DRAFT GUIDELINES ON "TRADE CREDIT INSURANCE"

1. Introduction

1.1 Trade credit insurance protects businesses against the risk of non-payment for goods and services by buyers. It usually covers a portfolio of buyers and indemnifies an agreed percentage of an invoice or invoices that remain unpaid as a result of protracted default, insolvency / bankruptcy. It contributes to the economic growth of a country by facilitating trade and helps in improving economic stability by addressing the trade losses due to payment risks.

1.2 These guidelines set out the regulatory framework;

(a) to promote sustainable and healthy development of trade credit insurance business.

(b) to facilitate general insurance companies to offer trade credit insurance covers to suppliers as well as licensed banks and other financial institutions to help businesses manage country risk, open up access to new markets and to manage non-payment risk associated with trade financing portfolio.

(c) to enable general insurance companies to offer trade credit insurance with customised covers to improve businesses for the SMEs and MSMEs, considering the evolving insurance risk needs of these sectors.

2. Short title, commencement

2.1 These guidelines shall be known as the "Trade Credit Insurance Guidelines 2021".

2.2 The Insurance Regulatory and Development Authority of India (hereinafter referred as Authority) issues these guidelines under section 14 of the IRDA Act, 1999. These guidelines shall come into force with effect from ------ 2021.

2.3 These guidelines shall supersede the guidelines on trade credit insurance issued by the Authority vide ref: IRDAI/NL/CIR/CRE/044/03/2016 dated 10th March, 2016.

3. Scope and Applicability

3.1 The scope of cover under trade credit insurance policy shall be the credit risk that has a direct link with an underlying trade transaction, i.e. the delivery of goods or services. If no such direct link exists, the outstanding amount is not insurable under a trade credit insurance policy. The cover may include but not be limited to the following risks.

i. **Commercial Risks:**

a. Insolvency or Protracted Default of

(i) the buyer;
(ii) bank/`s responsible for payment in case of Letter of Credit transactions;
(iii) stock holding agent in case of consignment transactions;

b. Rejection by

(i) the buyer after delivery subject to conditions of contract;
(ii) the buyer before shipment, where the goods are manufactured or being manufactured exclusively as per the requirements of the buyer and cannot be sold elsewhere;

c. Non-receipt of payment on account of collecting Bank`s failure;

ii. **Political Risks:** Political risk cover is available only in case of buyers outside India and in respect of those countries agreed upon at the proposal stage. Political risks include the following.

a. Operation of a law or of an order, decree or regulation having the force of law which, in circumstances outside the control of the insured and/or the buyer, prevents, restricts or controls the transfer of payment from the buyer's country to India;

b. Occurrence of war between the buyer's country and India;

c. Occurrence of war, hostilities, civil war, rebellion, revolution, insurrection or other disturbances in the buyer's country;

d. Imposition of any law or order, decree or regulation having the force of law which, in circumstances outside the control of the insured and/or of the buyer, prevents the import of the goods into the buyer's country;

e. Cancellation, in circumstances outside the control of the insured and/or of the buyer, of a previously issued and currently valid authority to import the goods;

f. Incurring, in respect of goods shipped from India, of any additional handling, transport or insurance charges which are occasioned by interruption or diversion of voyage outside India and which is impracticable to be recovered from the buyer;

g. Any other cause, save and except in the case of merchanting exports in which case this risk will stand excluded, which arises from an event occurring outside India but not being a cause inherent in the nature of the goods or that is within the control of the insured and/or the buyer or that is specifically excluded from the purview of cover under the policy.

3.2 These guidelines shall apply to all insurers transacting general insurance business, registered under the Insurance Act, 1938. However, ECGC Ltd (formerly Export Credit Guarantee Corporation of India Ltd) is exempted from the application of these guidelines.

3.3 These Guidelines shall be in addition to and not in derogation of the provisions of any other laws, rules, regulations or guidelines, for the time being in force.

4. Definitions

(a) In these Guidelines, unless the context otherwise requires, the terms herein shall bear the meanings assigned to them below.

(i) **"Buyer"** means any legal entity, including a natural person, that is liable to the insured for payment of the gross invoice value of the shipments made or services rendered by the insured.

(ii) **"Credit Limit"** is the limit set by the insurer under the policy against a buyer for losses, occasioned owing to commercial risks. The liability of the insurer, against a buyer, is limited to the credit limit set on the buyer.

(iii) **"Factoring"** means the business of financing or acquisition of trade receivables of assignor by accepting assignment of such receivables.

(iv) **"Financial Guarantee"** comprises of any bond, guarantee, indemnity or insurance, covering financial obligations in respect of any type of loan, personal loan and leasing facility, granted by a bank/credit institution, financial institution or financier, or issued or executed in favour of any person or legal entity in respect of the payment or repayment of borrowed money or any contract, transaction or arrangement, the primary purpose of which is to raise finance or secure sums due in respect of borrowed money.

(v) **"Government Buyer"** means any entity that is authorized to enter into commitments in the name or on behalf of the government of its country, including the government itself or government agencies whose commitments are guaranteed by the government.

(vi) **"Insolvency (Bankruptcy)"** A judicial or administrative procedure whereby the assets and affairs of the buyer are made subject to control or supervision in the jurisdiction defined under the policy by the court or a person or body appointed by the court or by law, for the purpose of reorganization or liquidation of the buyer or of the rescheduling, settlement or suspension of payment of its debts.

(vii) **"Invoice Discounting e-Platforms"** means any authorized institutional platform facilitating the financing or discounting of trade receivables through sole or multiple financiers through electronic platform.

(viii) **Micro & Small Enterprises** shall be as defined by the MSMED Act, 2006 and amendments thereof.

(ix) **“Project Cover”** means insurance of receivables, against non-payment by the principal or buyer, provided to a contractor engaged in but not limited to long term infrastructure, civil and industrial projects and services. The project period should be more than six months.

(x) **“Protracted Default”** means failure by a buyer to pay the contractual debt within a predefined period calculated from the due date of the debt.

(xi) **"Retention”** means the portion of the risk which an insurer/reinsurer assumes for his own account.

(xii) **"Reverse Factoring arrangement"** means any arrangement in whatever name or form, between a borrower and a financer, wherein a borrower receives or is supposed to receive finance, either directly or indirectly, for borrower's purchase of trade receivables, goods or services.

(xiii) **"Seller"** means any business entity who sells the underlying goods or services, for a trade credit transaction, on agreed terms.

(xiv) **"Trade Credit transaction"** means a transaction between two business entities, for supply of goods or services on agreed terms.

(xv) **"Trade receivable"** means a receivable owned by the Policy Holder arising out of a trade credit transaction**.**

(xvi) **"Whole turnover policy"** means a trade credit insurance policy that covers all trade credit receivables of all buyers, pertaining to a seller.

(b) The Words or expressions used in these Guidelines but not defined herein and defined in the Insurance Act, 1938 or the IRDA Act, 1999 shall have the same meaning as assigned to them under the said Acts.

5. Requirements of underwriting Trade Credit Insurance Business

The insurers underwriting trade credit business shall adhere to the following.

(a) General provisions:

5.1 A trade credit insurance policy may be issued to the following, subject to detailed guidelines given in the ensuing provisions.

a) Seller / Supplier of goods or services.
b) Factoring company as defined in The Factoring Regulation Act 2011 & amendments thereof.
c) Bank / Financial Institution, engaged in Trade Finance, licensed and regulated by respective Statutory Bodies which have better quality appraisal and effective risk management system

5.2 A trade credit insurance for Banks / Financial Institutions and factoring companies shall cover the loss on account of non-receipt of payment from a buyer, due to commercial or political risks, against the bills / invoices purchased or discounted.

5.3 A trade credit insurance policy shall not cover

a) Reverse factoring;
b) Government Buyers as defined under paragraph 4 (v) above.
c) financial guarantee in any form

d) Any other risk cover that may be specified by the Authority from time to time.

5.4 A Trade Credit Policy may be issued for covering trade related transactions other than loan default of seller. A trade credit insurance policy shall not cover any receivable arising from transactions made other than trade credit transaction.

5.5 A trade credit insurance policy can be sold as

i) A Whole turnover basis to cover all buyers of that particular segment or product or country.

ii) Cover for individual buyer only for:

a) Micro & Small Enterprises (as defined in paragraph 4 (viii) above
b) Project covers (as defined in paragraph 4 (ix) above)

iii) Single Invoice Covers through bill discounting / factoring shall be allowed only on Invoice Discounting e-Platforms such as TReDS.

5.6 A trade credit policy shall grant an indemnity of maximum:

a) Upto 60 percent of trade receivables from each buyer for all Banks / Financial Institutions / Factoring Companies. However, insurers shall not grant maximum indemnity coverage where there is adverse claim experience.

b) Upto 90 percent of the trade receivables from each buyer for all policyholders other than Banks / Financial Institutions / Factoring Companies.

c) Upto 95 percent in case of political risks only for Micro & Small Enterprises when they are the policy holders.

5.7 A Trade Credit Insurance Policy shall contain

a) "Maximum liability amount" which is the maximum loss that can be paid under one single policy. If the total loss occurring during the policy year exceeds the amount of the agreed maximum liability, the aggregate claim amount under this policy is limited to this amount.

b) Well-defined credit limits for each of the Buyers

5.8 The cover under trade credit insurance policy shall be available only to pre-agreed buyers and upto the limits agreed.

5.9 Insurers shall ensure that an efficient credit risk management system is in place either independently or in collaboration with reinsurer/s.

(b) Underwriting & Risk Management

5.10 Every insurer underwriting trade credit insurance business shall have Board approved Underwriting and Risk Management Policy in addition to or forming part of the underwriting policy prescribed under Guidelines on Product Filing Procedures for General Insurance Products which shall be filed with the Authority.

5.11 The Underwriting policy relevant to trade credit insurance products, at the minimum, shall cover the following.

a) Risk appetite for underwriting e.g. exposure to specific industry/sector etc.;

b) Underwriting criteria and tools for credit assessment;

c) Mechanism for carefully assessing the credit insurance business risk and develop risk early warning system for major risk types;

d) System to carry out stress tests periodically for trade credit insurance business;

e) Impact on reserving and solvency requirements.

f) Proposed risk monitoring and control of key product risks identified;

g) Proposed reinsurance arrangement;

h) Plans to enhance skills for internal underwriting, risk management, claims, reinsurance expertise; training to improve risk identification capabilities;

i) Distribution channel/s and target market;

j) Business development plan

k) Internal Control Management i.e., the insurance company carrying out trade credit insurance business should be centrally managed by the head/corporate office, branches to carry out trade credit insurance business under the control of head/corporate office.

6. Claims Handling

6.1 The insurer shall have a comprehensive "Claims Manual" which gives the manner in which the claims shall be processed, documentation, delegation of authority, policy holders servicing, grievance redressal etc.

6.2 The insurer shall also have a strong and efficient recovery mechanism in place to follow-up on defaults.

7. Reinsurance Arrangements

7.1 The insurer shall conduct trade credit insurance business with adequate reinsurance support at all times. The insurers shall revise their reinsurance programmes commensurate with their exposure and experience year on year.

7.2 The retentions of the insurer for trade credit insurance shall be as per the applicable reinsurance regulations & amendments thereof.

8. Product Filing Procedure

8.1 An insurer issuing policies of trade credit insurance shall be subject to the provisions of Guidelines on Product Filing Procedures for General Insurance Products. The insurers intending to undertake any change in the rates, terms or conditions of such products in accordance with these guidelines shall follow the relevant procedures of File& Use or Use& File as applicable within three months from the date of issue of these guidelines. The insurers may be guided by the illustration on product filing given as under.

Illustration on the filing of trade credit insurance product:

Since Trade Credit insurance covers are Business to Business covers and cannot cover individuals' risk, the product will fall under Commercial products that are sold to entities other than individuals and will include firms, companies, trusts etc.

Hence, the insurers may exercise the following options:

(a) File the product under File and Use irrespective of Sum Insured limit and it may be offered to all entities.

Alternatively, the Insurers intends to offer product differentiation and, therefore,

(b) Files one product under File and Use with Sum Insured limit upto Rupees Five Crores or as may be amended from time to time to offer it to Micro and Small commercial customers and;

(c) Files a second product under Use and File procedure with Sum Insured above Rupees Five Crores or as may be amended from time to time to offer it to other commercial customers.

8.2 All the existing trade credit insurance policies shall remain valid as per original contract terms and conditions, till the expiry of the current contract period and these policies shall not be cancelled unless the policyholder chooses to do so.

9. Maintenance of Data / Furnishing of Information

9.1 The Insurer should maintain, at the minimum, the following information.

a) Policy-holder wise earned and gross written premium
b) Loss ratio for the trade credit insurance product
c) Policy-holder wise -Buyer wise claims reserves
d) Policy-holder wise -Buyer wise claims paid
e) Policy-holder wise -Buyer wise claims recovery
f) Country wise data

9.2 The Insurer shall provide the above data/information as and when required by the Authority. The additional information/forms may be prescribed by the Authority from time to time.

9.3 However, the information on every loss known to the insurer, which is in excess of one percent of the net worth of the insurer, as and when intimation is received by the insurer, shall be reported in writing to the Authority.

10. Powers of the Authority

10.1 The Authority shall have the right to call, inspect or investigate any document, record or communication of the insurer and/or Policy-holder, if the Authority has reason to believe that an insurer carrying on trade credit insurance business is acting in a manner likely to be prejudicial to the interests of policy-holders or if it is of the opinion that the continued writing of trade credit insurance business is detrimental to the financial soundness of the insurer.

10.2 Violation of these Guidelines shall invite penal action under the provisions of the Insurance Act, 1938 which includes prohibiting insurer against entering into any new or particular trade credit insurance business transaction after giving the insurer an opportunity of being heard.

10.3 In order to remove any difficulties in respect of the application or interpretation of any of the provisions of these guidelines, the Chairperson of the Authority may issue appropriate clarifications from time to time.

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Annex

Guidelines on Trade Credit Insurance, 2016 stands repealed with the issuance of Trade Credit Insurance Guidelines, 2021		
Reference	**Date**	**Subject**
IRDAI/NL/CIR/CRE/044/03/2016	10th March, 2016	Guidelines on Trade Credit Insurance

History of Trade Credit Insurance Guidelines:

Guidelines on Trade credit insurance were first issued vide IRDA/NL/CIR/CRE/205/12/2010 dated 13th December, 2010 and revised vide IRDAI/NL/CIR/CRE/044/03/2016 dated 10th March, 2016.