भारतीय बीमा विनियामक और विकास प्राधिकरण
INSURANCE REGULATORY AND DEVELOPMENT AUTHORITY OF INDIA

Ref. IRDA/ENF/MISC/ONS/88/05/2016

Final Order in the matter of
M/s. Kotak Mahindra Old Mutual Life Insurance Company Limited

Based on reply to Show Cause Notice dated 22nd January, 2016 and submissions made during Personal Hearing chaired by Mrs. V.R.Iyer, Member (F&I), Insurance Regulatory and Development Authority of India (IRDAI) on 28th March, 2016 at 12:00PM at the office of Insurance Regulatory and Development Authority of India, 3rd Floor, Parishrama Bhavanam, Basheerbagh, Hyderabad.

The Insurance Regulatory and Development Authority of India (hereinafter referred to as "the Authority") carried out an onsite inspection of M/s. Kotak Mahindra Old Mutual Life Insurance Company Limited (hereinafter referred to as "the Life Insurer/Company") from 19th August, 2013 to 27th August, 2013. The Authority forwarded the copy of the Inspection Report to the Life Insurer vide letter dated 30th September, 2013 seeking comments on the same which was responded to by the Life Insurer on 20th October, 2013. Post scrutiny of the first compliance, the Authority raised further queries vide email dated 26th December, 2014 which was responded to vide letter dated 18th January, 2015. On examination of the submissions made in these communications, the Authority issued Show Cause Notice on 22nd January, 2016 which was responded to by the Life Insurer vide letter dated 15th February, 2016. As requested therein, a personal hearing was given to the Life Insurer on 28th March, 2016. Mr. G.Murlidhar, MD, Mr. Gaurang Shah, Director, Mr. Sunil Sharma, Appointed Actuary, Mr. Cedric Fernandes, CFO, Mr.Cheruvu Muralikrishna, Chief Compliance Officer and Mr.Kaushal Bhute, Chief Manager were present in the hearing on behalf of the Life Insurer. On behalf of the Authority, Mr.Lalit Kumar, FA & HoD(Enforcement), Mr. V.Jayanth Kumar, JD(Life), Mr.Prabhat Kumar Maiti, JD (Enforcement) and Mr. K.Sridhar Rao, Sr. Assistant Director (Enforcement) were present in the personal hearing.

The submissions made by the Life Insurer vide letters mentioned herein, in their written reply to Show Cause Notice and those made during the course of the personal hearing were taken into account.

The findings on the explanations offered by the Life Insurer to the following charges and the decisions are as follows.

Charge No.1

The Life Insurer sold a good number of new policies during 2011-12 and 2012-13 in respect of 'Accumulated with Profit' type of contracts such as Kotak Child Advantage Plan, which are similar to Variable Insurance Products (VIP).

Violation of Circular No. IRDA/ACTL/CIR/VIP/187/11/2010 dated 23/11/2010.

Submission by the Life Insurer

The product is a conventional with profits product and the features are different from the VIP Products. The difference between the product in question and VIP was discussed with the Authority and post consensus that the product is not VIP, it was communicated to the Authority vide letter 19/11/2010. Further it is to confirm that post IRDAI Product Regulations, 2013, this product has been discontinued.

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Decision

Though the Company referring some discussion, with regard to features of the product, there was no categorical written opinion from the Authority that the said product does not fall under VIP category. Hence the Life Insurer should note that mere discussion should not be construed as approval from the Authority. As per the point no.23 of the Circular referred herein, all the existing individual products which have a separate and identified savings component shall be re-filed with the Authority, in accordance with the Guidelines and fresh approval is to be obtained. Hence the Life Insurer has not ensured the same. The Life Insurer is hereby *warned* for the violation. The Life Insurer is advised to ensure that categorical approval from the Authority shall be obtained for any queries for which clarifications are sought hereinafter.

Charge No.2

In case of Accumulated with profit products, the Life Insurer had reduced the first year commission rates from 40% to 35%. It was observed that the insurer deducted charges from individual policyholders' accounts at the previous rate of 40% rather than 35% of the first year premium and agents were paid commission at the rate of 35%.

Violation of File and Use Procedures.

Submission by the Life Insurer

Modification in the File and Use i.e., First year commission payable was reduced from 40% to 35% in respect of both Conventional and Accumulating With-Profit products to comply with Section 40A of Insurance Act, 1938 on commissions. The difference between the commissions will emerge as surplus which would in-turn be allocated to the policyholders. This was also communicated to IRDA vide letter dated February 01, 2011, while changing the Commission for these plans to comply with the regulations.

Decision

There is no categorical approval from the Authority for the modifications effected. However, as the modifications made were to comply with the act provisions, *no charges are being pressed.* The Life Insurer is cautioned and advised that any modifications to be carried out in the original File and Use shall be in line with the procedure prescribed in the File and Use Guidelines.

Charge No.3

In respect of group policies, the Life Insurer funded a considerable sum against differential amount for service tax for the year 2012-13 instead of collecting the same from the group policyholders. The entire amount was paid by the Life Insurer by debiting the policyholders' account.

Violation of Section 41 and Section 64VB of Insurance Act, 1938.

Submission by the Life Insurer

The observation was mainly in respect of individual members under Group Credit Term policies under the Non-Par segment which covers around 13.45 Lakhs members spread over 600+ branches of the Master Policyholder(MPH) and quite a few in rural areas. The

waiver was on account of only differential service tax on change of service tax rates. The shortfall on account of service tax per member was low per each member. The administrative cost and hassles of recovering the differential service tax from each individual member would be very difficult. Hence to deal with this practically, the company decided to waive off this shortfall of service tax in the interest of the members of Group Credit Term policy. This practice continued till the FY 2013-14 and 2014-15. Further it is to be noted that Group credit term policies are classified under Group Non-part products segment. Hence the differential service tax would be ultimately borne by the Shareholder. As the company assumed the risk only after the premium payable from each member (except for differential service tax) under the policy was received, the company has not violated Section 64VB of Insurance Act, 1938. This credit cover is needed by the member under the policy and service tax was waived off in view of the practical circumstances. Hence it may be construed that the company has not offered either directly, indirectly as an inducement to a member to take or renew he policy. This may not be treated as violation of Section 41 of Insurance Act, 1938.

Decision

The amounts waived towards any account, (though it is not a part of the designated premium), to take out or continue a policy may be treated as an inducement and may attract provisions of Section 41 of Insurance, 1938. Further as submitted herein the waiver was made applicable for subsequent financial year's viz., 2013-14 and 2014-15, by the time service tax quantum would be known to master policy holders while enrolling new members, hence there would not be any hindrance in collecting the service tax. Hence the Life Insurer is *warned* for continuing the waiver for subsequent years also. The submissions that the cost of recovering the service tax from the members would be more and that the entire amount, anyhow charged to share holders, are taken on record. The Life Insurer is advised to ensure scrupulous compliance of Section 64VB and Section 41 of Insurance Act, 1938 hereinafter.

Charge No.4

In respect of Top-Up cases, date of application of NAV as per ULIP Guidelines, 2005 has not been complied.

Violation of Clause 10.6 of ULIP Guidelines. 32/ IRDA / ACTL/DEC-2005 dated 21.12.2005.

Submissions by the Life Insurer

As per the referred ULIP Guidelines, 2005 a top up premium is an amount of premium that is paid by the policy holders at irregular intervals besides basic regular premium payments specified in the contract and is treated as single premium. Accordingly, treatment of NAV allotment for To-up premium request is subject to checkpoints such as a) Top up premium is accompanied with an increase in Top-up sum assured hence underwriting acceptance may be required b) Where the annualised premium is greater than Rs.1 Lakh, AML checks need to be carried out before processing the Top-up request and 3) Top up specifications are provided in product file and use. Hence due checks needed before processing the top up request. Hence the Company is of the view that Top-up premium should be treated as new business premium and the appropriate NAV has been applied.

Decision

As per the relevant guidelines, in respect of premiums received up to 3:00PM by the Life insurer along with local cheque or a demand draft payable, the closing NAV of premium received date shall be applicable. In respect of premiums received after 3:00PM with a local cheque or demand draft the closing NAV of the next business day shall be applicable. Further in respect of premiums received with outstation cheques/demand drafts as the place where the premium is received, the closing NAV of the day on which cheques/demand draft is realised shall be made applicable. On scrutiny of the observations it is noticed that there were local cheques in some of the cases. Hence it is construed that the Life Insurer has not ensured the compliance with the guidelines. The Life Insurer is *warned* for the same. Further, the Life Insurer is advised to ensure compliance of the provisions of relevant Regulations/guidelines/circulars issued by the Authority from time to time with respect to application of NAV.

Charge No.5

In case of linked lapsed policies, the Life Insurer is in practice of deducting one month extra mortality charge. The sample case examined belongs to a 100% allocation charge product and therefore there is ultimately no implication on the policyholder. However, the policy administration system of the insurer was in the process of deducting such extra charges across entire lapsed cases.

Violation of File and Use Procedures.

Submissions by the Life Insurer

The grace period in the Policy Administration System is kept to be 5 days in excess of the grace period of 15/30 days applicable in respect of monthly and non-monthly mode policies respectively. The intention of granting additional 5 days of grace period was done as a customer centric measure to avoid the administrative hassles to the policyholders in case the policyholder delays the payment by 1 or 2 days. This practice was put in place keeping in view policyholders' benefit and convenience. If this practice would not have been allowed, the policies would have lapsed requiring revival process. This has spared the policyholders from the payment of revival charges of Rs.500 when premium is paid in these 5 days. When the policy gets revived, the mortality charge from the date of revival to the next policy month anniversary is not deducted. Hence there is no impact. It is to confirm that the policy administration system has since been modified and removed additional 5 days of grace period. It is further to certify that, the company has verified all the policies where mortality charges were deducted as such, and no policy has been foreclosed due to collection mortality charges after the completion of normal grace period.

Decision

The Life Insurer has to follow the 'grace period' as specified in the file and use application. It is understood that the practice adopted was neither documented in the File and Use application nor sought any subsequent approval for the same. Hence this is a gross violation of File and Use Guidelines. The Life Insurer is *warned* for the same. The submissions made above are taken on record and the Life Insurer is advised to be vigilant while modifying the features of the original file and use hereinafter.

Charge No.6

In respect of group policies, claims are settled in favour of Group Master Policy Holder. The Life insurer was obtaining an upfront letter from the nominee or legal heir that the monies were received by them and the Life Insurer is not obtaining any confirmation of actual receipt of claim monies. As per the process the said upfront letter from the nominee or legal heir was made compulsory to settle the claim. This gives scope for misuse of claim monies by the master policy holders. The Life Insurer had no control on the balance monies, if any, payable after adjusting the outstanding loans to the nominee or legal heir of the deceased member even in cases of Loanee or Creditor schemes.

Violation of Clause C-7 of Group Insurance Guidelines, No.015/IRDA/Life/Circular/GI Guidelines/2005 dated 14/07/2005.

Submission by the Life Insurer

As per the directions given by the Authority, in the final order with respect to the Company's previous inspection report 2011-12, the Company initiated the change in the process of settlement and hence asked the Group Master Policy Holders to follow the modified process of claim settlement. Out of 149 Group Credit policies for the period under audit, the process as directed had been implemented and changed the claim process in 148 group credit policies except one Group policy because, the policy holder had conveyed practical difficulties, that the nominees being belonging to socially under-privileged class, they may not have bank accounts. The master policy holder insisted that the payment may be made in favour of them and in turn they make the balance payments to nominees after deduction. Owing to mutual disagreement the policy was discontinued for enrolling new members, post March 31, 2012. However, in order to service existing members under existing policy the company had to continue the practice of paying claims to master policy holder. It is further to certify that systems and checks are in place to ensure that the balance of claim is reached the claimant/beneficiary. It is to confirm that the company has in fact changed the process of settlement of claims in line with Group guidelines and Authority's directions, with just this exception. Further the company hereby certifies that it has processes and checks in place to ensure that claim amount, in excess of outstanding loan, under Group Credit term policies is paid to the nominee/ultimate beneficiary of the deceased member.

Decision

The submissions that the i) revised claim settlement process has been changed in all the group policies except in the case referred by the Authority ii) Under the policy where the revised process could not be completed, stopped new business and further certification that there are systems and checks in place to ensure the eligible claim amount is reached the beneficiary/claimant with regard to ensuring that the balance claim over and above outstanding loan reaching the nominee/beneficiary are noted. However, the Life Insurer should have endeavoured to ensure compliance of the said guidelines in case of this group policy also. However considering i) and ii) mentioned in this paragraph, *no charges are being pressed.* The Life Insurer is advised to ensure compliance with the said Guidelines in this case also hereinafter. The Life Insurer further advised to ensure compliance with all the relevant Regulations/Guidelines/Circulars issued by the Authority from time to time with regard to settlement of claims under Group policies. The action taken report in the case of the group policy referred herein shall be furnished within 60 days from the date of this order.

Charge No.7

It was observed that claims under Group Master Policy were repudiated on the grounds of "non-disclosure in health declaration" by the individual member. However, DOGH (Declaration of Good health of the borrower i.e., member covered) to be filled by individual member providing his/her details for the insurance coverage and health condition under a group policy contract was in English language and in most of the cases the members covered signed in vernacular language and no declaration was obtained to the extent that the contents of DOGH were explained to the member/s to be covered.

Violation of Regulations* 3(4) and *4(2) of IRDA (Protection of Policyholders' Interests) Regulations, 2002.

Submission by the Life Insurer

There have been only 121 cases that have been repudiated for medical non-disclosure out of the total 13673 group claims processed for 2011-12 and 2012-13 which is only 0.91%. Further out of 121 claims repudiated for medical non-disclosure, there were only 4 claims where scribe signatures were not in place. In all other claims either life insured had signed in English or in case of signatures in vernacular language, there was a scribe's signature evidencing that the contents were explained to the Life Insured. However, these four cases were repudiated where enough evidences of a wilful mis-representation of facts are there. Despite (the members whose claims were repudiated) being seriously ill (with pre-existing disease like Cancer, HIV and Cirrhosis of Liver) and virtually on death bed they have applied for loans and secured the same with insurance policies. Copies of four Claim files also submitted in support of the submissions. Hence the claims were repudiated in order to be fair to the policyholders at large. It is to submit that the company has made requisite changes to the membership forms to ensure non-recurrences of such instances. The lapse was only an administrative with no intention of jeopardizing the interests of the lives assured. Further the process has been tightened to ensure that the scribe signature is present in vernacular cases.

Decision

It shall be noted that the forms and documents used in the grant of cover may, depending on the circumstances of each case, be made available in languages recognized under the Constitution of India. In the instant case, the Life Insurer should have at least ensured that the contents of the proposal forms are made understood by the policy holder. If this is not ensured, the same may lead to unintentional non-disclosure by the Members of the Group. The Life Insurer, hence not adhered to compliance of the Regulations mentioned herein. The Authority as per the powers vested on it vide Section 102(b) of Insurance Act, 1938, levies *a penalty of Rs.5,00,000 (Rupees Five Lakhs only)* on the Life Insurer for the lapse. Further the life insurer is advised to review such claims to ensure that no genuine claim is repudiated. The Life Insurer is directed to strengthen the systems for scrutiny of proposal papers before risk is covered thereby to ensure that such administrative lapses do not recur.

Charge No.8

It was observed that some master policyholders were claiming the death claim benefits in batches / lots though the dates of death of the members covered were different and the group policyholder or organizer was aware of the fact of the incident or event. It clearly shows that the master policyholders did not claim the benefits as and when they receive the death intimations from the nominees / legal heirs of the deceased members. This resulted in

delay in settlement of claims by the Life insurer. There was no intimation / correspondence with the nominee or legal heir of the deceased member by the Life insurer (at least in case of claims). This lead to undue delays in settlement of claims though the reason for delay was on the part of the master policyholders.

Violation of Regulation 8 of IRDA (Protection of Policyholder s' Interests) Regulations, 2002.

Submissions by the Life Insurer

The said master policy holders are lending institutions which operate in remote locations. The Company understand that they get to know about the death of a particular borrower only when they stop getting their EMIs and they go to collect the EMI that has become due. Thereafter, they assist the family in the claim settlements and inform the Company about the claim along with necessary claim documentation. Hence, it may appear that the claims are intimated in batches / lots. Further it is to submit that once the claims are intimated to the Company, the claims are being processed promptly. Around 98% of claims are settled within 2 weeks from date of receipt of all documents for Financial Years 2011-12 and 2012-13. However, Authority's concerns are noted and it is to assure that the company would communicate to master policy holders and sensitize them in this area to ensure that the period from date of death to date of intimations is reduced.

Decision

While considering the submissions made and assurance given, *no charges are being pressed.* The Life Insurer shall take all the necessary steps in this regard as assured under intimation to the Authority.

Charge No.9

The Life Insurer had created multiple code numbers for single corporate agent or broker based on the location of the business procured or the location of the customer. No control was there on the business generated by specified persons of a corporate agent. The details / information regarding specified person-wise business solicited were also not provided. The limited number of specified persons or qualified persons compared to the large number of places of new business procured tantamount to sourcing of significant part of the business through unlicensed persons.

Violation of IRDA Circular No. IRDA/CIR/010/2003, dated 27/03/2003.

Submissions by the Life Insurer

The Channel Partners comprise of entities that operate either locally, regionally or nationally. Location-wise codes are created for each of the Company's employees linked to corporate agents & brokers purely for the purpose of tracking and monitoring business. System codes are meant for internal tracking/renewal/MIS/analysis. In many instances, one corporate agent may have separate codes for their own separate business verticals. Hence number of codes does not imply number of places of business. However, post feedback from inspection team in August, 2013, the Company had reviewed the codes and deactivated about 980 inactive codes. The processes and checks in place to ensure that each proposal is sourced by Specified Person only. The Company's sales team assists/accompanies the Specified Person while closing the sale. Most of the Specified Persons sell standardized/simplified products, leading to relatively better productivity. The Company also

constantly tracks number of policies per Specified Person per month to ensure that the same is within reasonable limits. Further data on number of policies per specified persons for the period from April, 2015 to December, 2015 in comparison with the same pertaining to financial year 2012-13 is submitted to establish that the number of policies per specified persons per month is within reasonable limits. Further the Company hereby certifies that

- *The proposal sourced by the Corporate Agents of the company has been solicited by the respective specified persons only.*
- *The company has accepted Life Insurance business with concerned broker purely on the basis of the fact that the entity is a registered and licensed broker with IRDA and it is presumed that the Brokers solicit the business through authorized persons only.*

Decision

The limited number of specified persons or qualified persons compared to the large number of places of new business procured gives scope to infer that significant part of the business through unlicensed persons. However, based on the submissions and certifications *no charges are being pressed*. The Life Insurer is hereby directed to ensure continuous compliance of Regulation 14 IRDAI (Registration of Corporate Agents) Regulations, 2015 and any other relevant regulatory prescriptions hereinafter.

Charge No.10

Outsourcing agreements were entered with related parties of the Broker and payouts are made under the guise of the same.

Violation of Regulation 19 of IRDA (Insurance Brokers) Regulations, 2002 and Clause 8.4, 9.12 of Outsourcing Guidelines, No. IRDA/LIFE/CIR/GLD/013/02/2011 dated 01.02.2011

Submission by the Life Insurer

The activities outsourced were non-core activities and the Outsourcing guidelines do not prohibit outsourcing of these activities. The said activities require specialised infrastructure and capabilities. As the entity was an established entity for these activities, the same were outsourced to it. The agreement was on the basis of the entity's representation of its credentials in providing the said services. Further to submit that the vendor does not fall into the category of entities which are prohibited from undertaking outsourcing activities under the Guidelines, hence there is no violation of Clause 8.4 of the said guidelines. These activities did not create any conflict of interest which could have caused loss to the company or policy holder; hence there is no violation of Clause 9.12 of Outsourcing Guidelines also. The agreement with the vendor was purely on principal to principal basis and was independent of any other relationship with its group entities. Payments made under the outsourcing agreements were specifically for rendering of the specified services with no linkage to business relationship with any of its group companies. All the payouts made were disclosed in Expense of Management Returns as related party and also were reported in Outsourcing returns, as mandated in Outsourcing Guidelines.

Decision

While considering the submissions made, *no charges are being pressed*. However, the Life Insurer is advised to ensure continuous compliance of Regulations and

provisions of guidelines mentioned herein. The Life Insurer also hereby advised to ensure continuous compliance with all the relevant Regulations/Guidelines/Circulars issued by the Authority from time to time hereinafter.

Charge No.11

Arrangements were made with the related parties of the CAs and Brokers and channelizing the extra payouts in the name of 'customer meets', 'road shows', 'mailer campaigns' etc., activities'.

Violation of i) clause 21 of IRDA Circular No.017/IRDA/Cicrular/CA Guidelines/2005 dated 14/0/72005 ii) Regulation 19 of IRDA (insurance Brokers) Regulations, 2002 and iii)Clause 8.4 and 9.12 of Outsourcing Guidelines, No. IRDA/LIFE/CIR/GLD/013/02/2011 dated 01.02.2011.

Submissions by the Life Insurer

It is to submit the Company has been continuously compliant with Ratio of expenses of management as per Rule 17D of Insurance Rules, 1939 (2011-12 99.56%, 2012-13 99.13%, 2013-14 98.78% and 2014-15 98.16%). Notwithstanding to the same, the payments referred to in the charge are expenses incurred by the Company in carrying out various promotional and publicity activities across the country and also in the areas where the company's intermediaries operate, as an enabler to spread awareness of the company and its products. Theses payouts are linked to the services rendered by them and are unrelated to volume of the insurance business. These activities are in the nature of Advertisement Campaigns, Publicity & Marketing Campaigns, Road shows, Insurance customer meets, Customer service Camps, Direct Mailer campaigns etc. For carrying these activities company seeks help of various vendors who have presence and expertise to carry out such activities. While selecting the parties the company has considered capabilities of the vendor in providing services, their presence in concerned areas etc. The amounts paid under these agreements are reasonable in relation to the size and premium earned by the company as below.

Year	*2012-2013 (Rs in Thousand)*	*2011-2012 (Rs in Thousand)*
Premium Income (a)	27777846	29374331
Total Promotional & Publicity expenditure (b)	*1000487*	*975149*
*Percentage to Premium Income (b/a*100)*	***3.60%***	***3.32%***
Promotional & Publicity expenditure of Vendors related to CA\ Brokers (c)	*201432*	*185536*
*Percentage to Premium Income (c/a*100)*	***0.73%***	***0.63%***

It is to inform that the payouts have been duly reported under payments made to related parties of intermediaries in return under expenses of management for the period 2011-12 and 2012-13.

Further, as per outsourcing guidelines, 2011 issued by the Authority, 'Outsourcing' is defined as "Insurer's use of a third party to perform activities on a continuing basis that would normally be undertaken by the Insurer itself, now or in the future". The activities mentioned

above are of a nature which an insurer would not be able to do by itself. Hence there has been no violation of Clause 8.5 and 9.12 of the said guidelines. Based on this understanding the agreements were also not reported in outsourcing returns mandated under the guidelines.

The Company has not paid any insurance agent by way of commission or remuneration in respect of any policy of life insurance an amount which exceeds the limits specified in Section 40A and hence the Company has not violated Section 40A of Insurance Act, 1938. The Company has also not made any payouts to the Corporate Agent/Broker any amount other than the permitted agency commission, whether as administration charges or reimbursement of expenses or profit commission or in any other form. The company has not entered into additional relationship with the corporate agent/Broker for payment of remuneration. Hence there are no extra payouts channelized to corporate agents or brokers. Hence the Company is in no violation of Clause 21 of Corporate Agency Guidelines and Regulation 19 of IRDA (Insurance Brokers) Regulations, 2002.

Decision

The submissions made are taken on record. However, as per Clause 13 of Outsourcing Guidelines, 2011, Insurers are advised to refer to IRDAI for further clarifications in case any ambiguity regarding the classification of the activities as core or non-core which are not specified in the said guidelines. Hence the Life Insurer unilaterally shall not decide whether a particular activity is outside or inside the scope of outsourcing activities mentioned in the Outsourcing Guidelines, 2011. As per the submissions made, it is construed that Life Insurer has not complied with Clause 13 referred herein. The Life Insurer is *warned* for the same. The Life Insurer is advised to ensure continuous compliance with the provisions of relevant extant Regulations/Guidelines hereinafter

Charge No.12

The Life Insurer was in practice of refunding the insurance premium amount along with the interest as per the directions of consumer disputes redressal forum/Ombudsman in respect of mis-selling of a policy. In this regard it was observed that the insurer had debited such interest amount for mis-selling as litigation fee of policies to policy holders' account instead of shareholders' account leaving the existing policyholders in financially disadvantageous situation.

Violation of IRDA Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002 (Refer Form A-PL- Profit and Loss Account item "Expense other than those directly related to the insurance business")

Submission by the Life Insurer

Expenses relating to interest/compensation paid to policyholders for compliance to the directions of consumer disputes redressed, forum/ombudsman have been debited to the Revenue Account in accordance with Section 40-B (4) which states that "all expenses of management and charges incurred whether directly or indirectly in respect of life insurance business transacted by the insurer in India should be fully debited in the Revenue Account as expense". In absence of specific guidelines on accounting treatment of

interest/compensation, the normal accounting principles were followed. The total amount involved was Rs.53,418 and post observation by the Authority, the same was debited towards interests and penalty to the Shareholder's Account.

Decision

The expenses relate to interest/compensation paid to policy holders for compliance to the directions of consumer disputes redressal forum/ombudsman etc are not expected to be due in normal course of the insurance business. Hence such expenses should be debited to Shareholders Account without affecting the interest of the policy holders. Considering the submission that now, the Life Insurer debited the same to Shareholders' Account, *no charges are being pressed.* The Life Insurer is advised to ensure continuous compliance as such.

Charge No.13

On scrutiny of details of pre-payments in trial balance as 31.03.2013, it was noticed that an amount Rs.10.47 Crores was shown as Pre-paid reinsurance. The total premiums received in the revenue account (net of reinsurance premiums) paid for the unexpired portion of the year is shown as prepaid expenses. The reinsurance premiums are paid only for those policies where the risk cover is granted by the Life Insurer, for which the Life insurer had received the premiums. The accounting policy of the Life Insurer states that 'Reinsurance premium and reinsurance commissions are recognised over the period of risk'. Hence, the accounting policy in respect of recognition of reinsurance premium over the period of risk is not in line with relevant regulations.

Violation of Schedule A-Part 1- Regulation 2 of IRDA (Preparation of Financial statements and Auditors' Report) Regulations, 2002 and Point no.2 of Schedule I (Regulation 3) of IRDA (Assets, Liabilities and Solvency Margin of Insurer) Regulations, 2000.

Submissions by the Life Insurer

1) *As per Schedule A-Part 1- Regulation 2 of IRDA (Preparation of Financial statements and Auditors' Report) Regulations, 2002, the accounting policy to be followed for payments made to the Reinsurer is not specified. Hence the accounting standards issued by the ICAI are followed in accordance with Schedule A-Part 1- Regulation 2 of IRDA (Preparation of Financial statements and Auditors' Report) Regulations, 2002. For Reinsurance payments, the company has followed an accounting policy of "Recognizing reinsurance premiums over the period of the Risk". Reinsurance premium is calculated and paid for a full policy year to the Reinsurer. When recognising the individual reinsurance premium in the books of account, the reinsurance premium relating to a period beyond the financial year is booked as prepaid reinsurance as no reinsurance credit is taken in actuarial reserving for individual business. This ensures that the reinsurance premiums are reflected in the books of account on an accrual basis. The company has followed this accounting policy, since inception, to adhere to the accounting principles of "accrual" and "matching concept" in accordance with accounting standards issued by the ICAI and for the accounts to show a "true and fair" position. These accounting policies are an integral part of the Financial Statements which have audited by various reputed statutory auditor firms since inception. The Auditors report*

too states that Financial statements are in accordance with IRDA (Preparation of Financial statements and Auditors' Report) Regulations, 2002.

2)In view of the facts explained above, the nature of Prepaid Reinsurance (amount Rs. 10.05 Crores as at March 31, 2012 and amount Rs. 10.50 Crores as at March 31, 2013) as at is that of a realisable asset on the date of the balance sheet and is not in the nature of an unrecoverable Reinsurer's balance. Therefore, it is not an asset to be taken at zero value for the purpose of calculation of available solvency margin. The solvency ratio as at March 31, 2012 was 3.06 and as at March 31, 2013 was 2.93 which was well above the statutory requirement of 1.5.

Hence for the reasons explained above, there is no violation of Schedule A-Part 1-Regulation 2 of IRDA (Preparation of Financial statements and Auditors' Report) Regulations, 2002 and Point no.2 of Schedule I (Regulation 3) of IRDA (Assets, Liabilities and Solvency Margin of Insurer) Regulations, 2000 IRDA Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002.

Decision

The Life Insurer is taking credit of unexpired portion of re-insurance premium, under the head of prepaid re-insurance. Hence it is expected that the Life insurer should not take credit of the reinsurance ceded beyond the financial year. However it is evident from the Actuarial reports (Form KT1) pertaining to the relevant year (2012-13) that the Life Insurer has taken credit of reinsurance ceded beyond the financial year, while calculating the Required Solvency Margin. The same is a deviation from the matching concept. In view of the same the Life Insurer has deviated from the general accounting principle as well as from the prudent valuation practice. However considering that this practice is not having considerable impact on the solvency margin for the year 2012-13, *no charges are being pressed*. The Life Insurer is directed to discontinue the practice with immediate effect under intimation to the Authority.

Charge No. 14

The reserve for premium waiver benefit was made at the time of death of the life assured. The reserve amount is the present value of the future premium. However, no explicit reserve was made for this benefit before the death or disability occurs.

Violation of 2(2) of Schedule IIA of IRDA (Assets Liabilities and Solvency Margin of Insurers) Regulations, 2000.

Submission by the Life Insurer

Enough prudence is in place in the Company's reserving methodology and the Company attempted to reduce the complexity of models by reserving implicitly for the inbuilt premium waiver benefit. However, the Company assured itself that the implicit method of allowing for the premium waiver benefit does not impact the financial stability or the solvency of the company. Further it is to certify that post observation by the Authority, now explicit reserves are being created to be in line with extant regulations.

Decision

Considering the submissions made, *no charges are being pressed*. The Life Insurer is advised to ensure continuous compliance of Regulations mentioned herein.

Summary:

In conclusion, as directed under the respective charges, the penalty of ***Rs.5,00,000 (Rupees Five Lakhs only)*** shall be remitted by the Life Insurer by debiting shareholders' account within a period of 15 days from the date of receipt of this Order through NEFT/ RTGS (details for which will be communicated separately). An intimation of remittance may be sent to Mr. Lalit Kumar, F.A. & HoD (Enforcement) at the Insurance Regulatory and Development Authority of India, 3rd Floor, Parishrama Bhavanam, Basheerbagh, Hyderabad-500 004.

Further

a) The Life Insurer shall confirm compliance in respect of all the directions referred to in this Order, within 21 days from the date of issuance of this order. Timelines, if any as applicable shall also be communicated to the Authority.
b) The Order shall be placed before the Audit committee of the Life Insurer and also in the next immediate Board meeting and to provide a copy of the minutes of the discussion.

c) If the Life Insurer feels aggrieved by any of the decisions in this order, an appeal may be preferred to the Securities Appellate Tribunal as per Section 110 of the Insurance Act, 1938.

Place: Hyderabad
Date: 06 -May-2016

(V R Iyer)
Member (F&I)