLDERS' INTEREST REGULATIONS

These regulations are in addition to any other regulations made by the IRDA, which may, inter alia, provide for protection of the interest of the policy holders. They apply to all insurers, insurance agents, insurance intermediaries and policyholders. Their main elements are (1) Point of sale, (2) Proposal for insurance, (3) grievance redressal procedure; (4) matters to be stated in life insurance policy, (5) matters to be stated in general insurance policy; (6) claims procedures in respect of life insurance policy, (7) claims procedures in respect of general insurance policy, (8) policy holders’ servicing and (6) general.
1.8.1 Point of Sale

A prospectus (i.e. a document issued by an insurer or in its behalf to the prospective buyer of insurance containing such particulars as are mentioned in Rule 11 of Insurance Rules and includes a brochure/leaflet. It should also specify the type and character of riders on the main product indicating the nature of benefits following thereupon) of an insurance product should clearly state the scope of benefits, the extent of insurance cover (i.e. an insurance contract whether in the form of a policy/cover note/certificate of insurance/any other form prevalent in the industry to evidence the existence of an insurance cover) and in an explicit manner explain the warranties/exceptions/conditions of the insurance cover and, in case of life insurance, whether the product is participating (with benefits) or non-participating (without benefits). The allowable riders(s) on the product should clearly spell out with regard to their scope of benefits and, in no case, the premium relatable to health-relatable to health-related or critical illness riders in case of term/group products should exceed 100 per cent of premium under the basic product. All other riders put together should be subject to a ceiling of 30 per cent of the premium of the basic product. Any benefit arising under each of the riders should not exceed the sum assured under the basic product. However, the benefit amount should be subject to section 2(11) of the insurance Act.

An insurer/its agent/other intermediary should provide all material information in respect of a proposed cover to the prospect to enable him to decide on the best cover that would be in his/her interest. Where the prospect depends upon their advice, they must advice him dispassionately. If, for some reason, the proposal and other connected papers are not filled by the prospect, a certificate may be incorporated at the end of the proposal form (i.e. a form to be filled in by the proposer for insurance for furnishing all material information (that is, all important, essential and relevant information in the context of underwriting the risk covered by the insurer) required by the insurer in respect of a risk in order to enable the insurer to decide whether to accept or decline to undertake the risk and in the event of acceptance of the risk, determine the rates/terms/conditions of a cover to be granted) from the
prospect that the contents of the form and documents have been fully explained to
him and that he has fully understood the significance of the proposed contract.

In the process of sale, the insurer/its agent/any other intermediary should act
according to the code of conduct prescribed by (i) the IRDA, (ii) Councils established
under Section 64-C of the Insurance Act and (iii) the recognized professional
bodies/association of which they are members.

1.8.2 Proposals for Insurance

Except in cases of marine insurance cover, where current market practice do
not insist on a written proposal form, in all cases, a proposal for grant of a cover,
either for life business or for general business, must be evidence by a written
document. An insurer should furnish a copy of the proposal form to the insured free
of charge, within 30 days of the acceptance of a proposal. The forms and documents
used in the grant of cover may, depending upon the circumstances of each case, be
made available in languages recognized under the Constitution of India. In filing the
form of proposal, the prospect is to be guided by the provisions of Section 45 of the
Insurance Act. Any proposal form seeking information for grant of life cover may
prominently state the requirements of Section 45 of the Insurance Act. Where a
proposal form is not used, the insurer should record the information obtained orally or
in writing, and confirm it within 15 days with the proposer and incorporate the
information in its cover note or policy. The onus of proof would rest with the insurer
in respect of any information not so recorded, where the insurer claims that the
proposer suppressed any material information or provided misleading or false
information on any matter material to the grant of a cover.

Whether the benefit of nomination is available to the proposer, in terms of the
insurance Act or the conditions of policy, the issuer should draw the attention of the
proposer to it and encourage the prospect to avail the facility. The insurer with speed
and efficiency should process the proposals and all decisions should be
communicated by it in writing within a reasonable period not exceeding 15 days from
receipt of proposals by the insurer.
1.8.3 Matters to be stated in Life Insurance Policy

A life insurance policy should clearly state:

a) The name of the plan governing the policy, its terms and conditions.

b) Whether it is participating in profits or not;

c) The basis of participation in profits such as cash bonus, deferred bonus, simple or compound reversionary bonus;

d) The benefits payable and the contingencies upon which these are payable and the other terms and conditions of the insurance contract;

e) The details of the riders attaching to the main policy;

f) The date of commencement of risk and the date of maturity or date(s) on which the benefits are payable;

g) The premium payable, periodicity of payment, grace period allowed for payment of the premium, the date of the last installment of premium, the implication of discontinuing the payment of installments(s) of premium and also the provisions of a guaranteed surrender value.

h) The age at entry and whether the same has been admitted.

i) The policy requirements for (a) conversion of the policy into paid-up policy, (b) surrender, (c) non-forfeiture and (d) revival of lapsed policies;

j) Contingencies excluded from the scope of the cover, both in respect of the main policy and the riders;

k) The provision for nomination, assignments and loans on security of the policy and a statement that the rate of interest payable on such loan amount would be as prescribed by the insurer at the time of taking the loan;
l) Any special clauses or conditions, such as, first pregnancy clause, suicide clause and so on;

m) The address of the insurer to which all communications in respect of the policy should be sent;

n) The document that are normally required to be submitted by a claimant in support of a claim under the policy;

While forwarding the policy to the insured, the insurer should inform him that he has a period of 15 days from the date of receipt of the policy document to review the terms and conditions of the policy, and where he disagrees to any of those terms or conditions, he has the option to return the policy stating the reasons for his objection, when he would be entitled to a refund of the premium paid, subject only to a deduction of a proportionate risk premium for the period on cover and the expenses incurred by the insurer on medical examination of the proposer and stamp duty changes. In respect of a unit linked policy, in addition to the above deductions, the insurer would also be entitled to repurchase the unit at the price of the units on the date of cancellation. In respect of cover, where premium charged is dependent on age, the insurer should ensure that the age is admitted as far as possible before issuance of the policy document. In case, where age has not been admitted by the time the policy is issued, the insurer should make efforts to obtain proof of age and admit the same as soon as possible.

1.8.4 Claims Procedure of a Life Insurance Policy:

A life insurance policy should state that the primary documents which are normally required to be submitted by a claimant in support of a claim. Upon receiving a claim, it should process the claim immediately. Any queries or requirement of additional documents, to the extent possible, should be raised all at once, within a period of 15 days of the receipt of the claim. A claim should be paid or disputed giving all the relevant reasons, within 30 days from the date of receipt of all relevant papers and clarifications required. Where, in the opinion of the insurance
company, the circumstances of a claim warrant an investigation, it should initiate and complete such investigation at the earliest, and in any case not later than 6 months from the time of lodging the claim.

Subject to the provision of section 47 of the Insurance Act, where a claim is ready for payment but the payment cannot be made due to any reasons of a proper identification of the payee and such an amount would earn interest at the rate applicable to a savings bank account with a scheduled bank (effective from 30 days following the submission of all papers and information). Where there is a delay on the part of the insurer in processing a claim for a reason other than the one covered above, it should pay interest on the claims amount at a rate which is 2 per cent above the bank rate prevalent at the beginning of the financial year in which the claim is reviewed by it.

1.8.5 Policyholder servicing

An insurer carrying on life or general business, should at all times, respond within 10 days of the receipt of any communication from its policyholders in all matters, such as:

a) Recording change of address
b) Noting of new nomination or change of nomination under a policy
c) Noting an assignment on the policy
d) Providing information on the current status of a policy indicating matters, such as, accrued bonus, surrender value and entitlement to a loan
e) Processing papers and disbursal of a loan on security of policy.
f) Issuance of duplicate policy

Issuance of an endorsement under the policy noting a charge of interest or sum assured or perils insured, financial interest of a bank and other interests; and Guidance on the procedure for registering a claim and early settlement
1.9 INVESTMENT PATTERN AND POLICY

The provisions of the Insurance Act, 1938, have governed the pattern of investment of LIC funds. Till very recently, it had to invest at least 50 percent of its controlled funds in government and other approved securities; 15 percent in “other” investments which included loans to state governments for housing and water supply schemes, municipal securities not included in category one, government guaranteed loans to municipal committees and co-operative sugar factories; and up to 35 percent in “approved” investments which included shares and debentures of public and private limited companies, of co-operative societies, immovable property, loans to its policy-holders, and fixed deposits with scheduled banks and co-operative societies. It is to be noted that while it was the minimum percentage which was specified for categories one and two, for category three the maximum proportion had been specified. The authorities have modified these provisions sometime back. The portfolio restrictions which were in force since 1995 and which are in force in 2001-02 are given in Tables 1.1 AND 1.2.
Table 1.1: Portfolio Restrictions on LIC and GIC Effective from 1995

<table>
<thead>
<tr>
<th>LIC Investments in</th>
<th>LIC Percent</th>
<th>GIC Investments in</th>
<th>GIC Percent</th>
</tr>
</thead>
<tbody>
<tr>
<td>i) Central Government marketable securities being not less than</td>
<td>20</td>
<td>(i) Central govt. securities being not less than</td>
<td>20</td>
</tr>
<tr>
<td>ii) Loans to Housing Bank including (i) above, being not less than</td>
<td>25</td>
<td>(ii) State govt. securities and other government guaranteed securities including (i) above, being not less than</td>
<td>30</td>
</tr>
<tr>
<td>iii) State govt. securities including govt. guaranteed marketable securities, inclusive of (ii) above being not less than</td>
<td>50</td>
<td>(iii) Loans to HUDCO and to state Govts. For housing and firefighting equipment, not less than</td>
<td>15</td>
</tr>
<tr>
<td>iv) Socially oriented sectors including public sector, cooperative sector house building by policy holders, own your house scheme, inclusive of (iii) above not less than</td>
<td>75</td>
<td>(iv) Market sector not more than</td>
<td>55</td>
</tr>
<tr>
<td>v) Private corporate sector, loans to policy-holders for construction and acquisition of innovative property</td>
<td>25</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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Table 1.2: Portfolio Restrictions on Life Insurance and General Insurance in Force in 2001-02.

<table>
<thead>
<tr>
<th>S. No</th>
<th>Type of Investment</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Life Insurance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>I.</td>
<td>Government Securities</td>
<td>25%</td>
</tr>
<tr>
<td></td>
<td>Government Securities or other approved securities (including (i) above)</td>
<td>Not less than 50%</td>
</tr>
<tr>
<td>II.</td>
<td>Approved Investments as specified in Schedule – I</td>
<td>Not less than 15%</td>
</tr>
<tr>
<td></td>
<td>Infrastructure and Social Sector</td>
<td>Not exceeding 35%</td>
</tr>
<tr>
<td>III.</td>
<td>Others to be governed by Exposure Norms. (Investments) in ‘Other than in Approved Investments’ in no case exceed 15% of the Fund</td>
<td></td>
</tr>
<tr>
<td>General Insurance</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(i)</td>
<td>Central Government Securities being not less than</td>
<td>20%</td>
</tr>
<tr>
<td>(ii)</td>
<td>State Government Securities and other Guaranteed securities including (i) above being not less than</td>
<td>30%</td>
</tr>
<tr>
<td>(iii)</td>
<td>Housing and Loans to State Government for Housing and Fire Fighting equipment, being not less than</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Investments in Approved Investments</td>
<td>Not less than 10%</td>
</tr>
<tr>
<td></td>
<td>a) Infrastructure and Social Sector</td>
<td></td>
</tr>
<tr>
<td></td>
<td>b) Others to be governed by Exposure Norms. However the investments in ‘Other than in Approved Investments in no case exceed 25% of the Assets</td>
<td>Not exceeding 55%</td>
</tr>
</tbody>
</table>

Source: IRDA, Annual Reports
1.9.1 Major Principles Guiding LIC’s Investment Policy

The major principle underlying LIC investment policy appears to be security of funds; maximization of the rate of return on investment is of secondary importance. Therefore, the investment for speculative purposes or in assets which promise high capital gains have to be strictly avoided by insurance companies. The basis of investment policy in India is broadly similar to the one followed by insurance companies in other countries. The high prescribed ration of investment in government securities was partly to ensure the provision of funds to the public sector.

A second principle (related to the first one) governing the LIC investments are that it should finance priority sectors and socially desirable activities in the economy. It is for this reason that a certain minimum ratio has been laid down for investment in 'other' assets. In view of India's mixed economic system, it is necessary that financial institutions meet part of the financial requirements of the private sector. The LIC is therefore allowed to hold part of its funds in the form of industrial securities. Contrary to popular belief, the proportion of the LIC funds (35 percent) earlier allowed to be invested in industrial securities in India was higher than the ration allowed in many other countries. For example, insurance companies can invest in shares only up to 25 percent in Canada, 30 percent in Canada, 30 percent in Japan, and 15 percent in Norway, of their respective total investible resources. While LIC is allowed to invest in industrial securities, it is required to spread such investments widely in order to minimize the risk. The government has laid down periodically the maximum proportion of equity capital of any one company, which LIC can hold.

The LIC's investment in industrial securities has been a matter of considerable public controversy in India. The ideological bickering rather than an understanding of investment principles, financial requirements of different sectors, and the overall availability of funds to those sectors have aggravated the situation. All the parties concerned – industrialists, radicals, and the LIC management – have to be blamed for this state of affairs. The "socialists" have perhaps ungenerously criticized LIC for favoring the private sector, overlooking the fact that a certain portion insurance funds has to be
invested in assets yielding a high rate of return if policy-holders are to benefit, and that LIC investment in "approved" securities has always been far below the prescribed level. The criticism of the "socialists" would have been invalid had the management invested LIC funds in a large number of small, needy companies instead of providing a large amount of funds to a few well established, big business houses. Similarly, there was no justification for the private sector to interpret as backdoor nationalization the policy of increasing the proportion of a given company's share capital, which LIC can hold from 10 percent to 30 percent.

How far the investment policy of LIC helped policyholders' has Is there a need for changing the prescribed pattern of investment for policyholder's benefit? There are many who think that LIC policyholders have not received a fair deal; that they pay high premium rates but receive low bonus rates. Major factors behind this state of affairs are high expense ratio, high premium rates which are not related to the actual mortality experience (i.e., they have remained high although mortality rates have gone down), and low rates of return on LIC investments. The first two factors do not concern us here. As far as the third is concerned, it is not possible to change the prescribed pattern of investments under Indian conditions. LIC has to provide funds to the priority sectors and to government. It is, however, possible to increase the rate of interest on these investments. Once the rate of interest on government investments is appropriately raised, greater benefits would accrue to policyholders within the present framework.

1.10 CAPITAL REQUIREMENTS OF INSURANCE COMPANIES

Section 6 of the Insurance Act, 1938 and the regulations framed there under lay down the minimum entry-level pre-requisites for registration of Indian Insurance companies. Any company proposing to carry on life or general insurance business shall have a paid up capital of Rs.100 crore. In case of a re-insurer, the requirement has been placed at Rs.200 crore. The foreign joint venture partner, either by itself or through its subsidiary companies or its nominees, may participate to the extent of 26 per cent of the paid up equity in the insurance company. The guiding principle for laying down such stringent requirement has been as much to restrict entry to reputed groups with long-term
commitments and also to ensure that adequate capital is injected to fund various requirements evolving with operations and to fuel growth of the insurer.

Fundamentally, while carrying out their operations, insurance companies require capital to take care of the effect of the statutory reserve; the actual cost of acquiring business and the strains associated with the business acquired which could be substantial; and losses likely to result from the insurance and/or the investment risks associated with the business. In addition, the insurer is required to bear the expenses towards IT, costs of training its agent force and advertisement and sales promotion expenses. The statutory stipulations of meeting the solvency requirements sometimes necessitate injection of capital at regular intervals. These aspects are elaborated upon in the ensuing para:

A life insurer expects to cover its expenses through the loadings on premium rates for conventional business and the charges it levies on unit-linked business. Any excess of the actual expenses over the expense loadings in the premium rates and the charges on unit-linked business, because of initial expense overrun results in deficit in the Revenue Account (Policyholders’ Account). Funding the deficit in the Revenue Account requires injection of capital at regular intervals.

The insurer has to undertake certain initial expenses towards commencement of business operations. These costs along with a timeframe for achieving economies of scale to bring the actual expenses in line with expense loading and operating charges may sometimes result in expense overrun during the said timeframe. These expenses need to be funded with regular injection of capital.

The regulatory requirements do not allow the insurers to tap any other avenue for funding their activities than through capital infusion through the shareholders. The registration requirements prohibit insurers from resorting to borrowings to fund their activities.

For expanding their operations through new products, services and territories, insurers who already have a deficit in the Revenue Account, may have to inject further equity at
regular intervals. Similarly, extension of further services and/or putting in place systems to improve their existing operations may also require additional capital expenditure.

IRDA (Assets, Liabilities and Solvency Margin of Insurers) Regulations, 2000 mandates insurers to set up required reserves in respect of insurance liabilities on a prudent basis. The first year premium received from the policyholders would not be sufficient to establish such reserves due to initial high acquisition costs of new business (also referred to as initial business strain). The initial business strain and the manner of its release over the term of the policy would vary with the features of the individual products launched by the insurers.

The lapse rate of the insurer could be an additional reason for the strain on the Policyholders' Account. The insurer expects to cover the initial strain on its capital over the term of the policy. However, a high lapse rate could cause a drain on the capital of the insurer. Lapse control mechanisms that include special campaigns for educating customers/prospective customers, special revival campaigns, incentives to the marketing officials to control first premium lapses, and training for agents to emphasize upon need-based marketing of insurance products are all part of the strategies adopted by the insurers to control the lapse rates.

Induction of capital is also influenced by the regulatory stipulation to provide for the solvency margin requirements. Further, these requirements also grow as the business of the insurers grows. Presently, the Authority has prescribed a solvency margin of 150 per cent of the Required Solvency Margin.

During 2003-04, the Authority, while interpreting the provisions of Section 49 of the Insurance Act, 1938, issued directions to all life insurers stipulating stringent conditions under which insurers could declare bonus in the absence of actuarial surplus. The conditions laid down by the Authority provide that the deficit in the Revenue Account can be wiped out through a transfer of the surplus in the Shareholders' Account or by drawing upon the shareholders' equity capital. This direction issued by the Authority, in some instances, required further injection of equity capital by the
shareholders. Insurers have injected further equity capital in their operations to meet the demand of the competitive market conditions for declaring bonus.

The premium rates and charges for life insurance products are based on the actuarial assumptions on the identified parameters, which include investment returns, operating expenses, inflation, lapse rates, mortality and morbidity rates, and applicable tax provisions. If there is a negative deviation in the actual experience as against what was anticipated at the time of pricing of products, it would result in a loss to be borne by the Policyholders' Account, which may ultimately have to be borne by the shareholders, due to various compulsions, both statutory and for competitive reasons.

It has been observed that new insurers, who have increased market share, have reported a deficit in the Revenue Account. Further, such deficits have been funded through injection of equity capital at regular intervals. Promoters who are not comfortable with the regulatory stipulation of receiving up to 10 per cent of the actuarial surplus arising from participating business, have refrained from injecting capital into the company at regular intervals. In case of non-participating business, 100 per cent of the actuarial surplus is distributed to the shareholders.

As per the present limits on Foreign Direct Investment (FDI) the insurers can seek funding of equity from foreign partners only up to 26 per cent. As such, any increase in equity by the insurers puts an additional strain on the Indian promoter to fund 74 per cent of such increase. Such a stringent requirement for an industry, which is capital intensive in the initial years, places an additional strain on the Indian promoters, not only because of their capacity to raise fresh capital but also due to regulatory stipulations placed on the promoter company.

A similarity can be drawn from the banking industry. As per the exposure norms prescribed by the Reserve Bank of India, investments by a bank in a single financial services company should not exceed 10 per cent of the bank's paid-up capital and reserves. Further, the bank's aggregate investments in all its subsidiaries/financial services companies should not exceed 20 per cent of the bank's paid-up capital and
reserves. The bank is also required to ensure compliance with the minimum capital adequacy requirements.

**Life Insurers:** Life insurance industry operations, by its very nature, results in the initial strain which the shareholders expect to recover on stabilization of their operations. As insurance premiums within a country grow, there would be increasing pressures to bring additional equity capital for reserving, adequacy of capital and the re-insurance of the business underwritten. With comfortable foreign exchange reserves, inflow of foreign capital is not critical. However, higher FDI limit for the insurance sector would open up avenues for more players to enter the market, thereby making the industry more competitive and efficient. Further, in case of the existing players who are unable to inject fresh funds due to the high contribution of 74 per cent, increase in the foreign stake would facilitate their ability to shore up the equity base of the insurers.

A study of the business underwritten by the life insurers who entered the industry post liberalization reveals that the growth in their market share has been driven by their capacity to inject additional capital over the years 2000-01 to 2003-04. Such aspects as would have affected the growth in first year premium of these insurers: the types of products launched by them, marketing arrangements tapped by them and the brand equity built by them. The fact that the promoters have been able to inject additional capital at regular intervals has enabled them to absorb the deficit arising in the Policyholders Account. The total deficit of the life insurers in the Policyholders’ Account stood at Rs.1678.77 crore as on 31 March, 2004. The paid-up equity capital of these insurers increased from Rs.539.79 crore for four companies in the year 2000-01 to Rs.3081.71 crore in 2003-04 for twelve companies. During the same period, the gross premium underwritten by these life insurers increased from Rs.6.45 crore to Rs.3120.33 crore. The twelve private sector insurers underwrote “first year premium” of Rs.2440.71 crore in the year 2003-04.

While all the twelve life insurers who have entered the market in the last four years have reported losses during the years of their operations, these losses have been in line with the projections made at the time of registration.
Non-life Insurers: The scenario in the case of the non-life insurers in respect of capital requirements is diametrically opposite. Based on the type of business underwritten by non-life insurers, and their capacity to bear the underlying risks, a significant portion of the business gets re-insured thereby lowering the requirement for maintenance of solvency margins. A study of the retention ratios of the eight insurers who have entered the industry in the post liberalization era revealed that the during 2003-04, the retention ratios ranged between 78.50 per cent and 22.09 per cent. This wide range in the ratios is on account of the variation in the individual portfolios of insurers. While at the one end, an insurer had underwritten a significant component of its business in the motor segment, another sought reinsurance cover for the mega projects due to lack of capacity to bear the associated risks. The net retention of the eight non-life insurers in Fire, Marine and Miscellaneous segments was 22.30, 42.48 and 60.44 per cent respectively, as against 18.52, 44.29 and 55.24 per cent in the year 2002-03. As these insurers have increased their retentions with stabilization of their operations, the need for injecting further capital beyond the minimum entry level requirement of Rs. 100 crore has not arisen. In fact, other than ICICI Lombard, which has increased its paid up equity to Rs.220 crore from Rs.110 crore in 2001-02, no other insurer has brought in additional equity during the last four years of their operations. In the case of Cholamadalam M S additional equity to the extent of 26 per cent was brought in by the foreign partner on being inducted as a shareholder subsequent to registration of the insurer.

The cost of procuring business in this segment is also lower. As such, the non-life insurers, on account of the nature of their operations, break even early. A comparison of the operations of the eight non-life insurers with their projections revealed that these insurers generated profits in the second/third year of their operations. Of the eight non-life insurers, only two reported net losses in the Shareholders’ Account. These two insurers had commenced operations in the second half of 2002-03, and the year 2003-04 was the first full year of their operations.
Health Insurance sector:

At the time of opening up of the industry, it was anticipated that the insurers would particularly provide impetus to the health sector. It was also envisaged that insurance companies would be established to cater to the demand for insurance in the health sector. This has, however, not materialized in a significant way. No insurance company has been set up exclusively for the health sector. Though the premium in the health segment, in the case of non-life insurers has increased, and health coverage is being provided as riders by life insurers, and as standalone products by one insurer, there is still a lot of ground to be covered. Perhaps, lowering the capital requirement in the case of health insurers from the present levels of Rs.100 crore, could provide impetus for developing this sector.

Issues pertaining to reinsurance:

The capital requirements for reinsurers are stringent at Rs.200 crore, and this has been a deterrent to the entry of reinsurers into the Indian market. Other than the national reinsurer, General Insurance Corporation (GIC), there is no other reinsurer in the country. The foreign operators are reluctant to establish reinsurance companies in India at 26 per cent. For the present, the foreign reinsurance companies have established liaison offices in India, and they are procuring business from the country either directly or through the re-insurance brokers. The reinsurance business being placed in the foreign markets is in excess of the business retained by the direct insurers as well as the national reinsurer, GIC. A review of the regulations for establishing re-insurance companies is pertinent for increasing the foreign direct investment to 74 -100 per cent. This would facilitate higher retention of premium within the country. In addition, it would also result in attracting reinsurance business from the neighboring countries, thereby moving India to the position of a regional reinsurance hub in Asia in due course.
1.11 CORPORATE GOVERNANCE AND LIFE INSURANCE COMPANIES

Insurance companies mobilize funds from the policyholders and invest the same for a long-term horizon, which is full of several kinds of risks. Therefore, the basic objective of the management of an insurance company is to ensure safety, security and growth of policyholders' fund and the primary objective of corporate governance in an insurance company is to protect the policyholders against insolvency by efficient management of financial, accounting and technical functions. However, financial management in an insurance company is a bit different from other non-insurance financial companies because of a wide range of contract tenures reflected in a complex system of liability. Therefore, policyholders' protection by providing enough solvency margins confronting the various types of operational risks particularly in the area of finance and investment is the major concern for risk management. The major risks, which need to be addressed through corporate governance by a life insurance company, are basically of two types, namely technical/insurance risk and investment risks, which need to be addressed by an insurance company.

1.11.1 Types of risks

Technical Risk

Risk of miscalculating premiums and miscalculating technical provisions and growth risk arising out of excessive growth not matched by sufficient resources or due to wrong selection or wrong pricing of products.

Investment Risk

Investment risk is considered to be an important factor contributing to the insolvency of an insurance company. The major sources to investment risk are: depreciation risk—arising out of depreciation value of investment, liquidity risk—arising out of inability of timely encashment of investment, matching risk—arising out of insufficient cover of liability, derivative risk—arising out of off-balance sheet operation, thin market, wrong pricing and credit risk—arising out of reinsurance.
1.11.2 Managing Financial Risks

Financial risks in an insurance company can be minimized through well-designed corporate governance practices supported by regulatory and voluntary initiatives, promoting sound financial management practices. The major initiatives are: quantitative restrictions—quantitative limits of investments in various instruments and locations. Prudent person rules—includes investment by persons with good management quality integrity—under well-settled internal control and corporate governance mechanism. Portfolio diversification and location dispersal of investment. Provisioning for probable investment risk. Accurate valuation and asset accounting—bringing to light the real value of assets, potential loss of value and actual liability of the insurance company. However, governance of investment strategy can also play an important role in efficiency improvement and risk minimization.

Active Investment Strategy

Stock selection and market timing irrespective of trading costs form the basis of this strategy. The fund managers aim at beating the market by taking the advantages of market movement. Very often, there is over-diversification, which adds disproportionate costs to the fund there on causing strain on the performance of the funds. Active investing requires reasonable knowledge in market forecasting, macroeconomic and interest rate forecasting, etc. Very often, fund managers are incapable of that and they may be unable to get out of the market at an appropriate time and land up in trouble with illiquid stocks, depreciation in asset value and fall in NAV. Good governance of active investment strategy are called for.

Strategy of Indexation

Indexation is a passive investment strategy aimed at market return by investing in stocks under a particular index. Indexation strategy is cheaper and less technical and selection is comparatively easy. But the initial selection of stocks must be done easily to avoid chronic under performing stocks and stocks with inflated premium. Future potential for growth liquidity must be taken into account. It is often thought that long-term
The passing on of risk transfers to the reinsurer by the primary non-life insurer is called ceding. The primary insurer is known as ceding company. The ceding company retains certain amount of insurance on its own account, which is known as retention. The difference between retention and the total amount of acceptance is reinsured. The original office to which the business is reinsured is called reinsurer or guaranteeing office. It is also a contract of indemnity.

No matter what kind of reinsurance contact it is, the risks between the insurer and the reinsurer can be shared on a proportional or non-proportional (also known as excess of loss) basis. In a proportional agreement, the reinsurer pays for losses in the same proportion as the amount of premium he receives. Such contacts can be on a quota or surplus share basis. In a non-proportional agreement, an attachment point is fixed. When a claim arises, the reinsurer pays nothing unless the claim amount is greater than the attachment point. Such a contract is written per risk, per occurrence or as an aggregate loss.

The maximum amount of a liability, which the insurer can assume, on a particular risk is called retention. The total amount of insurance in force, the average size of the policy and the surplus fund available with the insurer decide the retention amount. The size of the company, the age of the issue, the type of policy and the class of risk, also has an impact on the retention.

1.12.1 Mode of Reinsurance

There are two methods of reinsurance. These are:

(a) Treaty
(b) Facultative

**Treaty Reinsurance:** This method is designed to cover an entire category of risk or line of business in advance. It is obligatory and binding in nature for reinsured / reinsurers. As long as a risk meets all the conditions as given in the reinsurance contract, acceptance of that risk by the insurer is automatic.
investment goal can be achieved through indexing and the fund managers remain totally passive about the internal dynamics of the stocks. Corporate governance plays an important role to keep the fund manager awake in order to protect the interest of investors.

**Strategy of Value Investing**

Value investing is a painstaking strategy to discover future values of the stocks by analyzing companies. In-depth analysis of companies are undertaken to discover long-term business value and the value of management. Therefore, a close tie is established between the company and fund managers, which enable the fund managers to keep themselves informed about the development in the long-term perspective. Value investing thus developed on the relationship. This relationship enables the fund managers to aim at medium to long-term investment growth instead of short-term speculative gain. Regarding risk management, Narayana Murthy Committee states: Procedures should be in place to inform Board members about the risk assessment and minimization procedures. These procedures should be periodically reviewed to ensure that executive management controls risk through means of a properly defined framework. Management should place a report before the entire Board of Directors every quarter documenting the business risks faced by the company, measures to address and minimize such risks, and any limitations to the risk-taking capacity of the corporation. This document should be formally approved by the Board.

**1.12 REINSURANCE**

Reinsurance primarily deals with catastrophe risks that are not very predictable and cause the greatest risk for the insurance company. A single insurer may not be able to bear the damaging financial impact of such losses. Therefore, an unbearable loss is broken down into bearable units by risk transfers. Reinsurance is an arrangement by which an original insurer who has insured a risk, insures a part of that risk again with another insurer, that is to say, he reinsures a part of the risk in order to diminish his own liability.
**Facultative Reinsurance:** This is for the reinsurance of current single risk and the options are open for both the reinsured and reinsurers. In a facultative contract relationship, the reinsurer retains the faculty or power to either accept or reject each individual risk offered to it by the insurer.

**1.12.2 Advantages of Reinsurance**

The advantages of reinsurance are:

- It safeguards capital and reinforces stability.
- It enables the insurer to take up large claims and expand capacity.
- It helps the insurance company to upgrade itself. The reinsurer can provide important underwriting training and skill development and share expertise gained from other countries.
- The reinsurer can contribute towards designing the product, pricing and marketing new products. It can also offer back office support such as faster processing of claims and automation of operations.
- Reinsurance can also help a company to withdraw from a line of business.

**1.12.3 Reinsurance and IRDA**

Several guidelines are laid by the IRDA to ensure fair play. Some of these are as follows:

- Every insurer should retain should retain risk proportionate to its financial strength and business volumes.
- A certain percentage of the sum insured on each policy by an insurance company is to be reinsured with the national reinsurer. The sum insured is the amount of money guaranteed to be paid under an insurance policy before any bonuses are added. A national reinsurer has been made compulsory only in the non-life sector.
- The reinsurance program will begin at the start of each financial year and has to be submitted to the IRDA. Forty-five days before the start of the financial year.
• Insurers must place their reinsurance business, in excess of limits defined, outside India with only those reinsurers who have a rating of at least BBB (S&P) for the preceding five years. This limit has been derived from India’s own sovereign rating, which currently stands at BBB.

• Private life insurance companies cannot enter into reinsurance with their promoter company or its associates, though the LIC can continue to reinsure its policies with GIC.

Reinsurer

GIC is the major reinsurer. Currently, all the insurance companies have to give 20 percent of their reinsurance business to GIC. The aim is to ensure that GIC’s role as the national reinsurer. Insurance companies retain only a part of the risk (less than 10 percent) assumed by them, which can be safely borne from their own funds. The balance risk is reinsured with the other insurers. However, GIC further reinsures the amount with the international companies such as Swiss Re (Switzerland), Munichre (Germany), and Royale (UK).

1.13 BANCASSURANCE

It is the distribution of insurance products through the branches and multiple communication channels of bank that include ATMs, tele-banking and internet banking. This concept originated in France and soon spread to other countries of Europe. In some cases, bancassurance is done because the bank has its own insurance companies or the insurance companies own the banks. It is synergy of both the services. The merger between Citibank and ‘Travellers’ Insurance into the ‘Citigroup’, is an example for this.

RBI has recognized ‘bancassurance’ wherein banks are allowed to provide physical infrastructure within their select branch premises to insurance companies for selling their insurance products to the banks’ customers with adequate disclosure and transparency and in turn earn referral fees on the basis of the premium collected. Bancassurance benefits the banks, the insurers and the insured.
Advantages for the Banks

- It is a source of revenue. Fee-based income can be increased through selling risk products like insurance.
- Insurance is known for customer loyalty. Life insurance contracts are long term in nature with a period ranging from ten years to thirty years and over. Banks can increase and retain their customer base by offering life insurance products.

Advantages for the Insurers

- Banks have a very wide network of branches. This widens customer base of the insurer.
- Banks possess inside information about the financial needs and saving preferences of their customers.
- Market researchers have shown that the consumers trust banks more than insurance companies.
- Banks with their brand image and existing customer relationship are the best marketers for sale of insurance products.
- The distribution costs are lower than that of other channels.

Advantages to the Insured

- Better value and cheaper premiums due to lower distribution costs
- Convenient and a one-stop financial market
- Decreased prices and a sound insurance product

Life Insurance Corporation of India has tied up with the Corporation Bank and the Oriental Bank of Commerce. Aviva Life’s partners are ABN Amro, American Express, Canara Bank and Lakshmi Vilas Bank. Each one of these handles a specific customer base. Bajaj Allianz has tied up with six banks, viz., Bank of Punjab, Bank of Rajasthan, Jammu and Kashmir Bank, Lord Krishna Bank, Karur Vysya Bank and Punjab and Sind Bank – the first, public sector bank to tie up with it. Bajaj Allianz is the only private general insurer to have tied up with six bancassurance partners.
Guidelines for Banks

Scheduled commercial banks are permitted to undertake insurance business as agents of insurance companies on basis of fee, without any risk participation. The subsidiaries of banks are allowed to undertake distribution of insurance products on agency basis. Banks which satisfy the eligibility criteria given below are permitted to set up a joint venture company for undertaking insurance business with risk participation, subject to safeguards. The eligibility criteria are:

- The net worth of the bank should not be less than Rs. 500 crore.
- The CRAR of the bank should not be less than 10 percent.
- The level of non-performing assets should be reasonable.
- The bank should have net profit for the last three consecutive years.
- The track record of the performance of the subsidiaries, if any, of the concerned bank should be satisfactory.
- Banks that are not eligible for the joint venture option can have an investment option of up to 10 percent of the net worth of the bank or Rs. 50 crore, whichever is lower.
- Other regulatory changes include the Insurance Regulatory and Development Authority (IRDA) regulations with respect to the licensing of corporate agents.

All the banks entering into insurance business will be required to obtain prior approval of the Reserve Bank. The Reserve Bank will give permission to banks on a case to case basis, keeping in view all the relevant factors including the position in regard to the level of non-performing assets of the applicant bank in its present or proposed line of activity, viz., insurance business. It should be ensured that the risks involved in insurance business do not get transferred to the bank and that the banking business does not get contaminated by any risks which may arise from insurance business. There should be ‘an arm’s length’ relationship between the bank and the insurance business.
1.14 LIFE INSURANCE SERVICES MARKETING

Marketing, as the term is commonly understood today, was developed initially in connection with the selling of consumer-packaged goods and later with the selling of industrial goods. The Committee on Definitions of the American Marketing Association (AMA) defined marketing as the performance of business activities that direct the flow of goods and services to the consumer. The characteristics of services are the justification for the claim that services marketing is different to marketing physical products. Many of the developments in services marketing are fairly recent. The factors affecting the developments within services marketing are organization size and structure, regulatory bodies, growth in service industries, characteristics of services, customer/employee interaction, and specific service sectors. Services marketing are the process of researching and promoting to a market with non-physical goods known as services.

Insurance marketing is basically just the marketing of insurance products. Insurance marketing emphasizes the importance of the customer preferences and priorities. Major objectives of life insurance marketing are increasing customer awareness, successful distribution of insurance products, developing corporate image, improving customer service, improving customer base and its spread, and etc. Factors impeding the application of insurance marketing are insufficient experience of insurers while expanding insurance business, non-existence of long-term development strategies of insurance companies and the fact that insurers orient mostly to short term needs; and while trying to apply more actively insurance marketing means it is necessary to change the whole organizational management structure of an insurance company, the channels of insurance products sales, technologies of communication with clients, and etc.

Insurer has to analyse the nature of the customer’s needs and plan their products and services in such a way that they can give satisfaction to the customers and face the competitors. Planning needs analysis of the insurance market to take a decision, prediction, and forecasting as to future needs of customers. All these programs involve a number of functions (7Ps), which are to be planned carefully. The combination of these functions is known as insurance service marketing mix.
Marketing mix is the planned package of elements, which will support the organization in reaching its target markets and specific objectives. The marketing mix has its origin in marketing of goods for consumer markets and consists of the well-known 4Ps: Price, Promotion, Place, and Product. Numerous modifications to the 4Ps have been proposed, the most concerted criticism came from the services marketing area.

Borden (1965) was the first one to conceive the ideas of marketing mix, but did not formally define the marketing mix. He explained it as important elements or ingredients that makeup a marketing program. Borden's original marketing mix had a set of 12 elements: product planning, pricing, branding, channels of distribution, personal selling, advertising, promotions, packaging, display, servicing, physical handling, and fact finding and analysis. Lazer and Kelly (1962) and Lazer, Culley and Staudt (1973) suggested three elements of marketing mix: the goods and services mix, the distribution mix, and the communication mix. McCarthy (1978) regrouped Borden's 12 elements into four elements and was the first who offered the marketing mix, which is also known as the four Ps. He defined the marketing mix as a combination of all of the factors at marketing manager's command to satisfy the target market. This marketing mix approach has been criticized for being incomplete, because it does not bear in mind services marketing. Booms and Bitner (1981) create 7Ps by adding Participants, Physical Evidence, and Process to the original 4Ps. Their creation aims to include service in the marketing mix, and therefore the additional Ps are called —Service Ps. The marketing mix with the 7 Ps is highly appropriate towards businesses that offer services. The 7Ps of marketing mix have been studied by some researchers in marketing fields. Still, the expanded marketing mix suggested by Booms and Bitner (1981) has been considered to be a valuable tool for marketing service. These 7 Ps are the suitable marketing mix elements for life insurance services.
1.15 LIFE INSURANCE MARKETING MIX

1.15.1 PRODUCT:

A product is anything that can be offered to a market to satisfy a need or want. The products, which can be marketed, include physical goods, services, persons, places, organizations, and ideas. In the deeper sense, the product is not a physical item but a perception of the consumer or the user. LaLonde (1977) found product related criteria to be most important, followed by distribution, price, and promotion. According to Woodruffe (1995), the product element of the marketing mix refers to how the offering is put together—typically this will include aspects relating to quality, styling, colour, design, brand name, packaging sizes, and other features. A service product is anything—either in isolation or in combination—that an organisation offers to potential customers to satisfy their needs. The service product constitutes the foundation of an organisation's existence.

Life insurance companies offer different insurance products with different features to cater different needs of the customers. By means of buying a life insurance product, a customer buys the promise offered because he believes in the promise being made by the insurance company. Life insurance companies have several products such as term assurance, endowment assurance, money back policies, pension plans. There are also group insurance schemes than can be taken by employer for their employees. Nowadays, investment plans (ULIPs) are very popular in the market. These insurance products are always readily marketable.

1.15.2 PRICE:

Price is the mean of setting the exchange value between two parties. Price, in marketing mix terms, covers all aspects of pricing such as discount pricing, extended credit, list price, and payment period. Kandampully (2002) describes—pricing in service organizations is less influenced by cost, but more by customer's perceptions of quality, satisfaction, and value. The actual pricing of a service is thus often determined by matching the customer's perception of value. With this pricing method, pricing is considered as a marketing mix variable, thereby considered together with the other
marketing mix variables before a marketing program is put together. Zeithaml and Bitner (2003) defines three basic marketing price strategies which service companies can attend, the strategies are competition-based, cost-based, and demand-based pricing strategies.

Pricing in life insurance is somewhat complex as compared to the pricing strategies of other financial products. The price (premium) for a life insurance product is determined by expected claim costs, investment income, administrative costs, and fair profit loading. The claims cost is based on the mortality rate realized on different age groups. The Actuary on considerations that depend on the experience of the insurer in the past and his assessment of the trends in the future decides the premium rates. Pricing in today's insurance business environment requires actuaries to be knowledgeable in an ever-expanding group of issues because of the nature of diversified products. In case of life insurance, there is limited scope to use price as a strategic weapon.

1.15.3 PLACE:

Place is another important element of marketing mix. Place refers to the location where the product or service is available to the customer, including distribution channels. Place contributes an important factor in the marketing of services. Black (2002) found that customers sometimes use the same products through different channel. In case of life insurance, it is a combination of decisions regarding channels of distribution. The emerging new opportunity for life insurance companies towards integration of the financial services industry is bancassurance. Bancassurance prospects in India are really bright because huge banking infrastructure across urban, semi-urban and rural India and life insurers are using this channel.

New distributors like stockbrokers, financial planners, general agents, and financial institutions etc. involve lower distribution costs, variable as opposed to fixed expenses, lower front-end commission costs, and the opportunity of selling the products in conjunction with other investment-related products. Strategy of worksite marketing is more useful in case of marketing of pension and health plans. The widespread diffusion of the Internet has created an explosion in the growth of electronic channels, including direct channels (that is, individual company web sites), electronic markets, or electronic
intermediaries over which multiple buyers and sellers do business), and other cybermediaries. However, consumers have not shown a marked preference for purchasing insurance product via the Internet. The traditional system of —agents—is the dominating one in India and this will continue to be a major distribution channel for insurers, since this system has core roots in rural sector.

1.15.4 PROMOTION:

The ‘promotional mix’ is a term used to describe the set of tools that a business can use to communicate effectively the benefits of its products or services to its customers. Market communication performs three basic roles in marketing—to inform, to persuade, and to remind. Traditional promotion employs a variety of methods—including advertising, sales promotion, public relation, and personal selling—to attract the attention of existing and potential customers, and to inform them of the products, services, and special offers made available by the firm. Each of the categories of promotion mix has now become familiar in many areas of services marketing.

In case of life insurance services, promotion is done through a mix of advertising, personal selling, and sales promotion. Promotion communicates with the potential market so as to persuade the prospective customers to try a new insurance product. Online advertising is one marketing tool that is worth the money. As the Internet takes on more power and influence all of the time, having a web presence will put an insurance company on the cyber map and get it noticed. Block line advertising in trade journals, industry publications and periodicals is the way to go. Television ads and print ads are excellent forms of insurance marketing. All life insurance companies have started using PR tools to make better image about them in the minds of general public. Personal selling is extremely labour intensive but is the best form as far as insurance is concerned, dealing with one customer at a time.

1.15.5 PEOPLE:

People, process, and physical evidence are the three —Ps—which are especially applicable to services marketing mix. These three elements are highly interrelated with
each other. People are the main critical resource in any organisation, particularly service organisation. Because of the simultaneity of production and consumption in services, the service staff occupies the key position in influencing customer's perceptions of service quality. Woodruffe (1995) solely uses service personnel in the —People[] part of the services marketing mix. Recruiting the right staff and training them appropriately in the delivery of their service is essential, if the service provider wants to obtain a form of competitive advantage.

Life insurance companies have to give more attention in training and development their employees and agents. Building strong relationship with their agents as well as the customers will help in meeting customers’ needs and serving them efficiently. Satisfaction depends on the nature of interaction between customers and the people representing insurance companies. Training the employees and agents to introduce new products and use of information technology for efficiency both at staff and agent level are the key areas to look into.

1.15.6 PROCESS:

A process is the method and sequence of actions in the service performance. Unlike goods, services are processes. Services are the end results of deeds, acts, performances, and activities performed by the firm's employees alone or in conjunction with various equipments, machinery, facilities, and so on. In assessing process, customers evaluate whether the service follows a production-line approach or whether the process is a customized one in which the customer is given personalized attention. Shostack (1984) points out that since services are intangible and therefore described in words by people, companies have to be really clear in defining the service process. The risks of relying on words alone in describing services are the oversimplification of the service, incompleteness of the description, subjectivity of different readers and the biased interpretation of the words used to describe the service.

The process involved in life insurance industry should be customer friendly. The speed and accuracy of payment is of vital important. The process methodology of life insurers should be such that it provides total ease and convenience to the customers.
Badly designed and poor processes lead to slow and inefficient delivery and make it difficult for insurance employees and agents to do their job well. Consequently it will result in low productivity and service failures.

1.15.7 PHYSICAL EVIDENCE:

The physical evidence is defined as the environment in which the service is delivered and where the service provider and the customers interact, and any tangible commodities that facilitate performance or communicate the service. According to Zeithaml and Bitner (2003), to evaluate services before its purchase and to assess their satisfaction with the service after it is bought; customers tend to rely on tangible cues, or physical evidence. The appearance of building, landscaping, interior furnishing, equipments, printed materials, and other visible cues all provide tangible evidence of a firm’s service quality. This sort of physical evidence provides excellent opportunities for a service firm to send clear and consistent marketing messages regarding the firm’s purpose the intended market segment, and the nature of the service.

In case of insurance business, apart from office environment, materials such as brochures, policy documents, and periodic statements are the tangibles, which will influence the customers. Insurance companies and intermediaries need to manage all these physical evidences carefully as they can have a profound impact on the impression of the customers. Although all insurance companies provide similar essential service, the differences that do exist are the physical evidence.

1.16 AN OVERVIEW OF LIFE INSURANCE PRODUCTS

The basic customer needs met by life insurance policies are protection and savings. Policies that provide protection benefits are designed to protect the policy holder (or his dependents) from the financial consequence of unwelcome events such as death or long term sickness/disability. Policies that are designed as savings contracts allow the policyholder to build up fund to meet specific investment objectives such as income in retirement or repayment of a loan. In practice, many policies provide a mixture of savings and protection benefits.
The common types of life insurance policies are:

- Endowment Assurance
- Money Back Plan
- Whole Life Assurance
- Unit Linked Plan
- Term Assurance
- Immediate Annuity
- Deferred Annuity
- Group Life Insurance
- Riders

1.16.1 Endowment Assurance

There are basically two variants of this policy: (a) Non Participating (Without Profit) Endowment Assurance. (b) Participating (With Profit) Endowment Assurance

Non-Participating Endowment Assurance:

This policy offers a guaranteed amount of money (the sum assured) at the maturity date of the policy in exchange for a single premium at the start of the policy or a series of regular premiums throughout the term of the policy. If the policyholder dies before the maturity date then usually the same sum assured is paid on death. Of course, the policy could be structured with a sum assured paid on death, which is different from that paid at maturity.

The policyholder may be allowed to surrender the policy before maturity and receive a lump sum (surrender value or cash value) at the time, on guaranteed or non-guaranteed terms. If the policyholder wishes to keep the policy in force but without paying further premiums, a reduced sum assured (paid up value or paid up sum assured) may be granted. There is usually a provision to take a loan up to 90% of the surrender value.
Participating Endowment Assurance

The structure of this policy is similar to that of the non-participating policy except that the initial sum assured under the policy is expected to be enhanced by payment of bonuses (distribution of the profits made by the insurance company) to the policyholder. In the Indian context, bonuses usually take the form of additions to the initial sum assured and become payable in the event of the occurrence of the insured event, i.e. survival up to the bonuses (dividends) as regular cash payments. In this case, the policyholder may have the option of using the cash bonus to offset the future premiums payable.

1.16.2 Money Back Plans

This is a popular savings cum protection policy because it provides lump sum at periodic intervals. For example, given an initial sum assured of Rs. 1000 and a term of 20 years, the policy may provide for part payment of the sum assured as follows:

- 20% at the end of 5 years
- 20% at the end of 10 years
- 20% at the end of 15 years
- 40% at the end of 20 years

This is usually sweetened by providing a guaranteed addition to the initial sum assured every year. Continuing with the above example, if the guaranteed annual addition is say Rs 100 per 1000 sum assured, then the policyholder gets 400 of the initial sum assured plus guaranteed addition of Rs 2000 [=100X20] at the end of the 20 year term. In the event of death of the policyholder within the specified term, the entire (initial) sum assured plus the accrued guaranteed additions (accrued up to that point of time) become payable.

The money back policy illustrated above is a non-participating policy. The policy can also be offered in the ‘participating’ format in which case the guaranteed additions will be replaced by ‘bonuses’.
As with endowment assurance, a surrender value on guaranteed or non-guaranteed terms may be paid if the policyholder chooses to withdraw from policy. Alternatively the policyholder may have the option of converting the policy into a paid-up policy. Usually there is no loan facility attached to this policy.

1.16.3 Whole Life Assurance

This policy provides a benefit on the death of the policyholder whenever that might occur. Basically it provides long-term financial protection to the dependents. It is particularly useful as a means of protecting some of the expected wealth transfer that a parent would be aiming to make to his/her children when he or she died. Without the policy, the wealth transfer is likely to be very small if the parent died young. Such policies can also be a tax efficient way of transferring wealth at any age depending on legislation (often reducing the liability to inheritance tax).

There are both non-participating and participating versions of this policy. Non-participating policies offer a guaranteed sum assured on death. Under participating polices, initial guaranteed sum assured on death. Under participating policies, the initial guaranteed sum assured may be increased by bonuses or cash refunds may be given. Where the initial guaranteed sum assured is increased by bonuses, the sum assured together with the accrued bonuses becomes payable on the death of the policyholder.

As with endowment assurance, a benefit may be paid if the policyholder chooses to withdraw from the policy. Similarly, there may be a ‘paid up’ policy option. The policyholder may also have the option of taking a loan up to say 90% of the surrender value.

1.16.4 Unit Linked Plans

A unit-linked plan is also an investment-oriented product. As compared to other investment plans, the investment portion of the unit linked plan functions like a mutual fund. It is invested in a portfolio of debt and equity instruments, in conformity with the announced investment policy. Hence, it grows or erodes in line with the performance of
that portfolio. Of course, throughout the period of investment, the policyholder enjoys an insurance cover as stipulated.

1.16.5 Term Assurance

This is a pure protection policy, which provides a benefit on the death of an individual within a specified term for example, one, ten or twenty-five-years. Premiums may be paid regularly over the term of the policy [or some shorter period] or as a single premium at outset. Generally, there is no payment if the policyholder survives to the end of the policy. However there is term assurance policies, which offer some proportion of premiums paid on survival to the maturity date of the policy.

A popular variant of the term assurance policy is the decreasing term assurance policy under which the sum assured decreases over the term of the policy. This type of policy can be used to meet two such specific needs. First, it can be used to repay the balance outstanding under a loan [e.g. credit life insurance] in the event of the death of the policyholder. Secondly, it can be used to provide an income for the family of the deceased policyholder from the time of death up to the end of the policy term.

Term assurance policies are typically offered in the non-participating format. These policies are usually structured with no 'surrender value' and 'paid up' policy options. The main attraction of a term assurance policy is that it provides a death benefit at a lower cost than under an endowment or whole life policy for the same level of benefit.

1.16.6 Immediate Annuity

This type of policy meets the policyholder's need for a regular income, for example, after his or her retirement. The policy can also be structured to provide an income for a limited period, for example to pay the school fees of the policyholder's children. The regular income is purchased by paying a single premium at the inception of the policy. Strictly speaking the regular income ceases on the death of the policyholder. There are however variants of this policy under which a (reduced) income may be paid to
the spouse (of the policyholder) over his or her lifetime; or the single premium may be returned to the dependents of the deceased policyholder.

Immediate annuities can be offered either in the non-participating format or in the participating format. In the case of a participating annuity, the income paid to the policyholder is a guaranteed amount plus a bonus added by the insurance company. Usually no payment is made to the annuitant on withdrawal. Put differently, there is no surrender value option associated with this type of policy.

1.16.7 Deferred Annuity

The usual structure of this policy is that the policyholder pays regular premiums for a period up to the specified ‘vesting date’. These premiums buy amounts of regular income, payable to the policyholder from the vesting date. A single premium at the start of the policy is a possible alternative to regular premiums.

A deferred annuity enables the policyholder to build up a pension that becomes payable on his or her retirement from gainful employment. At the vesting date of the annuity, the alternative of a lump sum may be offered in lieu of part or all of the pension, thereby meeting any need for a cash sum at that point, for example to pay off a housing loan.

1.16.8 Group Life Insurance:

The group insurance is a plan of insurance which covers similar / homogeneous groups of individuals under a single policy (i.e. master policy). In contrast to individual insurance, the insurance company enters into group insurance contracts with an employer, a labour union or a voluntary association. The individuals covered in the group insurance scheme are not parties to the contract. The amounts as well as terms of the insurance are negotiated by the group policyholders only. For the groups of reasonable size and a fairly uniform risk, the insurance is concerned not with assessing the risks of the individuals in the group but with assessing the broad risk characteristics of the group as a whole. This translates in to reduced insurance/ under-writing and lower administration cost to the insurer. Hence, the premium rate is lower on group policies as
compared to similar individual policies. It is paid by the employer/trustee/group/association on behalf of the individuals they represent. The amount of insurance cover is decided upon for the group as a whole. This may be either uniform for all members or a graded amount for different categories based on salaries and so on.

Some of the group insurance schemes available in India now are: i. Employees Deposit Linked Insurance Scheme (EDLI) under the Employees Provident Fund Act, ii. Group Insurance Scheme of LIC in lieu of EDLI, iii. Group Gratuity Scheme under the Payment of Gratuity Act, iv. Groups Super Annuation Scheme, v. Group Saving Linked Insurance Scheme, vi. Voluntary Retirement Scheme, vii. Group Leave Encashment Scheme, viii. Group Annuity Scheme and ix Group Credit Term Scheme to cover the risk of mortality of borrowers and a mortgage programme are lending operation of a bank/finance company.

1.16.9 Riders

Riders are add-ons to the life insurance policies described above. These add-ons can be purchased with the base policy on payment of a small additional premium. The commonly offered riders in the Indian context are:

- Accidental Death Benefit (ADB) Rider
- Critical Illness (CI) Rider
- Waiver of Premium (WOP) Rider
- Term Rider

Tax Breaks

At the time of writing, the tax breaks from a policyholder’s perspective are as follows:

➢ The premium payable under a life insurance policy can be deducted from taxable income under section 80 C of the Income Tax Act, 1961. In the case of an individual, this insurance policy can be on the life of the individual or on the life of the spouse of the individual this insurance policy can be on the life of any child of the individual. The deduction under section 80 C is also available for premiums payable under a non-
commutable deferred annuity; and for contribution made by the individual to any notified pension fund set up by a Mutual Fund or by the UTI.

➢ The premium paid by an individual under an annuity plan of the Life Insurance Corporation of India or of any other insurer (as approved by the IRDA) is deductible from the taxable income of that individual subject to a maximum amount of Rs. 10,000 [Section 80 CCC of the Income Tax Act].

➢ Any sum received under a life insurance policy, including the sum allocated by way of bonus on such policy is exempt from tax under section 10 (10D) of the Income Tax Act.

Consideration in Choosing a Policy

Bear in mind the following consideration in choosing a policy.

➢ Review your own insurance needs and circumstances. Choose the kind of policy that has benefits that most closely fit your needs. A life insurance agent or a financial advisor can help you in this task.

➢ Be sure that you can handle premium payments. Can you afford the initial premium? If the premium increases later and you still need insurance, can you still afford it?

➢ Don’t buy life insurance unless you intend to stick with you plan. It may be very costly if you quit during the early years of the policy’s term.

➢ If you are thinking of surrendering your insurance policy or replacing it with a new one, you should carefully assess the surrender value and the rights and benefits of the new policy vis-à-vis the existing policy.

1.17 AN OVERVIEW OF LIFE INSURANCE DISTRIBUTION CHANNELS

Distribution is a key determinant of success of all insurance companies. In case of life insurance, it is combination of decisions regarding channels of distribution. Life insurers market various insurance covers either directly or through various distribution channels—individual agents, corporate agents including bancassurance and Brokers.
These are generally called the traditional channels. In today's scenario agents continue as the prime channel for insurance distribution in India and almost all the players follow this model primarily. However, with new developments in consumers' behaviour, evaluation of technology and deregulation, new distribution channels have been developed successfully and rapidly in recent years. This section discusses the various insurance distribution channels and the related problem.

1.17.1 AGENTS:

All life insurance companies have an agency-building distribution strategy under which they recruit, train, finance, and supervise their agents/advisers. For decades, agency was the only distribution channel for life insurance in India. Even today more than 70% of business is carried through insurance agents. Through agency, personal contact and relationship can be established with the customer. The system of agents is a major source of both presales and post sales services to customers, since it has the direct relationship with customers. Due to personal contact, it can provide valuable feedback about the need and expectation of consumers. However, it is nowadays considered as an old fashioned channel and not fully updated with latest technologies.

1.17.2 BROKERS:

Insurance brokers are professionals who assess risk on behalf of a client, advice on mitigation of that risk, identify the optional insurance policy structure, bring together the insured and insurers, and carry out work preparatory to insurance contracts. Brokers represent the customer and will sell the products of more than one company. They seek to determine the best fit for the client and can effectively address the mind block faced by the public about the various companies. The system of brokers is generally applicable in the case of life insurance for the high-end and corporate/group segment.

1.17.3 BANCASSURANCE:

Bancassurance in its simplest form is the distribution of life insurance products through a bank's distribution channel. Insurance companies see bancassurance as a tool for increasing their market penetration and premium turnover. It takes various forms in
various countries depending upon the demography and economic and legislative climate of that country. While bancassurance has become a success story in Europe, it is relatively a new concept in Asia. It was introduced in India when insurance industry was opened up for private players.

In India, a bank can tie up with one general insurance and one life insurance Company as mandated by IRDA regulation. The banking sector in India comprises of more than 67,000 branches and around 20 crores bank accounts. However, initial investment in systems and processes and people training is considerably more. People handling insurance sometimes don't know much about the products and once they make customers they are not much bothered about their customer queries. Moreover, it will be useful for selling only certain lines of products. In India bancassurance practice is yet to be much popular.

1.17.4 INDEPENDENT FINANCIAL ADVISOR:

IFAs are authorised agents of insurance companies having tie-ups with more than one insurance company. They are qualified persons or institution who can provide advice on financial products. Independent financial advisors are commissioned agents whose primary business is the sale of property and casualty insurance for several insurers. IFA assembles different financial products in accordance to customer needs and provide value added product by creating customized financial product. Today, IFA show their significant presence as distribution channel in both life and non-life insurance business. Technically, independent financial advisors who sell life insurance policies usually do so as brokers.

1.17.5 DIRECT MARKETING:

Insurers have also resorted to direct marketing wherein insurance companies get in touch with the customers without the aid of an intermediary. A separate department has been set up and officers were deputed to solicit and administer insurance business. The advantage of this system is the reduction of cost incurred by the agency system. Company owned sales team concept is now employed by a majority of new players and
has proved more effectiveness in customer creation and retention. However, as compare
to the system of agents, contribution of direct marketing is considerably low and it was
25.73 % (public: 26.86% and private: 23.63%) in the year 2009-10.

1.17.6 WORKSITE MARKETING:

Under this Strategy, life insurers send team to a target group and explain the
products either individual or group products suitable to them at their place of work on a
voluntary, payroll-deduction basis. The target group may be employees of a particular
company, educational institute or any kind if organisation. Insurance companies will be
able to sell insurance products particularly pension and health plans through this channel.
One possible reason for insufficient development of this channel in India is that
employers generally expect some kind of incentive to provide the facilities to the life
insurers for making presentations and making arrangements for deduction of premium
from salaries. With changes in human resources management polices and compensation
packages, group products or work site products do have a definite market that cannot be
ignored.

1.17.7 RETAIL CHAIN:

Another innovative distribution channel that could be used are the non-financial
organizations. The Indian retail market is the most fragmented in the world and at
present, organized retail channel is around 3% of total retail business. But the organized
sector is expected to grow at rate of around 30% per annum. With this huge growth rate
of retail sector it can become viable distribution channel for life insurance products. In
the life segment, group creditor insurance may be the most suitable product for this
channel. However, repeat business or renewal of business cannot be assured in this
system. Scope of retail business in life insurance is limited as compared to non-life
insurance.

1.17.8 INTERNET:

Initially, insurance was seen as a complex product and buyers preferred face-to-
face interactions with intermediaries. Nowadays, the advantage of technology allows
insurers to increase their reach into the market. All insurers have websites through which they provide information about products and services. In India Internet penetration is still low legality of agreements are posing difficult problem. The insecurity associated with transactions over the net is still an inhibiting factor. Internet has not been evolved into a means for direct selling of insurance in the current scenario. In the Indian market, where insurance is sold after considerable persuasion even after face-to-face selling, the selling over the net, which must be initiated by the client, would take some more time.

1.17.9 DISTRIBUTION CHANNEL FOR MICRO INSURANCE:

The huge untapped market for insurance is the rural and social sector. Micro-insurance is defined as the protection of low income households against specific perils in exchange for premium payments proportionate to the likelihood and cost of the risk involved. It provides an opportunity to the insurance companies to meet their social responsibility as well as secure a strong footing in the rural market. The active distribution channels for micro insurance in India are NGOs, MFIs, and SHGs (self-help groups), Micro agents, Cooperative Banks and RRBs (regional rural banks), and Post Offices. The MFIs/NGOs have been identified as main delivery channels by most of the insurance companies. These have a large network, catering to huge number of clients. However most of the MFIs have limited ability to process the insurance claims as such they try to customize the insurance product in order to simplify the operational process involved. As far as Formal Banks and RRBs, Post Offices and Internet & Rural Kiosks are concerned they have not developed their potential in delivering the insurance product.

1.18 CURRENT SCENARIO OF LIFE INSURANCE MARKETING IN INDIA

The life insurance market in India is undergoing tremendous transformation. The market has progressed a great deal from the pre-liberalization era, when there was only one player, the government –run LIC (The Life Insurance Corporation of India Ltd.), to the present situation where there are 24 companies. LIC is the market leader and there are now 23 other companies in the private sector.
During the pre-liberalization era, life insurance grew at a very slow pace—with only one company enjoying monopoly. LIC was a government organization formed in 1956 by merging 256 companies. The purpose was to provide life insurance coverage to the Indian population and design and develop products/policies to suit the needs of Indians, who included a mix of the poor and the rich, with more of the former. LIC has contributed a lot towards building awareness about and developing the life insurance business in India. LIC’s efforts were commendable, but it lagged behind international development and standard, in terms of both products and services. The average penetration of life insurance globally was 3.92% in 1999, whereas in India it was only 1.42%.

All this led the Government of India to rethink about the structure of the life insurance industry and in this context, various committee, Mukherjee Committee, etc., were appointed. Going by the recommendations of these committees, the life insurance sector was finally opened up to private companies in 1999. The first private company to commence operations thereafter was HDFC, in a joint venture with Standard Life of the UK. Following thereon, in just about a decade, many other companies joined the fray to grab a slice of the Indian life insurance market. The growing interest of private companies in India’s life insurance business can be gauged by the fact that there are now 23 private players, in addition to the public sector LIC. Most of the private companies are joint ventures of Indian companies with international insurance and financial service business houses, which again brings to the fore the immense potential offered by the Indian life insurance market.

Increasing Competition

Opening of the insurance sector to private companies has increased competition, and also challenged the monopoly of LIC. The journey began with DFC and presently, there are a host of companies, including those engaged in telecommunications, various financial services, and banking—comprising both private and nationalized banks.
Enthusiastic entry of Foreign Firms

Foreign firms were just waiting to tap the unexplored life insurance market of India. Just after opening of the sector in 1999, several Indian private companies with one or more foreign firms from the life insurance sector. Although the maximum investment ceiling is 20% as fixed by IRDA (Insurance Regulatory and Development Authority) for foreign players, this is likely to increase in the near future. This move will promote more foreign investment and will further the penetration of life insurance among the India population.

The changing positioning of Life Insurance

During the pre-liberalization period, the life insurance business had focused primarily on tax saving, apart from, of course, providing a same security cover for the beneficiaries, in the event of untimely death of the insured. This was making the selling of life insurance a hard job. After liberalization, the scenario has altered dramatically. The positioning of life insurance has changed from that of a means to cover life risk and save taxes, to an investment opportunity. The introduction of unit linked insurance plan (ULIP) by LIC was the starting point, which was taken up aggressively by the private companies. In fact, during recent years, ULIPs are the highest contributors to the business growth of most life insurance companies in India. However, the recent downslide of the stock market resulted in reduced results on ULIP plans and this setback, though temporary, has forced the companies to rethink their positioning strategies and alter them according to current market requirements.

Discovery of New Product Market Segments

The repositioning of life insurance as an investment avenue has led to the discovery of new segment such as pension plans. The altered pension policy for its employee by the Government of India has also led to a positive impact on this segment of business for the insurance companies.
Heavy expenditure on Advertisement and Brand Building

Life insurance companies are sending on advertising and brand building like never before. This has helped both the private companies and LIC to make customers better aware of their products and services. The private life insurance companies, in particular, are benefiting a great deal from their promotional efforts.

Rising Customer Awareness

The customer in modern India is now more aware about insurance through various media. This has led the insurance companies to adopt GRM (Customer Relationship Management) packages and other tools to attract and retain customers. As pointed out by the renowned marketing guru, Philip Kotler, ‘Gaining one customer is 10 times more costly than maintaining an existing one.’ The observation is all the more true for service industries, where dissatisfaction could result in rapid negative word-of-mouth publicity and immediate loss of business to organization.

Changing Distribution Channels

Life insurance is no longer sold only by agents. Other channels, like bancassurance, corporate agents and the Internet, are being used by companies as important means for selling insurance products. Agency channels have their own importance, but the insurance companies are also marketing aggressively through other channels. Both LIC and private sector companies have tied up with channels other than agents such as commercial banks and retail shops, to sell their products. SBI Life is, however, obtaining much of its business primarily from bancassurance and shopassurance in marketing of life insurance products.

Product Innovation

The success of insurance companies today is hinged on the launching of new and innovative products. The introduction of ULIP plans, pension plans, market-linked schemes, guaranteed return schemes, etc., has altered the market composition to a significant extent. A recent product of LIC, Jeevan Astha, has contributed more than Rs.
8500 Cr of business to the company. Private companies are trying to be even more innovative and are ahead in new product offerings, as compared to LIC.

**Role of Media in Brand Building**

Increased reach of media to the Indian population, availability of television sets in rural India and access to cable T.V, satellite T.V, etc., have transformed the television viewing habits of the Indian population. Life insurance companies are taking advantage of this to build sales and increase awareness. Some of the tools used by the companies are: television, print, radio, outdoor and Internet advertisements, sponsorship of television and other programs, free seminars, road shows, sales promotion activities, short films and slides in movie halls, tele-calling, SMS marketing, partnering with marketers of other consumer durable products, mobile video vans, participation in trade fairs etc.

**Changing Service Requirements of Customers**

Today, the buzzword of is customer satisfaction. This is leading to increased use of management tools, like Customer Expectation Management and Customer Relationship Management.

**Market Penetration by Private Life Insurance Companies:**

Private companies have provided strong competition to the market leader, LIC, and taken away some of its market share. The monopoly market condition of only LIC for life insurance of yesteryears, has transformed into an oligopoly market. Now, insurance seekers have more options to select from, resulting in availability of better products and services.

**Generation of Employment**

The service sector has become one of the prime employment providers of the Indian economy and life insurance contributes significantly to this. The sector provides good employment opportunities in the form of career agents/ advisors, both full-time and part-time. The trend can be easily seen from the placement programs of B-schools, where the life insurance companies seek their future managers in large numbers.
In view of these changes, it becomes essential for companies to reframe their marketing strategies and to focus on enhancing their market share, understand the requirements of customers and provide innovative products and services to cater to their needs. Some strategic solutions are delineated as under:

- Market research to understand customers’ requirements so as to develop need-based products.
- Continuous product innovation.
- Positioning of life insurance, not only as a risk covering and tax saving tool, but also as an investment and future income generator.
- Pricing the pre-cuts/policies in such a way that they can be made best use of by the masses.
- Effective use of media to send the right message to the customers, so that they can appreciate need for life insurance.
- More effective training of employees and sales force (especially agents) to generate more sales and gain market share.
- Building long-term profitable relations with the customer, because investments in life insurance happen over a life-time.

The era of monopoly in the life insurance business in India is over and no company can now afford to sit idle. The leader, LIC, is losing its market share and private players are making their presence felt. As competition in the insurance sector hots up, the future belongs to those who understand the varied requirements of the Indian populace and provide products and services to meet the same.
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CHAPTER-2

REVIEW OF LITERATURE AND METHODOLOGY