CHAPTER - I

INTRODUCTION

1.1 GENERAL INTRODUCTION

The Indian Banking system is unique and perhaps has no comparison in
the banking history of any country in the world. The demography of the country
clearly indicates its diverse culture, overwhelming population - of which a major
(large) portion still remains illiterate and also an equally large reservoir of
managerial and technologically advanced talent, with extreme disparities in
income. By considering these factors and to ensure equitable development and
growth for all the regions, the planners and policy makers of our country since
independence have combined both socialistic and capitalistic features in the
country’s economic policy frame work. Accordingly, the banking system have to
serve the goals of economic policies enunciated in successive five year plans,
particularly policies concerning equitable income distribution, balanced regional
economic growth and reduction and elimination of private sector monopolies in
trade and industry. All these make the functioning of banks rather challenging.

The banking sector assumes much importance especially in our country,
which faces the problems of acute shortage of capital, depressed industrial
development, poor means of transport and communication.

The initiation of financial sector reforms in early 1990’s has provided the
much needed impetus to the Indian banks in proliferating their business activities.
Today, the banks are no longer restricted to their traditional activity of accepting
deposits and making advances but are allowed to diversify into areas like insurance, mutual funds, stock trading, housing finance, pension funds, investment banking, etc. which till the other day was the domain of other non–banking organizations. Although reforms in the financial sector played an important role in diversification of banking sector but the, explosive growth of financial market in early 1980’s had been the other reason for such a change. Developments in financial markets resulted in disintermediation. This forced banks to enter into new areas of business in order to retain their customer base.

The business of banking around the globe has been changing due to the integration of global financial markets, development of new technologies, universalization of banking operations and diversification in non–banking activities. Due to all these revamps, the boundaries that have kept various financial services separate from each other have disappeared. Thus, the comingling of different financial services has provided synergies in operations and development of new concepts.

Banks are now able to operate across a broader range of activities, including insurance, via, legally independent risk carriers. The insurance companies and banks are not competing within just the life insurance industry and banking industry respectively any more but within the wider financial services market place.

Customer preferences regarding investments are changing. For medium term and long term investments there is a trend away from deposits and toward insurance products and mutual funds. This shift in investment preferences has led
to a reduction in the share of personal savings held as deposits, whichever traditionally the core element of profitability for a bank, managing client’s money. Banks have sought to offset some of the losses by entering life insurance business.

Over the last few decades, the liberalization and deregulation of the financial sector have drawn the world of the banking and insurance closer together. Inter - bank competition has thickened and banks face increasing competition from non - banking financial institutions and the financial markets. The liberalization of financial sector in India has exposed Indian banks to a new economic environment that is characterized by increased competition and new regulatory requirements. As a result there is a transformation in every sphere of activities of the banks in India especially in their governance, nature of business, style of functioning and delivery mechanisms.

The accelerated process of globalization of financial markets and integration of Indian financial sector with the rest of the world has enhanced both opportunities and challenges. Change is the only constant factor in the world and banking is not an exception to this in the competitive world.

Earlier, our country was supply based and it was an era of seller’s market. But at present the situation has changed and the nation has entered into an era of buyer’s market. As the economy grows, not only does it demand stronger and vibrant financial sector but also necessitate to provide more sophisticated and variety of financial products and services. India is considered as one of the fast developing economies among the emerging market economies, and with that the financial sector has also grown vibrant along with the financial reforms.
Today, Banks have realized that customer’s life style is changing and the only way to retain and acquire customer is customer centricity. Banks are adopting technologies to improve customer service, design flexible and customized products, which increase sales opportunities and differentiate themselves in a market where product features are easily closed.

To cope with the challenges, banks have adopted differentiation strategy by building a better innovative product delivery system that shifted from arched type banking to peoples’ lifestyle banking. Life style is the way a person lives including the person’s individual attitude to the world. In India lifestyle depends on person’s background, family, education and nature of the work. It is a process of establishing relationship between banking products offered in the market and targeted lifestyle groups. It involves segmenting the market on the basis of life style dimensions, positioning the product in a way that appeals to the activities, interests and opinions of the targeted market and undertaking specific promotional campaigns which exploit lifestyle appeals to enhance the market value of the offered product. Customer’s need and preferences are changing. These changes can become great business opportunities for alert bankers and a threat for the bankers who fail to adopt them. It is very essential to know how customers behave in modern banking. Customer behavior is also influenced by personality, Socio – demographic characteristics and life style. Today traditional methods of purchasing goods and services have been changing. In the global banking system, there has also been a structural and functional change of profound magnitude. Banking sectors function under a huge pressure to increase their business volume by focusing more on customer retention besides enhancing relationship with them.
An important landmark in the development of the Indian banking sector in the recent years has been the initiation of the reforms following the recommendations of the first Narasimhan Committee on financial system. This committee was setup in August 1991 by the Government of India as a part of its economy-wide structural adjustment programme, and in response to the unsatisfactory economic and qualitative performance of the public sector banks (Sarkar 1999) owing to lack of competition, low capital base, low productivity and high intermediation cost. The financial sector reforms which started in early 1990’s, have uprooted many of the outdated regulatory fences which banks were required to follow in order to carry out their activities.

This provided more liberty to banks and they started exploiting different areas of operation. Gradually, many of the banks, apart from their indigenous function which was banking, started having substantial interests in all sorts of financial businesses like insurance, funds management, mutual funds, securities trading, etc. Eventually, such banks acquired the status of financial conglomerate and slowly began moving towards universal Banking framework.

With the advent of universal banking concept in the Indian banking sector commercial banks are focusing on product innovation to meet customer satisfaction effectively. In view of these objectives, banks have opted for diversification into allied areas of banking business.

Reforms in the banking sector (especially after the first phase of financial reforms) laid the basis for a sound banking system (Velayudham, 2002) and at the same time provided the much required impetus to Indian banks to carry out
their business operations in the competitive and deregulated environment. In fact deregulation has triggered competition and this was presumed to intensify beyond in 2009 and beyond when the Indian Banking sector would be thrown open to foreign participants (Rajadhyaksha, 2004). Thus it is evident that competition, here, does not mean just in terms of the number of competitors, but it is in terms of pro-liberalization of innovations, specialized markets, cross border trade in financial services and capital flows - all of which are to be supported by adequate information and communication technology.

A striking feature of this phase is that profitability had become the main criterion of working of the banks. Banks have moved from branch expansion to branch rationalization and from mass recruitment to voluntary retirement schemes (VRS) and with selective recruitment. Finally they moved from least technology to technology driven total branch automation and inter branch linking (Lakshminarasimha and Murali, 2004). This was deemed necessary because competition in the banking sector had increased tremendously with blurred product boundary. Banks now are facing competition not only from domestic, private and public sector banks but also from foreign banks, Non-banking financial companies, DFIs as well as Mutual funds and Insurance companies.

With increased competition in the banking sector as well as margins on traditional business being eaten away, today, banking is no longer limited to borrowing and lending of funds (Singh, 2001) but it is seen as a business related to information on financial transactions. Significantly, since the last decade of the 20th century banks have diversified into new areas to widen their business
Modern banking has seen banks diversifying along product and business lines which considerably enlarged the operations of the various public and private sector banks. Banks have ventured into areas like merchant banking, leasing, factoring, mutual funds, portfolio management, Venture capital, housing finance, stock trading, securitization of debts, etc., thereby proliferating in multidirectional way and in multidimensional manner.

Another area where banks have started emphasizing on is customer satisfaction. In fact, one of the biggest challenges for a service organization like bank is to meet rising customer expectations (Khan, 2004). Today, customers expect information and advice on tailor-made asset management, operations management and high technology services incorporating instruments such as derivatives (Singh, 2001). And it is believed that Information Technology plays a significant role in providing better customer service, presumably at a lower cost. Therefore, several innovative IT based services such as ATM, Electronic Fund Transfer, Anywhere Any time banking, Smart cards, Net banking, etc. are adopted by banks (Sureshchandar, Rajandran and Anantharaman, 2003) to facilitate customers in availing products of their choice.

Thus, in the Era of Innovative banking, Indian banks need to shore up their Balance Sheet in time, fund the sectors of the economy that need the money most, and acquire to get the scale up to take on competition especially in post 2009 so as to retain its customer base. Banks world over have realized that offering value added services facilitate to meet client expectation with the entry of new generation private sector and foreign banks with advanced base of
automation and multiple channels, because customers have become more discerning in the products and services offered to them. This makes it imperative for the Indian banks to provide a wide variety and the best possible products and services to ensure customer satisfaction. When these products are offered to the customer from the same bank branch, it automatically makes the branch a one-shop financial provider or a super market of financial services to its customers.

The RBI, being a regulatory authority of the banking system has recognized the need for banks to diversify their activities, permitted them at the right time to enter into insurance sector as well. Banks with their brand image and existing customer relationship offer a natural market for selling insurance products. Insurance is an ideal option as banks can fulfill the three major requirements for its successful insurance business viz., asset management and investment skills, distribution and capital adequacy. A bank, which is able to market insurance products has a competitive edge over its competitors and further more it can impart complete financial planning services to its customers under one roof. To sum up, for banks, insurance offers opportunities such as sophisticated product offerings, greater life cycle management, diversification and growth of revenue base from existing relationships, diversifying risk by tapping another area of profitability and the realization that insurance is a necessary customer need. Therefore, public sector banks entering into insurance business which is only a natural corollary and is fully justified too as ‘insurance’ is another financial product best owned to the bank customer. (Sumathi Kumaraswamy 2012)
The banking and insurance industry have changed rapidly in the changing economic environment throughout the world. Banking and Insurance Industry together contributes about seven percent GDP of our economy. The increased phase of market competition due to liberalization and privatization forced life insurers to be competitive by cutting cost and serving the customers in better way. In view to reach huge untapped market, the concept of Bancassurance was introduced by the IRDA. Bancassurance is a new and an emerging model of channel of distribution adopted by almost all the life insurance players to increase the market share and insurance penetration. (Anusha et.al 2012)

One of the most significant changes in the financial services sector over the past few years have been the appearance and development of Bancassurance. Banking institutions and insurance companies have found bancassurance to be an attractive- and often profitable – complement to their existing activities.

The successes demonstrated by various bancassurance operations, although not all of them have been successful, have attracted the attention of the financial service sector and further new operations continue to be set up regularly. Banks can prove to be vital distribution channel due to their existing wide network of branches all over. The Insurance Regulatory Development Authority (IRDA) has permitted banks to venture into marketing insurance products on a risk participation basis. In order to ensure that only the serious ones with the financial muscle enter into the selling of insurance products, the regulator has laid down certain prerequisites. Banks need to possess at least 50 crores of net worth and capital adequacy of minimum of 10 percent to make an entry.
Bancassurance refers to the selling of insurance policies through banks. Banks earn revenue through this sale. In India, the process began in 2000. IRDA came up with regulations on the registration of Indian companies. Government of India also issued a notification specifying “insurance” as a permissible form of business that could be undertaken by banks under Sec. 6(1) (0) of the banking Regulation Act, 1949. However it was clarified that any bank intending to take up the business would have to take specific approval from RBI. All scheduled commercial banks were permitted to undertake insurance business as the agent of insurance companies on the basis, of collecting fee as charger without any risk participation. Specific rules were framed for the setting up of joint venture companies for undertaking insurance business with risk participation. There has been no looking back ever since.

Traditionally, insurance products were sold only through individual agents and they accounted for a major chunk of the business in retail segment. With the opening up of this sector to private players, competition has become more intense and the public sector major LIC has been challenged with a flood of new products and new means of marketing. Insurance industry in India has been progressing at a rapid pace since the opening up of the sector to the entry of private companies in 2000 and the winds of liberalization and privatization policies of the Government. The huge untapped population provides unlimited scope of life insurance companies for market expansion and premium growth. The success of life insurance companies largely depends on the effectiveness of distribution channel. The appropriate selection of channel of distribution helps to
increase the volume of sales, brand promotion and brand building by providing quality services to the customers. In spite of the presence of multiple distribution channels and a wide range of new products; the performance of life insurance companies is unsatisfactory. Hence to improve insurance growth and market penetration of life insurance business a new concept called “Bancassurance” was introduced by IRDA in late 2002 where insurance companies have tie ups with different banks through Joint – Venture for selling insurance products.

The concept of Bancassurance originated in India when the Government issued notification under Banking Regulation Act which allowed Indian Banks to do insurance distribution. It started picking up after Regulatory and Development Authority (IRDA) passed a notification in October 2002 on ‘corporate Agency’ regulations. Bancassurance accounts for a share of almost 35 to 40 percentage of the premium income amongst the private players in India. It is a phenomenon where insurance products are offered through the distribution channels of the banking services along with a complete range of banking and investment products and services. Bancassurance tries to exploit synergies between both insurance companies and Banks.
Some of the examples of Bancassurance are given below

<table>
<thead>
<tr>
<th>Company</th>
<th>Bank List</th>
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<tr>
<td>Brila Sun life Insurance</td>
<td>Bank of Rajasthan, Andhra Bank, bank of Muscat, Development Credit Bank, Deutsche Bank and Catholic Syrian Bank, Citi Bank, IDBI Bank, Karur Vysya Bank Ltd</td>
</tr>
<tr>
<td>Aviva Life Insurance</td>
<td>Canara Bank, Lakshmi Vilas Bank, American Express Bank and ABN AMRO Bank</td>
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<td>HDFC Standard Life</td>
<td>Standard Union Bank of India, Indian Bank, HDFC Bank</td>
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<tr>
<td>Insurance</td>
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<tr>
<td>ICICI Prudential</td>
<td>ICICI Bank, Bank of India, Citi Bank, Allahabad bank, Federal Bank, South Indian Bank and Punjab and Maharashtra Co-operative Bank</td>
</tr>
<tr>
<td>SBI Life</td>
<td>SBI, BNP Paribas</td>
</tr>
<tr>
<td>Tata AIG</td>
<td>HSBC, Union Bank of India, IDBI Bank</td>
</tr>
<tr>
<td>Bajaj Allianz</td>
<td>Syndicate Bank, Centurion Bank and Standard Chartered Bank, Karnataka Bank, Punjab and Sind Bank</td>
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<td>ING Vysya</td>
<td>Karur Vysya Bank, Bharat Overseas Bank</td>
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<td>United India Insurance</td>
<td>Punjab National Bank, Andra Bank, Indian Bank, Federal Bank, South Indian Bank, Dhanalakshmi Bank</td>
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<td>New India Assurance</td>
<td>Union Bank of India, State Bank of India, Corporation Bank</td>
</tr>
<tr>
<td>Oriental Insurance</td>
<td>State Bank of Saurashtra, Oriental Bank of Commerce</td>
</tr>
</tbody>
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(Source: www.irda.gov.in and www.bimaonline.com)
Presently, 23 life insurance companies are operating in India and all have tie-ups with one bank or the other. Bancassurance is a type of agreement or partnership between bank and insurance company where banks get a fixed percentage or proportion of profit incentive depending on the volume of business. Most of the insurance company found bancassurance as a low cost attractive distribution channel when compared to other channels.

The bank insurance model (BIM), also sometimes known as bancassurance, is the partnership or relationship between a bank and an insurance company whereby the insurance company uses the bank sales channel in order to sell insurance products, an arrangement in which a bank and an insurance company form a partnership so that the insurance company can sell its products to the bank's client base. BIM allows the insurance company to maintain smaller direct sales teams as their products are sold through the bank to bank customers by bank staff and employees as well.

There was a time in the past when insurance policies were meant for a small part of public who were financially strong. Today the scenario has completely changed wherein insurance policies reach every person in almost every corner of our nation. This change in the financial horizon was ushered in with the birth of bancassurance in India. Banks which were meant for deposits, loans and transactions are allowed to provide insurance policies to people.

Researches and present day statistics speak about the need for a well equipped financial structure for a country to grow economically. The financial resources in the hands of people should be channelized in effective manner so as to
increase the returns from the basic financial structure of the nation and also the quality of life of people. Insurance policies are instruments/products that play a major role in upholding the financial structure of developed countries. Though the teething phase of insurance, one may say is just past, a desirable foothold is yet to be found. With growth in the number of middle class families in the country, RBI recognized the need for an effective method to make insurance policies reach the people of all economic classes. Implementing bancassurance in India is one such development that took place towards the cause. The need and the subsequent development of bancassurance in India began in order to improve the channels through which insurance policies are sold or marketed so as to make them reach the hands of common man, to widen the area of working of banking sector which has a network that is spread widely in every part of the nation and also to improve the services of insurance by creating a competitive atmosphere among private insurance companies in the market.

The Benefits of Bancassurance includes that it encourages customers of banks to purchase insurance policies and further helps in building better relationship with the bank. The people who are unaware of and are not within the reach of insurance policies can be benefitted through widely distributed banking networks and better marketing channels of banks. Increase in the number of providers causes increase in competition and hence better premium rates and better services from bancassurance will be expected as compared to traditional insurance companies.

The Demerits of bancassurance include the Data management of an individual customer’s identity and contact details which may result in the insurance company utilizing the details to market their products, thus compromising data
security. There is a possibility of conflict of interest between the other products of bank and insurance policies (like money back policy). This could confuse the customer regarding where he has to invest. Better approach and services provided by banks to customer remains a hope rather than a fact. This is because many banks in India are known for their bad customer service and this fact turns worse when they are responsible to sell insurance products. Work nature to market insurance products require submissive attitude, which is a point that has to be worked out by many banks in India.

1.2 BANCASSURANCE- GLOBAL EXPERIENCE

Bancassurance has grown at different places and taken shapes and forms in different countries depending upon demography, economic and legislative prescriptions in that country. It is most successful in Europe, especially in France, from where it started, Italy, Belgium and Luxembourg. The concept of bancassurance is relatively new in the USA. Bancassurance growth differs due to various reasons in different countries. The Glass-Steagall Act of 1933 prevented the banks of the USA from entering into alliance with different financial services providers, thereby putting a barrier on bancassurance. As a result of this life insurance was primarily sold through individual agents, who focused on wealthier individuals, leading to a majority of the American middle class households being under insured. With the US Government repealing the Act in 1999, the concept of bancassurance started gaining grounds in the USA also. In 2000 itself in France, bancassurance accounted for 35% of Life Insurance premiums; 60% of savings premiums; 7% of Property Insurance and 69% of new premium income in individual savings.
Bancassurance in European Countries

The development of bancassurance in various European countries, including France, Germany, Italy, Netherlands and Spain are examined according to the three dimensions mentioned below:

- The importance of country specific factors in promoting the bancassurance phenomenon
- The entry structures dominating in different countries.
- The level of bancassurance integration

Country specific factors in the bancassurance trend

The structure of the insurance and banking industries in various European countries shows to explain the varying developments of bancassurance. The French insurance market's inherent uncompetitiveness played a significant role in promoting Bancassurance by allowing banks to capture unprotected market shares. The ease of entry into the life insurance convinced banks that insurance distribution could be an effective way to utilize expensive branch networks to cross-sell a variety of products. The high degree of rivalry among banks themselves also meant that French banks would be reluctant to be left out of a market where other competitors flourished. In Germany, conservative marketing rules in the insurance industry had an opposite effect. It made it difficult for German banks to profitably distribute insurance products. Moreover, a tradition of cross-shareholdings in the financial industry has meant that banks have chosen to collaborate with insurance companies rather than develop inhouse Bancassurance.
**Italy's Bancassurance** development has been hindered by a weak banking industry. However, the potential for high growth rates in life insurance fares well for bancassurers but further consolidation in the industry is needed for Italian banks to compete with the large tied financial sales forces.

**Dutch Bancassurance** developments are associated very closely with the financial industry concentrated structure. The concentration of the industry in the hands of a few powerful players led to Bancassurance giants to market their products through multi-distribution channels.

An underdeveloped insurance market, similar to Italy, characterized the Spanish Bancassurance. This left plenty of scope for banks to exploit their longstanding ties with insurance companies with a view to cross-sell insurance products. Spanish insurance-banking links are ancient although the full cross-selling potential of Bancassurance has been exploited only recently. One of the features of recent years is the entry of foreign companies, which has promoted such links.

A major factor in promoting UK Bancassurance was the high costs associated with traditional insurance distribution channels. While there are highly competitive insurance companies in the United Kingdom, the long-standing reliance on expensive independent financial intermediaries gave banks the opportunity to free them and to develop cheap alternative channels of distribution.
Other factors too have contributed to the differing levels of Bancassurance integration in various European countries. One such factor relates to the existence of tax-advantageous life insurance products, which bear a strong resemblance to traditional savings products of banks. The main advantage of such products is the ease with which banks have been able to train their sales staff. French Bancassurance was undoubtedly boosted by 'bons de capitalisation', single premium long-term policies that entitled holders to avoid tax relief on the income generated over an accumulation period. Spanish Bancassurance was initially boosted by single premium policies free of withholding tax. In Italy, some bancassurers based their success on similar savings-like products. The growth of endowment products in the United Kingdom also facilitated Bancassurance development. Such products probably had the most impact in France and Spain. However, the tax advantages associated with these products have gradually eroded and banks have introduced a wider range of more complex insurance products over time in order to increase their market shares.

Another major factor for Bancassurance development is regulatory changes. In the Netherlands, Bancassurance became predominant in 1990, after the relaxation of ownership limitations between banking and insurance sector. In the United Kingdom, the polarization principle laid down in the Financial Services Act led banks eventually to build societies to tie to a single insurer, and thus made equity links between the two sectors more attractive. In Italy, the 1991 reform that relaxed equity constraints between the two sectors prompted a flurry of links in the financial sector. One of the reasons why Bancassurance has been slow to develop relates to the remaining constraint that investment of banks in
insurance companies cannot exceed 20% of bank capital, this occurred in a
country where banks are small by international standards. The reform of life
insurance marketing in Spain also played a significant role in boosting
Bancassurance sales. In France, the governments' implicit encouragement of
Bancassurance links probably had an impact on the generalization of this
strategy.

Clearly, national differences in Bancassurance stem from the varying
characteristics of the financial industry in each country. The degree of
competitiveness in domestic financial sectors made Bancassurance initiatives
more or less successful. Similarly, the design of life insurance products made it
more or less easy for banks to train their staff in selling insurance products;
moreover, tax advantages made some products highly attractive to consumers and
hence encouraged banks to enter the market. Finally, domestic regulatory
changes by and large relaxed constraints on cross-shareholdings between the
banking and insurance sectors, and thus acted as a facilitator to the bancassurance
strategy. Bancassurance growth is undoubtedly linked to regulatory reforms in
some countries such as in the Netherlands and Italy.

Entry Routes in Different European Countries

The bancassurers in different countries adopted different entry routes into
the insurance market. In France, banks mainly selected the go-alone route by
starting up their own insurance operations whereas in many other countries,
banks have been eager to associate with insurance companies to start up
operations. This is true of Italy, Spain and the United Kingdom. In contrast,
Dutch Bancassurance is yet limited mostly to marketing agreements that exclude
equity links. It is interesting to note that French banks, who predominantly chose to start up their own operations, achieved the greatest Bancassurance market shares.

**Level of Bancassurance Integration in Europe**

The degree of Bancassurance is compared between two dimensions: the market shares achieved by bancassurers in selected countries and the type of link between the two activities from distribution agreements to full ownership. The greater level of integration of French Bancassurance operations where insurance subsidiaries mainly serve the needs of their banking parents might explain why French banks were successful in achieving high market shares. Other countries achieved significant market shares by integrating their operations in a similar way. The exception among the countries reviewed is Germany. The German model of co-operation with the insurance industry appears to have prevented German banks achieving significant market shares in insurance.

**1.3 BANCASSURANCE IN INDIA**

India - a land of promise for bancassurance - with a democratic government and a population of one billion has a savings rate of 23 percentage of which the domestic households' savings with the bank constitute more than 50 percentage. This presents an enviable opportunity for insurers to take advantage of the strong banking platform. The banking network consists of 65,000 bank branches, of which 33,000 branches are in the rural areas and 14,000 branches in the semi urban areas, with each branch serving an average of 15,000 people. The opportunities and equally the challenges that Indian market presents are immense.
With expertise in financial needs, saving patterns of the customers they serve, banks provide something that insurance companies would find it nearly impossible to achieve on their own. Currently, many foreign insurers are partnering banks and non-bank financial corporations to leverage their local branch network and experience. Solid brand name, strong customer affinity, customized product and service delivery and flexibility to change are some key success factors in this country with its cultural and linguistic diversity and huge economic capability.

**Status of Bancassurance in India**

RBI had permitted Banks to enter the Insurance Sector, as the Insurance business takes a longer time to break even. Banks which do not have the archival and technical expertise, should be strong to withstand the initial losses, therefore the following norms or eligibility criteria for the banks were suggested by RBI which may be permitted to enter the insurance sector;

1. A minimum net worth of Rs. 500 crores.
2. CRAR not less than 10%.
3. NPAs within the reasonable level.
4. Made profits continuous during the last 3 years.
5. Satisfactory track record of the subsidiaries, if any.

The banks fulfilling the above norms would be permitted to take up the insurance business, individually or jointly with domestic or foreign partner. The maximum stake a bank can hold in a JV is 50 % and subsidiaries or associates can pick up additional stakes.
6. Any scheduled commercial bank would be permitted to undertake the
insurance business as agent of an insurance company on the basis of fee
or charges without risk participation obtaining a case-by-case clearance.

Until now only individuals could act as insurance agents. After the
opening of insurance sector to private players, RBI has selectively allowed banks
to promote insurance companies. The ostensible reason was to allow them to
make use of their surplus staff and branch network and increase earnings.

Now, the IRDA also has come up with guidelines pertaining to Referral
Arrangement with the banks. The same is reproduced below:

IRDA/CIR/003/2003 30th January 2003 RE: Referral Arrangement to all
the CEOs of Insurance Companies.

Arising out of the notification of the Monetary and Credit Policy by
Reserve Bank of India on October, 2002 permitting banks to undertake referral
business through their network of branches for selling insurance products with
prior permission of IRDA and RBI for which the Authority has been receiving
enquiries from insurance companies about IRDA's guidelines on the subject.

All insurers entering into agreements or arrangements with banks under
the referral fee model or renewing such agreements or arrangements may take
note that the following points form part of any agreement or arrangement.

1. The referral fee shall be for access to bank's customer database and it
should not exceed the ceilings on agency commission prescribed under
the Insurance Act, 1938 and the IRDA Regulations and shall form part
of acquisition cost of business and shall not form part of management expense. This will include arrangements where bank branches operating outside India are sharing customers' base of NRI account holders.

2. The participation by bank's customers shall be purely on voluntary basis and this should be stated prominently in all publicity materials distributed by the bank and the insurance company. It should also be clearly mentioned that the contract of insurance is between insurance company and the insured and not between the bank and insured.

3. There should be no linkage either direct or indirect between the provision of banking services by the bank to its customers and use of the insurance products.

4. There should be no interest surcharge, concession dependent upon non use or use of the insurance service by the customer.

5. Any administrative or management expenses to be incurred for distributing literature and other information on insurance should be brought out in the agreement. Information exchange should be exclusively for the promotion of the business and not for any other purposes during the validity of the agreement.

6. The bank will not be paid any referral fee for promotional campaigns.

7. The insurance company shall not provide any details of its customers to the bank on account of confidential obligations.
8. The insurance company and the bank shall enter into a referral fee arrangement based on a Memorandum of understanding or an Agreement which needs to be filed with the Authority.

9. The bank which enters into referral fee arrangements should not be permitted to enter into any similar arrangements with more than one life insurance company or more than one general insurance company. This is important to ensure that a bank does not act defacto as an insurance agent or as an insurance broker without any license.

10. The insurance company should enter into a separate agreement with the bank for allowing the use of premises and the use of existing infrastructure of the bank and a copy of the same should be filed with the Authority. In no case the fee for such services rendered or offered by the bank should be linked to premium and it should be on a flat basis. Such fee shall not form part of acquisition cost of business.

11. All agreements should be for fixed period and should be with prior approval of the boards of both the insurance company and the bank.

12. The bank should comply with IRDA Regulations for acting under the referral fee arrangement and IRDA shall have the discretion to apply its own criteria to reject or discontinue such arrangements.

If insurers have already entered into such agreements or arrangements they must ensure that copies of the same stand filed with the Authority.
Corporate agency regulations

Banks can act as corporate agents for only one life and one non life insurance company for a commission, as per the current regulatory framework set up by IRDA. The banks are not eligible for any payout other than commission. It is also mandated that banks should also observe code of conduct prescribed towards both customer and the principal who is the insurer.

Broker Route

Banks cannot become brokers, as regulations require brokers to be exclusively engaged in insurance broking. RBI does not allow banks to promote separate insurance broking outfits. Even otherwise MNC banks or their parent corporations are not inclined to promote broking subsidiaries in view of FDI cap of 26%. This virtually closes all options for banks or their subsidiaries to become brokers.

Referral Arrangement

Banks which are not eligible for corporate agency license as per RBI guidelines can adopt a referral model wherein they merely part with their client database with insurers for a fee. IRDA had earlier issued guidelines on Referral arrangements (IRDA/Cir./004/2003, dated 14-02-2003) with Banks, etc. The referral arrangement with a bank is for access to its customer database, provision of physical infrastructure and for display of publicity material of the insurer. A bank could not enter into a referral agreement with more than one insurer. The bank and customer’s participation was purely voluntary and there was not to be any linkage between banking services to customers and the use of insurance
products. Referral route is extended for insurers to acquire customer database of banks, which can provide a large number of prospective policyholders. The bank’s role is linked to the sale of the database above, while the insurer is expected to solicit customers from the database and complete the transaction through its own resource.

With time, it was observed that the difference between corporate agency and referral was obliterated. Several banks charged hefty fee for entering into the referral agreement, over and above the fee which was linked to sale. Further, upfront fee was being collected for providing infrastructure for locating insurer’s staff and advertisements in bank premises. It was also observed that in a few cases, referral banks were actually soliciting the customers for sale of insurance, through untrained staff.

As the regulatory framework was found to be inadequate, the referral system had degenerated into rogue agency system and was dismantled through regulations by IRDA in 2010.

**Insurance through Joint ventures**

Apart from the options mentioned above, fully integrated Bancassurance involves much more comprehensive relationship between insurer and bank, where banks will have a counter within and sell/market the insurance products as a core activity. This includes banks having wholly owned insurance subsidiaries with or without foreign participation. In the Indian case several banks like ICICI Bank and HDFC Bank in private sector and State Bank of India in the public sector, have resorted to this model and have set up joint ventures.
**Bancassurance products**

All life insurance products are by nature products which belong to the wider financial services sector. However, a bancassurance operation in particular, the decision on the types of insurance products which it wants to sell is very closely related to the methods of distribution which it plans to use. This is because the effort and expertise needed to sell a given product must be appropriate to the skills and cost base of the chosen distribution method. A product which is very hard for the available distribution channels to sell is not going to be successful for the operation, whether in terms of sales volumes or of profits.

Apart from the traditional insurance products, bancassurers have developed special products in order to fulfill certain needs which emanate from banking transactions, or to improve certain products in order to make them more attractive and useful to the customer.

These products can be broken down into three categories:

1. Finance and repayment products
2. Depositors’ products
3. Simple standardized package products

**Finance and Repayment Products**

The concept of this group of products is fairly simple. A financial institution which grants loans or credit to individuals is concerned with the case of early death or permanent disability of the borrower, where the outstanding loan
or credit amount may not be recoverable. This will happen where the financial standing of the surviving family does not support the outstanding amounts to be easily recoverable, or when the repossession of the item purchased by the loan amount might not be saleable, or when any resale amount is not sufficient for the repayment of the loan.

Along with the financial loss, the lender also runs the risk of damaging its reputation among customers, since it will acquire such reputation through the repossession of items on the unfortunate death of its clients, and the harassment of the unfortunate members of the family. The borrower on the other hand has similar concerns. He does not wish to leave an outstanding loan to be repaid by his family after his death. He is also concerned about his possible inability to repay the loan or credit amount if he becomes permanently disabled. A category of products that can satisfy both parties is the finance and repayment product. Some of the best known products in this category are:

i) Credit insurance

Credit insurance can be offered in cases where a loan is granted to the customer and serves as additional security for the bank while providing financial protection to the customer’s property in the case of his death prior to the repayment of the loan. This normally involves a decreasing term life cover with an initial sum insured which is equal to the amount of the loan. For example, if the amount of loan taken is 10 lakhs, then the policy will have an initial sum assured of Rs 10 lakhs. The sum insured would decrease in line with the repayment of the loan amount. Upon the death of the insured person the amount
payable would be equal to the outstanding loan amount, with or without the accrued interest at that time. If the outstanding loan amount decreases on a predetermined basis, then it is possible to calculate the appropriate premium at the date on which the loan was granted. In cases where the loan amount fluctuates according to the needs of the borrower or due to fluctuations in interest rates, a monthly premium based on the outstanding loan amount is a more equitable solution, provided, that the outstanding amount is available for calculating the premium. Annual premium or single premium contracts can be offered in cases where the loan amount at all periods can be predetermined. Where the loan amount can fluctuate, single premiums are not permitted. In the case where a single premium is charged, the premium amount is frequently added to the loan amount. Almost all loans covered under credit insurance schemes are of short repayment duration, i.e. up to 5 years. In cases where this scheme is a compulsory part of a loan, the premiums charged can reflect the fact that there is no selection against the insurer on medical grounds (antiselection). In such cases the company can limit itself to simplified underwriting. The reduced processing costs can be passed on in the form of lower premiums. In cases where this scheme is not compulsory, further medical or occupational questions are asked for underwriting purposes. The extra work involved may force premiums to be increased. Permanent total disability benefit may be offered together with the decreasing term insurance since the ability of the borrower to repay the loan may depend on the borrower maintaining his income. In some cases temporary total disability benefit covering the instalments payable is also offered. It is also possible for a bank to pay the premiums, which are very low, and use this as a
marketing tool in order to attract new customers and sell its products more easily. The marketing tool is to offer “free” protection in the case of death or permanent total disability. The bank will include the cost of protection in the interest rate charged to borrowers. Credit insurance is suitable for arrangements such as

- Mortgage loans
- Business loans
- Personal loans
- Hire purchase arrangements.

This cover can also be issued as a group policy covering all customers. The master policy remains with the bank and a certificate of insurance is given to each customer.

ii) Overdraft insurance

Usually banks offer overdraft facilities to their customers. This is an automatic credit up to a pre-agreed amount. For salaried customers this amount is usually two or threetimes their monthly salary. This facility has no repayment term, provided, the salary isdeposited in the bank and the credit always stays within the pre-agreed amount. In thecase where the customer who was using the credit facility dies, this amount has to berepaid by the heirs of the deceased. This practice usually creates problems for both the heirs and the bank. Overdraft insurance can help. Overdraft insurance can be offered intwo different ways:

a) The cover is equal to the credit facility used and a monthly premium is paid according to this amount. In the case where the customer dies and this credit
facility has been used, the outstanding amount due will be repaid to the bank by
the insurance company. In deciding whether to offer this option, the insurer must
consider the risk because people who know their health are limited.

b) The cover equals the maximum pre-agreed credit facility. In case of
death the outstanding amount due will be repaid by the insurance company. If
there is an excess between cover and the outstanding amount due, this amount
will be paid to the heirs of the customer. Premiums in this case can be paid on a
monthly or annual basis. In overdraft insurance the premium is usually adjusted
every year according to the age of the customer. A maximum age for this benefit
usually exists. The premium can be paid by the customer or by the bank as an
offer to its customers. This type of product is suitable for arrangements such as

- Overdraft facilities
- Credit cards and
- Unstructured debts.

iii) Capital repayment

For loans offered for mortgage, educational, personal or business reasons
a repayment scheme through an insurance policy is possible. The customer is
granted the loan and he pays only the loan interest to the bank. He also takes out
an endowment that has a cover equal to the loan amount and with a duration
equal to the repayment period of the loan. The premium is selected so that the
maturity payout is very likely to be able to cover the full loan amount. The policy
is always assigned to the bank and serves as a repayment tool whether the
customer survives or not. These products have proved particularly attractive to customers in countries where life insurance products enjoy favorable tax treatment, or where interest rates charged by lenders on loans repaid by insurance policy proceeds are lower than for capital repayment loans. Due to the high investment element of these products, the premiums for such products are much higher than those of the credit and overdraft insurance that we have mentioned above, although the total cost of the loan to the borrower may not be very different.

**Depositors’ products**

The second category of these special products consists of the so-called depositors’ products. The main types of depositors’ products are:

**a) Depositors’ insurance**

This benefit is designed to attract the public to deposit money with a particular bank. It can be offered in all deposit accounts but usually a minimum deposit amount is required. The level of cover is usually determined by factors such as price and underwriting. A possible product is level with the term of insurance of the premium rate changing every year. Another possibility is to offer accidental death cover. Reasonable limits must be set regarding maximum age and maximum amounts. The premium in this case is usually paid by the bank but it can also be paid by the depositor with a proper marketing approach. The amount of cover is usually a multiple of the cash balance in the deposit account. In the case of the death of the depositor, this cash balance is increased accordingly.
b) Objective achievement insurance (bank savings plans)

This policy can be offered in special deposit accounts where systematic deposits are required to reach a predetermined objective amount at maturity. However, if the depositor dies or suffers total permanent disability, the difference between his objective amount and the cash balance of the account is paid to the depositor or the depositor’s estate in addition to the cash balance. This can be offered by a decreasing term insurance only or in combination with permanent total disability benefit. In cases where the deposit amounts are not predetermined it is advisable to offer coverage which is a multiple of the average cash balance amount during the preceding 6 or 12 months, so that problems of anti selection can be reduced. However, it would still be possible for a customer to increase the account balance rapidly and gain significant life cover without underwriting. For depositors’ insurance, accidental death cover is another option. Here, reasonable limits are set regarding maximum age and maximum amount of coverage and by this product can offer attractive profit margins.

c) Pure investment products

These products have no “insurance” elements, and so contain no risk. They have traditionally been the domain of banks, but in some countries they enjoy a favorable tax treatment if they are offered by an insurance company.

Simple standardized package products

These products are usually group policies which combine covers and which cost the customer less compared when they are bought individually. These
products are usually sold over the counter by bank employees, so they are usually uncomplicated. Household insurance together with waiver of premium on death cover would be an instance.

**Other products**

The objective of product development in most cases is to offer the widest possible range of products so as to enable sales people to select the most suitable plan for each customer’s specific needs. A further range of products and riders which the bancassurers want to offer to clients could include

**a) Products**

- Whole life
- Endowment
- Unit-linked products
- Term insurance products
- Accident and sickness products
- Hospitalization products
- Pension products

**b) Riders (additional benefits attached to the main basic policy) such as**

- Family income benefit
- Waiver-of-premium benefit
- Permanent total disability benefit
- Income replacement benefit
In deciding whether to offer these products further the bancassurer would need to consider whether these can be effectively sold by the employees and agents involved in the bancassurer’s sales operation.

**Distribution channels in bancassurance**

The type of distribution channels that a company uses affects the design and pricing of its products, as well as the way in which the products are promoted and perceived in the marketplace. Some bancassurers started out by selling simple products which could be sold in large volumes but that usually had low margins to cover expenses and profits. If one compares how products and distribution are related to the profits of an organization, one will come to the conclusion that the more complex the products sold are, the higher the required margins need to be. Many banks entered bancassurance with a defensive strategy in their attempt to avoid market share erosion by insurance companies. Very soon, though, they realized that they could gain market share if they expanded their product range, developed a sales culture within their organizations, created a multi-channel distribution structure and exploited the potential of the customer information that can enable the identification of customer needs. Bancassurers make use of various distribution channels

- Career agents
- Special advisers
- Salaried agents
- Bank employees
• Corporate agencies and brokerage firm
• Telemarketing
• Worksite marketing
• Seminar Selling
• E-commerce
• Direct response

Using the broker channel concept, where the broker advises the customer and selects from among products offered by a number of companies can also be attractive to banks. However, it is not understood as bancassurance (where there is a relationship with a particular insurance company). For the insurance company, this channel has disadvantages in that it is difficult to forecast how much business the insurer will receive from the broker. Insurers do not favor the broker channel in bancassurance.

The main characteristics of each of these channels are

Career agents

They are full-time commissioned sales personnel holding an agency contract. Although some insurance companies offer such contracts to part timers, within bancassurance operations such people are usually excluded. Career agents are generally considered to be independent contractors. Consequently an insurance company can exercise control only over the activities of the agent which are specified in his contract. Despite this limitation on control, career agents with suitable training, supervision and motivation can be highly
productive and cost effective. Moreover their level of customer service is usually very high due to the renewal commissions, policy persistency bonuses, or other customer service-related awards paid to them. However, many bancassurers avoid this channel, believing that agents might oversell out of their interest in quantity and not quality. Such problems with career agents usually arise, not due to the nature of this channel, but rather due to the use of improperly designed remuneration and or incentive packages.

**Special advisers**

They are highly trained employees usually belonging to the insurance partner, who distribute insurance products to the bank’s corporate clients. Usually they are paid on a salary basis and they receive incentive compensation based on their sales. Otherwise, they present the same characteristics as those of career agents, with the exception of their training which focuses on the group and business insurance sectors.

**Salaried agents**

They have the same characteristics as career agents. The only difference in terms of their remuneration is that they are paid on a salary basis and they receive incentive compensation based on their sales. Some bancassurers, concerned at the bad publicity which they have received as a result of their career agents concentrating heavily on sales at the expense of customer service, have changed their sales forces to salaried agent status.
Bank employees

They can sell simple products. However, the time which they can devote to insurance sales is limited, for instance, due to limited opening hours and to the need to perform other banking duties. A further restriction on the effectiveness of bank employees in generating insurance business is that they have a limited target market, based on those customers who actually visit the branch during the opening hours. In many set-ups, the bank employees are assisted by the bank’s financial advisers. In both cases, the bank employee establishes the contact to the client and usually sells the simple product whilst the more affluent clients are attended by the financial advisers of the bank which are in a position to sell the more complex products. The financial advisers either sell in the branch but otherwise some banks also have established mobile sales forces. If bank employees only act as “passive” insurance sales staff (or do not actively generate leads), then the bancassurer’s potential can be severely impeded. However, when bank employees are used as “active” centers of influence to refer to warm leads to salaried agents, career agents or special advisers, production volumes can be very high and profitable to bancassurers. The branch manager of the bank has a decisive position: he generates the prospect lists, which are turned over to the sales people in the branch. Furthermore, he has to motivate his sales people to sell, to control the volume of business sold directly via the branch, and to monitor the warm leads.
Set-up or acquisition of agencies or brokerage firms

In the US, quite a number of banks cooperate with independent agencies or brokerage firms whilst in Japan or South Korea banks have founded corporate agencies. The advantage of such arrangements is the availability of specialists needed for complex insurance matters and – in the case of brokerage firms – the opportunity for the bank clients to receive offers not only from one insurance company but from a variety of companies. In addition, these sales channels are more conceived to serve the affluent bank clients.

Direct response

In this channel no salesperson visits the customer to induce a sale and no face-to-face contact between consumer and seller occurs. The consumer purchases products directly from the bancassurer by responding to the company’s advertisement, mailing or telephone offers. This channel can be used for simple packaged products which can be easily understood by the consumer without explanation.

Worksite marketing

Vastly popular in the USA, this channel is used to target employees of the insurer, or a group company. In this method, the insurer launches non-medical insurance cover for the employees of a group company and offers special discounts to all those who propose to take the cover. There is however no obligation on the part of the employees to buy the policy. Worksite marketing is easier to implement if there is a perceived positive image of the parent company.
itself among employees. Secondly, simple forms and simpler illustration of benefits can go a long way to establish sales growth. Cultural and social differences, coupled with a below average company image, may be the major hurdles for growth. Worksite marketing channel has high chances of success, due to the trust and loyalty factor towards their ‘own’ company, as the insurer is perceived to be their ‘own insurance company’. The premium payment usually is monthly mode, and deducted from the salary; thus making the entire process simple. The chance of lapsation of policy is therefore nonexistent, creating win-win positions for both, the insurer and the employee.

E-commerce

This channel is the fastest growing and most convenient way of purchasing insurance cover. Online sales of insurance policies can be encouraged by designing special non-medical term policies, which are easy to understand, and which do not warrant expert advice from trained advisors. E-commerce sites that offer the lowest quotes from all insurers are being introduced by entrepreneurs and they are slowly making their mark. Growth of broadband connections and personal computers, will certainly fuel the growth of online purchases of insurance policies, especially by the white-collar employees, for whom time and convenience are top-most factors in any buying decisions.

It seems very difficult for a single distribution channel to successfully reach the bancassurer’s goals and specific target markets. Many bancassurers are using multiple distribution channels. In this way they avoid becoming locked into one channel and they can offer services to a greater number of target markets.
Multiple distribution channels provide another valuable feature. They enable the enterprise to offer customers multiple options of access. Therefore, if a customer wants to see someone about a particular service one day but wants to transfer funds at a later date, the availability of both branch office and 24-hour telephone access increases the service value to that customer.

**Cultural issues in distribution**

The managers of banks and of life insurance companies will have quite a different attitudes and behavior. There may be differences in the way of thinking and business approaches of bankers and managers of insurance companies. These differences create a communication and implementation problem in bancassurance operations. Banks are traditionally demand-driven organizations with a reactive selling philosophy. Life insurance organizations are usually need-driven and have an aggressive selling philosophy. It has been observed that this friction at the level of bank employees and life insurance salespeople arises from

- differing philosophies towards selling (push v/s pull strategy)

- the jealousies of bank employees regarding remuneration of life sales staff, and

- fears of “cannibalization” of deposits, e.g. the bank employee fears that the salesperson encourages withdrawal of bank deposits, putting the position of bank employee in greater jeopardy. As a result the team spirit is negatively influenced and, since this is a crucial factor for the success of any operation, it has to be confronted.
Cultural differences between the banking and the insurance industries must be understood, respected and lived with in order for the bancassurance venture to succeed. The development of a single culture is another possible solution but this requires a very strong commitment from the top management. This commitment must be continuously conveyed to all bank employees and life insurance agents. One way of achieving this is to develop a “statement of mission” for the new organization and to get the staff to commit to fulfilling this statement. This can help to ensure that there is a common path for the bank and the life insurer. Many organizations try to overcome these cultural differences through the elimination of insurance sales people and the provision of insurance products and services exclusively through bank employees. However this practice creates four major problems:

- By eliminating the sales force, bank employees are forced to cross borders to a different profession where different skills are required and where the competition practices are different.

- The products that bank employees offer are usually simple packaged products or pure investment products – in many cases without a risk element. However, simple packaged products are not always the best solution for the customer who is undoubtedly the centre of any success. Since the insurance industry offers tailor made products and services to its customers, the bancassurers who are using only bank employees to distribute their products will feel the pressure to switch to better products or to develop proper distribution channels. All over the world, more and
more consumers are becoming better informed and seek to buy the most appropriate product through a preferred distribution channel.

- Using only bank employees to sell insurance can severely limit the success of the bancassurer. The bank’s target market is then only the customer-base of the bank accessible to bank employees, who come into the branch. More and more, bank customers can manage their affairs without entering the bank branch and are therefore inaccessible to bank employees.

- Customer service offered in conjunction with the insurance policy is likely to be relatively poor since it is limited to banking hours. Insurance company agents can offer customer service at times more likely to suit the customer.

a) Training system

A carefully designed and well-executed training system will provide all relevant parties with the necessary knowledge and will enable them to perform their duties in relation to the referral process.

b) Selection procedures and system of allocation of branches to agents

Carefully designed and well-executed selection procedures will help safeguard the quality of agents servicing bank branches and increase commitment on the part of both the branches and the agents to the referral process. Similarly, an intelligent system of allocation of branches to agents will help ensure that agents are allocated to branches on a sound basis that aims to support the development of the agent-branch relationship.
c) Measurement, evaluation and reward system

A well-designed system of recording and measuring activity of bank staff and evaluating and rewarding performance based on the recorded activity, will complement the existing staff appraisal system with regard to performance in relation to the referral system. This encourages employees to be objective about their performance in making referrals. It also encourages employees to identify improvements to their performance and to the operation of the referral system.

d) Control system

An effective, non-bureaucratic system of controls will help mitigate the various risks that may undermine the smooth operation of the referral system. Examples of controls here include:

Regular reporting of activity to the management of the bank and of the bancassurer, for example, regarding the

1. Number of new warm leads generated,

2. Proportion of warm leads converted into sales,

3. Lapse experience on in-force contracts.

The report should include comparable figures for earlier periods, results should be split so as to allow sources of differences to be identified (e.g. by branch and by product line).
Benchmarking of the bancassurer’s performance is compared with other financial institutions, to identify differences and to pinpoint where the bancassurers might make improvements.

**Remuneration and incentives**

Compensation packages and incentive schemes are critical factors for the success of bancassurance. The way compensation is allocated encourages the distribution channels to act according to what the organization feels is important. Compensation objectives should also contribute to the overall objectives of the organization. A compensation program, therefore, must be tailored to the needs of an organization and its employees. To raise productivity and lower costs in today’s competitive economic environment, organizations are increasingly setting compensation objectives based on a pay-for-performance standard. In bancassurance operations the need is to motivate each of the following groups:

- Bank employees involved in generating leads and sales
- Sales agents (if the bancassurer uses that approach)
- Bank branch management (for their effort in managing life insurance sales through the branch network)
- Sales agency managers (if at location)

Motivation is particularly important for the sales agents out in the field for whom self-discipline is the key to success. The remuneration terms should be attractive to each of the groups involved. In particular, the designer of the
remuneration package should seek to develop a package which helps each one of the
groups to feel that they get a fair reward for their contribution. The possible range of benefits and incentives in a life insurance agent’s compensation package is unlimited.

Before proceeding to the design of the compensation package, an organization must consider the following

- The compensation package is perhaps the most important element in a sales organization which will influence the volume of business, the costs, the profitability, the productivity and the customer care.

- The way in which the package encourages certain behaviors and discourages others determines the kind of sales force a company attracts and retains. Indeed, it helps to set the tone for the whole sales organization within the company. In order to maintain their competitive position, financial services providers need to be sure they have the right people, in the right jobs, with the right skills, and at the right price. A package therefore needs to be designed to attract and retain the kind of people the company needs in order to develop the kind of sales organization the company wants.

- In developing this package an organization must clearly have in mind the vision how it wants to be in the future, not just now.

- Before its implementation the package must be clearly communicated and explained to every single person involved in the bancassurance venture.
Products are always designed to cover certain expenses. Lower incurred acquisition costs will offer two important advantages: higher profitability to the company and or lower prices to the customers. On the other hand, lower costs imply lower income to sales personnel which may result in higher agent turnover. This in turn can lead to higher costs for the company (e.g. extra costs of recruitment, training, etc.) and consequently lower profitability. Where the policy is with profits, the policyholder will also see reduced benefits. Product pricing is therefore another crucial factor and thus a careful balance between all parties must be achieved. Bancassurers should seek to align the compensation package with their financial targets. This encourages the sales force to work in a way which will make those financial targets easier to achieve. For example, if the expected profitability of product A is very low compared to product B, then the bancassurer will prefer its sales force to sell product B. It can encourage this by paying higher commission rates on product B.

**Remuneration of bank employees**

The remuneration depends on whether the bank employee or the bank’s financial advisers are involved in the sales process or whether the bank employees are providing warm leads. Any commission payable by the insurance company is, as a principle, to be credited to the bank’s profit centre for the bancassurance operation. The management of the bank sets the commission level for each manager and employee engaged in the bancassurance operation. Selling in the bank’s branches (by employees or by financial advisers): For simple packaged products the payment of commission to the bank employee is not
recommended since these products have low profit margins and do not require particularly great selling efforts. Instead employees could be rewarded with gifts and or salary increments based on their selling performance in promoting both banking and insurance products. Such performance could be quantified via the use of a points system whereby the various products are allocated with a number of points. For compulsory products linked to banking facilities no commission or other benefit will be offered since these do not require any selling effort on the part of employees. If, however the financial advisers of the bank are selling – usually the more complex products like in the case of special advisers of the insurance company – the remuneration to the bank may be the full commission for a particular plan. The financial advisers are usually paid on a salary basis and they receive incentive compensation based on their sales.

**Warm leads**

In return for providing warm leads, the bank will get a share, say 50 percentage, of the normal first year commissions. The actual split might be agreed upon the basis of the work done by each of the agent and the bank employee in achieving the average sale, which may vary, for example, by product type. A basis is needed for allocating this amount between branch staff (who provides the warm leads) and the bank’s owners. A possible basis would be

- Bank employees: 25 percentages
- Bank profitability: 25 percentages or 50 percentages

**The bank employees’ commission can be split as follows**

Employee who generates the warm lead: 15%

Branch group award: 10%
The structure shown above generates benefits as follows:

- Financial rewards for employees who generate warm leads
- Financial rewards for managers and other staff of the bank branch who have supported bank activities while the assurance business was being generated
- Recognition of the branch’s contribution to bank profits (which can be reflected in the performance rating by the bank of the branch management).

Group awards or bonuses are more desirable when the contribution of the individual employee is either difficult to distinguish or depends on group cooperation.

**Training for bancassurance**

Training is a critical part of overall business performance. But even before any training starts, it is important to determine

Who needs to receive training?

What kinds of training are required?

Who will be responsible for providing training and for testing what the student has learned from the training.

**Sales force training for bancassurers**

Sales agents and their managers in any selling organization, including insurance, develop a range of knowledge and skills, for example
Product knowledge,
Application of selling techniques, and
Motivation skills.

a) Bank products and distribution channels: The sales force will need to have basic knowledge of the banking products sold by the operation and of the range of distribution channels in force (not just the channels used to sell life insurance).

b) Building up a relationship with bank staff: In many cases, the sales agent is reliant on the quality and quantity of warm leads from bank employees. In turn the sales agent can influence the value of leads – either positively (by achieving a high success rate in turning them into sales and commission) or negatively. Sales agent needs to learn to cooperate with bank employees and must learn how to build effective relationships with people whose job motivation may be very different to his or her own.

c) The bank’s expectations of customer service: The sales agent and sales manager must understand and be prepared to meet the standards for customer service which the bank expects in respect of its customers. The bank’s standards will cover not only insurance business but other relationships (e.g. banking relationships) with the customer. The sales staff must be trained to implement the standards.

Bank employee training for bancassurers

The bank employees will need to be trained in the following aspects of the insurance business:
Much of this list will be new to staff who are used to banking transactions, so it is comparatively long. However, proper and regular training of bank employees is to the success of the operation.

**Quality customer service**

Quality customer service refers to every single activity that the company, its employees and the distribution channels undertake for its customers. In all cases the objective of every person in the company should be to give added value to every transaction or communication, providing additional incentives to customers and enabling the company to:
– distinguish it from competitors,

– improve its image among customers,

– keep its existing customers,

– attract new customers, and

– create additional sales among existing customers.

In a bancassurance venture quality customer service is even more important because the bank refers its customers to the insurance company. The bank’s relationship with the customer can be damaged by poor service from the insurer. For this reason bank employees must be well informed about the customer service standards set by the insurer when they refer them to their customers. At the same time the insurance company staff (including the administrators who will deal with the customer’s questions in future) must be aware of the standards expected by the bank on behalf of “their” clients. These service standards should be written down and agreed upon between the bank and the insurance company. The first step in quality customer service is the development of the right mental attitude amongst bank staff and sales force so that both parties recognize that their primary role is to satisfy the customer. Helping bank staff and sales force to develop the awareness of their own abilities and inherent strengths, to conquer anxieties and to share their ideas and experiences will help the staff’s performance and help them to appreciate their customers’ concerns. A two-way referral system, where the salesforce refers
customers to the bank for banking facilities, can be helpful because trust will be enhanced. Bank employees will be more understanding and more willing to help.

**1.4 REGULATIONS FOR BANCASSURANCE IN INDIA**

RBI Guidelines for the Banks to enter into Insurance Business

Following the issuance of Government of India Notification dated August 3, 2000, specifying ‘Insurance’ as a permissible form of business that could be undertaken by banks under Section 6(1)(o) of the Banking Regulation Act, 1949,

**Insurance business for banks**

1. Any scheduled commercial bank would be permitted to undertake insurance business as agent of insurance companies on fee basis, without any risk participation. The subsidiaries of banks will also be allowed to undertake distribution of insurance product on agency basis.

2. Banks which satisfy the eligibility criteria given below will be permitted to set up a joint venture company for undertaking insurance business with risk participation, subject to safeguards. The maximum equity contribution such a bank can hold in the joint venture company will normally be 50 percent of the paid up capital of the insurance company. On a selective basis the Reserve Bank of India may permit a higher equity contribution by a promoter bank initially, pending divestment of equity within prescribed period.
The eligibility criteria for joint venture participant are as under

I. The net worth of the bank should not be less than Rs.500 crore

II. The CRAR of the bank should not be less than 10 percent

III. The level of non–performing assets should be reasonable

IV. The bank should have net profit for the last three consecutive years

V. The track record of the performance of the subsidiaries, if any, of the concerned bank should be satisfactory.

3. In cases where a foreign partner contributes 26 percent of the equity with the approval of Insurance Regulatory and Development Authority or Foreign Investment Promotion Board, more than one public sector bank may be allowed to participate in the equity of the insurance joint venture. As such participants will also assume insurance risk, only those banks which satisfy the criteria given in paragraph 2 above, would be eligible.

4. A subsidiary of bank or of another bank will not normally be allowed to join the insurance company on risk participation basis. Subsidiaries would include bank subsidiaries undertaking merchant banking, securities, mutual fund, leasing finance, housing finance business, etc.

5. Banks which are not eligible for ‘joint venture’ participant as above, can make investments up to 10% of the net worth of the bank or Rs.50 crore, whichever is lower, in the insurance company for providing infrastructure and services support. Such participation shall be treated as an investment and should be without any contingent liability for the bank.
The eligibility criteria for these banks will be as under

I. The CRAR of the bank should not be less than 10 percent

II. The level of NPAs should be reasonable

III. The bank should have net profit for the last three consecutive years.

6. All 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 case to case basis keeping in view all relevant factors including the position in regard to the level of non-performing assets of the applicant bank so as to ensure that non-performing assets do not pose any future threat to the bank in its present or the proposed line of activity, viz., insurance business. It should be ensured that 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 ‘arms length’ relationship between the bank and the insurance outfit.

**Need for Bancassurance in India**

Researches and present day statistics speak about the need for a well equipped financial structure for a country that helps it to grow economically. Now when there is a talk of statistics, it is needed to check out the Insurance density and Insurance penetration. Even though it has dramatically increased over the years (as is evident from the figures of 2000-01 and 2009-10), it is still lesser than many developed countries. In other words these two parameters indicate that there is ample scope of penetration in the said segment.
The financial resources in the hands of people if channelized in an effective manner will not only help it increase the returns from the basic financial structure of the nation but also improve the quality of living of people. Insurance policies being instruments/products that play a major role in upholding the financial structure of developed countries maintains its importance amongst the entire kitty of financial product offerings.

The need and subsequent development of bancassurance in India began for the following reasons

a) To improve the channels through which insurance policies are sold/marketed so as to make them reach the hands of common man.

b) The size of the country, a diverse set of people combined with problems of connectivity in rural areas, makes insurance selling in India a very difficult proposition. Insurance companies require immense distribution strength and tremendous manpower to reach out to such a huge customer base. This distribution could undergo a sea change if all insurance companies proposed to bring insurance products into the lives of the common man by making them available at the most basic financial point, the local bank branch, through Bancassurance. Imagine the reach today, when we are talking of more than 80500 branches of various banks across the country.

c) To improve the services of insurance by creating a competitive atmosphere among private insurance companies in the market.
Regulations of Bancassurance in India

In India banking and insurance sectors are regulated by two different entities. The banking sector is governed by Reserve Bank of India and the insurance sector is regulated by Insurance Regulatory and Development Authority (IRDA). Bancassurance, being the combination of two sectors comes under the purview of both the mentioned regulators. Each of them has elaborate and descriptive rules, restrictions and guidelines.

Reasons for entering into Bancassurance

Insurance is an ideal option as banks feel they fulfill the three major requirements for a successful Insurance business that is asset management, investment skills and capital adequacy. Banks would also like to fulfill all the financial needs of their customers.

For the following reasons banks are entering into Insurance business such as

**a. Wide network of branches**

Banks can prove to be a vital distribution channel due to their existing wide network of branches.

**b. Corporate clients**

Banks can utilize their existing clientele, which includes corporate as well as retail clients to market insurance products. Depending on the relationship with its clients it would become easier to influence the insurance purchase decisions of its clients. Customers too, having banked with a particular bank for a long period repose a sense of trust and faith in the bank.
c. Customer database

Customer database - raw information on the customers spending habits, investment purchase can prove to be a goldmine. Such information channelized in the right manner which will help work out marketing strategies and arrive at result-oriented decisions targeting prospects.

Personalized Service

Since banks have direct contacts with customers, the service area can be tackled easily. Customers, other than their day-to-day financial requirements will also get assistance for premium payment, surrender, transfer of policies and many more.

d. Rural penetration

The existing wide network of banks in rural areas can be utilized for selling insurance products. Having been accustomed to the customers' choices banks are in a better position to understand the needs of the customers and sell tailor made policies. Customers too, considering their long-standing relationship with banks, find them trustworthy. Servicing of policies will also become easier.

e. Cross-selling products

Banks in their normal course of functions lend finance in the form of loans for cars, or for buying a house to clients. They can combine insurance products and sell them as a package. In the current scenario banks can cross sell their products along with the insurance products.
f. Fee based service

Insurance products can be sold as a fee based service. In an age where banks are trying to venture into selling mutual funds and other financial products besides stock Broking, etc, selling insurance products could also give an additional boost to the banks bottom line.

Bancassurance arrangement

Distribution Agreements

a) Separate sales force: One party's distribution channels gain access to the client base of the other party. This is the simplest form of bancassurance. Once a bank and the insurance company enter into a distribution agreement, according to which the bank automatically passes on to a friendly insurance company all warm leads emanating from the bank's client base, this can generate very profitable income for both partners. For the bank the costs involved—besides those for basic training of branch employees—are relatively low.

b) Hand In Glove: A bank signs a distribution agreement with an insurance company, under which the bank will act as their appointed representative. The financial investment required by the bank is relatively low. The products offered by the bank can be branded.

Joint Venture

This is the creation of a new company by an existing bank and an existing insurance company.
Mergers and Acquisition

a) A bank wholly or partially acquires an insurance company.

b) The acquisition of a bank that is wholly or partially owned by an insurance company is also possible. In this case the main objective is usually to open the way for the insurance company to use the bank's retail banking branches and gain access to valuable client information as well as to corporate clients, allowing the insurance company to tap into the lucrative market for company pension plans. Finally it offers the insurance company's sales force bank product diversification (and vice versa).

Start Ups or Greenfield Approach

a) A bank starts from scratch by establishing a new insurance company wholly owned by the bank.

b) A group owns a bank and an insurance company, which agree to cooperate in a bancassurance venture.

c) A bank and an insurance company agree to have cross shareholdings between them. A member from each company might join the board of directors of the other company.

Delivery approaches of Bancassurance

Career Agents

Career Agents are full time commissioned sales personnel holding an agency contract. An insurance company can exercise control only over the activities of the agent, which are specified in the contract.
Special Advisors

Special Advisors are highly trained employees usually belonging to the insurance partner, who distributes insurance products to the bank's corporate clients. Usually they are paid on a salary basis and they receive incentive compensation based on their sales.

Salaried agents

Salaried Agents have the same characteristics of career agents. The only difference is in terms of their remuneration being paid on a salary basis and they receive incentive compensation based on their sales.

Bank employees

Bank employees can usually sell simple products. However the time, which they can devote to insurance sales, is limited.

Set up or acquisition of agencies or brokerage terms

Banks cooperate with independent agencies or brokerage or have founded corporate agencies. The advantage of such sub arrangements is the availability of specialists needed for complex insurance matters and in case of brokerage firms-the opportunity for the bank's clients to receive offers not only from one insurance company but from a variety of companies.

Direct response

The consumer purchases product directly from bancassurer by responding to the company's advertisement, mailing or telephonic offers. This channel can be used for simple products, which can be easily understood by the consumer without explanation.
Internet

Internet banking will also prove an efficient vehicle for cross selling of insurance savings and protection products. There is now the Internet, which looms large as an effective source of information for financial product sales.

E-Brokerage

Banks can open or acquire an e-Brokerage arm and sell insurance products from multiple insurers. The advantage of this medium is scale of operation, strong brands, easy distribution and excellent synergy with Internet capabilities.

Outside Lead Generating Techniques

One last method for developing bancassurance eyes involves "outside" lead generating techniques, such as seminars, direct mail and statement inserts. Seminars in particular can be very effective because the insurance counselor can make a presentation to a small group of business people (such as the local chamber of commerce), in a non-threatening atmosphere field questions on the topic, then collect business cards. Adding this technique to his or her lead generation repertoire, an insurance counselor often cannot help but be successful.

Benefits of Bancassurance

To Banks

1. Increased Return on Assets
2. Fee income which is risk free
3. To reduce operating costs
4. Customer retention
5. To prepare to eventually diversify into insurance business
Banks those effectively cross-sell financial products can leverage their distribution and processing capabilities for profitable operating expense ratios. In addition, a bank's branch network allows the face-to-face contact which is so important in the sale of personal insurance. Banks also enjoy significant brand awareness within their geographic regions, again providing for a lower per-lead cost when advertising through print, radio and or television. Banks have extensive experience in marketing to both existing customers (for retention and cross selling) and non-customers (for acquisition and awareness). They also have access to multiple communication channels, such as statement inserts, direct mail, ATMs, telemarketing, etc. Proficiency of banks in using technology has resulted in improvements in transaction processing and customer service.

To Insurers

1. Lesser procurement costs
2. Known customer and therefore risk assessment is easier
3. Increase in market penetration
4. Personal insurance - sky is the limit

Banks offer an untapped and successful mode of distribution. Banks with their brand image and existing customer relationship offer a natural market for the selling of insurance products. Bancassurance also offers lower distribution costs and higher productivity. Traditionally, insurance products have been sold through fulltime sales agents. The commissions paid to the sales agents with the international productivity standard of 4-6 sales per month would make this distribution channel an expensive one. The reason the productivity is low in the
traditional sales agent distribution system is the amount of time the agent has to spend on prospecting or trying to find the right customer. Almost 80 percent of a sales agent's time goes towards prospecting. Banks on the other hand provide a cheaper and highly productive distribution system to insurance companies. Insurance companies also expect a greater quality of sale through bancassurance.

To Customers

1. Lower cost

2. Refined, high quality product

3. Double assurance or Credibility

4. Delivery at doorsteps

5. Convenience in payment

6. Easy & automatic renewals

For customers, bancassurance offers convenience and a one-stop financial supermarket. The customer has the satisfaction of the brand strength of the bank, his or her existing relationship and trust on the bank. The products sold through bancassurance can give better value and offer cheaper premiums due to lower distribution costs.

OPERATIONAL DEFINITIONS

Assess

It refers to determine the awareness, attitude and practice of bank customers regarding bancassurance and is measured by knowledge questionnaire, attitude scale and practice check list.
Awareness

It refers to the understanding of bank customers regarding bancassurance and is measured by the response given by the respondent on the issue of questionnaire regarding bancassurance and is interpreted as adequate, moderately adequate and inadequate knowledge.

Attitude

It refers to the perception of bank customers regarding bancassurance and is measured by the attitude scale.

Practice

It refers to the activities that the bank customers undertake in relation to bancassurance.

Bank Customers

A bank customer is a person who is utilizing one or more of the services provided by the bank and through whom the bank gets an opportunity to make an earning in return to the service they can provide the customer with.

Bancassurance

Bancassurance is selling insurance product through banks. Banks and insurance company come up in a partnership wherein the bank sells the tied insurance company's insurance products to its clients.