Mergers in general insurance sector: soon to be a reality

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On 9 February the Insurance Regulatory and Development Authority (IRDA) released an exposure draft of an order on Schemes of Arrangement and Transfers of Non-Life Insurance Business. In it the Indian insurance sector regulator sets out directions intended to cover all types of transfers of general insurance business including specifically, court-driven schemes of arrangements and amalgamations of general insurers under the Companies Act, 1956.

In this month's column we take a brief look at the process for transfer of business outlined in the exposure draft and some of the questions and concerns surrounding it.

Filling the void

The covering letter to the exposure draft states that it has been introduced since there is no explicit statutory framework under the Insurance Act, 1938, for amalgamation and transfer of non-life insurance companies. This gap, however, had previously been recognized by the legislative drafting committee and is sought to be remedied by the impending Insurance Laws (Amendment) Bill, 2008. This bill proposes to extend the statutory provision under section 35 of the Insurance Act, which is currently applicable solely to life insurance companies, to all insurance companies. Thereby these provisions will be extended to general insurers as well.

Complex and lengthy process

The directions envisage a multi-stage process involving multiple regulators for approving the transfer of a general insurance business. The key stages include: (a) the filing of a notice of intention by the transacting parties along with several supporting documents (such as financial reports and statements, an independent actuarial report and a draft scheme of arrangement which sets out the details of the proposed transfer); (b) a subsequent filing of an application with the IRDA (which can be filed only after two months from the date of the notice of intention); (c) the grant of an "in-principle" approval of the IRDA on the basis of the application and public announcements; (d) compliance with the process to obtain a high court order for the arrangement or amalgamation and the procurement of other regulatory approvals (e.g., from the Reserve Bank of India and the Foreign Investment Promotion Board); (e) a final IRDA approval to give effect to the amalgamation. This is all in all, a fairly complex and lengthy process.

Concerns galore

While the IRDA's move to introduce a framework for the amalgamation of private-sector general insurance companies is laudable, there appear to be several questions and concerns on the minds of market participants.

With the longstanding Insurance Laws (Amendment) Bill seeking to extend the framework under section 35 of the Insurance Act to general insurance companies, one wonders about the possible interplay between the exposure draft and the framework of section 35 in the event that the bill is passed. How will IRDA's directions co-exist with the amended section 35?

In its present form, the exposure draft appears to be a curious mix of the existing provisions of section 35 of the Insurance Act and the regulator's ingenuity. The provisions of section 35 work well in isolation. However, in the context of life insurance company mergers one feels that their application on an "as is" basis to general insurance companies, especially with the additional requirement to comply with the process under the Companies Act to obtain high court sanction, is bound to lead to a more cumbersome and long drawn process.

Insurers are also not completely convinced of the need for an independent actuarial report on the proposed transfer. Apart from the fact that there is likely to be a dearth of actuaries who are not professionally connected to the insurers involved, the very basis for requiring an actuarial report in the general insurance business (where the majority of risks are short-term in nature) has been questioned by industry players.

Lastly, the tone of the exposure draft conveys the impression that the IRDA may be stepping into what is clearly the high court's domain and perhaps also positioning itself to review the order of the high court. Given its unsavoury (albeit successful), experience with turf wars, the IRDA may as well clear the air on this issue, as it is not in anyone's interest to stir up a debate on jurisdictional issues.

What is certain is that the IRDA will have received a flood of comments by 22 February, which was the deadline for responding to the draft. It will be interesting to see how it reacts.

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