

Liberalization... really?

The Insurance Laws (Amendment) Bill, 2008

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The eagerly awaited second generation economic reforms that the Indian government intended to unleash with insurance sector reforms remain a nonstarter. The government had been hoping to inject fresh enthusiasm into foreign investors by pushing the long-overdue Insurance Laws (Amendment) Bill, 2008, in the recently concluded budget session of parliament. However, Indian lawmakers failed to deliver on their promise and action on the bill remains in abeyance. Insurance reforms have been stuck in a legislative quagmire for around nine years. It took roughly four years for the proposals to be adapted into the bill, and five years after that, the bill has yet to become law. The key proposals contained in the bill are as follows:

Increased foreign investment cap

An increase in the foreign investment ceiling in Indian insurance companies to 49%, from the existing 26%, is one of the most important proposals in the bill. Supporters of the proposal argue that the increase will provide much-needed succour to capital-starved insurance companies, but detractors are not convinced of the case for enhanced foreign capital participation. There remains a lack of political consensus on the issue and this is widely regarded as a stumbling block to the passage of the bill. Furthermore the standing committee of parliament has already rejected the plans to increase the foreign investment ceiling, arguing instead that insurance companies should be allowed to seek capital from sources other than foreign investment.

Many legal practitioners are of the view that the increased foreign investment limit may only provide partial relief to insurance companies, many of which require more capital than the higher foreign investment ceiling would allow.

More flexible capital structures

The Insurance Act, 1938, is the key statute governing the insurance sector and lays down rigid requirements with respect to the capital structure of insurance companies. The act mandates that the paid-up capital of insurance companies must consist of only ordinary shares, each of which has a single face value. In view of this stipulation, the Insurance Regulatory and Development Authority (IRDA), which regulates the sector, had prohibited insurance companies from issuing preference shares or other forms of hybrid instruments used for the augmentation of capital. However, the Insurance Laws (Amendment) Bill contains proposals to soften this stance by recognizing forms of capital other than equity shares of single face value and by expressly delegating the authority to the IRDA to form regulations with respect to hybrid capital.

SEZ relaxations

One of the more radical proposals in the bill is to allow non-admitted insurers to operate in special economic zones (SEZs) in India. This would enable non-admitted insurers to insure risks situated in SEZs and to operate

outside the regulatory oversight of the IRDA. Industry players have long been seeking exemptions from some domestic regulations (exchange controls, insurance, banking, etc.) for businesses situated in SEZs. However, the operationalization of such exemptions will be a challenge for policymakers.

Other noteworthy proposals

Another key development that is being watched with interest by global insurance players is the inclusion of Lloyd's of London within the bill's definition of a "foreign company". This has been done to enable Lloyd's of London to establish joint ventures with Indian companies in the insurance sector. The bill also proposes to allow foreign reinsurers to open branch offices in India with some capital controls. The Securities Appellate Tribunal, established under the Securities and Exchange Board of India Act, 1992, is proposed to be the appellate authority for decisions made by the IRDA. Currently there is no provision for appeals to a quasi-judicial forum against the decisions or orders of the IRDA.

The Insurance Act, 1938, requires Indian promoters to reduce their stake to 26% within ten years. However, the bill proposes to dispense with this stipulation.

Wait and watch

While many industry players admit that their patience is running out, they also concede that the results will be worth the wait if and when the Insurance Laws (Amendment) Bill takes the shape of law.

Action now shifts to the monsoon session of parliament. In the interim, stakeholders are busy telling themselves to "wait and watch".

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