CHAPTER –II
THE ORIGIN AND GROWTH OF INSURANCE
IN THE INDIAN CONTEXT

This chapter deals with the history of insurance. It explains the origin and growth of insurance business in the Indian context. The concept of insurance has been prevalent in India since ancient times amongst Hindus. Overseas traders practiced a system of marine insurance. The joint family system, peculiar to India, was a method of social insurance of every member of the family on his life. The law relating to insurance has gradually developed, undergoing several phases from nationalization of the insurance industry to the recent reforms permitting entry of private players and foreign investment in the insurance industry.

History of insurance:

Insurance probably made a beginning in the ancient land of Babylonia in the 18th century B.C., Babylonia king Hammurabi developed a code of law, known as the Code of Hammurabi, which codified many specific rules governing the practices of early risk-sharing activities. For instance, the code dictated that traders had to repay merchants who financed trading voyages unless thieves stole goods in transit, in which case debts would be cancelled.

This was similar to the system of insurance known as bottomry which existed in Phoenicia in 1200 B. C. In this system, backers loaned money to
merchants to finance voyage. Merchants offered their ships (the hull was known as the ship’s bottom’) as collateral for such loans. When a trip succeeded, the merchant would pay the trip’s backer the original loan plus interest, the equivalent of a premium. If a ship went down on its voyage, the trip’s backer would cancel the merchant’s loan.

The Greeks and Romans developed the earliest systems of life insurance. They formed societies which paid dues that went toward paying for the burial of members. Sometimes these societies also paid for the living expenses of deceased members’ of the families. During the Middle Ages (5th to 15th centuries A. D.), workers joined together for helping the families in the group in the event of death or illness of the group members.

Insurance as we know it today took its shape in 17th century England. The policy of life of William Gybbons on June 18, 1633 was the first recorded evidence. There was a place called Lloyd’s Coffee House in London, owned by Edward Lloyd, where merchants, ship-owners and underwriters met to discuss and transact business. In 1871, Lloyd’s Act was passed incorporating the members of the association into a single corporate body with perpetual succession and corporate seal. It extended from marine insurance to other insurance and guarantee business. Today, Lloyd’s has become the world’s best known insurance brand. It is commonly misunderstood that Lloyd’s is an insurance company. Actually, it is a society of members, known as underwriters’, both corporate and individual, who underwrite in syndicates on
whose behalf professional underwriters accept risk. Thus, supporting capital is provided by investment institutions, specialist investors, international insurance companies and individual.

**History of India’s Insurance Business:**

In “Rigiveda” we find the term “Yogakshema Bahamayam” which is more or less akin to the well being and security of people. This makes it clear that the traces of sharing the future losses were available even in ancient India\(^1\). This suggests that a form of “community insurance” was prevalent around 1000 BC and practiced by the Aryans.

Life insurance was first set up in India through a British company called the Oriental Life Insurance company in 1818 followed by the Bombay Assurance company in 1823, the Madras Equitable Life Insurance Society in 1829, the Bombay Mutual Life Assurance Society 1871 and the Oriental Life Assurance Company in 1874. All of these companies operated in India but did not insure the lives of Indians. They were insuring the lives of Europeans living in India.

The first General Insurance Company viz., Triton Insurance Co. Ltd., was established in Calcutta in 1850 whose shares were held mainly by the Britishers\(^2\). Insurance business was conducted in India without any specific regulation for the insurance business. They were subject to Indian companies Act1866. After the start of the “Be Indian Buy Indian Movement” (called Swadeshi Movement) in 1905, indigenous enterprises sprang up in many
industries. Not surprisingly, the Movement also touched the insurance industry leading to the formation of dozens of life insurance companies along with provident fund companies (provident fund companies are pension funds). The first indigenous general insurance company was the Indian Mercantile Insurance company Limited set up in Bombay in 1907.

In 1912, two sets of legislation were passed: 1) The Indian Life Assurance Companies Act and 2) The Provident Insurance Societies Act. The features of the legislation:

(a) They were the first legislations in India that particularly targeted the insurance sector.

(b) They left general insurance business out of it. The Government did not feel the necessity to regulate general insurance.

(c) They restricted activities of the Indian insurers even though the model used was the British Act of 1909.

The birth of the Insurance Act 1938:

In 1937, the Government of India set up a consultative committee. Mr. Sushil C. Sen, a well known solicitor of Calcutta, was appointed the chair of the committee. He consulted a wide range of interested parties including the industry. It was debated in the Legislative Assembly. Finally, in 1938, the Insurance Act was passed. This piece of legislation was the first comprehensive one in India. It covered both life and general insurance companies. It clearly defined what would come under the life insurance business, the fire insurance business and so on. It covered deposits, supervision of insurance companies,
investments, commissions of agents, directors appointed by the policyholders among others. General insurance business is defined to mean fire, marine and miscellaneous insurance business whether carried on singly or in combination with one/more of them\(^3\). To implement the 1938 Act, an insurance department was first set up in the Ministry of Commerce by the Government of India. Later, it was transferred to the Ministry of Finance.

**Nationalization of Insurance in India:**

After India became independent in 1947, National Planning modeled after the Soviet Union was implemented. The genesis of nationalization of life insurance came from a document produced by Mr. H. D. Malaviya called “Insurance business in India” on behalf of the Indian National congress. The Finance Minster C. D. Deshmukh announced nationalization of the life insurance business in 1956. Life insurance business was nationalized on 19\(^{th}\) January 1956\(^4\). The Government brought together life insurers under one nationalized monopoly corporation and Life Insurance Corporation of India was born.

At that time there were 154 Indian life insurance companies. In addition there were 16 non-Indian companies and 75 provident societies issuing life insurance policies. Most of these companies were centered in the metropolitan areas like Bombay, Calcutta, Delhi and Madras.

The reasons behind the nationalization of life insurance were (1) the government wanted to channel more resources to national development programmers. (2) it sought to increase insurance market penetration through
nationalization. (3) the government found the number of failures of insurance companies to be unacceptable. The government argued that the failures were the result of mismanagement and nationalization would help to better protect policyholders.

General insurance was not nationalized in 1956 along with the life insurance. The reason was addressed by the then Finance Minister C.D. Deshmukh, in his budget speech of 1956.

“I would also like to explain briefly why we decided not to bring in general insurance into the public sector. The consideration which influenced us most is the basic fact that general insurance is a part and parcel of the private sector of trade and industry and functions on a year to year basis. Errors and omissions in the conduct of its business do not directly affect the individual citizen. Life insurance business, by contrast, directly concerns the individual citizen whose savings, so vitally needed for economic development, may be affected by any acts of folly or misfeasance on the part of those in control or be retarded by their lack of imaginative policy”.

**Nationalization of General Insurance Business:**

Sixteen years later, in 1972, non-life insurance was finally nationalized (with effect from 1st January 1973). At that time there were 107 general insurance companies. They were mainly large city-oriented, operating at different levels of sophistication. Upon nationalization, these businesses were assigned to the four subsidiaries (roughly of equal size) of the General
Insurance Corporation of India (GIC). The General Insurance Business (Nationalization) Act 1972 provides that the Central Government shall form a Government company in accordance with the provisions of the companies Act 1956, to be known as General Insurance Corporation of India for the purpose of superintending, controlling and carrying on the business of general insurance. The authorized capital of `75 crores of the Corporation, out of which `5 crores is the subscribed capital wholly contributed by the Central Government.5

The General Insurance Corporation was incorporated as a holding company in November 1972 and it commenced business on January 1, 1973. It had four subsidiaries: (1) the National Insurance Company, (2) the New India Assurance Company, (3) the Oriental Insurance Company, and (4) the United India Insurance Company with head offices in Calcutta (now Kolkata), Bombay (now Mumbai), New Delhi and Madras (now Chennai) respectively. Collectively these subsidiaries are known as the NOUN for their initials. All the five entities are government companies registered under the Indian Companies Act, 1956.6

Here were several goals in setting up this structure: (1) The subsidiary companies were expected to set up standards of conduct, sound practices and provision of efficient customer service in general insurance business. (2) The GIC was to help control the expenses of the subsidiaries. (3) It was to help with the investment of funds for its four subsidiaries. (4) It was to bring general insurance to the rural areas of the country, by distributing business to the four
subsidiaries, each operating in different areas in India. (5) The GIC was also designated the national reinsurer. By law, all domestic insurers were to cede 20% of the gross direct premium in India to the GIC under the section 101A of the Insurance Act of 1938. The idea was to retain as much risk as possible domestically. This was in turn motivated by the desire to minimize the expenditure on foreign exchange. (6) All the four subsidiaries were supposed to compete with one another.

Insurance Sector Reforms:

In 1993, Malhotra committee, headed by former Finance Secretary and RBI Governor R.N. Malhotra, was formed to evaluate the Indian insurance industry and recommended its future direction. The Malhotra Committee Report strongly recommended that the General Insurance Corporation should cease to be the holding company and concentrate on reinsurance business only. The four subsidiaries should become independent companies. The report also noted that the subsidiaries were overstaffed.  

In 1994, the committee submitted the report and suggested some of the key recommendations.

(1) Structure

- Government’s 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 corporations
- All the insurance companies should be given greater freedom to operate.
(2) Competition

- Private companies with a minimum paid up capital of `1 billion should be allowed to enter the industry.
- No company should deal in both life 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.
- One State Level Life Insurance Company should be allowed to operate in each state.

(3) Regulatory body

- Insurance Act should be changed.
- An Insurance Regulatory body should be set up.
- Controller of Insurance (currently a part from the Finance Ministry) should be made independent.

(4) Investments

- Mandatory Investments 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 (Their current holdings to be brought down to this level over a period of time).
(5) Customer service

- LIC should pay interest on delays in payments beyond 30 days.
- Insurance companies must be encouraged to set up unit linked pension plans.
- Computerization of operations and updating of technology to be carried out in the insurance industry.

After the report of the Malhotra Committee, changes in the insurance industry appeared imminent. Unfortunately, instability of the Central Government in power slowed down the process. The dramatic climax came in 1999. On March 16, 1999, the Indian Cabinet approved an Insurance Regulatory Authority (IRA) Bill designed to liberalize the insurance sector. The government fell in April 1999 just on the eve of the passage of the Bill. The deregulation was put on hold once again. On December 7, 1999, the new government passed the Insurance Regulatory and Development Authority 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 the Insurance Regulatory and Development Authority.

New licenses are being given to private companies. The Insurance Regulatory and Development authority has separated out life, non-life and reinsurance insurance businesses. Therefore, a company has to have separate licenses for each line of business.
The Insurance Regulatory and Development Act 1999 was set up. “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 therewith or incidental thereto and further to amend the Insurance Act, 1938, the Life Insurance Corporation Act, 1956, and the General Insurance Business (Nationalization) Act, 1972.”

With the General Insurance Business (Nationalization) Amendment Act 2002 coming into effect from March 21.2002, GIC of India ceased to be a holding company of its subsidiaries, their ownership was vested with the Government of India. The GIC was doing only reinsurance business in India. The effect of the US economic meltdown was not felt in the Banking and Insurance Sectors in India because majority of them were with the government.8

The following table shows the number of life and non-life insurance companies in India.

**TABLE 2.1**

<table>
<thead>
<tr>
<th>Type of insurance</th>
<th>Life insurance</th>
<th>General insurance</th>
<th>Re-insurance</th>
<th>others</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Sector Companies</td>
<td>1</td>
<td>4</td>
<td>1</td>
<td>2</td>
<td>8</td>
</tr>
<tr>
<td>Private sector Companies</td>
<td>23</td>
<td>18</td>
<td>-</td>
<td>-</td>
<td>41</td>
</tr>
<tr>
<td>Total</td>
<td>24</td>
<td>22</td>
<td>1</td>
<td>2</td>
<td>49</td>
</tr>
</tbody>
</table>

*Source: Website.*
<table>
<thead>
<tr>
<th>Life Insurance Companies in India^9</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Life Insurance Corporation of India (Public Sector)</td>
</tr>
<tr>
<td>2. MetLife India Life Insurance</td>
</tr>
<tr>
<td>3. ICICI Prudential</td>
</tr>
<tr>
<td>7. TATA AIG Life Insurance</td>
</tr>
<tr>
<td>8. HDFC Standard Life</td>
</tr>
<tr>
<td>11. Kotak Life Insurance</td>
</tr>
</tbody>
</table>
General Insurance Companies in India:

1) New India Assurance Co Ltd (Public Sector)
11) Tata AIG General

2) United India Insurance Co Ltd (Public Sector)
12) Cholamandalam MS

3) Oriental Insurance Co Ltd (Public Sector)
13) Shriram General Insurance

4) National Insurance Co Ltd (Public Sector)
14) Future Generali

5) ICICI Lombard
15) Bharti AXA

6) Bajaj Allianz
16) Universal Sompo

7) Reliance General Insurance
17) Raheja QBE General

8) IFFCO Tokio
18) SBI General Insurance

9) HDFC ERGO
19) L & T General Insurance

10) Royal Sundaram

Standalone Health Insurance Companies:

20) Star Health Insurance

21) Apollo Munich Health Insurance

22) Max Bupa Health Insurance

Export Credit Guarantee Insurance:

23) Export Credit Insurance (Public Sector)
Agriculture Insurance Company:

24) Agriculture Insurance (AIC) (Public Sector)

Re-Insurance:

GIC-Re (Re-Insurer) (Public Sector)

REGULATORY AUTHORITIES:

1. The Insurance Regulatory and Development Authority (IRDA)

Reforms were initiated with the passage of Insurance Regulatory and Development Authority (IRDA) Bill in 1999. IRDA was set up as an independent regulatory authority, which has put in place regulations in line with global norms. IRDA has been framing regulations and registering the private sector insurance companies. It launched the IRDA online service for issue and renewal of licenses to agents. Anyone income of the Insurance Regulatory and Development Authority established under the relevant Act 1999 is fully exempt from the A. Y.2001-2002\(^{10}\).

Powers, Duties and Functions of IRDA

The IRDA Act, 1999 lays down the duties, powers and functions of IRDA. The Authority shall have the duty to regulate, promote and ensure orderly growth of the insurance business and re-insurance business. The powers and functions of the Authority shall include,

- Issue to the applicant a certificate of registration, renew, modify, withdraw, suspend or cancel such registration
 Protection of the interests of the policy holders 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

 Specifying requisite qualifications, code of conduct and practical training for intermediary of insurance intermediaries and agents

 Specifying the code of conduct for surveyors and loss assessors

 Promoting efficiency in the conduct of insurance business

 Promoting and regulating professional organizations connected with the insurance and re-insurance business

 Levying fees and other charges

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

 Control and regulation of the rates, advantages, terms and conditions that may be regulated by the Tariff Advisory Committee

 Specifying the form and manner in which books of account shall be maintained and settlement of accounts shall be rendered by insurers and other insurance intermediaries

 Regulating investment of funds by insurance companies

 Regulating maintenance of margin of solvency

 Adjudication of disputes between insurers and intermediaries or insurance intermediaries
Supervising the functioning of the Tariff Advisory Committee

Specifying the percentage of premium income of the insurer to finance schemes for promoting and regulating professional organizations engaged in insurance and reinsurance business

Specifying the percentage of the life insurance and general insurance business to be undertaken by the insurer in the rural or social sector, and

Exercising such other powers as may be prescribed

2. Tariff Advisory Committee

The Tariff Advisory committee is a body corporate, which controls and regulates the rates, advantages, terms and conditions offered by insurers in the general insurance business. The Advisory committee has the authority to require any insurer to supply such information or statements necessary for discharge of its functions. Any insurer failing to comply with such provisions shall be deemed to have contravened the provisions of the Insurance Act. Every insurer is required to make an annual payment of fees to the Advisory Committee of an amount not exceeding in case of reinsurance business in India, one percent of the total premiums in respect of facultative insurance accepted by him in India, and in case of any other insurance business, one percent of the total gross premium written direct by him in India.
3. Insurance Association of India, Councils and Committees

All insurers and provident societies incorporated or domiciled in India are members of the Insurance Association of India and all insurers and provident societies incorporated or domiciled elsewhere than in India are associate members of the Insurance Association. There are two councils of the Insurance Association, namely the Life Insurance Council and the General Insurance Council. The Life Insurance Council, through its Executive Committee, conducts examinations for individuals wishing to qualify themselves as insurance agents. It also fixes the limits for actual expenses by which the insurer carrying of life insurance business or any group of insurers can exceed from the prescribed limits under the Insurance Act. Similarly, the General Insurance Council, through its Executive Committee, may fix the limits by which the actual expenses of management incurred by an insurer carrying on general insurance business may exceed the limits as prescribed in the Insurance Act.

4. Ombudsman

The Ombudsman are appointed in accordance with the Redressal of Public Grievances Rules, 1998, to resolve all complaints relating to settlement of claims on the part of insurance companies in a cost-effective, efficient and effective manner. Any person who has a grievance against an insurer may make a complaint to an Ombudsman within his jurisdiction, in the manner specified.
The Ombudsman act as a counselor and mediator and make recommendations to both parties in the event, that the complaint is settled by agreement between both the parties. However, if the complaint is not settled by agreement, the Ombudsman may pass an award of compensation within three months of the complaint, which shall not be in excess of which is necessary to cover the loss suffered by the complainant as a direct consequence of the insured peril, or for an amount not exceeding rupees two million, whichever is lower.

**Territorial Jurisdiction of Ombudsman**\(^{13}\)

The governing body has pointed twelve Ombudsman across the country allotting them different geographical areas as their areas of jurisdiction. The Ombudsman may hold sitting at various places within their area of jurisdiction in order to expedite disposal of complaints. The offices of the twelve insurance Ombudsmen are located at (1) Bhopal, (2) Bhubaneswar, (3) Cochin, (4) Guwahati, (5) Chandigarh, (6) New Delhi, (7) Chennai, (8) Kolkata, (9) Ahmedabad, (10) Lucknow, (11) Mumbai, and (12) Hyderabad.

**Legislative and regulatory matters:**

The Insurance Act, 1938 was brought into force from 1\(^{st}\) July, 1938 as “an Act to consider and amend the law relating to the business of insurance” It applies to both life and general insurance business.
The Act has been amended a number of times notably by the passing of the Insurance Regulatory and Development Authority Act, 1999. The various laws which have a direct or indirect bearing on practice of insurance are:

4. The Bill of Lading Act, 1855.
5. The Indian Ports (Major Ports) Act, 1963.
8. The Indian Post Office Act, 1898.

**Investments:**

**1. Life Insurance Business:**

Every insurer is required to invest and keep invested certain amount as determined under the Insurance Act. The funds of the policyholders cannot be invested (directly or indirectly) outside India. An insurer involved in the business of life insurance is required to invest and keep invested at all times, assets, the value of which is not less than the sum of the amount of its liabilities.
to holders of life insurance policies in India on account of matured claims and
the amount required to meet the liability on policies of life insurance maturing
for payments in India. The following table shows the Investment regulations of
life insurance business in India.

**TABLE 2.2**

**Investment Regulations of Life Insurance Business**

<table>
<thead>
<tr>
<th>Type of Investment</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government Securities</td>
<td>At least 25%</td>
</tr>
<tr>
<td>Government Securities or other approved securities including the aforesaid</td>
<td>Not less than 50%</td>
</tr>
<tr>
<td>Approved investments</td>
<td></td>
</tr>
<tr>
<td>(a) Infrastructure and social sector</td>
<td>Not less than 15%</td>
</tr>
<tr>
<td>(b) Others to be governed by exposure/prudential income 20%</td>
<td></td>
</tr>
<tr>
<td>Other than in approved investments to be governed by exposure/prudential norms</td>
<td>15%</td>
</tr>
</tbody>
</table>

*Source: Gazette of India Extraordinary Part III Section 4. IRDA (Investment) Regulations, 2000*

**2. General Insurance Business:**

An insurer carrying on general insurance business is required to invest
and keep at all times his total assets in approved securities in the following
manner. The investment should be made not less than 20% on Central
government securities and 30% on State government securities. On Housing
and loans to Statement government not less than 5%, on investment in
approved investments not less than 40% and not less than 25% on other than in
approved investments.
TABLE 2.3
Investment Regulations of Non-life Insurance Business

<table>
<thead>
<tr>
<th>Type of investments</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Central government securities</td>
<td>Not less than 20%</td>
</tr>
<tr>
<td>State government securities and other guaranteed securities including the aforesaid</td>
<td>Not less than 30%</td>
</tr>
<tr>
<td>Housing and loans to state government for housing and firefighting equipment</td>
<td>Not less than 5%</td>
</tr>
<tr>
<td>Investments in approved investments</td>
<td></td>
</tr>
<tr>
<td>(a) Infrastructure and social sector</td>
<td>Not less than 10%</td>
</tr>
<tr>
<td>(b) Others to be governed exposure / prudential norms</td>
<td>Not exceeding 30%</td>
</tr>
<tr>
<td>Other than in approved investments to be governed by exposure/prudential norms</td>
<td>Not exceeding 25%</td>
</tr>
</tbody>
</table>


Important events in the History of Indian Insurance Industry:

1912 - First piece of insurance regulation promulgated –Indian Life Insurance Company Act, 1912

1928 - Promulgation of the Indian Insurance Companies Act

1938 - Insurance Act 1938 introduced, the first comprehensive legislation to regulate insurance business in India

1956 - Nationalization of life insurance business in India
1972 - Nationalization of general insurance business in India
1993 - Setting-up of the Malhotra committee
1994 - Recommendations of Malhotra Committee released
1995 - Setting-up of Mukherjee committee
1996 - Setting-up of an (interim) Insurance Regulatory Authority (IRA)
1997 - Mukherjee committee Report submitted but not made public
1997 - The government gives greater autonomy to LIC, GIC and its subsidiaries with regard to the restructuring of boards and flexibility in investment norms aimed at channeling funds to the infrastructure sector
1998 - The cabinet decides to allow 40% foreign equity in private sector companies - 26% to foreign companies and 14% to non-resident Indians, overseas corporate Bodies and foreign institutional investors
1999 - The standing committee headed by Murali Deora decides that foreign equity in private insurance should be limited to 26%. The IRA Act was renamed the Insurance Regulatory and Development Authority (IRDA) Act
1999 - Cabinet clears IRDA Act
2000 - President gives assent to the IRDA Act
2002 - Delinking of four Public Sector General Insurance companies from the holding Company General Insurance Corporation of India.
2007 - Detariffication
END NOTE