Insurance & Reinsurance - India

Onwards and upwards? Cabinet approves increase in foreign ownership cap

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Author

Neeraj Tuli

On October 4 2012 the Cabinet approved an increase in the cap on foreign investment in the insurance and pension sectors from the existing 26% to 49%. The decision clears the way for the measure to be considered by Parliament in its winter session. However, whether the increase will clear the political and legislative obstacles in its path remains uncertain.

Sector reform

The Cabinet's approval of this increase is the latest in a chain of events spanning more than 20 years. The government's 1991 industrial policy signalled the advent of a liberalised Indian economy and paved the way for private participation in the insurance sector. In 1993 the government set up the Malhotra Committee to review the structure of the regulation and supervision of the insurance industry, and to suggest reforms. In a 1994 report the committee recommended, among other things, that the private sector be permitted to enter the insurance industry and foreign insurers be allowed to enter the Indian market by forming joint venture companies with Indian partners.

Cap on foreign ownership

There was considerable delay in actioning the Malhotra recommendations and particular debate over the correct level of the cap on foreign ownership. In 1999 the Insurance Regulatory & Development Authority (IRDA) was set up as an autonomous body to regulate the insurance industry and develop the insurance market. In August 2000 private competition was permitted with a foreign ownership cap of 26%.

The 26% cap was intended to be temporary. In the 2004 budget the then-finance minister, P Chidambaram, announced that the cap would be raised from 26% to 49%. This was strongly opposed by a number of political parties and the coalition government found it politically difficult to push through the increase. The Insurance (Amendment) Bill 2008 was finally introduced in the *Rajaya Sabha* (the upper house of Parliament), seeking to "raise the foreign equity in Indian insurance companies from 26% to 49%". Other key changes proposed in the bill included:

- allowing overseas reinsurers to open branch offices to carry out reinsurance business in India;
- allowing Lloyds to enter the market through a joint venture with Indian partners and its syndicates to operate through reinsurance branch offices;
- lowering the capital requirements for standalone health insurers to Rs50 million (approximately $9 million) from Rs1 billion (approximately $180 million);
- deleting the provisions that give agents a statutory right to receive commission on the cessation of an agency; and
- ending the limits on insurers' management expenses.

The *Rajaya Sabha* referred the bill to a parliamentary committee. The committee issued a report in December 2011, in which it rejected the increase in the foreign investment limit. A period of speculation followed over whether the government would:

- press ahead with the bill, including the increase to 49%;
- push through the bill without the increase to 49%; or
- let the bill remain in abeyance until after the elections in 2014.

In the meantime, the constantly changing regulatory environment and general discontent with the pace of liberalisation had an adverse impact on economic growth in the insurance sector and in India generally, and on the perception of India worldwide. Reports indicated that foreign investors were looking for an exit route, withholding or refusing investment in existing ventures or delaying their plans to enter India. Some foreign investors withdrew from the market entirely. As a result, the government has decided to press ahead with the increase to 49%, thereby signalling (along with a number of other government measures) that India is again open for business.

Comment

The bill is expected to be put before Parliament in its 2012 winter session. However, its passage is unlikely to be smooth as there are voices of dissent from within both the ruling coalition and the opposition. The IRDA is supportive of the increase to 49%; its chairman recently pointed out that "unless we go for 49%, we will not have the kind of capital required to underpin the growth of [the] insurance industry". The finance minister has also made a case for the increase, pointing out that private insurers require a capital infusion to move forward and an increase in the foreign investment limit is a precursor to that infusion.

If the bill is passed, an inflow of fresh capital, an increase in the number of insurance joint ventures and faster development of the market are expected. For now, uncertainty remains and the industry must wait and see.

For further information on this topic please contact Neeraj Tuli at Tuli & Co by telephone (+91 11 2464 0906), fax (+91 2464 0904) or email (n.tuli@tuli.biz).