Perspectives on importance and role of Insurance in economic development
and
Proposed amendments to Indian Insurance Laws

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Why a Thriving Insurance Industry Is Critical to Economic development

- Insurance plays a crucial role in economic development by helping people and businesses recover from financial setbacks and continue to operate.

- Insurance can also help to reduce uncertainty, which can lead to increased economic activity and growth.

- In these uncertain times, the role of insurance in economic development becomes particularly pronounced.

- Insurers drive growth by reducing the impact of economic threats, giving people and businesses a greater chance to prosper.

- But in order for insurance firms to step up to the plate and serve their essential role, leaders must prepare for challenges and opportunities that lie ahead.

WHAT IS THE ROLE OF INSURANCE IN ECONOMIC DEVELOPMENT?

- In the present era insurance sector plays a vital role in both developed and developing countries.
- Insurance markets working as a financial intermediary to contribute economic growth of the country as well as risk management more efficiently
- When analyzing how insurance shapes the economy, it’s clear that providers serve four critical functions:
- Protecting against financial loss
- Promoting economic growth
- Providing capital
- Stabilizing the economy in crisis

Stabilization

- Insurance has a key function of economic stabilizer in times of individual shocks, smoothing the consumption of individuals facing idiosyncratic or aggregated shocks such as natural disasters or financial crises.

- Insurance is also a source of stable funding for both the financial markets and the economy as it fosters lending and investment with a long-term perspective.

- This has to do with insurance companies being far more “future-oriented” than other companies, such as banks, for example.

Distribution

- As is often said, insurance is about connecting “the misfortunes of the few to the fortunes of the many” which naturally creates a form of distribution.

- Insurance creates an invisible net of solidarity between economic agents, interconnecting them in time and place around shared preferences and priorities.

- Insurance organizes the concept of solidarity through its fundamental pooling principles –

aggregating and mutualizing risks by pricing them depending on their statistical occurrence for the larger pool and not for the individual.

Innovation

- Insurance entertains a paradoxical relationship with innovation.

- On the one hand, insurance fosters innovation by protecting innovators from external shocks and protecting wealth, while, on the other hand, it can limit innovation by adapting its coverage to new types of risks or adapting its own functioning to technological changes.

- Some examples of this are cyber risks, or, autonomous vehicles --which could call for the reinvention of insurance itself.

The Role of Insurance in India's Economic Growth

- In the dynamic landscape of India's burgeoning economy, the concept of risk is omnipresent.

- From the micro-level concerns of individuals to the macro-level challenges faced by businesses and industries, navigating risk is an integral part of the economic journey.

- In this scenario, insurance emerges as a crucial player, providing a safety net that not only shields individuals and enterprises from unforeseen events but also fosters economic growth by mitigating risk.

Understanding the Indian Economic Landscape

- India, with its diverse and complex economic structure, is characterized by a vast population, a burgeoning middle class, and a rapidly expanding industrial sector.

- However, this growth trajectory is not without its challenges.

- Natural disasters, health crises, economic uncertainties, and other unforeseen events pose significant risks to individuals, businesses, and the overall economy.

Insurance as the Channel of Growth

- The primary role of the insurance sector in any economy is to convert the potential savings of the public into investment projects.
- In this respect, the role of insurance can be considered important in channeling resources.
- Improving the allocation of resources by continually screening fund seekers and monitoring fund recipients.
- Continuously mobilizing potential savings of the public.
- Improving risk management and liquidity of funds.

The Role of Insurance in Mitigating Individual Risks

- At the individual level, insurance serves as a financial safety net, offering protection against life's uncertainties.
- Health insurance, for instance, plays a pivotal role in ensuring that individuals have access to quality healthcare without the fear of exorbitant medical bills.
- As the cost of healthcare rises, insurance provides a mechanism for people to manage their health-related risks effectively.
- Similarly, life insurance provides financial security to families in the unfortunate event of the breadwinner's demise.
- The presence of a robust insurance sector empowers individuals to take calculated risks, be it in entrepreneurship, investments, or pursuing higher education, knowing that a safety net is in place.

Risk Mitigation for Businesses and Industries

- On a broader scale, businesses and industries face a myriad of risks ranging from natural disasters to market fluctuations.
- Insurance acts as a buffer, allowing businesses to recover and rebuild in the aftermath of unforeseen events.
- Property insurance, for instance, protects businesses from the financial fallout of damage to physical assets, whether due to fire, natural calamities, or other incidents.
- Furthermore, liability insurance shields businesses from legal liabilities, ensuring that they can operate without the constant fear of litigation jeopardizing their existence.
- This, in turn, fosters an environment conducive to entrepreneurship and innovation, two critical drivers of economic growth.

Insurance and Infrastructure Development

- India's ambitious infrastructure development projects, crucial for sustained economic growth, are not immune to risks.

- Construction projects, in particular, are susceptible to delays and cost overruns due to unforeseen events such as natural disasters, regulatory changes, or labor strikes.

- Insurance solutions tailored for the construction industry play a pivotal role in managing these risks, providing the necessary financial support to ensure projects stay on track.

- Moreover, as India continues to invest in smart cities and industrial corridors, insurance becomes an indispensable tool for mitigating risks associated with large-scale infrastructure development. Insuring these projects not only protects the investments made but also instills confidence in investors, paving the way for increased participation in the nation-building process.

Agriculture and Rural Development

- A significant portion of India's population is dependent on agriculture for their livelihood. However, the agricultural sector is highly susceptible to the vagaries of nature, with unpredictable weather patterns, pests, and diseases posing constant threats.

- Crop insurance emerges as a crucial instrument in stabilizing the income of farmers, offering financial protection against yield losses due to natural calamities.

- By providing farmers with a safety net, crop insurance encourages them to adopt modern farming practices, invest in better seeds and technology, and ultimately contribute to increased agricultural productivity.

Insurance as a Catalyst for Financial Inclusion

- In India, a significant portion of the population remains under banked or unbanked.
- Insurance, with its emphasis on risk management and financial security, acts as a bridge to bring more people into the formal financial sector.
- Micro insurance products catered to the needs of low-income individuals offer a cost-effective way for them to protect their assets and livelihoods.
- The integration of insurance into financial inclusion initiatives not only safeguards vulnerable populations but also contributes to the overall economic resilience of the nation.
- As more individuals and businesses become part of the formal financial ecosystem, the potential for sustained economic growth increases.

Technology's Role in Revolutionizing Insurance

- The advent of technology has brought about a paradigm shift in the insurance sector, making it more accessible, efficient, and customer-centric.

- Insurtech solutions, such as mobile-based insurance platforms and data analytics, are transforming the way insurance products are designed, underwritten, and distributed.

- For instance, the use of satellite imagery and weather data enables more accurate risk assessment in agriculture insurance, reducing fraud and streamlining claim processes.

- Similarly, the adoption of artificial intelligence and machine learning algorithms enhances the ability to predict and mitigate risks across various sectors.

- Insurance serves as an economic development tool by fostering financial stability, encouraging investment, and improving in risk management.

- Acting as a conduit for transforming savings into productive investments, insurance channels resources effectively while enhancing resource allocation and promoting long-term growth.

- Through its role in protecting against financial losses, supporting credit systems, contributing to government revenue, and facilitating global trade, insurance plays a pivotal role in driving sustainable economic stability and advancement.

- As India continues its journey towards becoming a global economic powerhouse, the role of insurance becomes even more pronounced.

- A resilient and adaptive insurance sector, coupled with technological advancements, not only mitigates risks but also facilitates a conducive environment for innovation, investment, and sustained economic growth.

- Individuals, businesses, and policymakers must recognize the pivotal role insurance plays in navigating risk and fostering a robust economic future for the nation

Proposed Amendment to Insurance Act

- In a major step toward achieving 'Insurance for All by 2047,' the government plans to introduce a transformative bill in the upcoming Budget session to amend the Insurance Act, 1938.

- This amendment aims to modernize the regulatory framework, expand insurance coverage, enhance competition, and drive economic growth.

- The Insurance Act, 1938, has long been central to India’s insurance regulation, but modernization is needed to align with evolving market dynamics.

Background

- India’s insurance industry is on the brink of transformative changes with the anticipated introduction of the Insurance Amendment Bill
- This landmark reform builds on past efforts, primarily, the Insurance (Amendment) Act, 2021, under which foreign direct investment in Indian insurance companies was increased from 49% to 74%.
- Under the Bill, the government is likely to have no FDI cap in the insurance sector and permit foreign investors to own up to 100% in Indian insurance companies.
- In addition, the government is considering the issuance of composite licenses, thereby permitting an insurance company to offer all types of insurance under one license and entity.

- To bring in a diversity of insurance products for consumers and enhance competition in the sector, the government has proposed some amendments to the Insurance Act of India.

- The amendments are proposed to the Insurance Act, 1938, the Life Insurance Corporation Act, 1956, and Insurance Regulatory and Development Authority Act, 1999.

- If the proposal is approved, the Insurance Regulatory and Development Authority of India (IRDAI) will form regulations to implement the new framework which would affect policyholders and the Indian insurance sector as a whole.

- This proposal aims to amend insurance laws to ensure better accessibility and affordability of insurance for all and promote industry expansion.

- The amendments have been constituted following a comprehensive review of the sector's legislative framework, in consultation with IRDAI and the industry.

- The proposed Insurance Amendment Bill is a significant step towards strengthening and modernizing India's insurance sector.

- The Department of Financial Services, Ministry of Finance, has by way of an Office Memorandum released on 26 November 2024, proposed certain amendments to the Insurance Act, 1938, the Life Insurance Corporation Act, 1956 and the Insurance Regulatory and Development Authority Act, 1999

The Proposed Amendments aim the following:

- to ensure accessibility and affordability of insurance to citizens;
- foster expansion and development of the insurance industry;
- streamline business processes.

Broadly, the major Proposed Amendments are as follows:

The Insurance Act, 1938

- **Definitions:**

- **Class of insurance business:** It is proposed to be defined to mean class of (i) life insurance business (ii) general insurance business (iii) health insurance business (iv) reinsurance insurance business or (v) such other class of insurance business as may be notified.

- **Insurance Business:** It is proposed to be defined to mean business of effecting insurance contracts, whereby insurer undertakes to assume the risk and to pay the insured an agreed compensation for loss, damage or liability arising from a contingent event on agreed terms and conditions and subject to agreed limitations.

- **Indian Insurance Company:** Definition is proposed to be modified to mean only a public company registered under the Companies Act, 2013.

- The requirement of such company's sole purpose being to carry on LIB / GIB / RIB / HIB is done away with. Section 3AA proposed which permits foreign investment in such companies up to 100%.

- **Insurer:** Existing definition is proposed to be modified to mean an entity carrying on insurance business.

- **Insurance Intermediary:** Existing Definition is proposed to be included in the Act and will include managing general agents.

- **Premium:** It is proposed to be defined to mean consideration payable under a contract of insurance to the insurer by the policyholder.

- **Composite License for Insurers:**

- Under section 3, it is proposed that IRDAI will be empowered to grant certificate of registration to any applicant for such class or classes of insurance business for which it is eligible.

- Under section 6, it is proposed that in case of an insurer carrying on business in more than one class of insurance business, IRDAI will have the power to specify a paid-up equity capital which is not less than the sum of the paid-up equity capital required for each of such class of insurance business.

- For Indian insurers, this will offer an opportunity to diversify their portfolios and remain competitive in this market wherein the new entrants will face low entry barriers.

- This would also mean a wide array of options for customers.

- **Reduction in paid-up Capital:** It is proposed that the IRDAI will have the power to reduce the paid-up equity capital to INR 50 crores for any class of insurance business serving underserved or special segments.

- **Insurers permitted to engage in other businesses:**

- It is proposed that insurers will be permitted to engage in other forms of business (in addition to insurance business) as below:

- Carrying on and transacting of guarantee and indemnity business.

- Managing, selling and realizing any property which may come into the possession of the company in satisfaction or part satisfaction of any of its claims.

- Establishing and supporting or aiding in the establishment and support of associations, institutions, funds, trusts and conveniences calculated to benefit the company's employees or ex-employees or the dependents / connections of such persons, granting pensions and allowances.

- Acquiring and undertaking the whole or any part of the business (of nature similar to what is permitted in the Act) of any person or company.

- Doing all such things as are incidental / conducive to the promotion / advancement of the business of the company.

- **100% FDI in Indian Insurance Company:** It is proposed that foreign investors including portfolio investors will be permitted to invest up to 100% in equity share of an Indian insurance company.

- Allowing 100 per cent FDI in insurance will attract significant interest from global insurance players.
- Many international insurers can now enter the Indian market which will drive Indian insurers to adopt global best practices in product & processes, innovation as well as cutting-edge technologies.

- This will ultimately help consumers access the best products and services

- **Reduction in minimum net owned funds :**It is proposed that minimum net owned funds required for registration of FRBs will be reduced to INR 1000 crores from current INR 5000 crores.

- **Transfer of Shares:** It is proposed that prior IRDAI approval will be required for registration of transfer of shares where nominal value of shares intended to be transferred by any individual, firm, group, constituents of a group, or body corporate under the same management, jointly or severally exceeds 5% of the paid-up equity capital of the insurer.

- Currently, prior approval is required where nominal value of shares exceeds 1% of paid-up equity capital of the insurer.

Opening Agent Ties:

- For decades, insurance agents in India have worked under the regulation wherein they could represent only one insurer in each category - life, general, or health insurance.
- As per the proposed changes, the government wants to change this rule by allowing agents to partner with multiple insurers across categories.
- This could translate to more choices and better products, and possibly better premiums for the customers.
- However, IRDAI will continue to play a crucial role here to ensure that these new partnerships don’t lead to a conflict of interest.

- **Validity of registration of insurance intermediary:**

- In this regard, it is proposed that:

- 3 years validity period of registration of insurance intermediaries will be done away with.

- All existing registered insurance intermediaries will be required to make an application to IRDAI for continuation of their registration, within 3 months from commencement of the amendment.

- The registration thus obtained will remain in force subject to payment of prescribed annual fee, until it is suspended or cancelled by the IRDAI.

IRDAI will have the power to suspend / cancel in some prescribed circumstances like if insurance intermediary:

- contravenes provision of the Act, or IRDAI Act, or rules and regulations, or any directions / orders;
- defaults in complying with / contravenes the Companies Act, 2013, FEMA or certain other prescribed laws;
- is convicted of an offence under any law;
- fails to pay annual fee;
- its holding company or joint venture partner (having principal place of business outside India) is debarred to carry on insurance intermediation business in that country, etc.

Administrator appointment:

- is proposed that IRDAI will have the power to appoint administrator if it has reason to believe that insurer is acting in a manner likely to prejudice the interests of the policyholders.
- Currently, this power is limited to appointing administrator for life insurers.
- **Constitution of Executive Committee of Life Insurance Council and General Insurance Council:**
- It is proposed that the Central Government will have the power to nominate 2 persons to the Committees.

Appointment of Actuary by insurer.

- The Authority shall, by regulations, specify the qualifications and experience necessary for appointment of an actuary by an insurer for the purposes of this Act.
- The Authority may, by regulations, specify the duties and powers of the actuary so appointed by the insurer.

- **Penalty under the Act extended to insurance intermediaries:**

- It is proposed that the penalty prescribed under the Act will extend to insurance intermediaries along with insurers.

- Proposed penalty is minimum of INR 1 lakh, extendable to INR 5 lakhs for each day. Maximum penalty under this provision will be capped at INR 10 crores.

- **Penalty for misstatement or furnishing false documents:**

- In this regard it is proposed that, if an insurer / insurance intermediary makes a statement / furnishes any document, statement, account, report or return which is false and which he knows / believes to be false, he will be liable to a minimum penalty of INR 1 crore, extendable to INR 5 crores.

- **Differential Capital Requirements**:

- Existing regulations impose uniform capital requirements on all insurance companies, regardless of their size or scope.
- The bill suggests differential capital norms, which would allow different levels of capital investment based on the scale and focus of insurance companies.

- **Reduction in Solvency Norms**:
- Insurance companies are required to maintain a certain solvency margin to ensure they can meet their future obligations.
- The amendment seeks to reduce these solvency norms, potentially lowering the financial barriers for new entrants and encouraging a more competitive market.

- **Changes in Investment Regulations**:
- The Amendment proposes that the IRDAI will set all investment requirements and restrictions for insurers through regulations, rather than having these prescribed in the Insurance Act and its current regulations.
- This shift aims to streamline and adapt investment norms more flexibly.
- This increase simplifies the process for smaller investments and facilitates easier market participation.
- **One-Time Registration for Intermediaries**:
- The bill proposes a one-time registration process for insurance intermediaries, streamlining their entry into the market and reducing bureaucratic hurdles.
- The Amendment allows for the perpetual validity of insurance intermediary registrations—such as corporate agents and brokers—upon payment of an annual fee set by the IRDAI.
- Previously, these registrations were valid for only three years and required renewal every three years.

- **Net Owned Funds**
- The Amendment Act proposes to lower the net owned funds requirement for foreign re-insurers from INR 5,000 crores to INR 500 crores.
- This significant reduction aims to enhance the attractiveness of the Indian market for foreign reinsurers, particularly smaller and new- age players, addressing a long standing request from global reinsurance firms.

- **Expansion into Financial Products**: Insurers may be allowed to distribute other financial products, broadening their service offerings and integrating more financial solutions under one roof.

- **Electronic Submission :** The Amendment Act aims to improve business efficiency by allowing the electronic submission of returns required under the Insurance Act.

- The IRDAI will set the submission frequency through separate regulations, enhancing ease of compliance.

- **IRDAI Act**

- Retirement age for whole-time members of IRDAI is proposed to be increased to 65 years (same as that of Chairperson), from current 62 years.

- Cooling off period barring future employment of Chairperson and members is proposed to be reduced to 1 year from 2 years.

- It is proposed that IRDAI will not have the power to delegate the power to make regulations and the power to register an insurer.

- It is proposed that IRDAI will exercise its power to make regulations in consultation with the Central Government and the Insurance Advisory Committee and subject to prior publication.

- These reforms reflect the government's intent to modernize India's insurance sector and make it more dynamic, competitive, and consumer friendly.

- By opening the doors to 100% FDI and addressing structural limitations, the Bill has the potential to align India's insurance industry with global standards, while fostering innovation and growth.

- The Bill once implemented will enhance insurance penetration in India.

- For consumers, this will mean better insurance products, competitive pricing, and improved service delivery.

- All in all, the Bill promises long-term benefits for all stakeholders.

- **How will the Insurance Amendment Bill impact the industry?**

- Currently, India has 27 life insurers, 25 general insurers, and 7 standalone health insurers, highlighting a diverse and competitive insurance landscape as the sector prepares for these significant changes.

- The amendments aim to improve returns for policyholders and enhance their overall experience by facilitating access to a wider range of insurance products and services.

- By allowing composite licensing and reducing capital and solvency requirements, the bill is expected to encourage the entry of more players into the insurance sector.

- The entry of new insurance companies and the expansion of existing ones are likely to spur economic growth and create job opportunities across the country.

- The proposed changes are designed to enhance both operational and financial efficiencies within the insurance industry, making it easier for insurers to do business and better manage their resources.

Thank You