



Ref: IRDAI / Enf / ORD / ONS / 193 / 10 / 2019

Order in the matter of CHOLAMANDALAM MS GIC Ltd

Based on the

(i) Show Cause Notice (hereinafter referred to as "SCN") reference No.IRDA/Enf/SCN/2019/NL/Chola_Insp.rpt dated 16th July, 2019 in connection with the on-site inspection conducted by the Insurance Regulatory and Development Authority of India (herein after referred to as 'the Authority' or 'IRDAI') during 14th to 24th March, 2017.

(ii) Cholamandalam MS GIC Ltd (hereinafter referred to as "Cholamandalam" or as "General insurer") response dated 6th August, 2019 to the aforesaid SCN.

(iii) The submissions made by general insurer during the Personal Hearing held on 28th August, 2019 at 3.00 PM, taken by the Chairman of the Authority at its office at Hyderabad and subsequent submissions made by the general insurer vide letter dated 6th September, 2019.

Background:

2. The IRDAI had conducted an onsite inspection of Cholamandalam MS GIC Ltd during 14th to 24th March, 2017. The inspection report, inter alia, revealed certain violations of provisions of the Insurance Act, 1938, Regulations, Guidelines and various circulars issued there under.

3. A copy of the inspection report was forwarded to Cholamandalam on 10th January, 2018 seeking their response. On examining the submissions made by Cholamandalam vide letters dated 14th February, 2018, 7th June, 2018 and 29th March, 2019, a SCN was issued on 16th July, 2019, which was responded to by the general insurer vide letter dated 6th August, 2019. As requested by the general insurer therein, personal hearing opportunity was granted on 28th August, 2019.

4. Mr. S S Gopalarathnam, MD, Mr Venugopalan, CFO, Mr V Suryanarayanan, President and COO, Mr S Vedanarayanan, President-Emerging Business and Mr Suresh Krishnan, Chief Compliance Officer were present in the personal hearing on behalf of the general insurer. On behalf of the Authority, Mr. Prabhat Kumar Maiti, GM (Enforcement) and Mr. K.Sridhar, AGM (Enforcement) were also present.

5. The submissions made by the general insurer in reply to the SCN and those made during the personal hearing on 28th August, 2019 have been considered by the Authority and on that basis the decision on each of the charges is given as under.

SCB

6. Charge no.1

Violation of

- 1) Para 9.6(ii), 9.9 and 9.12 of Outsourcing guidelines circular no. IRDA/Life/Cir/GLD/013/02/2011 dated 1st February, 2011.
- 2) Circular no. IRDA/CAD/Cir/Agn/137/08/2010 dated 25-08-2010 directing insurers to display agency name, code, contact details and other contact details prominently on the first page of the policy document.
- 3) Guideline 1, 3(ix), 8, 11, 22 & 26 of File and Use guidelines circular ref.no 021/IRDA/F&U/SEP-06 dated 28.9.2006, Circular no. IRDA/NL/Cir/ F&U/003/01/2011 dated 6th Jan, 2011 and circular no.048/IRDA/De-tariff/Dec-07 dated 18th Dec, 2007.

7. Inspection observation:

- a) The insurer is making pay-out to vendors based on the discount offered on the premium to customers. The pay-out structure to vendor is designed in such a way that payment to vendor is more if discount is less and vice-versa.
- b) Providing motor dealer contact details in the policy document and referring him as intermediary.
- c) Insurer referred to de-tariff discount, in the payout structure agreed with the vendor, which implies insurer was charging erstwhile tariff premium without making any reference to the base rate approved under F&U guidelines.

8. Summary of Insurer submissions

- a) Motor dealers provide infrastructure and various other services to operate and the payment considerations for those services were made in terms of the value of the premium. The payout structure for the services to vendors/motor dealers was as per market practice at that point of time till the issuance of MISIP guidelines. Similar is the case with other vendors who had provided their infrastructure facilities to the Insurer for which payment towards such services were made. Before the advent of Motor Insurance Service Providers (MISP) Regulations, motor dealers were an Integral part in issuing policies on new vehicles on behalf of the respective panel Insurers. The IRDAI has already recognized the fact that other services are rendered by intermediaries in addition to soliciting insurance business in Insurance Marketing Firm (IMF) regulation.
- b) As motor dealer does the service of authorized service station for repairs, for facilitating the insured, the details were provided in the policy documents and reference of intermediaries is an unintentional mistake which has been rectified in the subsequent period.



c) The approved detariff discount is what we have filed with IRDAI on the basis of original tariff rate as the reference is always linked to tariff rates and hence there is no violation of F&U guidelines.

9. Decision on charge no.1

a) The payout structure agreed by the insurer, for the services offered by the vendor, is based on the discount given to the policyholder on gross premium. Agreeing to pay the remuneration to vendor based on the discount offered to customer but not based on the level of services offered, exhibits that the insurer has not undertaken the cost-benefit analysis of the outsourced activity. Further, the Insurer agreed to pay a service fee of upto 55% of the gross premium i.e more than what it retains for the risk accepted. By any standards, the action of the insurer cannot be justified. Insurer made service fee payment to Vendor M/s V3 Motors as a percentage on the premium linked to the discount given by insurer to customers, without having any upper cap/limit on the fee payable.

In the above manner, the insurer violated the Outsourcing guidelines circular ref.no. IRDA/Life/Cir/ GLD/013/02/2011 dated 1st February, 2011 by agreeing to payment terms not in the interests of the insurer.

Therefore for the above mentioned violation, in exercise of the powers vested in the Authority as per the provisions of Section 102(b) of the Insurance Act, 1938, the Authority hereby imposes a penalty of Rs 1 lakh (**Rupees One lakh only**). The insurer is further directed to undertake a cost benefit analysis and adequate due diligence of all such outsourced activities for effective oversight.

b) Insurer failed to adhere to the Authority circular on providing of information of agency name, code and mobile contact details prominently in bold letters in the policy document and instead provided its vendor details. The intention of the circular was to make the agency contact information available to policyholders for post sales servicing. The insurer is warned for the lapse and is advised to ensure compliance to Clause 'i' under sub-regulation 1 of Regulation 11 & 12 of IRDAI (Protection of Policyholders' Interests) Regulations, 2017 by having proper internal control mechanism to provide in the policy document, the name and contact details of the persons involved in the sales process.

c) If the insurer's submission that the mention of detariff discount was merely for the purpose of reference is to be believed, the discount percentage on erstwhile tariff referred in arriving at the base premium should be the same across all the private car motor policies as per F&U approval, but cannot vary from policy to policy. From the available documents, it is observed that the detariff discount referred is in the range of 0% to 55%. However, it is not clear whether the referred discount is only on erstwhile tariff or is also inclusive of discount for good risk factors. The insurer is advised to ensure compliance to the rating structure as approved under the F&U procedure and the regulations issued from time to time. Further, the insurer should ensure that while quoting rates to prospects henceforth, it needs to refer to the filed rates but not to the erstwhile tariff rates.



10. Charge no.2

Violation of

- Clarification 6 of circular ref.no.IRDA/HLT/Misc/Cir/259/12/2011 dated 01-12-2011.
- Clause 15 of schedule I of IRDA (Health Insurance) Regulations, 2013 which clearly specifies that 'no commission shall be payable to any intermediary on the acceptance of a ported policy'.

11. Inspection observation:

It was observed that the insurer paid insurance commission to intermediaries in respect of porting-in health policies. The details of the five sample cases examined of financial year 2015-16 are as below:

	Request ID	Policy issued date	Gross Commission paid (In Rs.)
1	PR 873146	20-10-2015	911.85
2	PR 986272	16-02-2016	911.85
3	PR 991264	22-02-2016	1063.83
4	PR 814230	06-08-2015	1474.05
5	PR 812143	03-08-2015	2481.15

Concerns/violations:

- The detail of commission recovery has not been provided by insurer, as informed in its submission.
- Insurer has not provided details of when the system lapse has been noticed and rectified.

12. Summary of insurer submissions:

Due to some gap in our systems since 2013, for certain cases, such commissions were paid on ported policies. The systems have been set right and commissions are not paid on ported health policies. The commission paid wrongly to intermediaries has now been reversed in our books of accounts and adjusted against their dues, wherever possible. Till date, an amount of Rs.6842.73 has been adjusted till date out of the amount paid to intermediaries for such ported policies. The company is in the process of recovering the commission either by adjusting it against future payments (wherever the intermediaries are continuing) or recovering the payments in other cases and the details/status would be informed periodically on the amount recovered. The details of commission paid on ported policies are as given below:



Financial Year	Number of policies	Commission paid (in Rs.)
2012-13	12	3,521
2013-14	5	5,744
2014-15	485	5,90150
2015-16	799	9,66,408
2016-17	477	6,04,028
2017-18	404	4,72,171
2018-19 (till Nov' 2018)	462	3,09,658

The error in the system has been noticed and rectified from November, 2018. There are no instances where commission is paid for ported policies after system modification. The process of system check has now been made part of our internal audit program.

13. Decision on Charge no.2

The Authority vide clarification 6 of circular ref.no.IRDA/Hlt/Misc/Cir/259/12/2011 dated 1st December, 2011, in regard to the portability circular dated 9th September, 2011, has clearly communicated to all non life insurers that *"As portability is an option given directly to the insured, there is no role of an intermediary and, hence, no commission shall be payable by an insurer to any intermediary in the year of porting"*.

The Regulations prohibiting payment of commission to an intermediary on the acceptance of a ported policy has been notified by the Authority on 16th February, 2013. Even after notifying the Health Regulations, the insurer continued paying commission to intermediaries on ported policies.

The non compliance to Regulations by paying commission on ported health policies was observed during the on-site inspection in March, 2017 on examination of sample cases and the same was brought to the notice of the insurer vide point 27 of the exit report dated 24th March, 2017 and also in the final report shared with the insurer vide letter dated 10th January, 2018.

Thereafter insurer in its response to the inspection observation in February, 2018 has informed that *'Due to some in gap in our systems, for certain cases, such commission were paid on ported policies. **The systems have been set right and commissions are not paid on ported health policies**'*.

On noticing the insurer submission being without the date from when the system was rectified, the company was further asked vide email dated 7th May, 2018 to confirm:

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- That the commission paid wrongly on health ported in policies has been recovered and to provide policy wise recovery details of all such cases.
- To inform during which period, the system lapse was existing allowing the commission on ported policy and when the system error has been rectified.



- *To provide a screen short of a ported policy issued after the system rectification in support of submission on not releasing commission. “*

In response, the insurer vide e-mail dated 7th June, 2018 has stated that

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- *The commission paid wrongly to intermediaries have now been reversed in our books of account. We are now in the process of recovering the excess commission either by adjusting it against future payments (wherever the intermediaries are continuing) or recovering the payments in other cases. The details of recovery of such cases would be sent separately.*
- *The lapse is existing since issuance of IRDA (Health Insurance) Regulations, 2013. **The system has now been rectified.***
- *We would send the screen shot after we get any new proposal for portability of health insurance policy. “*

Taking note of the insurer's non submission of the system rectification date, the insurer has been issued show cause notice.

In response to show cause notice, the insurer vide letter dated 6th August, 2019 informed that the system has been rectified from November, 2018 and an amount of Rs.6842.73 paid to intermediaries on such ported policies has been recovered.

From the response to the show cause notice, it is noticed that even after the insurer's submission in February, 2018 on informing rectification of system and again confirming the same in its email dated 7th June, 2018, insurer continued the practice of paying commission on Health ported policies and has paid the commission of Rs.3,09,658 on 462 such ported in health policies during FY 2018-19 itself till November, 2018. Further, in the matter of recovery of the commission/brokerage wrongly paid to intermediary, the insurer informed that they recovered the commission only on the sample of five (5) policies which were indicated in the Inspection observation, but is silent on the other 2639 cases of wrong commission payment out of total 2644 cases, as informed by insurer in its submission to the show cause notice.

All the above clearly indicate the lack of internal control/audit mechanism at insurer's office in

- identifying the system errors/gaps for efficient functioning,
- not acting on system gaps, even after bringing such gaps to its notice thereby leading to non-compliance to the Regulations and further,
- giving incorrect information/confirmation in its submissions made to the Authority.

The violation was brought to the insurer's notice during the on-site inspection, in the exit report shared with the insurer, in the final report forwarded on 10th January, 2018 and as per insurer's confirmation, the non compliance to the Regulations continued till November, 2018. Even if it is assumed that the system is rectified on 1st November 2018, the violation of insurer has continued for 586 days from the date of bringing to its notice through exit report and for 2001 days from the date of notifying the Regulations i.e., 16/02/2013 to 01/11/2018.



In exercise of the powers vested in the Authority as per the provisions of Section 102(b) of the Insurance Act, 1938, the Authority hereby imposes a penalty of **Rs.1,00,00,000/- (Rupees ONE CRORE only)** for the violation of Clause 15 of schedule I of IRDA (Health Insurance) Regulations, 2013 which clearly specifies that 'no commission shall be payable to any intermediary on the acceptance of a ported policy'. The general insurer is also directed to ensure recovery of commission paid to intermediaries on ported policies and wherever recovery is not possible, the same shall be debited to Shareholders' account.

14.Charge no.3

Violation of Circular no.IRDA/NL/Cir/ F&U/003/01/2011 dated 6th Jan, 2011, circular no.048/IRDA/De-tariff/Dec-07 dated 18th Dec, 2007 and Guideline 1, 3(ix), 8 & 11 of File and Use guidelines ref. 021/IRDA/F&U/SEP-06 dated.28.9.2006 by offering rates/discounts other than those filed & approved by IRDA.

15.Inspection observation:

On examining 5 sample cases of SFSP policies, it is observed that insurer rated the risks below the rate filed with the Authority by giving extra discount in premium.

16.Summary of insurer submissions:

The policies have been underwritten with rates based on our past experience and the premium discount is decided with due consideration on exposure based rating blended with company experience and only after due approval from delegated authorities. All such cases/quotes are recommended by underwriters, approved by Managing Director and placed before the Board of Directors on a periodical basis.

17. Decision on Charge no.3

It is noted from the insurer's submission that the rating of the risks was done on burning cost of the risks based on the company's own past experience and also under intimation to the Board. The rating of all the 5 sample policies examined were issued by the insurer prior to the Authority circular dated 12th November, 2014 wherein the Authority has allowed similar procedure of rating the risks thereby allowing insurers to rate risks after considering the industry burning cost of a particular segment and insurer's own past experience. Hence, the submission is noted and no charge is pressed. The insurer is advised to be careful henceforth in rating of risks and to ensure compliance to the rating structure filed with the Authority under the F&U guidelines and to the Authority circular ref.no.IRDA/NL/Pro/115/05/2017 dated 5th May, 2017.



18. **Summary of Decisions:**

Charge No.	Violation of Provisions	Decision
1	1) Para 9.6(ii), 9.9 and 9.12 of Outsourcing guidelines circular no.IRDA/Life/Cir/ GLD/013/02/2011 dated 1 st February, 2011. 2) Circular no. IRDA/CAD/Cir/Agn/137/08/2010 dated 25-08-2010 3) File & Use guidelines	Penalty of Rs.1 lakh and Warning
2	1) Clause 15 of schedule I of IRDA (Health Insurance) Regulations, 2013 which clearly specifies that 'no commission shall be payable to any intermediary on the acceptance of a ported policy'. 2) Clarification 6 of circular ref.no.IRDA/HLT/Misc /Cir/259 /12/2011 dated 01-12-2011.	Penalty of Rs.1 crore and direction
3	File & Use guidelines	Advisory

19. **Further,**


i. The penalty of Rs.1,01,00,000/- (**Rupees One Crore one lakh only**) shall be remitted by the insurer through NEFT / RTGS (bank account details will be communicated separately) within a period of 15 days from the date of receipt of this Order. An intimation of remittance of penalty shall be sent to Shri Prabhat Kumar Maiti, General Manager (Enforcement), IRDAI, Sy.no.115/1, Financial District, Nanakramguda, Hyderabad- 500032.

The Order shall be placed before the Board of the general insurer in the upcoming Board Meeting and the general insurer shall provide a copy of the minutes of the discussion.

ii. The general insurer shall submit an Action Taken Report to the Authority on direction given within 90 days from the date of this Order.

20. If the general insurer feels aggrieved by this Order, an appeal may be preferred to the Securities Appellate Tribunal as per the provisions of Section 110 of the Insurance Act, 1938.

Place: Hyderabad
Date: 22-10-2019


22/10/19
(Dr. Subhash C. Khuntia)
Chairman