

THE INSURANCE LAWS (AMENDMENT) ACT, 2015: AN ANALYSIS

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Introduction

Insurance as a concept was first discussed in India in early works like the Manusmriti, Arthashastra and Dharmashastra. Therefore it has been a part of Indian society for a very long time. The Oriental Insurance Company was the first insurance company in the country and was set up in Kolkata back in 1818. It mainly catered to the European community's needs. In 1870, Bombay Mutual Life Assurance Society was set up as the first Indian Insurance Company. The National Insurance Company is the oldest existing insurance company in the country and it was established in 1906.¹

The legal framework of the insurance sector in India has run a complete circle from being unregulated to completely regulated and presently, partly deregulated. A number of legislations govern Insurance Law in the country. The first law to govern all types of insurance was the Insurance Act, 1938.² It provided for strict state control over all insurance businesses. The Life Insurance Corporation then completely nationalized Life Insurance in India in 1956.³ The General Insurance Business (Nationalisation) Act, 1972 was brought in with the objective of nationalizing 100 general insurance companies that were then merged to form four companies headquartered in the four metropolitan cities. These were, the National Insurance Company, the New India Assurance Company, the Oriental Insurance Company and United India Insurance Company.⁴ It was not until 1999 that private insurance companies were also allowed. The Insurance Regulatory and Development Authority Act, 1999 was brought in that deregulated the insurance

¹ Sree Visakh, *The Insurance Laws (Amendment) Bill: Analysis Time*, THE FORTUNE STROKE, <http://www.fortunestroke.in/2015/03/the-insurance-laws-amendment-bill-2015.html> (last updated Sept. 14, 2015) [**Hereinafter 'Visakh'**].

² The Insurance Act 1938

³ The Life Insurance Corporation Act 1956.

⁴ The General Insurance Business (Nationalisation) Act 1972.

sector and allowed private companies to participate.⁵

The Act also provided for foreign investment in the insurance sector but this had a cap of 26% of equity share capital of the company. About 20 out of the 23 private life insurance companies had more than 22% foreign investment and about 14 out of the 17 private non-life insurance companies had more than 22% foreign investment.⁶ The Insurance sector in India has seen low penetration because of the lack of funds to permit growth of the sector and therefore, a need for permitting an increase in foreign investment was seen. With this in mind, the Insurance Laws (Amendment) Bill 2008 was tabled which sought to increase the foreign investment cap from 26% to 49%.⁷ This bill was amended and revised but the Parliament failed to pass it in the winter session of 2014. In order to show that they did in fact intend to bring in all the changes sought to be brought by the bill, the Central Government notified the Insurance Laws (Amendment) Ordinance 2014 on 26th December 2014.⁸ This gave interim legal standing to the new amendments. It finally became a law on 20th March 2015 as the Insurance Laws (Amendment) Act 2015 after it was granted Presidential assent.⁹

The present paper shall delve into problems faced by the insurance sector due to which the amendment has been brought in and then it shall look into the important changes brought by the new amendment and seek to analyse them.

Need for Amendment

Other than the need for funds for growth, there were a number of other problems in the insurance sector that necessitated changes. For starters, the Insurance

⁵ The Insurance Regulatory and Development Authority Act 1999.

⁶ Insurance Regulatory and Development Authority of India, Annual Report 2013-2014 (28 (Sept. 14, 2015) <http://www.policyholder.gov.in/uploads/CEDocumenAR%20January%202015%20issue.pdf>

⁷ The Insurance Laws (Amendment) Bill 2008.

⁸ The Insurance Laws (Amendment) Ordinance 2014.

⁹ A Harlalka, S Shah and S Reis, *49% FDI in Insurance: A Long Successful Battle*, NISHITH DESAI ASSOCIATES, <http://www.nishithdesai.com/information/research-and-articles/nda-hotline/nda-hotline-single-view/article/49-fdi-in-insurance-a-long-successful-battle.html?no_cache=1&cHasf4e4a14a7215b6ff739c2c> (last updated Sept. 14, 2015) [hereinafter 'Harlalka, Shah and Reis'].

Regulatory and Development Authority of India (IRDAI) that regulates the insurance sector did not have adequate powers. Other agents such as the Central Government directly regulated many aspects of the sector. An instance of this is that prior permission of the Central Government was required before a foreign insurance agent could insure property in India. Also, when agents sold wrong insurance policies to the buyers, they were rewarded with large sums from the insurance companies and the IRDAI did not have enough power to look into these situations.¹⁰

Another issue was that the only means by which common people could get insurance policies was through insurance banks or agents. Thus a long and tedious process would have to be followed in order to get policies processed and this also increased chances of fraudulent activities on the part of the banks and agents. Due to the nexus between the two groups, the policyholders would have to approach both of them and they kept putting the responsibility on the other party.¹¹

Further, there was a lack of flexibility in insurance premiums. That is, most companies had fixed premiums and since a majority of people in the country work for daily wages, they were wary of taking such insurance policies.¹²

As per the 190th Law Commission Report in 2004, the grievance-redressal mechanisms were also inadequate. The Ombudsman scheme under the Redressal of Public Grievances Rules, 1998 and the remedy under the Consumer Protection Act 1986 were unsatisfactory and ineffective to deal with the complaints of the policy holders.¹³

Also, according to s.45, an insurance company could repudiate the contract if any

¹⁰ VISAKH, *supra* note 1.

¹¹ *Ibid*

¹² Standing Committee on Finance, *Forty-first Report on the Insurance Laws (Amendment) Bill, 2008*, PRS INDIA,

<http://www.prsindia.org/uploads/media/1230002517/SCR%20Insurance%20Laws%20Bill.pdf> (last updated Sept. 14, 2015).

¹³ Law Commission of India, *190th Report on the Revision of the Insurance Act, 1938 and the Insurance Regulatory and Development Authority Act, 1999* LAW COMMISSION OF INDIA 3 (Sept. 14, 2015) <http://lawcommissionofindia.nic.in/reports/InsuranceReport-2nddraft1.pdf>.

claim was fraudulently made, even after two years. However, the insurance companies often misused this provision and refused to pay for claims by stating ill-substantiated excuses.¹⁴ Thus, there was a need to bring in appropriate amendments to deal with these issues.

The Insurance Laws (Amendment) Act 2015

This Act makes amendments to three core insurance legislations:

- (1) Insurance Act, 1938
- (2) General Insurance Business (Nationalisation) Act, 1972
- (3) Insurance Regulatory and Development Authority Act, 1999

The provisions of the Act have retrospective effect from 26th December 2014 (i.e. the day the Ordinance was passed).¹⁵

i. Hike in FDI Cap

The most important change has been that the foreign investment ceiling has been raised from 26% to 49% cumulatively.¹⁶ The first 26% will be by automatic route, while for the remaining 23%, Foreign Investment Promotion Board (FIPB) approval is necessary.¹⁷ This 49% includes direct and indirect FDI as well as FPI.¹⁸

These changes are in line with the 2015 budget and with the Ordinance. However, while the Ordinance had made it possible for insurance companies to issue different classes of shares like equity shares, preference shares and other

¹⁴ VISAKH, *supra* note 1.

¹⁵ The Insurance Laws (Amendment) Act 2015.

¹⁶ S Khaitan and S Shrivastava, *Insurance Reforms finally become and Reality* KHAITAN LEGAL ASSOCIATES, (Mar. 19, 2015) 1 <http://www.ec3legal.com/publications/Legal-Update-on-analysis-of-Insurance-Laws-Amendment-Bill-2015-by-Khaitan-Legal-Associates.pdf>; The Insurance Laws (Amendment) Act §3(iv) (b) (2015).[hereinafter 'Khaitan And Shrivastava']

¹⁷ Ramandeep Singh, *The Insurance Amendment Bill 2015: Summary* BANK EXAMS <http://www.bankexamstoday.com/2015/03/the-insurance-amendment-bill-2015.html> (last updated Mar 17, 2015).

¹⁸ HARLALKA, SHAH AND REIS, *supra* note 9.

instruments, the amendment act says that only equity shares can be issued by Indian insurance companies for foreign investment.¹⁹

Therefore, foreign investments will substantially increase over the next couple of years. Foreign companies will only be happy to increase their ownership in Indian insurance companies that are valuable to them. The increase in FDI cap will help to increase penetration in the insurance sector.

ii. Introduction of the concept of 'Control'

The concept of 'control' has also been introduced. All Indian insurance companies have to be owned and controlled by Indians.²⁰ That is, more than 50% of the equity share capital has to be owned by Indian residents at all times. Control includes the right to appoint the majority of the board of directors or to control the policy decisions and management.²¹ The definitions of ownership and control are in line with the definitions under the FDI Policy 2014.²² This requirement of control by Indian residents may prove to be a disincentive for foreign joint venture partners because they may want a greater say in controlling Indian insurance companies since they cannot have majority ownership anyway. The foreign partners are often responsible for bringing in technical know-how and good practices, and taking all sorts of power away from them will leave them with no incentive to work for the benefit of the Indian joint ventures. This will thus have a negative impact on the hike in FDI Cap as well.

iii. FDI Cap applicable to all Insurance Intermediaries

Previously, the 26% cap on FDI was specifically for insurance companies, brokers, third party administrators, loss assessors and surveyors. There was some ambiguity with respect to other intermediaries. The new rules have however specified that this FDI cap will apply to all other insurance intermediaries.²³ However, the

¹⁹ *Ibid.*

²⁰ KHAITAN AND SHRIVASTAVA, *supra* note 16.

²¹ The Insurance Laws (Amendment) Act §3(iv)(b) Explanation (2015).

²² HARLALKA, SHAH AND REIS, *supra* note 9.

²³ KHAITAN AND SHRIVASTAVA, *supra* note 16; Consolidated FDI Policy 2015, 6.2.18.7.2(g) at p. 73.

problem that arises now is with respect to those intermediaries that already have more than 49% foreign investment as they did not have any restriction previously. It is yet to be determined whether these intermediaries will have to bring down their foreign shareholding or whether status quo will be granted.

iv. Foreign Reinsurance

Earlier, only domestic companies were allowed to provide reinsurance. The General Insurance Company was the only insurance company selling re-insurance in the country. However, the amendment has made it possible for foreign reinsurers such as Lloyds of London, to set up wholly owned branch offices in India and start reinsurance business.²⁴ This is obviously a welcome move as it will not only restrict the monopoly of General Insurance Company, but also lead to an increase in on-shore reinsurance activity in the country. However, the IRDAI is yet to set out guidelines and requirements that have to be fulfilled by these foreign reinsurers before they can start business.

v. Capital Availability

The act also allows for new and innovative ways of raising capital while being regulated and supervised by IRDAI. The four public sector general insurance companies in India, which previously had to be 100% government owned under the General Insurance Business (Nationalisation) Act 1972, are now allowed to raise capital. This is because of the need to expand the insurance business in the country in both rural and social sectors. The government equity however should not fall below 51% in these companies under any circumstances.²⁵ With more capital being made available and by making the insurance sector more capital intensive, there shall be a greater distribution to un-served or under-served parts of the country. There shall also be better methods of distribution that can be

²⁴Trilegal, *Update: Insurance Laws (Amendment) Act, 2015* (Apr. 10, 2015) <http://www.trilegal.com/index.php/publications/update/insurance-laws-amendment-act-2015> (last updated Sept. 14, 2015); The Insurance Laws (Amendment) Act §3(vii)(d) (2015). [hereinafter as 'trilegal'].

²⁵Ministry of Finance, *Major Highlights of the Insurance Laws (Amendment) Bill, 2015 Passed by Parliament* PRESS INFORMATION BUREAU <http://pib.nic.in/newsite/PrintRelease.aspx?relid=117043> (last updated Mar. 13, 2015); The Insurance Laws (Amendment) Act §103 (2015).

developed by use of technology, which will lead to more efficient service delivery. It will also encourage innovation in product formulations that will meet the diverse insurance needs of all the citizens.

vi. Empowerment of IRDAI

The Act has given the IRDAI the authority to regulate qualifications, eligibility and other conditions that have to be fulfilled for agents that are assigned to insurance companies.²⁶ Agents are also enabled to work more broadly across different companies in different business categories as long as they do not fall in conflict of interest.²⁷ This is also regulated by the IRDAI. The scope of insurance intermediaries has been expanded so as to include insurance brokers, reinsurance brokers, corporate agents, insurance consultants etc.²⁸ The IRDAI has been given the power to regulate code of conduct and functions of the loss assessors and surveyors.²⁹

Another very important function is that before a foreign company insures property in India, it has to receive the approval of the IRDAI.³⁰ Previously the approval of the Central Government was required. This will probably lead to more clarity with regard to such insurance covers and regulations that govern them. Obviously the IRDAI will be in a better position to judge than the central government.

IRDAI also has the power to withhold licenses of Indian insurance companies under two situations: (i) in case of a joint venture with a foreign insurer, if the foreign insurer is barred in their home jurisdiction and (ii) IRDAI can cancel a license if the company has not obtained the requisite approvals from IRDAI before amalgamation or transferring business.³¹ This provision has a potential to be misused as it may lead to unnecessarily punishing the Indian insurance company for a fault of the foreign insurer in their home jurisdiction. In any case, the foreign

²⁶ VISAKH, *supra* note 1; The Insurance Laws (Amendment) Act § 49 (2015).

²⁷ *Ibid.*

²⁸ The Insurance Laws (Amendment) Act § 105 (2015).

²⁹ MINISTRY OF FINANCE, *supra* note 25; The Insurance Laws (Amendment) Act § 82 (2015).

³⁰ KHAITAN AND SHRIVASTAVA, *supra* note 16; The Insurance Laws (Amendment) Act, §4 (2015).

³¹ KHAITAN AND SHRIVASTAVA, *supra* note 16 at p. 3; The Insurance Laws (Amendment) Act §6(v) (2015).

company will not have enough control over the insurance company and therefore, it may be a little harsh to cancel the Indian insurance company's license for no fault of their own since they are still complying with all laws and regulations that are applicable to them.

Further, the statutory cap on commission payable to agents has been done away with and the IRDAI has been given the authority to regulate this instead. In so regulating, it will have to take into account the nature and tenure of the policy and the interests of the agents.³² This is also a welcome move as it will add flexibility as IRDAI will be able to determine the maximum commission that is permissible and will also be able to make changes whenever necessary.

vii. Consumer Welfare

According to the new Act, insurers will be responsible for the acts and omissions of their agents. They will also be responsible for any violations of the code of conduct that the agents are supposed to follow. Mis-selling is one of such practices and the insurer will be liable to pay a penalty of up to Rs.1 crore.³³ Obviously such provisions will benefit the consumers. The insurance companies will be more wary of mis-selling by their agents and will take stricter action and will not reward them for sales through such misrepresentation. However, it may also be argued that it is unfair to punish the insurance companies for the acts of their agents and it is too harsh a punishment. It may not always be practically possible for the insurance companies to monitor the agents to make sure they are always acting in accordance with the law. Both the risk as well as the cost of compliance shall be increased on the part of the insurance companies. However, at least now the insurance companies will be more wary while appointing their agents and overall, the consumers will be protected.

³² TRILEGAL, *supra* note 24; The Insurance Laws (Amendment) Act 2015, s 101(xv)(jd).

³³ Kapil Mehta, *Insurance Amendment Bill: Necessary but not Sufficient* LIVE MINT, (Mar 11, 2015) <http://www.livemint.com/Opinion/9BIRSbrpRVVGSvzuVZFNQP/Insurance-amendment-Bill-necessary-but-not-sufficient.html> (last updated Sept. 14, 2015); The Insurance Laws (Amendment) Act §49 2015.

The Act has also amended s.45 of the Insurance Act 1938 that deals with repudiation of life insurance contracts. The old provision had said that a contract could not be repudiated 2 years after the policy was in effect except in cases of fraud. However, the new provision states that a contract cannot be repudiated 3 years after the policy has been in effect. The fraud exception has been done away with.³⁴ This provision is clearly pro-insured i.e. it serves the interests of the policyholders better. The insurance companies will have to increase safeguards and compliances so as to reduce the risk of issuing policies based on misstatements.

Multi-Level Marketing (MLM) distribution, whereby a scheme for the purpose of soliciting and obtaining insurance business through people not authorized for the said purpose, has been prohibited by the Act.³⁵

Trading in Insurance has also been banned. The practice of assigning your life insurance to an unrelated person in return for money is called Trading in Insurance. After such trade, the assignee would be liable to pay subsequent premiums and also receive all benefits.³⁶ This would generally lead to a situation whereby the assignee would benefit the most if the assignor would die early. This would be a very unpleasant situation and would lead to public policy issues. Therefore, trading in insurance has been rightfully done away with.

The law recognizes partial assignments as opposed to total assignment. Such partial assignment can be made to pay off a loan. The amended law also gives special protection to spouses, children and parents who are recorded as nominees in life insurance policies. They are beneficially entitled to the policy proceeds and no other legal heir can claim such proceeds from them. Previously, an assignment would cancel nomination, but now, it will not cancel the nomination although it may affect the rights of the nominees to the extent of the loan.³⁷

³⁴ MINISTRY OF FINANCE, *supra* note 25; The Insurance Laws (Amendment) Act §55 (2015).

³⁵ *Ibid*; The Insurance Laws (Amendment) Act §50 (2015).

³⁶ MEHTA, *supra* note 33; The Insurance Laws (Amendment) Act §45 (2015).

³⁷ *New Insurance Law Underwrites Customer Protection THE TIMES OF INDIA*, (15 March 2015) <http://timesofindia.indiatimes.com/business/india-business/New-insurance-law-underwrites-customer-protection/articleshow/46573936.cms> (last updated Sept. 14, 2015); The Insurance Laws (Amendment) Act §45 2015.[hereinafter as 'the Times of India']

The Act also proposes electronic processing of claims and more flexibility in paying premiums.³⁸ Electronic processing will help in improving payouts of claims and also detection of fraudulent claims more easily. The flexibility that is provided is basically that if the policyholder is unable to pay the total premium for a particular month, he may be allowed to pay as much as he can and this would have to be compensated for in the next month. Such a policy will attract more people to take insurance policies.

viii. Compulsory Divestment Removed

The provision that mandatorily required Indian Promoters to sell its stake in an insurance company in excess of 26% within 10 years from the start of business has been done away with.³⁹ The main objective of having the divestment policy was to reduce concentration of ownership in insurance companies. However, lawmakers did not give effect to this provision anyway. Further, it is a welcome omission because now Indian promoters are at par with foreign partners.

ix. Health Insurance

Health Insurance was previously regulated as a part of general insurance. But now, health insurance is sought to be regulated on a standalone basis.⁴⁰ The act defines 'health insurance business' including travel and accident cover and retains capital requirements at Rs.100 crore.⁴¹ This has been done with the aim of giving health insurance more importance by giving it a more focused regulatory system. The high capital requirements will help make sure that non-serious players do not interfere.

x. Grievance Redressal and Appellate Process

The Act also proposes the setting up of an independent grievance redressal authority (perhaps in the form of the Financial Redress Agency).⁴² This authority

³⁸ VISAKH, *supra* note 1; The Insurance Laws (Amendment) Act § 26 (2015).

³⁹ TRILEGAL, *supra* note 24.

⁴⁰ *Ibid.*

⁴¹ MINISTRY OF FINANCE, *supra* note 25; The Insurance Laws (Amendment) Act §3(iii), § 3(vi). Act 2015.

⁴² MEHTA, *supra* note 33.

will have powers similar to that of a civil court and would consist of judicial and technical members.⁴³ It is yet to be seen whether such an authority is established. If it is, it would probably replace the existing ombudsmen scheme.

The Act also provides for appeals against the decisions of the IRDAI to the Securities Appellate Tribunal (SAT).⁴⁴ Thus the relationship between the IRDAI and the insurers will be more confrontational. Previously, the only appeal lay with the Central Government and it wasn't very effective. Since the powers of the IRDAI have been increased so drastically, this only seems fair as it provides checks and balances on the powers of the IRDAI. However, it would be interesting to see whether the insurance companies find the confidence to actually challenge the decisions of the IRDAI as there is very little precedent on the same.

Conclusion

The recent changes brought by the Amendment Act are a welcome move and are indicative of the parliament's intention to move towards the economic development of the nation. The act seeks to make the insurance laws more consumer-friendly and this is commendable in a country that claims to be a socialist welfare state. Most of these changes were being demanded by the insurance industry for a very long time. The increase in economic rights will incite foreign partners to bring more insurance products into the Indian market. However, a number of problems may also arise due to these changes. The act states that the policyholder now has to prove that no wrong statements were made at the time of issuance of policy. Before, the insurance company would have to prove there was a misstatement. This will obviously make the procedure for claiming insurance quite difficult. Further, the strict compliances provided by the Act coupled with the increased liability of insurance companies in case of non-conformity or other discrepancies may act as a deterrent to new companies that were contemplating entering the insurance sector.

In fact Mr. Varadarajan, a Supreme Court advocate, has commented that due to the increase in the number of practical problems faced by the insurers and the fact

⁴³ VISAKH, *supra* note 1.

⁴⁴ TRILEGAL, *supra* note 24; The Insurance Laws (Amendment) Act § 94 (2015).

that the effect of these provisions shall be tested by different judicial and quasi judicial bodies at different levels, there will be more litigations and though this may benefit the lawyers, it will be inconvenient for the parties concerned.⁴⁵

However, the positives appear to outweigh the difficulties. An estimated \$3.2 billion of additional investment is expected in the insurance sector. This will give the insurers the required funds.⁴⁶ The changes are in accordance with the evolving insurance sector in the country and the regulatory practices around the world. They are expected to facilitate the insurance industry attain its complete growth potential and add to the growth of the economy as a whole. The future of the industry may be held to be secure for the moment.

⁴⁵ THE TIMES OF INDIA, *supra* note 37.

⁴⁶ P Mahrotri, A Antony and U Krishnan, *India Insurance Bill may attract \$3.2 billion from Investors*, BLOOMBERG (Mar 13 2015) <http://www.bloomberg.com/news/articles/2015-03-13/indian-insurance-bill-may-attract-3-2-billion-from-foreigners> (last updated Mar 13, 2015).