20 March 2013

New life insurance regulations in India

Milliman

Perhaps as the last order of business for the outgoing Insurance Regulatory and Development Authority (IRDA) chairman, Mr. J. Hari Narayan, a slew of regulations have been introduced affecting various aspects of life insurance in India.

In this edition of the Asia e-alert, we present a summary of these new regulations, highlighting the key provisions that will have the most impact on the Indian life insurance sector.

New regulations

Regulations on non-linked insurance products

These regulations cover various aspects of non-linked insurance products. Life insurance companies are required to ensure compliance with these regulations before 30 June 2013 for group products and before 30 September 2013 for individual products.

The significant regulatory changes in relation to non-linked insurance products include:

1. Minimum floors on sums assured have been introduced for single and regular premium products depending on the age of the insured.
2. For individual products, the minimum policy term and the minimum premium term (for non-single premium policies) have both been set at five years.
3. Maximum commission (or remuneration to distributors in any form) limits have been introduced for all non-linked insurance products. The key changes include:
   - The first year commission (FYC) limits for non-pension regular premium products with premium terms lower than 12 years have been reduced from the current limits. The limits on maximum commission increase with premium term, although the highest limit is the same as that currently permitted.
   - The maximum distributor remuneration for group products is set at 2% of premium, subject to absolute INR-denominated caps.
   - No commission payment is permitted on business procured through the direct marketing channel.
4. Minimum guaranteed surrender values have been introduced at different policy durations. These levels are higher than the existing minimum guaranteed surrender value requirements. Companies are also required to pay ‘special surrender values' based on asset shares underlying the policies. These asset shares are required to be calculated in accordance with the professional guidance provided by the Institute of Actuaries of India.
5. ‘Variable insurance products,’ which have been defined as any non-linked products for which benefits depend upon regular interest rate credits, are now subjected to the same regulations as those applicable to unit-linked products.
6. Benefit illustrations are now required to be presented assuming gross investment returns of 4% p.a. and 8% p.a. The regulations also require illustrations to be provided based on the rates specified by IRDA or the Life Insurance Council (which are currently at 6% p.a. and 10% p.a.)
7. Significant regulations are introduced around the management of participating business, covering the need to set up an asset share framework; a governance mechanism involving a ‘with-profits committee’ which would include an independent director of the Board, the CEO, Appointed Actuary and an independent actuary; and the granting of power to the IRDA to prescribe methodology to allocate expenses between different funds.

The new regulations appear to be an attempt by the IRDA to improve the level of transparency and value for money for policyholders of non-linked life insurance products.

Regulations on linked insurance products

These regulations are largely in line with the earlier unit-linked guidelines released by the IRDA in September 2010. They split linked insurance products into unit-linked products and variable-linked products and provide regulations for each of them separately. As with non-linked products, life insurance companies are required to ensure compliance with these regulations before 30 June 2013 for group products and before 30 September 2013 for individual products.

The key changes in these regulations as compared with the previously released unit-linked guidelines include the following:

- Maximum commission (or remuneration to distributors in any form) limits have been introduced in line with those now applicable under the new non-linked product regulations.

- Companies are now not allowed to offer the so-called 'highest NAV guaranteed' products and any closed ended funds. However, companies can provide guarantees at a product level (as opposed to a fund level) even at maturity.
- The regulations now require companies to provide comprehensive information to IRDA in respect of the guarantee charges levied on the products offering investment guarantees.
- Benefit illustrations are now also required to be presented using investment returns of 4% p.a and 8% p.a.
- There are no changes to the maximum reduction in yield to policyholder at maturity as prescribed by the IRDA in earlier guidelines. However, insurance companies are required to demonstrate compliance with these requirements using six different gross investment return assumptions at the time of filing of the product.

Regulations on reinsurance of life insurance business

These regulations attempt to standardize the reinsurance treaties between life insurers and their reinsurers.

The key highlights of these regulations include:

- Life insurance companies are required to reinsure a percentage (as may be specified by the IRDA, but not exceeding 30%) of their sum assured with 'Indian reinsurers.' If any business is to be reinsured with a foreign reinsurance company, the reinsurer should have maintained a credit rating of BBB (Standard and Poor's) or equivalent over the past five years.
- Each life insurer would be required to file a board approved program of reinsurance with the IRDA at least 45 days prior to the commencement of each financial year, which would include a review of existing reinsurance arrangements and a reinsurance retention policy. In addition, all reinsurance arrangements would need to be filed with the IRDA within 30 days of the commencement of each financial year.
- The regulations specify minimum retention limits that vary from INR500,000 to INR2 million for pure protection products, and INR1 million to INR3 million for savings-oriented products, based on the age of the life insurer. Any reinsurance arrangements that breach these limits are required to be reported to the IRDA for approval.

Regulations on Appointed Actuaries

Under these regulations, in order to be eligible to act as an Appointed Actuary, an individual needs to satisfy the following criteria:

- 10 years of relevant work experience, out of which two years should have been in the respective field.
- At least two years of post-qualification experience (qualification in the specialised area).
- Should be a Fellow or Affiliate member of the Institute of Actuaries of India, with specialisation (as evidenced by qualification and/or work experience) in the relevant area (life, general or health). Existing Appointed Actuaries have been granted five years to comply with this requirement.
- Be aged less than 65 years (after 1 January 2014).

Regulations on investments

The main change in the investment regulations is that insurance companies with large investment assets are now allowed to acquire a higher percentage (10% to 15%, depending on the size of the insurer's investment assets) of the equity and debt of the 'investee' company.

Regulations on scheme amalgamation and transfer of life insurance business

These regulations set out the approval process, including the information requirements, for any merger or acquisition proposals for insurers operating in India.

Regulations on standard proposal form for life insurance

In order to promote 'needs-based selling' and transparency at the time of sale, these regulations set out a standardised proposal form for life insurance companies. It will be mandatory for life insurance companies to collect a completed form for each policyholder. These regulations would come into force after six months of their publication in the official gazette.

Regulations on the places of business

These regulations standardise the requirements for opening of new places of business by insurers in India. While insurers would need to seek permission from the IRDA for opening new places of business in Tier-1 centres, they are required to only notify the IRDA after opening new places of business in Tier-2 and lower centres.

In addition, insurers are required to have specific plans for opening new places of business as part of their board approved business plan.

Other regulations

There are also amendments in some other regulations:

- Insurance brokers regulations
- Registration of Indian insurance companies regulations

Industry reactions

Many in the industry were surprised by these new product regulations, which many had thought (or hoped) would not get issued in their current form, especially after the retirement of the outgoing chairman.

The changes in the product regulations will result in considerable effort re-pricing and re-launching existing product ranges.

Many insurers who currently sell ‘variable insurance products’ may now focus on selling traditional products. This is because the various caps on charges on such variable insurance products are now similar to those on unit-linked products and which result in a significantly lower compensation to the distributor.

The profitability of traditional products may also come down, given that surrender values will increase materially.

Barring the administrative effort involved in designing and launching these new products, there are drafting errors, inconsistencies and a lack of clarity in the new regulations. This in itself is likely to make the product re-launch process a tedious one for everyone concerned.

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