inotes
Newsletter from India's Leading Insurance Broking House
April 2011

Summary

- Group life insurance - *safeguarding your employees interest*
- **Interview** - *Life insurance*
- **Industry Statistics**
- **View Point**



# Message from the Editor

Dear Readers,

End of a magnificent year for the Indian insurance industry in terms of growth. While the flash figures indicate the general insurance industry (including the health, credit and agriculture market) closing in at around Rs. 46600 crores (22% growth), the Life industry ends at about 126000 crores, clocking a 16% growth rate. This despite the Indian insurance market being softer than ever before across all lines! Whether rates are going to harden this year remains to be seen but the stage seems set for the health and motor third party premiums to step up.

While the impact of hardening rates following the Japan earthquake and tsunami which closely followed the quake at New Zealand and prior to that the floods at Australia, (resulting in a cumulative loss of about 45-50 billion USD to the global insurance industry) has not been felt globally as yet, understandably, the earthquake rates have gone up about 50% in Japan. Business interruption risk having caught on in the recent years in Japan has resulted in the insurable losses being considerably higher than what was initially estimated.

By and large we have been focussing upon topics related to the general insurance industry and to take a break from it, in this issue we have put forth an article which focuses upon the various group life insurance benefits available for Corporates and have Mr. TR Ramachandran, CEO & MD, Aviva India, sharing his views with our readers. Our sincere thanks to him.

As we begin the new fiscal, we look forward to an equally exciting year ahead.

**V Ramakrishna**
Editor – *i-notes* & Chairman – India Insure

# Group Life Insurance - safeguarding your employees interest

Employees consistently rate benefits as one of the key factors in job satisfaction and so it is important for an employee benefits package to be attractive to both current and prospective employees. The economic downturn has changed many a paradigm and has intensified employers' focus on maximizing their employee benefits spend so that it can be treated as a business value that can be measured, managed and turned into a competitive advantage. As per a recent survey conducted by India Insure on 'Trends in Employee Benefits', majority of the survey respondents have indicated that the main objective in providing Employee benefits insurance is to stay on par with competitors. This clearly substantiates the fact that 'employee benefits insurance' is increasingly being deployed as a talent management tool.

One way organizations can show concern for their employees is to shoulder the two responsibilities they worry about most: Savings for their families and Savings for retirement. Group life & retirement insurance plans enable organizations to effortlessly provide employees with both, savings and security. In return, organizations can be assured of a committed and loyal workforce.

Group insurance and retirement products available to corporates can be broadly classified into:

- Group Superannuation scheme
- Group Term Life Insurance
- Group Gratuity scheme
- Leave Encashment scheme

## Group Superannuation scheme

Longevity has been increasing throughout the world including India during the last century. Achieving longer life-spans is both a laudable objective and a true achievement for society. At the same time, improving mortality presents society with a real challenge in ensuring that all individuals have an adequate income throughout their old age. Longevity risk is the risk that individuals live longer than anticipated, with consequent shortfalls in incomes. The uncertainty around the quantum by which future life-spans will increase poses a serious financial threat to individuals and their families.

As a thoughtful employer, it's imperative to chalk out a comfortable retirement plan for your employees. Group Superannuation schemes offered by life insurance companies (also known as pension schemes) can be a good option for organizations to systematically plan for the increasingly crucial post-retirement days of their employees.

Superannuation schemes are of two types - Defined contribution and Defined benefit.

**Defined contribution scheme** is one in which the employer decides the contribution to the scheme. This contribution is ascertained as a percentage of the salary. The pension amount is ascertained at the time of retirement, depending on the accumulated amount and the type of annuity scheme opted by the annuitant.

**Defined benefit scheme** on the other hand takes into account the amount of benefit an employee will get on his retirement. Actuarial valuation is conducted to ascertain the funding rate. Based on various factors like years of contribution left, accumulated funds with interest, interest rate estimates etc, the funding is ascertained.

As the costs of funding of defined benefit pensions have increased due to increasing life expectancies and highly uncertain projected interest rates scenario, many companies have shifted to defined contribution pension funds.

Earlier companies used to create a privately managed trust and as and when a member retires, purchase annuity from a Life Insurance Company to provide pension for such retiring member. Because of the administrative hassles involved in managing the Trust, companies today are increasingly outsourcing the management of the Superannuation Fund to a life insurance company.

Contributions to the superannuation scheme can be made either by the employer alone or by both the employer and the employee (in which case the scheme is called a Contributory Pension Fund Scheme). The annual contributions made by the employer are treated as deductible business expenses.

On retirement, the employee can withdraw up to 33% of the accumulated amount from their pension fund (which is tax-free) and the rest of the money is used to buy an annuity from an insurance company of his

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choice. In case of resignation, the accumulated corpus from the previous employer can be transferred to the superannuation scheme of the new employer, provided the rules of both schemes permit such a move. In case the employee does not wish to withdraw the fund immediately may be because the new employer does not have a similar scheme, he can retain the benefit entitlement within the fund until retirement.

With the plan being handled by an Insurer, employees can expect their investments to be handled prudently and claims to be promptly settled.

### Group Term Life Insurance

Group term life insurance is often provided as part of a complete employee benefit package. In most cases, the cost of group coverage is far less than what the employees would pay for a similar amount of individual protection. Group Term Life provides “no-frills” life insurance coverage at “no-frills” rates.

Group term life is typically provided in the form of yearly renewable term insurance policy. When group term insurance is offered through the organization, the employer usually pays for all or most of the premiums. The amount of coverage is normally equal to two or three times the employee’s annual salary. The unit rate of the premium is based on the average age of the group, past mortality records and nature of risk associated with the job.

The Sum insured under the policy can be opted as:

- A multiple of salary
- Designation wise life cover
- Flat life Cover

The GTL policy also has add-ons like

- Double Accident Benefit - payment of double the sum assured on death due to accident
- Critical Illness Benefit – payment of the sum assured when the employee is diagnosed with any critical illness as specified in the policy
- Disability benefit – payment of sum assured when the insured is disabled

As with other life insurance schemes, group life insurance allows you to choose your beneficiary and the insurance benefits go to the beneficiary (nominee) named on the policy if the employee dies before the term of the policy.

Group Term life insurance is today preferred by corporates over Group Personal Accident insurance because it covers both natural and accidental death worldwide on a 24*7 basis. This policy can be offered as a NIL exclusion policy. It is a very easy policy to administer and highly cost efficient compared to individual Term Life Insurance policy.

**Voluntary Group Term Life Insurance & Top Up facility**

If the organization is not willing to have this policy in place, at least 70% employees of the company can form a group and take this policy. On the other hand, if the employees want they can pay premium themselves and have additional coverage over and above the coverage provided by the employer.

In both these cases, the premium rate will increase but will still be far less than an individual term life insurance policy.

Also the PF Act 1952, mandates that all employers to whom the Employee’s Provident Fund and Miscellaneous Provision Act, 1952 applies, have a statutory liability to subscribe to EDLI scheme. The GTL policy can be offered as a better substitute to the EDLI scheme of RPFC with higher coverage and reduced cost.

Group term coverage remains in force for the employee until employment is terminated or until the specific term of coverage ends. Some companies offer the option of converting the group coverage to an individual policy if the employee leaves employer or resignation or retirement.

Life insurance is an important foundation of a strong financial plan, and it is essential for employers to help employees maintain that financial security especially since most Indians are underinsured.

### Group Gratuity scheme

Gratuity is an important form of social security benefit provided by employers in India as a mark of gratitude for the services rendered by the employee. Gratuity is a lump-sum payment made by an employer for long and continuous service and is governed by “The Payment of Gratuity Act, 1972” which is applicable to all enterprises with more than 10 employees. To receive gratuity, the employee should have completed at least 5 years of continuous service and the amount is calculated based on the last drawn basic salary.

The employee is eligible for 15 days of pay for each completed year of service. The gratuity benefit is payable on cessation of employment (either by resignation, death, retirement or termination, Permanent Disability). The maximum amount of gratuity payable to an employee was limited to Rs.3.5 lakhs but in May 2010, the Government has enhanced the maximum gratuity limit from 3.5 lakhs to 10 lakhs which means a significant improvement for many employees’ gratuity benefits. It is also likely to lead to increased costs for many employers, particularly because it also applies to benefits already accrued with the current employer.

Gratuity payment is a potential liability for an organization and tends to increase as the salaries and the service lengths increase. In case of large organizations, liability on account of Gratuity can become very big and if not handled properly it can affect the cash flow. An employer may pay out gratuity proceeds from his current revenue, however, to ascertain the gratuity liability of the employer and for more prudent financial planning, it is beneficial to set up a gratuity fund Trust and outsource it to a Life Insurance Company.

Insurance companies provide several attractive options to manage the gratuity liability as it is an area of core competency for them. The companies can benefit from their expertise in management of funds and from their economies of scale on investments. The insurance companies also provide flexibility in management of funds like switching of funds which increases the possibility of maximizing the returns depending upon the market conditions.

Other benefits in outsourcing the gratuity liability to an insurer include

- Investment of Trust Funds based on research
- Ease in administration
- Total Transparency
- Annual Actuarial valuation free of cost
- Maintaining the Books of Accounts of the Gratuity

The Clients are under no obligation to stay with any one insurance company for ever for managing this scheme. The funds can be shifted from one insurer to another. Many corporate clients in India have restructured their Group Gratuity schemes and are selecting an insurance company for managing this scheme based on the annualized returns generated, types of investment options, assets under management, fund management

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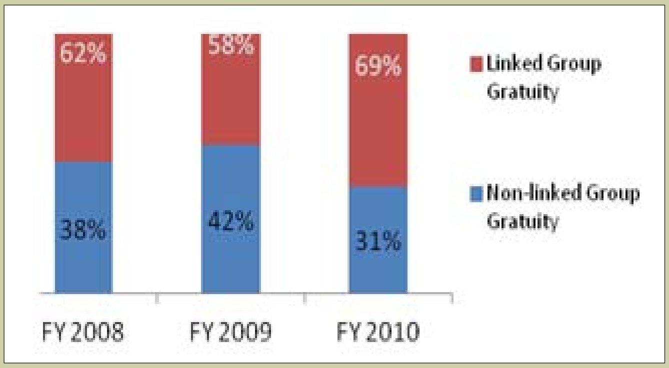
## Group Life Insurance - safeguarding your employees interest .... Contd. # 2

charges and obviously the service levels. The number of companies outsourcing their gratuity schemes to insurers has increased over the years, with PSU's also joining the bandwagon in the recent past.

Companies can invest the gratuity amount in traditional schemes or Unit Linked schemes of the Insurer. The trustees of the Gratuity Fund generally like to play it safe and opt for traditional schemes which are risk averse. Although the trend is slowly changing among the corporates and they are looking forward to exposing some portion of the fund to equity investment also.

**Split of Group Gratuity between Traditional & ULIP schemes**




*Source : Life Insurance Council*

Gratuity is an effective tool not only to reward loyal employees, but can also be used to retain them by offering higher benefits than that prescribed in the Act.

### Leave encashment

Many Indian employers offer leave encashment benefits schemes to their employees where accrued leaves can be encashed. Since such a liability increases with time, it may become difficult to pay the benefit as you go. Leave encashment liability for a company would depend upon the salary eligibility for leave encashment, the number of accumulated leaves, the upper limit or cap for leave accumulation, Leave encashment rules of the company, number of employees, etc. Normally, the leave encashment benefit is payable in cases of death, retirement, resignation, termination and disability leading to cessation of employment. It is therefore beneficial that the employer sets up a separate fund from which this benefit may be paid out.

Also, with the revision in the Accounting Standard (AS-15) of January, 1995 and the amendment in Section 209(3) of the Companies Act, 1957, it has become necessary for the employers to recognize the accrued liabilities in respect of Leave Encashment benefits available to all the employees in the books of final accounts.

Insurance companies now offer Group Leave Encashment Policies designed to fund for such benefits. The contributions that you pay to fund your scheme will be invested in the Insurance scheme ( either Traditional or ULIP scheme) funds and will be available for payment of the benefit when it falls due. The products also provide a host of features like Flexible Investment Options, Switching of funds. Additionally, the product also provides for term cover for all the employees covered under the policy.

### Conclusion

With the demographics of the workplace changing and workers spending more time at the workplace, it is imperative for employers to look at ways and means to provide a secure financial footing to their employees. Employees increasingly view benefits as the foundation of their financial safety net. At the same time, employees are not prepared to face significant unforeseen events such as premature death, income loss due to disability or even retirement for that matter. As a result, they continue to rely more than ever on workplace benefits and as such employers have an opportunity to offer valuable access to benefit programs and information.

Employers should also recognize that their traditional role as plan sponsor may not be the only way to provide value to their employees. Accessing the vibrant external marketplace for insurance products tailored for the organizations' needs can actually increase the total amount available due to improved plan choice. The employers can reduce the administrative burden of these plans by outsourcing it to insurers.

Organizations need to realize that health, retirement and all other benefits are strong factors contributing to loyalty and are a significant part of an employee's decision to choose and stay with an employer. As the make-up of the workforce and office dynamics continue to evolve, so will employee expectations regarding benefits. Organizations will need to keep these shifts in mind when developing and choosing benefits offerings. Innovative employee benefits solutions that are more flexible and responsive are more likely in the future to meet the needs of employees.



## News TitBits

### General insurance may turn costlier, says IRDA

*Source: Business Standard*

The Insurance Regulatory & Development Authority (Irda) warned that health insurance, motor insurance and other general insurance policies might turn costlier, with the settlement claims going up."The demand and supply position in the non-life industry will be such that prices should harden and I expect to see evidence of that in the course of the next few years. It will become even harder as we go along," Irda Chairman J Harinarayan told.

### India Inc now paying more for insurance

*Source: Financial Express*

The insurance renewals in the new fiscal have brought cheers for the general insurance companies while the India Inc has to shell out more for getting covers. For the first time the pricing for the general insurers has improved after three years of price war since the deregulation in the premium pricing began. Confirming the changes in the pricing, United India Insurance CMD G Srinivasan said the prices have gone up by 5-10% across property cover. In the case of group health insurance, it has gone up in the range of 40-50%.

### Motor insurance premium for third party liability cover hiked

*Source: Hindu Business Line*

The Insurance Regulatory and Development Authority (IRDA) has hiked motor insurance premiums for third party liability cover for various classes of vehicles with effect from April 25, 2011. The hike ranges from10 per cent to about 70 per cent for various categories of vehicles. "Premiums need to be reviewed regularly depending upon the average claims which have been awarded by the various courts, frequency of claims for each class of vehicle and inflation, amongst other factors," Mr J. Hari Narayan, Chairman, IRDA, said in a circular.

## Interview – *Life Insurer*

In the interview section for this issue, we have Mr. TR Ramachandran, CEO & MD, Aviva India sharing his views on the present and future of the life Insurance market in India .

**Life Insurance in India is a big opportunity especially with the large population and untapped potential. What according to you are going to be the key growth areas in the near future?**

Aviva Group continues to be positive about the long-term prospects of the industry, given the underlying economic and demographic drivers. The shift towards a large, working population with rising income levels and greater financial awareness will drive future growth.

We had recently conducted a research with IMRB on saving habits, concerns and aspirations of young parents in India and it was not surprising to note that the top concern of 81% of parents surveyed was their child's future education. Thus, Child Plans will continue to be popular. The research also indicated that nearly 52% of parents in India are saving for financial protection in case of death of primary wage earner and 45% for retirement. With only 4% insurance penetration, I think the industry needs to play a more proactive role in developing the market for protection products. Developing term insurance is a big opportunity and challenge in India. The challenge is to change the what-do-i-get-in-return psyche of Indian customers.

Given the Indian demographics and the lack of adequate Public Health eco-system, we expect health insurance business to also increase strongly in the immediate future. Further, the semi-urban and rural markets, offer a vast, untapped potential. The online medium is a key growth area in the near future. Term plans are increasingly being launched in the online platform, where insurers save on overhead costs. Insurers are passing this savings on to the customers.

**The life insurance industry is divided on the issue of whether banks should be allowed to distribute products of multiple insurance companies. What is your take on this?**

We believe that open architecture, where banks will be allowed to distribute products of multiple insurance companies, is the way forward for the growth of the insurance industry. This will not only help the banks reach out to more customers but will also give the banks' customers choice to opt from the insurance cover of several insurance companies. The simple question is that if banks are allowed to sell mutual fund products of multiple companies, why not insurance? With most of the banks opting to pick up stake in the insurance JVs, the decision on Open Architecture would be critical, especially for the sustenance of non-bank backed insurers.

**How do you perceive the Life Insurance industry to shape up in the next two years?**

Since liberalization, the Indian life insurance market has delivered a strong growth. The engine of growth has by and large been foreign life insurance companies, which have expanded the market by developing new distribution channels and products aimed at the individual life sector. Going forward, a lot of how the insurance industry will shape up will depend on the passing of the Insurance Bill. Currently the total capital deployed in the insurance sector is close to Rs 30,000 crores. The FDI in this (assuming 26%) is close to 7800 crores. If 49% happens, the sector stands to gain additional 7,000 crores as FDI. The additional FDI will help insurance companies expand their distribution, get in international systems to improve product development and customer service processes.

Post the regulatory upheaval of 2010, I believe 2011-12 will be years of transition. The industry will need to reinvent itself and recalibrate expenses. There will be a plethora of products in the protection space and the online channel will see traction. The products will be simpler and more transparent. With the products across companies being similar, the innovation will be in the customer services space. Technology will be the key driver for this.

With over 10 years of being in business, the claim settlement ratios of insurance companies will be critical as they will define the confidence level in the sector.

**How has the year been so far for AVIVA LIFE in terms of new business? What is your current product mix?**

Aviva has had a strong performance in 2010, where despite the adverse impact of regulatory changes of 1 September 2010, we have delivered positive growth of over 10%. More importantly, our journey towards broad-basing our product portfolio, widening the jaws between expenses and topline and customer centricity have all yielded desired results.

**How well has your company tapped the bancassurance channel of distribution? What are the other avenues of distribution you are looking at? How much business do your channel partners bring in?**

Aviva is the global bancassurance leader and in majority of our countries, bancassurance is the only distribution channel. In India too, we pioneered the concept of Bancassurance and till date nearly 2/3rd of our business is contributed by our bancassurance business. Additionally, we have also invested in a quality led small but high impact agency business. We have been working on version 2.0 of what the agency channel should look like. We are applying much more analytics to find out who our successful agents are and have found interesting trends, which are now being tested to enhance the quality of sales force.

Moreover, in the times to come, we see possible emergence of the open architecture model for banks to sell policies of multiple insurance companies. Independent financial advisers will also play a critical role as non-partial distribution agencies. We see the online platform playing a critical role in the sale of insurance products in future, subject to enabling regulations.

**With a plethora of Insurance policies in the market, how will a customer distinguish between the offerings of various insurance companies? What is your USP/ strategy that sets apart your company from the rest?**

From the customer perspective, we would recommend that he does a need-based analysis and takes advice from a financial consultant before buying any product. At Aviva, we have a tool for our sales team which does a need-based analysis before we offer any products. For example if a person is saving for his child's future education we would offer him either our unit-linked child plan or the traditional child plan based on his risk appetite. All child plans come with the waiver of premium option which ensures that the fund one planned for his child's future security is achieved.

Our products are designed basis customer insights and surveys and we have a wide range of product offerings covering all customer lifecycle needs ranging from savings, protection, investment, retirement and health.

We also have an in-house fund management team with the long-term view for investing as insurance is a long-term product. We have been consistently performing above our benchmarks.

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## Report Card - February 2011

**Gross premium underwritten by non life industry for and up to the month of February 2011*** **(Rs. In crores)**

| INSURER | FEBRUARY | | GROWTH OVER THE SAME PERIOD OF PREVIOUS YEAR | APRIL - FEBRUARY | | GROWTH OVER THE SAME PERIOD OF PREVIOUS YEAR |
|---|---|---|---|---|---|---|
| | 2010-11 | 2009-10 | | 2010-11 | 2009-10 | |
| New India | 519 | 474 | 9% | 6367 | 5431 | 17% |
| United India | 492 | 384 | 28% | 5559 | 4553 | 22% |
| National | 545 | 400 | 36% | 5381 | 4104 | 31% |
| Oriental | 384 | 360 | 7% | 4744 | 4139 | 15% |
| ICICI- Lombard | 367 | 273 | 35% | 3878 | 3002 | 29% |
| Bajaj Allianz | 241 | 213 | 13% | 2613 | 2245 | 16% |
| IFFCO-Tokio | 136 | 108 | 25% | 1637 | 1336 | 22% |
| Reliance | 141 | 137 | 2% | 1514 | 1846 | -18% |
| Tata-AIG | 92 | 76 | 21% | 1097 | 813 | 35% |
| HDFC ERGO | 95 | 69 | 37% | 1170 | 822 | 42% |
| Royal Sundaram | 94 | 79 | 19% | 1029 | 820 | 25% |
| Cholamandalam | 76 | 64 | 19% | 877 | 723 | 21% |
| Future Generali | 49 | 35 | 39% | 556 | 342 | 62% |
| Shriram | 83 | 52 | 62% | 687 | 358 | 92% |
| Bharti AXA | 52 | 32 | 62% | 491 | 244 | 101% |
| Universal Sompo | 25 | 20 | 25% | 259 | 155 | 67% |
| SBI General | 9 | 0 | | 30 | 0 | |
| Raheja QBE | 1 | 0.22 | 418% | 7 | 1 | 420% |
| L & T | 4 | 0.00 | | 10 | 0 | |
| **PRIVATE TOTAL** | **1463** | **1158** | **26%** | **15858** | **12714** | **25%** |
| **PUBLIC TOTAL** | **1941** | **1618** | **20%** | **22051** | **18228** | **21%** |
| **GRAND TOTAL** | **3404** | **2776** | **23%** | **37909** | **30942** | **23%** |
| **1.Credit Insurance** | | | | | | |
| ECGC | 71 | 71 | 0% | 783 | 732 | 7% |
| **2.Health Insurance** | | | | | | |
| Star Health | 36 | 134 | -73% | 1211 | 921 | 32% |
| Apollo Munich | 53 | 9 | 463% | 251 | 100 | 151% |
| Max BUPA | 3 | | | 21 | | |
| **Health Total** | **92** | **144** | **-36%** | **1483** | **1021** | **45%** |
| **3.Agriculture Insurance** | | | | | | |
| AIC | 388 | 162 | 139% | 1774 | 1422 | 25% |

* Source : IRDA

### Observations: Performance for Apr-February 2011 Period

- The industry (incl stand alone health insurers) has underwritten premium of Rs. 39392 crores recording a growth rate of 23% for Apr-Feb 2011 period compared to Rs.31964 crores collected during the same period last year.
- The private players have registered a growth of 25% during this period compared to 11% during the same period last year.
- The PSU's have registered a growth rate of 21% during this period compared to last year's 12%.
- The accretion achieved by the PSU's during this period is Rs.3823 crores; the private players: Rs.3144 crores and stand-alone health insurers: Rs. 462 crores towards the overall market accretion of Rs.7429 crores.
- The major contributors for the performance in the period Apr-Feb 2011 have been National with an accretion of 1277 crores, United India with an accretion of 1006 crores, New India with an accretion of 935 crores and ICICI with an accretion of 876 crores.
- Reliance (-18%) has recorded negative growth during this period.
- At the end of this period, the private players have collectively increased their market share from 41.09% to 41.83%.

## News TitBits

### PNB shortlists 3 cos to tie up for insurance venture

*Source: Times of India*

Punjab National Bank has shortlisted three life insurers—Aviva India, Bharti Axa and Metlife—as potential partners for its foray into life insurance with the help of the Boston Consultancy Group.

### GIC sets stringent rules for state-owned general insurers

*Source: Business Standard*

At a time when the government-owned general insurance companies are reeling under heavy underwriting losses, the General Insurance Corporation (GIC), fearing higher claims, has tightened the noose on these companies by offering lower reinsurance capacities, cutting commissions and putting in stringent underwriting conditions while renewing their contract. In some cases, the reinsurer has offered 50 per cent lower capacities than last year.

### Insurance industry to be worth $400 bn by 2020: FICCI Report

*Source: Economic Times*

India's insurance industry will outpace economic growth and is likely to reach $350-400 billion in terms of premium income by 2020, making it among the top three life insurance markets and among the top 15 non-life insurance markets by 2020, according to an industry study conducted by the Federation of Indian Chambers of Commerce and Industry (FICCI) and the US-based Boston Consulting Group.

### IRDA issues new norms regarding Solvency Ratios

*Source: Bloomberg*

The Insurance Regulatory and Development Authority, India's insurance industry regulator, issued new rules that relaxed solvency ratios for India's general insurance industry. Under the rules, the solvency ratio for general insurers has been reduced for March 2011 to 130 percent from 150 percent, the report said. This change has been brought about due to the low reserves being provided for by the Motor Third Party Pool at 126% for all the years since 2007-08 to 2009-10 as against actual losses varying from 172% to 194%.

### PSU Insurers' PPN cashless norms to cover four more cities

*Source: mydigitalfc*

The preferred provider network (PPN) list of hospitals, which can offer cashless medical treatment, will be extended to four cities including Hyderabad, Kolkata, Ahmedabad and Chandigarh, from April 1, 2011, said Segar Sampath, deputy general manager, New India Assurance Company.

### Agents told to renew 50% of policies or lose licence

*Source: mydigitalfc*

IRDA has proposed that the licences of life insurance agents be cancelled if they fail to annually renew at least 50 per cent of the policies sold by them, a move that would discourage misselling of products. IRDA asks non-life insurers to set a minimum benchmark for the performance of their individual agents and bars them from appointing any blood relatives of employees as agents.

### Cabinet approves PFRDA Bill

# Readers Speak - *Motor Pool - to be done away with?*

**In the last issue of inotes, we had invited our readers opinion on** *"Would disbanding the Motor Third Party Pool be beneficial to the insurance industry?"*

Below are some of the responses we received.

Response from **S Narayanan, MD, Iffco Tokio General Insurance Company**

The answer is categorical "YES". The roots of the rot that have set in motor TP insurance business can be comprehended after pondering over the following:—

- Motor TP pool was outcome of a scenario of avoidance of commercial vehicles' third party insurance due to low premium rates. This business will make sound proposition at good premium rates. Of course claims control/reduction methods, developed over a period of time through experience, will play a big role alongside modern technology in driving the profit margins.
- The pool share of a company is incumbent upon the overall market business share of the company. It does not reckon with the amount of motor insurance premium that the company does. Doing motor insurance may not be part of a company's business plan still thanks to motor pool; its balance sheet is saddled with unwanted motor third party premium and the cascading motor T.P losses. The Claim provisioning has now been jacked up to 153% of the premium received in comparison to earlier range of 125% to 127% of the pool premium received. The loss ratios for all the previous four years is to be provisioned for in the books of account in this year.
- In a de-tariff market scenario, the motor T P premium, determined by IRDA, is said to be "benevolently administered". The premium rating for the motor TP defies all logic. The premiums are not keeping pace with the quantum of TP losses. The lag became so huge (Rs 7000cr deficit) that IRDA had to issue order to the insurance companies to increase the TP claims provisioning in order to bridge the hiatus between TP premium received and TP claims liability. Though the premium has been increased by 68.5% effective from 25/04/2011, still there is no answer for the losses of last four years on motor pool account.
- The efforts for motor TP claims' containment and reduction by few Insurance companies are belied by such other companies who adopt lackadaisical approach towards claims investigation and legal contestation. Since the results of being vigilant while handling motor TP claims by some companies and malicious hobnobbing with the rot in the settlement process fall in the same cauldron called "TP Pool", there is no incentive for the good operators and punishment for the erring ones. There are no efforts to develop a joint claim settlement process, leading to uncoordinated laxity of many insurance companies in claims control.

Now that the premium rates have been revised and the formula for annual review of rates has been cemented (based on cost –inflation index, average claim size and frequency of claim, there is no justification for pool to continue. The reluctance of insurers to do this business will gradually wither away in the face of premium revision initiative and annual review of rates by IRDA. Now it is time to come out with smooth and efficient claim settlement process to reduce losses.

Response from **John Pulinthanam, DGM, National Insurance Company Ltd.**

Where are we in the attainment of the declared objective of making available "third party insurance to all commercial vehicle owners at reasonable rates and terms"? Was anything seriously done by the Industry (meaning the Pool) to attain this objective? Not anything visible.

**Let us look at the following:**

- Everyone speaks of fraud committed in different ways and varying degree in Motor third party claims. One of them is to get an insurance after the accident has occurred (due to break in insurance) or substitution of vehicle (with one which has insurance) in the police records. Fraudulent claims such as these can be prevented if a Data Sharing mechanism among insurers is introduced. One fear may be that of poaching of good clients. But a common data base with bare minimum information of type of vehicle, Registration no, Engine no/Chassis no and year of manufacture (without owner particulars) with insurance and claims history alone would go a long way in preventing fraud. As per powers vested on it under section 14(2) (e) of the IRDA Act, the Regulator also is within its authority to initiate steps in this regard if the Industry does not come forward.
- While I mentioned break in insurance and subsequent attempt of fraud to cover up accident with a policy, it would be unfair if I do not discuss the reasons for timely non-renewal of policy by many motorists. Here we need to see the geographical vastness of our country vis-à-vis the availability of insurance company offices. How can this gap be overcome? In this age of computerization and standardization it is not a difficult proposition to overcome this hurdle.
- Can Motor third party policies be issued through rural kiosks such as the customer service providers under the Banking Correspondent model? It is possible.
- IRDA, in its notification dated 15th April 2011 on increasing the Third Party premium also hints about this: *" Insurers are advised to be mindful of the concerns expressed by vehicle owners about the rates and* ***availability of insurance****. Considering the mandatory nature of Motor Third party Insurance, insurers are advised to ensure that motor Third party insurance is made available at their underwriting offices and that requests for insurance are processed expeditiously and policies issued promptly".*
- A dispute that often comes up in court is on liability for occupants of private car, pillion of two wheeler and occupants in a goods vehicle. The meaning of 'Third party' needs to be widened to include the above category of travelers as well so that by charging some extra premium as for passengers, the liability for this category of 'third party' is also covered; by this step 95% of cases will fall under Act policy covers.
- Along with 1.above, if data sharing on TP cases filed also can be implemented, many other things leading to fraud will fall in line. The GICouncil should empanel Investigating Agencies who can carry out immediate investigation of accidents involving TP injury or death and share information with policy issuing office – their fees being paid by the Company whose vehicle is involved in the accident. Along with implementation of the provisions of sec158(6) of MV Act, this will be very effective in fighting fraudulent claims.
- So far, premium for Third party was being revised only at intervals of 4/5 years. Now as per recent notification of IRDA referred above dated 15.4.2011:*" Long intervals between rate revisions cast an avoidable strain on policy holders as well as on insurance companies. Premium needs to be revised regularly depending upon the average claims which have been awarded by various courts , frequency of claims for each class of vehicle and inflation among other factors"*.

(Contd... 07)

Readers Speak...*Contd.... # 6*

**Do we require a Motor Third Party Insurance Pool of this nature?**

Once the above matters are done, motor third party insurance can be made available at reasonable rates and terms to consumers, thereby fulfilling the objective of Pool formation. In order to attain and sustain this objective, the Pool as such may not be required. It can be attained through collective steps by the insurers themselves through General insurance Council supported by the Regulator. Combined with the points 1 to 5 and the assurance that premium will automatically get revised every year depending on factors outlined in the IRDA notification, the relevance of the Motor Third Party Insurance Pool becomes redundant.

Response from **B.B. Rath, Sr. DM, United India Insurance Co. Ltd**

The pool was intended to provide a mechanism for containing the high claims ratio. Till 2007, the losses from commercial vehicle third party liabilities were entirely borne by the public sector. The high losses, in turn, resulted in the underwriting business being in the red. The pool mechanism had cut the losses to some extent. The pool functions as an exclusive reinsurance agency for third party motor insurance losses.

The downturn in investment earnings and sharp drop in premium income after the deregulation of fire and engineering business in 2007has lead to the insurers to think about dismantling IMTPIP. Investment income in the past had buffered the underwriting losses for the public sector.

Various schools of thoughts have come up for dismantling IMTPIP and procedure to be adopted after that like minimum quotas for the private sector in third party commercial vehicle risks & pool itself, could be restricted to the four public sector general insurers. But in my opinion there should upward revision in TP Premium for commercial vehicles based on the amount of Liability cover they want to opt for i.e. the Unlimited Liability Cover needs to be shelved.

*"Views expressed herein are purely personal and do not reflect the views of the Company"*

**Next Issue – *Portability of Health Insurance?***

With IRDA allowing portability of health insurance policies from July 1st 2011, Policyholders can now switch insurer and carry the benefits of the previous health insurance policy. The main reason for portability is pre-existing diseases (PED) waiting period of four years, not applicable after moving to a new insurer. The insurance regulator has said that insurers must allow policyholders to transfer the credit in terms of waiting period for pre-existing illness and bonus sum insured from one insurer to another.

While customers are undoubtedly thrilled at this prospect, there remains some unanswered questions like what about the conditions (not PED) that were developed before moving to the new insurer? Is it PED for new insurer and waiting period before they are covered? Insurers have waiting periods for specific diseases like kidney stones (may be two years waiting period) after joining the policy. Will portability make the insurer pay for these diseases even if the claim comes within two years? The insurer would not want kidney stone claims on day one and the policyholder leaving on day two.

Another issue is data transfer from the old to new insurer as there is no customer-wise health insurance database readily available. Also portability will favour only the younger age segment where Insurers would be ready to slash rates to attract portability of existing customers. What about the older generation having pre-existing diseases and earlier claims history? Will a new insurer be ready to accept them and expose itself to a higher risk of claim? Will portability be beneficial to elderly policy holders also? Your opinion is solicited!

Please send your responses in 200-300 words to knowledge@indiainsure.com

Interview – *Life Insurer... Contd.... # 4*

**How has your company fared on the group life products front? Have Indian corporates bought the idea that outsourcing the management of mandatory benefits like gratuity and leave encashment to Insurers is more beneficial in the long run?**

Aviva is in the process of building a strong group business. We have a strong client base of close to 300 corporates.

The group gratuity business has picked up in the recent past with many corporate opting to outsource their gratuity portfolio. For a corporate, managing funds is typically a non-core business, which is also governed by stringent income tax laws. By outsourcing it to the insurance firms, the corporates can avail of the expertise of external fund managers and have a more flexible investment portfolio. The corporates can also avail of tax benefits under the Income Tax laws. Leave encashment is yet to pick up as it does not come under the tax exemption bracket as yet.

**How have the IRDA norms on ULIPs impacted your business? Has the focus now shifted to traditional plans?**

The IRDA norms on ULIPs have reinforced the long-term nature of ULIPs and will protect the long-term interest of the customer as well as the industry. They are aimed at enhancing the transparency of ULIPs and will boost their attractiveness as a long-term savings product as they fulfil the dual benefits of providing prosperity and peace of mind to the policyholders and their families. We believe that the September guidelines of the IRDA will increase transparency in terms of charges, lower commissions, replacement of surrender charge with a small product discontinuance charge (Nil from fifth year), and will help customers make informed choices. Though these changes have fundamentally redefined the industry, they have not made a major impact on our business as we had pre-anticipated the changes, and were prepared for the same.

As far as the focus on traditional plans is concerned, in the last one year, we have made a conscious effort to enhance the traditional mix in our portfolio. This number has been steadily increasing every quarter. Our endeavour is to have a balanced portfolio with ULIPs and traditional products to meet all customer lifecycle needs of savings, protection, investment and retirement

**Your comments on the reforms brought about by the Insurance Regulatory and Development Authority in insurance in the past one year? What are the other changes you look forward to on the regulatory front?**

The IRDA regulation on public disclosures has given media and analysts the access to much more nuanced data rather than just first-year premium. This and the build-up to the IPOs will see companies focus more on other parameters than just new business premium.

The insurance regulator issued many regulations for the products as well, which as mentioned above, have reinforced the long-term nature of ULIPs and will protect the long-term interest of the customer as well as the industry.

There has also been a plethora of regulations around distribution which necessitate a re-engineering of distribution models and will eventually lead to a sharper and smaller but much more productive distribution sales force.

Our wish list includes the enhancement in the FDI limit to 49%, rationalization of DTC provisions that impact the customers buying Life Insurance for their long term savings and introduction of multiple bancassurance partnerships (open architecture).

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## View Point

**THE MOTOR THIRD PARTY POOL CLAIMS PROVISIONING – *a cause for concern***

Much to the chagrin of the general insurers, the IRDA directive issued to all the general insurers in the first fortnight of March could not have been better timed! The findings of the investigation carried out by IRDA to assess the adequacy of reserves declared by the Indian Motor Third Party Insurance Pool has left all the general insurers in a tizzy. Just when the insurers were making estimates of the year ending numbers, having their fingers crossed for having yet another catastrophe loss free year, and employees looking forward to the bonuses and incentives, this came in as a bolt from the blue.

The reserves having being maintained at 126% for the past 3years as against the finding of 172.3%, 181.81% and 194.15% for the years 2007-08, 2008-09 and 2009-10 respectively, insurers have been advised to take remedial measures to correct the deficiency maintained in the reserves for the next 3 years upto the period ending March 2014, and revising the provision made in the past 4 years including 2010-11 to 153%. Besides, IRDA has asked the companies to maintain the solvency ratio for all lines of business for the year ending March 2011 at 130% and increase it gradually before achieving 150% by March 2014. The actual gap between the incurred claims and provisions made by insurers is expected to go up by a whopping Rs 3750 to 4000 crores. While the profits made by the entire general insurance industry in the last fiscal was a little over Rs. 1200 crores, a loss of about Rs. 3000 to 3500 crores would be incurred by the general insurance industry this year on account of the motor insurance business.

Has the directive been fair to the insurers? Is this the best way to rectify an error of this magnitude? To increase the provision for Motor TP claims at this juncture and maintain the solvency ratio at 130%, would require a large number of insurers infusing more capital into their books. And all this just a fortnight before the financial year end , at such short notice?

While insurers have been approaching IRDA to consider the calculation of Solvency ratio at the fair value of assets rather than book value, this would only result in the figure appearing over 130% on paper, but in reality would not serve the purpose intended ie to have adequate reserves to meet any claim obligations at all times, expeditiously. Had the claims figure looked more promising, it would not have been a matter of such grave concern, but with the PSUs steadily maintaining their underwriting losses, the matter seems rather grim. Further these are the figures as on date and we observe that the claims ratio has only been rising, so would this be adequate? With IRDA in talks with the various associations we can only hope that the motor third party premium revision in rates becomes a reality soon as that could partly minimize the crisis in the industry presently.

This apart, a lot more questions arise. Was the job made simple for IRDA since they had all the claims data consolidated with the Pool? Would it have been possible had the Pool not taken birth? Have the provisioning in the past years before the Pool was formed being done appropriately by each insurer? Well, only time would tell the answers to these questions!

**P Srinivas Rao,** *SBU Head, North*

## News TitBits

- **Magma HDI Gen Insurance receives R1 licence from Irda**
- **Somali pirates closer to India; premiums up**
- **Health insurance premiums set to register 25% rise: Towers Watson Survey**
- **Buyers credit launched to boost project exports from India**

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