FDI IN INSURANCE SECTOR: IRDA REFORM RUSH

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This paper attempts to study the FDI in Insurance Sector in India focusing on the trend and pattern of FDI in insurance Sector, contribution of global partners, role played by IRDA in regulatory policies that have made a huge impact on the dynamics of this industry with special reference to the Insurance bill of 2014 that has seen the light of the day. To conclude the paper enlists the future prospects and suggestions with an analytical bent of mind as well as quantitative interpretation of the subject.

INTRODUCTION- INSURANCE INDUSTRY IN INDIA

Provision of adequate security to life and property is a fundamental duty of civilized society. The field of Insurance Law is a subject of immense public importance. Insurance offers security to individuals and transactions. It provides indemnification against losses arising from the happening of some events. It is a commercialized form of spreading risks. According to the Oxford Dictionary Insurance is defined as “An arrangement by which a company or the state undertakes to provide a guarantee of compensation for specified loss, damage, illness, or death in return for payment of a specified premium”.

The Insurance business is broadly divided into life, health, and non-life insurance. It not only provides an opportunity to develop a sense of independence security and freedom from anxiety but also stimulates expansion of trade and commerce. It is thus the backbone of the risk management system of any nation. It influences growth and development of a nation in myriad ways like protection, security and even as a means of tax saving instrument. Therefore, an efficient and competitive insurance industry is important to empower a nation in the true sense of the term.

The insurance sector in India has come a full circle of 360 degrees from being an open competition market before Independence to Nationalisation and then back to Liberalisation. The evolution of the insurance industry is known to all and the metamorphosis in this sector is noteworthy.

FDI AND FDI IN INSURANCE

Foreign Direct Investment is a measure of foreign ownership of productive assets and can be used a measure of growing economic globalisation. India is regarded as one of the most preferred destination owing to availability of minerals, raw materials, cheap and skilled labour and a large English speaking population[1]. Foreign Direct Investments are “usually preferred over other forms of external finance because they are non-debt creating, non-volatile and their returns depend on the performance of the projects financed by the investors.

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1 ASCL-Law relating to Foreign Direct Investment, published in 2009.www.als.edu.in

FDI also facilitates international trade and transfer of knowledge, skills and technology”.[2] There is enough evidence to show that FDI in Insurance sector is and has been a hot bed of controversy in India, thanks to the regulatory reforms and political scenario.

In 1993, the Union Government set up a committee under the Chairmanship of R.N. Malhotra, former Governor of RBI, to propose recommendations for reforms in the Insurance Sector and thus in 1999 the Insurance Regulatory and Development Authority was constituted under the IRDA Act as the apex statutory insurance regulatory body to oversee all insurance-related activity. The IRDA in 2000 allowed foreign equity stake in domestic private Sector Insurance Companies to a maximum of 26 percent of the total paid-up capital.[3]

The Government constituted a special agency to deal with foreign investments in India known as Foreign Investment Promotion Board whose main objective was to encourage FDI in India.

Today, India’s insurance sector is one of the largest in the world in terms of volumes of money involved with 52 companies in this sector, of which 28 are in non-life insurance business and 24 in life insurance. India’s Life insurance sector is the biggest in the world with about 36 crore policies and is expected to increase at a compound annual growth rate (CAGR) of 12-15 per cent over the next five years.[4]

INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY (IRDA)

For India to reach its rightful place as a developed nation, it must financially empower its entire population. Insurance industry is an integral part of the financial system of a country thus influencing economic development and growth. Insurance is the one of a country’s risk management that covers elements of life, disability and health. The inference is obvious. The role for IRDA is to protect the interests of holders of insurance policies, to regulate, promote and ensure orderly growth of the insurance industry and for matters connected therewith or incidental thereto.

The IRDA has done a very good job of ensuring a smooth and steady transition from a single player market to a competitive one. The process of reforms initiated some years ago has some achievements to its credit. It has enhanced competition, provided a choice to the customers, triggered innovative ways and means to carry out insurance activities, improved the efficiency level of the Industry, increased the coverage of insurance in terms of density and penetration, obligated the insurers to provide for the needs of social and rural sectors and

[2] Planning Commission of India,2002. Report of the Steering Group on Foreign Direct Investment: Foreign Investment India (Government Report). p 11, New Delhi: Planning Commission, Government of India. Accessed from http://planningcommission.nic.in.aboutus/committee/strgrp/stgp_fdi.pdf on 5th September,2008.

[3] World Bank Economic Review, 2000

[4] Indian Brand Equity Foundation-http://www.ibef.org/industry/insurance-sector-india.aspx

increased awareness about the necessity of insurance, to name a few.[5] The following are the key changes in the regulatory environment that have substantially impacted the industry dynamics.

a) 1999 → IRDA bill passed.

   Effect -Foreign Collaboration and formation of an independent Regulator.

b) 2001→IRDA issued Third party Administrator Regulations (TPAs); Foreign Players allowed to enter the Indian market up to a limit of 26 per cent.

   Effect- Entry of TPAs focussed on servicing health insurance business;

   2002→ IRDA Insurance Brokers and Licensing of Insurance & Corporate Agents.

   Effect→ Focus on insurance distribution through corporate intermediaries.

c) 2006→Entry of Standalone Health Insurance Players.

   Effect- Served as a means to cater to the health needs of the customers better.

d) 2007→ Creation of Indian Motor Third Party Insurance Pool $ Price Detariffication.

e) 2011→Scheme of Amalgamation (Mergers & Acquisitions) and Transfer of General Insurance Business

   Effect- Enabled consolidation, inorganic transactions in the industry.

f) 2012→ Introduction of Declined risk, Pool, TP premium increase.

g) 2013→ Licensing of banks as Insurance Brokers.

   Effect- Help reduce operational costs of insurance companies, due to marginal incremental expenditure by companies in setting up distribution chain. Also, spread insurance to uncovered areas say rural areas owing to entire bank branches network making the process of buying the life insurance product a simple process.

h) 2014- IRDA increased FDI hike from 26% to 49%.

   Effect- Huge capital investment from global partners would help expansion in several segments of the sector, deepened insurance penetration and empowering the customers also creating an environment for investment by the average middle class Indian &otherwise.

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[5] COLLOQUIUM 'Insurance Industry in India: Structure, Performance, and Future Challenges', Vikalpa, Volume 30, No 3, July, September 2005, pp. 93-119.

CONTRIBUTION OF GLOBAL PARTNERS

The sheer size of the Indian market has been the major attraction for foreign players. Most of the insurance companies in India have been formed by forming joint ventures with global partners. Whether it is the initiation of business or the development of procedures of regulations Indian Insurers owe a lot to the foreign partners.

Since 2001 there has been increase in penetration (from 2.3 % in FY01 to 3.4% in FY12), increased coverage of lives, substantial growth and increased competitiveness of the market (from four private players in FY01 to 23 private players in FY12).[6]

a) The entry of private players has helped educate the customers on the need for adequate insurance coverage in terms of the potential risks they are exposed to. Another aspect would be the right distribution model to address the different underserved segments such as senior citizens and NRIs which is one of the levers for increasing insurance penetration.
b) Enhanced competition.[7]
c) There is enough evidence from developed markets that internet penetration and usage has a positive correlation with performance and activities of insurance companies at various levels- lower customer acquisition costs, improved access to information, product innovation that cater to the needs of the customers and enhance convenience.[8]
   Foreign collaboration has brought in technical expertise that has comforted the internet users to conduct financial transactions online on one hand and facilitated developing and servicing of the market on the other. For example emails, ATMs, underwriting, fund management and actuary. This is indicative of the value which IT has added to this sector.
d) Since insurance is a push product, consultation selling continues to dominate. Traditional agents were supplemented by other channels including the Internet and bank branches.
   These developments were instrumental in propelling business growth, in real terms, of 19% in life premiums and 11.1% in non-life premiums between 1999 and 2003.[9]
e) Bancasuurance Partnerships is a concept of French origin referring to selling of Insurance through a Bank's established distribution channels and was introduced in India by the global partners. It is expected to drive near term growth and holds a promise for the future.

Capital for expansion, wider scope for growth, job opportunities, infrastructure facilities, new risk management practices are the indirect benefits which foreign collaboration has given to India.

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[6] Handbook on Indian Insurance Statistics 2011-2012 published by IRDA.
[7] Published in The Economic Times on November 17, 2014 http://articles.economictimes.indiatimes.com/2014-11-17/news/56174804_1_health-insurance-insurance-repository-life-insurance-corporation
[8] KPMG: 'Insurance Industry-Road Ahead, Path for sustainable growth momentum and increased profitability', www.kpmg.com/in
[9] Handbook on Indian Insurance Statistics published by IRDA.

IRDA REFORM RUSH

After a decade of strong growth, the Indian Insurance Industry was facing severe headwinds, grappling with slow growth, rising costs, deteriorating distribution and structure and stalled reforms. Faced with a persistent high inflation over the last few years and in turn, a high interest rate regime the economy seems to have lost some steam.[10] In 2010, the Insurance penetration was 4.4% which further dipped to 3.17% in 2012-2013.[11] As of FY 13, the total market size of this sector was US$ 66.4 billion and is expected to touch US$ 350-400 billion by 2020.

After a long lull in the previous Government in power this time the new government is gung-ho in flooding the economy with path-breaking reforms that has revitalised this sector in terms of growth. Stakeholders, IRDA, and the government are making concrete efforts to help the sector overcome this catharsis:

Relaxation of investment norms for insurance companies;
Release more funds for the infrastructure sector;
Taxation of life insurance policies;
Revival of Unit Linked Insurance products;
Faster regulatory approval for new products;
Tax on pension Products;
Open architecture on Bancassurance; and
More relaxed licensing norms.[12]

New regulations and mature amendments in the recent past by IRDA and RBI have helped give maximum benefit to the consumers.

a) E-policy has saved policy holders from preserving the physical copies of their insurance policies and hence reducing the cost of the insurers.
b) From January2014, only products that conform to the new guidelines announced by IRDA in the first half of 2013 have been allowed for sale leading the insurers to re-file their products for approval.
c) IRDA health insurance regulations have been tabled to improve the service standards with a view to enhance customer focus.
d) The IRDA has come up with a long-term motor third party insurance policy for two-wheelers with a three-year term. As per the regulatory body, the total premium for the third party coverage would be three times the yearly third-party premium for two-wheelers as decided by the Regulator.
e) Export Credit Guarantee Corporation of India ltd has signed a /Memorandum of Understanding (MoU) on cooperation with the Export Credit Insurance Agencies (ECA) of BRICS countries.[13]

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[10] Ernst & Young and CII, "Insurance Industry- Challenges, reforms and realignment".
[11] IRDA Annual Reports F.Y. 2000 to F.Y. 2013.
[12] Published on Moneycontrol.com, Available at: http://www.moneycontrol.com/master_your_money/stocks_news_consumption.php?cat=insurance&autono=761571

f) Owing to the Government's push for various financial sector reforms as part of larger efforts to bolster the country's economic growth, the Competition Commission of India in order to keep a tab on the possible unfair practices had initiated a study of the functional aspects of the country's growing financial sector, including banking and insurance segments.[14]

g) The proposal to hike FDI in insurance was spending since 2008, introduced by the previous government but dint see the light of the day owing to opposition from several quarters. FM Arun Jaitely, as part of the gung-ho government proposed increasing the FDI limit to 49% from 26% in the Insurance sector. To this effect, in July 2014, the Cabinet Committee on Economic affairs (CCEA) approved 49% FDI in insurance with a view to revamp the insurance sector.

h) "LIC has gained from competition, was challenged to innovate on products, bring in more technology, be more cost effective", says Usha Sangwan, MD, LIC.[15]

The insurers thus seek to increase their respective market shares and have started to be more service-oriented, cater to the needs with greater flexibility, offering practical solutions, making informed decisions in order to make long-term associations.

i) "For long, the insurance sector has been waiting for adequate funds for its expansion. Increasing the FDI cap in this sector will definitely give it the much needed fillip," says Rajeev Saxena, Insurance sector expert, Mazars. "As the sector expands, it will also lead to job creation in the sector."[16] More players would also mean strengthening the existing players, besides creating more jobs.

j) If the FDI limit is raised in the insurance sector, it could result in inflows of Rs. 40,000 crore to Rs. 60,000 crore over time, says Ajay Bagga, Chairman of OPC Asset Solutions.[17].

k) The higher FDI limit would also be beneficial for the pension sector. The Pension Fund Regulatory Development Authority (PFRDA) Bill ties the FDI limit in pension sector to that of the insurance sector. If the pension bill is also passed, then the FDI limit could be at 49%. This means 49% ownership by foreign companies in domestic businesses selling pension plans.

l) Typically investors invest in insurance and pension products on a long-term basis and this money could help fund infrastructure projects, which require long-term funding. The Reserve bank of India had recently allowed banks to raise 7-year bonds to fund infrastructure projects.[18]

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[13] Indian Brand Equity Foundation- http://www.ibef.org/industry/insurance-sector-india.aspx

[14] Published in The Hindu on September 29, 2013 http://www.thehindubusinessline.com/industry-and-economy/banking/banking-insurance-sectors-come-under-competition-watchdogs-scrutiny/article5181992.ece,

[15] *Supra* note 7.

[16] Published on Moneycontrol.com on November 18, 2014 http://www.moneycontrol.com/news/features/how-increasing-fdi-cap-will-benefitinsurance-sector_1231408.html?utm_source=ref_article

[17] Published in NDTV on July 24,2014. http://profit.ndtv.com/news/cheat-sheet/article-how-higher-insurance-fdi-limit-could-benefit-you-593104.

[18] Supra note 17.

m) Life Insurance Penetration in India is about 3.2% of Gross Domestic Product in terms of total premiums underwritten in a year, much lower than more than 10 percent in Japan and nearly 6% in Australia. Higher FDI limit could help in deepening the Insurance Penetration.[19]
n) Help spreading risk among the Insurers.

The aspect which needs special mention is that the bill says that the management and controlling power will stay with the Indian Partner company only. Thus, eliminating the risk of global partners getting control over the sector.

The Insurance Business is a capital-intensive industry and India is investment starved. Higher FDI cap is a welcome and a mature move from the Government. Additional Capital will lead to reduced cost of capital along with improved operating efficiency which in turn will result in better services to the consumer. Strengthening solvency.

SUGGESTIONS AND CONCLUSION

A key catalyst in the Indian insurance market growth has been the renewed surge of green-flagging reforms by IRDA since 2000. With this policy change, there have not only been structural changes but also changes in basic and working principles. Notwithstanding the metamorphosis, much needs to be done for future growth & development. Government's renewed surge of consumer-friendly reforms in the financial sector send a strong message to the global economy about the growth aspects of India's economic growth and owing to country's demography and population there is untapped potential which this industry must live up to.

The balance between cost-effective distribution and product innovation is an important lever for the growth of the industry led with the regulatory changes which will provide the much needed impetus.

Formulation and implementation of guidelines and regulations, proving for adequate safeguards, monitoring and ensuring compliance will help a long way in sustainable growth.

Understanding the changing perspective of the consumers, offering practical solutions and efficient quality service suited to the customer's over all financial requirements will result in customer satisfaction, customer retention, customer acquisition, employee retention and cost reduction.

Bancassurance that has acted as a 'Change Catalyst' so far with mixed reviews and holds promise for the future requires nurturing of partnerships between the Insurance Companies and the banks as well as understanding the mechanism better.

Insurance is a long-gestation business and this sector builds its market on goodwill and access on distribution network Insurers must find new ways and methods to deliver its products to its customers with the aim of increasing their respective market shares and brand value.

[19] IRDA Annual Reports.

Developments in the health insurance infrastructure have been lately introduced and must continue for better health service standards to the Indian population.

The industry workers and the regulator-IRDA must work in tandem and strive to take this industry to its next level of evolution impeding all odds and with such efforts being materialised the future of Indian Insurance Sector looks good.