CHAPTER 5

Regulatory framework and policy Perspective
5.1 INTRODUCTION

With such a large population and the untapped market area of this population, insurance happens to be very big opportunity in India. Today it stands as a business growing at the rate of 15 – 20 per cent annually. Together with banking services, it adds about 7 per cent to the county’s GDP. This indicates that the growth potential for the insurance sector is immense in India. Although Indian markets were privatized and opened up to foreign companies in a number of sectors in 1991, insurance remained out of bounds on both courts. The government wanted to proceed with caution. The government decided to set up a committee headed by Mr. R.N. Malhotra (the then Governor of the Reserve Bank of India to make suggestion for restructuring the general insurance sector.

5.2 VARIOUS COMMITTEES ON RESTRUCTURING OF INSURANCE BUSINESS

5.2.1 Malhotra committee Report

Liberalization of the Indian insurance market was recommended in a report released in 1994 by the Malhotra committee, indicating that the market should be opened to private sector competition. It also investigated the level of satisfaction of the customers of the LIC. Curiously, the level of customer’s satisfaction seemed to be high.

The committee was set-up with the following objectives:-

(a) To suggest the structure of the insurance industry, to assess the strengths and weaknesses of insurance companies in terms of the objectives of creating an efficient and viable insurance industry, to have a wide coverage of insurance services, to have a variety of insurance products with the high quality service, and to develop an effective instrument for mobilization of financial resources for development.

(b) To make recommendations for changing the structure of the insurance industry, for changing the general policy framework, etc.

(c) To take specific suggestions regarding LIC and GIC with a view to improve the functioning of LIC and GIC.
(d) To make recommendations on regulation and supervision of the insurance sector in India.

(e) To make recommendations on the role and functioning of surveyors, intermediaries like agents, etc. in the insurance sector.

(f) To make recommendations on any other matter which are relevant for development of the insurance industry in India.

5.2.2 Mukherjee Committee Report

Immediately after the publication of the Malhotra Committee Report, a new committee (called the Mukherjee Committee) was set-up to make concrete plans for the requirements of the newly formed insurance companies. Recommendations of the Mukherjee committee were never made public. But, from the information that filtered out it became clear that the committee recommended the inclusion of certain ratios in insurance company balance sheets to ensure transparency in accounting. But the finance minister objected. He argued (probably on the advice of some of the potential entrants) that it could affect the prospects of a developing insurance company.

5.2.3 Insurance Regulatory Act (1999)

After the report of the Malhotra committee came out, changes in the insurance industry appeared imminent. On March 16, 1999, the Indian cabinet approved an insurance regulatory authority (IRA) Bill that was designed to liberalize the insurance sector. In 1999 the government passed the insurance regulatory and development authority (IRDA) Act. This Act repealed the monopoly conferred to the Life Insurance Corporation in 1956 and to the General Insurance Corporation in 1972.

The authority created by the Act is now called IRDA. It has ten members. New licenses are being given to private companies. IRDA has separated out life, non-life and reinsurance insurance businesses. Therefore, a company has to have separate licenses for each line business.
Objectives of the Insurance Regulatory and Development Authority (IRDA):

- To protect the interest of and secure fair treatment to policyholders.
- To bring about speedy and orderly growth of the insurance industry for the benefit of the common man, and to provide long-term funds for accelerating growth of the economy.
- To set, promote, monitor and enforce high standards of integrity, financial soundness, fair dealing and competence of those it regulates.
- To ensure speedy settlement of genuine claim, to prevent insurance frauds and other malpractices and put in place effective grievance redressal machinery.
- 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 amongst market players.
- To take action where such standards are inadequate or ineffectively enforced.
- To bring about optimum amount of self-regulation in day-to-day working of the industry consistent with the requirement of prudential regulation (Annual Report of IRDA 2002-03).

Some Details of the IRDA Bill

On July 14, 2000, the chairman of IRDA set forth a set of regulations in the Indian Insurance Market.

5.3 REGULATIONS OF IRDA

The First covers the Insurance Advisory Committee that sets out the rules and regulation.

The Second stipulates that the “Appointed Actuary” has to be a fellow of the Actuarial Society if India. Given that there has been a dearth of actuaries in India with the qualification of a fellow of the Actuarial Society of India, this becomes a requirement of tall order. As a result, some companies have not been able to attract a qualified Appointment Actuary (Dasgupta, 2001). The IRDA is also in the process of replacing the Actuarial Society
of India by a newly formed institution to be called the Chartered Institute of Indian Actuaries (modeled after the Institute of Actuaries of London). Curiously, for life insurers the appointed Actuary has to be an internal company employee, but he or she may be an external consultant if the company happens to be a non-life insurance company.

**Third**, the Appointed Actuary would be responsible for reporting to the IRDA a detailed account of the company.

**Fourth**, insurance agents should have at least a high school diploma along with training of 100 hours from a recognized institution. More than a dozen institutions have been recognized by the IRDA for training insurance agent.

**Fifth**, the IRDA has set up strict guidelines on asset and liability management of the insurance companies along with solvency margin requirements. Initial margins are set high (compared with developed countries). The margins vary with the lines of business (for eg. Fire insurance has a low margins then aviation insurance).

**Sixth**, the disclosure requirements have been kept rather vague. This has been done despite the recommendations to the contrary by the Mukherjee committee recommendations.

**Seventh**, all the insurers are forced to provide some coverage for the rural sector.

**In respect of life insurer:**

- 5% in the first financial year
- 7% in the second financial year
- 10% in the third financial year
- 12% in the fourth financial year
- 15% in the fifth financial year

**In respect of general Insurer:**

- 2% in the first financial year
- 3% in the second financial year
- 5% thereafter.
Immediately after the passage of the Act, a number of companies announced that they would seek foreign partnership.

**Registration of new players under IRDA act**

Insurance Regulatory and Development Authority was constituted in 1999 by an Act of parliament to protect the interest of the policy holders and to regulate, promote and ensure orderly growth of the insurance industry. IRDA allows registration of new players in the insurance field. It also has the authority to renew, modify, withdraw, suspend or cancel such registration. IRDA insures the protection of interest of the policy holders in matters concerning assigning of policy, nomination by a policy holders, insurable interest, settlement of insurance claim, surrender value of policy and other terms and conditions of contracts of insurance. It specifies requisite qualification, code of conduct and practical training for intermediary or insurance intermediaries and agents. After creation of IRDA, insurance sector has seen tremendous growth. Before IRDA came into force there were only players in insurance field, namely, Life Insurance Corporation of India (LIC) and General Insurance Corporation of India (GIC). IRDA consists of ten member team that comprises a Chairman, five whole-time members and four part-time members.

**Role of Detariffing**

By detariffing one is not bounded by the limits of tariff. As tariff is a document which is set of instructions with specific guidelines to under write the different types of business. So far insurance industry is concerned no one can violate the tariff guidelines. Every insurer has to follow these guidelines and book the premium on the premium rates as given in the tariff. The tariff is a statutory document by which all insurers and their employees/agent are bound.

As tariff is set of fixed guidelines regarding premium rates as well as other insurance terms. On the other hand the word detariffs means there is no set rule. Nobody is bound by the specific guidelines. All the statutory binding is abolished. Every insurer can move as per his own choice. They can negotiate with the insured on every point (premium rates and risk coverage). By detariffing the most gainer shall be the customer. The customer who is the bread feeder of the whole business community. With the support of detariffing one can please his bread feeder up to any limit.
Today, we are living in an era of competition. And as there is a stiff competition in the market any by detariffing one can offer any premium rates considering the status of the client. So far as the disadvantages of detariffing are concerned the worst effect of this shall be the growth of unhealthy competition. All the insurance marketing force shall try to commit the most competitive rates. And there shall be huge down fall in business. It will be difficult for customer to pay the enough premiums according to the market rates. The customer will always insist on the lowest quotation and further exploit on negotiation table. As there shall be no rules or guidelines regarding premium rates the entire insurer shall try to beat its competitor. The insured shall definitely try to exploit the insurer by giving the wrong prices of other insurer at the time of negotiations. It is necessary that total freedom should not be given to the insurer since it will lead to a total chaos and unhealthy competition in the market. And no one should be allowed to cross the limits which are laid by the insurance companies.

Considering the overall aspects of detariffing it is a good step. It shall not only create a competitive spirit but also provide the best to its bread feeder. As the best provisions for the bread feeder is most wanted and most required requirement of this era. Everybody wants cheap and best products and that can only be provided by the way of healthy competition and healthy competition can be done by the way of detariffing.

Rationale of Tariff Free Regime

General insurance companies and other stake holders in the insurance market have been voicing the demand for removal of tariff as the existence of tariff was considered contrary to free market principles and insurance products need to be priced based on market forces. The authority has accordingly considered moving to a tariff free regime in due course.

In a market free of tariffs, any responsible insurer should have in place, the following internal capabilities, procedures and controls. The authority would like to highlight the various steps to be taken by the insurers to insure that the shift from a tariffed market to a market where the insurer are free to fix the rates and determine the terms and conditions of contract as early as possible. While this not assumes that all lines of business would be detariffed, it may be limited to lines other than motor in view of the size able share the motor
premium commands in the overall premium collected by insurer and large number of policy holders involved in this line of business. Whether the motor premium id detariffed or not it would be necessary to put in place sufficient safe guard to insure that all vehicles get insurance cover at reasonable rates as motor tariff would be impacted in ether scenario.

**New Changing Policy Regime in General Insurance**

All insurers will start with the policy terms and conditions as per existing tariffs. However, an insurer may review the terms and conditions and make changes there in for use after they are approved by IRDA, the IRDA will look at the changes from the point of view of the simplification of the language of the cover, underwriting prudence and technical soundness of the changes. Risks which are rated on the basis of international market terms may continue to the governed by terms and conditions acceptable to the reinsurance markets of repute.

Now India is on the new journey from a nation protected in guard of license and tariff regime to a nation competing on the global market condition. It is being predicted that the growth in India could exceed from other countries like China, Britain and Japan, to become the third largest economy in the world after china and America. In this strong economy the insurance sector development should not be obstructed by tariff any more.

The following IRDA Regulations are very effective tools and mechanism to take care of the policyholders in the detariff regime.


With the expected detariff regime this sector will enjoy freedom and autonomy for its growth in the line of other service sector like well developed banking system, so detariff is must in the general insurance industry without any doubt and delay.
5.4 INDIAN INSURANCE INDUSTRY

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

Life Insurers:
- Life Insurance Corporation of India (LIC)

General Insurers:
- General Insurance Corporation of India (GIC) (with effect from Dec’2000, a National Reinsurer)
  - General Insurance Corporation had four subsidiary companies. These subsidiaries have been de-linked from the present company and made as independent insurance companies. These companies are as under:-
    1. The Oriental Insurance Company Limited.
    2. The New India Assurance Company Limited.
    4. United India Insurance Company Limited.

5.5 INDIAN INSURANCE BUSINESS:

Insurance business is divided into four classes:

- Life Insurance
- Fire Insurance
- Marine Insurance
- Miscellaneous Insurance
  - Life Insurer transacts life insurance business and General Insurers transact the rest.
  - No composites are permitted as per law.

INDIAN LEGISLATION (as on 1.4.2000):

- Insurance is a federal subject in India. The primary legislation that deals with insurance business in India is:
CUSTOMER PROTECTION

Insurance industry has Ombudsman in 12 cities. Each Ombudsman is empowered to redress customer grievances in respect of insurance contracts on personal lines where the insured amount is less than Rs.20 lakhs, in accordance with the Ombudsmen.

5.6 INSURANCE COUNCILS

The insurance councils that were in existence under the provision of the India Insurance Act 1938 were not effective and practically defunct during the days of state monopoly. After the advent of the IRDA in February 2001, vide the power vested in it under section 64C and 64F of the Insurance Act, 1938, the IRDA revived the Life Insurance Council and General Insurance Council. These two councils, each headed by a member of IRDA, play significant roles in establishing industry standards. As a need was felt for the constitution of an appellate authority for the various decisions of the IRDA, on the lines of the Securities Appellate Tribunal, the Government notified the setting up of an appellate authority for the insurance industry, and also set up a single bench and a division bench, it is expected that shortly a full- fledged appellate body would be set up as envisaged in the Law Commission Report on the subject.

Regulation of insurance is not an exclusive Indian phenomenon. Insurance is amongst the highly regulated businesses in the world. Interestingly, a view is strongly emerging that, in India, the insurance council representing the industry and the IRDA should become a self-regulatory body and address itself to issues relating to the management of the industry as is being done in some countries abroad. However, some industry experts opine that while regulatory mechanisms are regaining lost ground in many countries, as self- regulation had turned out to be a poor proxy, a switchover from well-established regulatory systems to a liberal, self-regulatory mechanism might not be in the interest of the customers.
REFERENCES