Exposure Draft

Guidelines on Remuneration of Non-Executive Directors and Managing Director/Chief Executive Officer/Whole-time Directors of Insurance companies

In order to ensure sound remuneration or compensation practices and avoid situations resulting from excessive risk taking behavior due to inappropriate compensation structures or incentive plans and also taking into account the experience of past 5 years, it is proposed to replace the extant guidelines on remuneration of non-executive directors and managing director /chief executive officer/ whole-time director of insurers, issued vide circular ref IRDA/F&A/GDL/LSTD/155/08/2016 dated 05.08.2016.

The salient features of the proposed Guidelines are as under:

1. The Guidelines cover the remuneration of Non-Executive Directors, CEOs /WTDs /MDs of private sector insurers including the format in which remuneration details are required to be submitted to the Authority.

2. <u>For Non-Executive Directors (NEDs):</u>
   i. Apart from sitting fee and other expenses, it provides for payment of remuneration commensurate with an individual director's responsibilities and demands on time, which are considered sufficient to attract qualified competent individuals, in the form of fixed remuneration. Such remuneration, however, shall not exceed Rs. Twenty lakh per annum for each such director excluding Chairman. For the Chairman of the Board, the remuneration may be decided by the Board of Directors of the respective company.

   ii. NEDs shall not be eligible for ESOPs. Prior approval of the Authority shall be required for any allotment of sweat equity to the NEDs.

   iii. The maximum age and numbers of years which a person can serve as NED, including as Chairman has been aligned with the guidelines issued by RBI.

3. <u>For Whole Time Directors / Chief Executive / Managing Directors</u>
   i. The remuneration structure shall be divided between fixed pay, perquisites and variable pay.
   ii. Fixed Pay should be reasonable and all the fixed items, including perquisites, shall be treated as part of fixed pay.
   iii. Variable Pay
      a) Limit on variable pay: at least 50% of the remuneration subject to maximum 300% of the fixed pay. Where variable pay is up to 200% of the fixed pay, a minimum of 50% of the variable pay should be via non-cash instruments. The same limit would be 70%, in case the variable pay is above 200% of the fixed pay.
      b) Deferment – Minimum of 50% of the variable pay must be deferred on 'no faster than pro-rata' basis over a period of three years. No deferment required if the variable pay does not exceed Rs. 15 lakh.
      c) Variable Pay Formula – a variable pay formula with identified weightage has been prescribed with 70% attributing to quantitative parameters and 30% to qualitative parameters. The insurer is required to specify the performance parameters on the basis of which the variable pay will be evaluated.

   iv. Malus and Clawback – the deferred remuneration should be subject to malus/clawback arrangement in case of any negative trend in the performance of the insurer.

4. Tenure of MD&CEO and WTDs has been aligned with the RBI's stipulation in this regard.

5. Further, the remuneration guidelines also provide the broad principles for remuneration of risk control and compliance staff which are broadly in lines with RBI stipulations.

A copy of the Guidelines is placed as annexure-1. All are requested to offer their comments / suggestions on the proposed guidelines. The comments / suggestions should reach in the format attached as annexure-2 by 19th January, 2022 to Ms. Shruti Srivastava by e-mail at shruti.srivastava@irdai.gov.in with a copy to the undersigned at rksharma@irdai.gov.in .

R K Sharma
General Manager

Annexure-1

IRDAI/NL/GDL/____ /2020-21

XX/XX/XX

All Private Sector Insurance companies

Dear Sir/Madam,

Sub: Guidelines on Remuneration of Non-Executive Directors and Managing Director/Chief Executive Officer/Whole-time Directors of Insurance companies

1. Insurance companies are an important part of the financial system. Any risk that adversely effects the Insurance companies also gets transmitted to the other constituents, and through them, to the financial system. The compensation or remuneration practices are acknowledged as an important factor driving market conduct of Insurance companies which, if distorted, could result in poor customer outcomes and financial harm to the companies.

2. The distorted remuneration packages with focus on short term results without adequate regard to the long-term risks emanating from the decisions/actions of the senior employees will encourage excessive risk taking behaviour by employees and may threaten the stability of financial system and leave the firms with fewer financial resources to absorb losses in cases where the risks actually materialize. This could shake the faith of Insurance customers in the system. On the other hand, Remuneration structure well aligned with the long term growth, health and objectives of the company promote sustained development of the sector. It also plays a critical role against attritions.

3. (i) The Principles and Implementation Standards on sound compensation practices by the Financial Stability Board (FSB) lay emphasis on the following:
   a. Effective governance of compensation – active Board oversight
   b. Effective alignment of compensation to prudent risk-taking
   c. Effective supervisory oversight and engagement by stakeholders

   (ii) The Insurance Core Principle (ICP) – 7 of the International Association of Insurance Supervisors (IAIS) also requires the implementation of a remuneration policy covering the members of the Board of Insurance companies, senior management and Key management persons in control functions and other employees whose actions may have material impact on the risk, and supervisory oversight over the same.

4. Reference is also invited to the provisions of Section 34A of Insurance Act, 1938 which deals with appointment, remuneration of Managing Director/Chief Executive Officer and Whole-time Directors and the prior approval of the Authority on the matters thereof.

5. In this background, the Authority, in exercise of its powers under Section 14 of the IRDA Act, 1999 has issued Guidelines on remuneration vide circular IRDA/F&A/GDL/LSTD/154/08/2016 applicable to Non-Executive Directors and Managing Director / Chief Executive Officer / Whole-time Directors of Private Insurance Companies.

6. These Guidelines have since been reviewed based on experience gained. The objective has also been to bring in more precision and uniformity in the submissions of the insurance companies.

7. These guidelines have been divided into the following three parts:
   a. Annexure A – deals with the remuneration of Non-Executive Directors;
   b. Annexure B – deals with the remuneration of CEOs/WTDs/MDs;
   c. Annexure C – deals with the format in which proposed remuneration details of CEOs/WTDs/MDs are to be submitted to IRDAI;

8. The guidelines shall apply to all the applications received by the Authority, on or after the revised guidelines come into force, for approval of the remuneration part of the appointment/re-appointment applications or approval of the revision in remuneration of Whole Time Directors (WTDs)/ Chief Executive Officers (CEOs)/Managing Directors(MDs). In view of the above, the new Guidelines supersede all earlier instructions.

Yours faithfully,

(..........................)

Annexure-A

Insurance Regulatory and Development Authority of India (Remuneration of Non-Executive Directors of Private Sector Insurance companies) Guidelines, 2022

Non-executive directors of the company play a crucial role to the independent functioning of the board. They bring in external and wider perspective to the decision-making by the board. They provide leadership and strategic guidance, while maintaining objective judgment. They provide an independent view on the running of the business, governance and boardroom best practices. They oversee and constructively challenge management in its implementation of strategy within the Group's system of governance and the risk appetite set by the Board.

In view of the increased demands on non-executive directors' participation in board and committee meetings and the higher responsibilities they are expected to bear in the interest of higher level of excellence in corporate governance and in order to enable Insurance companies to attract and retain professional non-executive directors, it is essential that such directors are appropriately compensated.

1. The remuneration of non-executive directors shall be subject to the following stipulations:

1.1. **Remuneration Policy**

a) The Board of Directors, shall formulate and adopt a comprehensive remuneration policy for the non-executive directors. While formulating the Policy, the Board shall ensure compliance with the provisions of the Companies Act, 2013.

b) The Board may, at its discretion, provide for, in the Policy, payment of remuneration commensurate with an individual director's responsibilities and demands on time and which are considered sufficient to attract qualified competent individuals in the form of fixed remuneration. Such remuneration, however, shall not exceed Rs. twenty lakh per annum for each such director excluding Chairman. For the Chairman of the Board, the remuneration may be decided by the Board of Directors of the respective company.

1.2. Sitting fees and reimbursement of expenses

In addition to the directors' remuneration mentioned in para 1.b above, the Insurance companies may pay sitting fees to the non-executive directors and reimburse their expenses for participation in the Board and other meetings, subject to compliance with the provisions of the Companies Act, 2013.

Further, non-executive directors shall not be eligible for ESOPs. Any allotment of sweat equity to non-executive directors shall only with the prior approval of the Authority.

2. Age and tenure of NEDs

2.1. The upper age limit for NEDs, including the Chair of the board, shall be 75 years and after attaining the age of 75 years no person can continue in the said position.

2.2. The total tenure of an NED, continuously or otherwise, on the board of an insurer, shall not exceed eight years. After completion of eight years on the board of an insurer, the person may be considered for re-appointment only after a minimum gap of three years. This shall, however, not preclude him / her from being appointed as a director in another insurer subject to meeting the requirements.

3. Disclosure

Insurance Companies shall make disclosures on remuneration to such directors in accordance with the norms provided in Corporate Governance Guidelines, issued by IRDAI.

Annexure-B

Insurance Regulatory and Development Authority of India (Remuneration of Chief Executive Officer(CEO) / Whole-time Director/(WTD) / Managing Director(MD) of Insurance companies) Guidelines, 2022

1. The Board of Directors of the Insurance company shall formulate and adopt a comprehensive remuneration policy for MD/CEO/ WTDs. The said policy shall be reviewed at periodic intervals as specified by the respective Board. The policy should cover all aspects of the remuneration structure such as fixed pay, perquisites, bonus, guaranteed pay, severance package, stock options, pension plan, gratuity, etc. taking into account these guidelines.

2. The variable pay formula as per section 6.6 of the Guidelines and the details submitted in Annexure C of these guidelines shall be submitted to the Authority along with the recommendations of Nomination and Remuneration Committee (NRC) and the extract of the minutes of the Board meeting approving the same.

3. Insurance companies should ensure that for the MD/ CEO/WTDs:
    a) Remuneration is adjusted for all types of risk,
    b) Remuneration outcomes are symmetric with risk outcomes, and
    c) Remuneration pay-outs are sensitive to the time horizon of the risk.
    d) The mix of cash, equity and other forms of remuneration must be consistent with risk alignment.

4. A wide variety of measures of credit, market, liquidity risks and various other risks may be used by the Insurance companies in implementation of risk adjustment. The risk adjusted methods should preferably have both quantitative and judgmental elements.

5. Tenure **of MD & CEO and WTDs:**
    5.1. Subject to the statutory approvals required from time to time, the post of the MD & CEO or WTD shall not be held by the same incumbent for more than 15 years. Thereafter, the individual will be eligible for re-appointment as MD&CEO or WTD in the same insurer, if considered necessary and desirable by the board, after a minimum gap of three years, subject to meeting other applicable conditions.

5.2. During this three-year cooling period, the individual shall not be appointed or associated with the insurer or its group entities in any capacity[1], either directly or indirectly.

5.3. No person shall continue as MD & CEO or WTD beyond the age of 70 years. Within the overall limit of 70 years, as part of their internal policy, individual insurer's Boards are free to prescribe a lower retirement age for the WTDs, including the MD & CEO.

5.4. The MD & CEO or WTD who is also a promoter/ major[2] shareholder, shall not hold the said posts for more than 12 years. However, in extraordinary circumstances, at the sole discretion of the Authority, such MD & CEO or WTDs may be allowed to continue up to 15 years.

6. The remuneration structure for MD/CEOs/WTDs shall be as mentioned below:

6.1. Fixed pay and perquisites

Insurance companies are required to ensure that the fixed portion of remuneration, as defined in the Income Tax Act, is reasonable taking into account all relevant factors. All the fixed items of remuneration, including perquisites, shall be treated as part of fixed pay. Perquisites that are reimbursable shall also be included in the fixed pay as long as there are monetary ceilings. Contributions towards superannuation/retirement benefits shall also be treated as a part of the fixed pay.

6.2. Variable pay

(a) **Composition**

[1] Except in the capacity of the shareholder
[2] holding more than 5 percent.

(i) The variable pay can be in the form of share-linked [3]instruments, or a mix of cash and share-linked instruments. While designing the remuneration arrangements it should be ensured that there is a proper balance between the fixed pay and variable pay.

(ii) In case of listed insurers, share based employee benefits should comply with SEBI (Share Based Employee Benefits) Regulations. In case of unlisted insurers, valuation of share price for the purpose of variable pay, should be as per section 11UA of the Income-tax Act and the valuation should be certified by a Chartered Accountant / Statutory Auditors/merchant bankers.

(b) Limit on Variable Pay

(i) A substantial portion of remuneration i.e., at least 50% should be variable pay. The total variable pay shall be limited to a maximum of 300% of the fixed pay (for the relative performance period).

(ii) In case the variable pay is up to 200% of the fixed pay, a minimum of 50% of the variable pay should be via non-cash instruments; and in case the variable pay is above 200% of fixed pay, a minimum of 70% of the variable pay should be via non-cash instruments.

(iii) The variable remuneration should be reduced where:

a. There is deterioration in the financial performance of the insurer. The deterioration in the financial performance should generally lead to a contraction in the total amount of variable remuneration, which can even be reduced to zero; or

b. The misconduct of the CEO/WTD/MD led to significant losses for the insurer or significant adverse outcomes for its customers or other stakeholders; or

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3 "Share-linked instruments" include ESOP and cash-linked Stock Appreciation Rights (also called as Phantom Stock options).

c. fraud, gross negligence or material failure of risk management controls, including serious breach of internal rules or regulations have been observed, regardless of the scale of the damage.

(c) **Deferment of variable Pay**

a. For senior executives, including MD/CEO/WTDs, in adherence to Financial Stability Board (FSB) Implementation Standards, deferred[4] arrangements must invariably exist for the variable pay, regardless of the quantum of pay. A minimum of 50% of the variable pay must invariably be deferred over a period of at least 3 years. However, in cases where the cash component is under Rs. 15 lakh, deferral of such cash may not be required.

b. Further, the following may be noted:

(i) Deferred remuneration should either vest fully at the end of the deferral period or be spread out over the course of the deferral period. The vesting of deferral shall not be before one year from the commencement of the deferral period.

(ii) The deferral period shall be applicable even if the residual service of CEO/ WTD/ MD is less than deferral period.

(iii) No requests for waiver shall be entertained by IRDAI.

6.3. Share-linked instruments

The details of share-linked instruments granted shall also be disclosed in terms of the disclosure requirements stipulated for the financial statements of the insurance companies. Such instruments should be fair valued on the date of grant by the insurer using appropriate method. In case the shares of the insurance company are offered

[4] No faster than pro rata basis means – vesting should not be frontloaded. In other words, if the deferral arrangement is three years, not more than 33.33 % of the total granted ESOPs should vest at the end of first year. Further, not more than 33.33 % of total granted ESOPs should vest at the end of second year. Similarly, in case deferral arrangement is four years, not more than 25% of total granted ESOPs should vest in each of the first three years. Also, it is recommended to have higher portions getting vested in later parts of the vesting period.

as ESOPs to Managing Director / Chief Executive Officer / Whole Time Directors, then the same shall be governed by the SEBI's ESOP guidelines.

6.4. Malus and Clawback

(i) A malus arrangement permits the Insurer to prevent vesting of all or part of the amount of a deferred remuneration. Malus arrangement does not reverse vesting after it has already occurred.

(ii) A clawback, on the other hand, is a contractual agreement between the employee and the Insurer in which the employee agrees to return previously paid or vested remuneration to the Insurer under certain conditions.

(iii) The deferred remuneration should be subject to malus/clawback arrangements in the event of any negative trend in the performance of the Insurer in any year during the vesting period. However, while exercising such provisions due consideration may be given to the actual / realized performance of the insurer.

(iv) For legal enforceability, the claw back system shall be driven by observable and verifiable measures of risk outcomes. Insurers shall put in place appropriate mechanism to incorporate claw back mechanism in respect of variable pay.

6.5. Guaranteed bonus

(i) Guaranteed bonus is not consistent with sound risk management or the 'pay for performance' principles and should not be part of the compensation plan.

(ii) Guaranteed bonus should only occur in the context of

a. **Sign-on bonus**

i. Sign-on bonus may be paid while hiring new staff;

ii. Should be limited to the first year;

iii. Sign-on bonus should be in the form of share-linked instruments only, since upfront payments in cash would create perverse incentives.

b. **Retention bonus**:

i. Retention bonus is to be paid as per the board approved remuneration policy under **exceptional situations;**

ii. Such retention bonus may be paid only once during the entire tenure of CEO/MD/WTD;

iii. The retention bonus shall be paid over a period of at least two years and not more than 50% of retention bonus shall be paid in the first year;

(iii) Guaranteed bonus will neither be considered as part of fixed pay nor part of variable pay.

(iv) Further, insurance companies should not grant **severance pay** other than accrued benefits (gratuity, pension, etc.) except in cases where it is mandatory under any statute.

6.6. Variable pay formula

The following variable pay formula template should be used for arriving at the quantum of variable pay:

Part A

Sr. No	Parameters	Weightage	Target	Achievement
I	**Quantitative parameters**	**Minimum 70%**		
1	Premium Growth rate (%)			
2	% increase in Market share			
3	% increase in profitability			
	% increase in persistency/renewal ratio			

Sr. No	Parameters	Weightage	Target	Achievement
4	Expenses of Management (EoM) as a % of Regulatory limit			
5	% increase in Claim settlement*			
6	% decrease in policyholder grievances			
7				
8				
.				
.				
II	**Other Qualitative (Subjective) parameters**	**30%**		
1	Regulatory compliances			
2				
.				
.				
	Total	**100%**		**(may be more than 100%)**

* the claims closed without payment and claims repudiated should not be part of this calculation

(i) The Insurers may add other parameters in addition to the above mentioned mandatory parameters.

(ii) The weightage for each parameter may be given by the insurers based on their remuneration policy

Based on the above achievement, the payment for variable pay may be determined according to the below mentioned payment grid:

Part B

Sr. No	Achievement*	Variable pay as a percentage of fixed pay
1		
2		
3		
.		
.		

*Each cell in the Achievement column should be a range.

6.7. The applications for approval of remunerations should be submitted to the Authority within first three months of the performance period. The Proposals should be submitted as per the Form 'C' (Annexure C)

6.8. All the remuneration related details to be disclosed in the Annual Report of the insurersas per the IRDAI Corporate Governance Guidelines

6.9. **Accounting and renewal of remuneration:**

a) No revision in remuneration shall be permitted till the expiry of one year from the date of earlier approval.

b) In case the annual remuneration of the MD/ CEO/ WTDs individually exceeds Rs.1.50 crore (including all perquisites plus bonuses etc., by whatsoever name called), such excess shall be borne by the Shareholders' account.

c) No remuneration shall be paid to MD/CEO/WTDs by any of the promoter / investor or by the group companies of the promoters'/ investors' companies.

d) Insurance companies shall not permit MD/CEO/WTDs to insure or hedge their remuneration structure to offset the risk alignment effects embedded in their remuneration arrangement. To enforce the same, Insurance companies should establish appropriate compliance arrangements.

7. **Guidelines for risk control and compliance staff**

Members of staff engaged in financial and risk control, including internal audit, should be compensated in a manner that is independent of the business areas they oversee and commensurate with their key role in the insurance company. Effective independence and appropriate authority of such staff are necessary to preserve the integrity of financial and risk management's influence on incentive compensation. Back office and risk control employees play a key role in ensuring the integrity of risk measures. If their own compensation is significantly affected by short-term measures, their independence may be compromised. If their compensation is too low, the quality of such employees may be insufficient for their tasks and their authority may be undermined. The mix of fixed and variable compensation for control function personnel should be weighted in favour of fixed compensation. Therefore, the requirement of minimum 50% of total compensation to be paid in the form of variable pay will not be applicable for this category of staff. However, a reasonable proportion of compensation has to be in the form of variable pay, so that exercising the options of malus and/or clawback, when warranted, is not rendered infructuous. Subject to the above, while devising compensation structure for such staff, insurers should adopt principles similar to principles enunciated for WTDs/CEOs, as appropriate.

4. The interpretation of any provision of these guidelines by the Authority shall be final and binding on the parties concerned

Annexure-C

Form C

Details of Remuneration of the Whole Time Director/ Chief Executive officer/ Managing Director

(Rs.)

Particulars (1)	Existing (2)	Proposed (3)	Reasons for change (4)
PART –A: Fixed Pay (including perquisites) w.e.f.................. up to .... 1. Salary 2. Dearness allowance 3. Retiral / Superannuation benefits: (a) Provident Fund (b) Gratuity (c) Pension (d) .... 4. Leave Fare Concession/Allowance 5. Other Fixed Allowances, if any (please specify) [5] 6. Perquisites:			

[5] Consolidated allowance, if any, to be given with details of heads it subsumes.

Particulars (1)	Existing (2)	Proposed (3)	Reasons for change (4)
(i) Free Furnished House and its maintenance/ House Rent Allowance (ii) Conveyance Allowance/Free use of Insurer's car for (a) Official Purposes (b) Private Purposes (iii) Driver's Salary (iv) Club Membership(s) (v) Reimbursement of medical expenses (vi) Any other perquisites (please specify)			
Total Fixed Pay (including perquisites)			

Note:

(a) If any of the benefits is non-monetary in nature, e.g. free furnished house, its monetary equivalent as best as it is possible to determine, should invariably be given. In case the person to be appointed is already associated with the insurer, particulars of his existing compensation, etc. should be furnished.

(b) The reasons for any proposed changes in the remuneration should be suitably indicated under column (4).

(c) In case the Insurer proposes to give any sign-on/joining bonus (limited to the First Year), which should be in the form of share-linked instruments, its details (such as number of shares, grant date and price, monetary value, vesting schedule) should be furnished separately.

(d) Insurers should exclude only such perquisites from fixed pay, which are reimbursables without any monetary ceilings, e.g. hospitalization expenses, etc. Details of such perquisites should be annexed separately and need not be added while computing total fixed pay. Such exclusions are provided

Particulars (1)	Existing (2)	Proposed (3)	Reasons for change (4)
solely for such benefits/perquisites which are not quantifiable in advance. These exclusions would be subject to supervisory review.			
PART – B: **Max. Variable Pay** **For Financial Year/Performance Period …………………**			
1. Cash component • Upfront payment (with%) • Deferred Payment(with%)			
Total Cash component (A)			
Vesting Period (in years)			
Deferral arrangement (i) First Year (ii) Second Year (iii) Third Year (iv) ……………….			
2. Non –cash Components (Share – linked instruments):			

Particulars (1)	Existing (2)	Proposed (3)	Reasons for change (4)
(i) ESOP / ESOS a) Number of shares / share-linked Instruments b) Monetary Value c) Deferral (with %) d) Vesting schedule details			
(ii) **..........(Any other share linked instruments)** (a) Number of shares/share-linked instruments. (b) Monetary Value (c) Deferral (with%) (d) Vesting schedule details			
(iii) **Any other non-cash component** (please specify) and mention its monetary value, deferral, vesting schedule, etc.			
Total monetary value of non-cash component(s) (B)			
Total monetary value of Variable Pay (cash and non-cash components) (A+B) = C			
% of Cash Component in Total Variable Pay A/C			

Particulars (1)	Existing (2)	Proposed (3)	Reasons for change (4)
% of Non-Cash Component in Total Variable Pay B/C			
% of Variable Pay to Fixed Pay **% of Variable Pay in Total Compensation** (for the same FY/Performance Period)			
Total Compensation(Fixed Pay + Variable Pay)			

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