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Investment Market of Insurance Business: Does it Need more Attention in India?

SHEETAL SHARMA¹

ABSTRACT

The unforeseeable and uncertain events such as the coronavirus pandemic have enhanced the importance of the insurance industry and its growth in the coming years. This paper focuses on the insurance industry and how it has the potential to perform in the investment sector by involving investors in fundraising and insurers in continuing to further invest in assets for the operation and growth of the industry. It tries to draw a line between an insurance policy and an investment, arguing that an insurance policy is not an investment, and in today's emerging market of insurance products, it makes sense to invest in the insurance industry. It underlines and analyses the regulatory framework of investment, involving raising of capital through not only with equity shares but also from other forms of capital, investment by insurers in government securities, approved investments, and household finance, and lastly, investment by foreign investors with a welcome change of 100% FDI in Insurance Intermediaries. It attempts to underline the problems faced in the investment due to excessive norms on the foreign investors, less investment by insurers, obscured regulatory authority of insurance-cum-investment products, and the nature of these products to fall under the definition of securities. It tries to fill the gaps by concluding that the industry needs more attention in the capital market, in the protection of insurance investors and changes in the regulatory reforms and participation of investors in the industry will lead to the contribution of the industry in the investment market of India.

I. INTRODUCTION

A year of the pandemic has enhanced individual's awareness and perception about the importance of insurance in financial protection against uncertain losses and various other risks. Insurance as a financial product has always been recognized when there is a need to indemnify for the losses incurred and to reduce the risk of damages.

Since 2000 bought many private insurers in the dominated space of a large public sector, this industry has grown by innovation in insurance products, vibrant distribution networks, and targeted advertising and promotional campaigns by the insurers.

¹ Author is a student at Bennett University, India.

Hence, today's insurance industry, like other financial institutions such as banking and the stock market, is no longer important only to individuals who join the community to protect themselves from adverse consequences but has a major influence in ensuring long-term economic development in the financial market.²

This industry is a road full of potential due to increasing financial literacy and domestic savings yet in India, it is one of the least penetrated and untapped markets.³ This emerging insurance market needs more attention due to its growth in the coming years and it has a huge role to play in the investment where both households and insurers are the important players for raising funds and receiving higher returns to operate the industry.

Considering, on the one hand, the importance of insurance services provided in the world, full of uncertainties and risks, and, on the other hand, the need to raise more capital for insurers and to receive higher returns on the investments made by the insurers, it is mandated to highlight the regulatory authority Insurance Regulatory and Development Authority of India (IRDAI) and the regulatory framework of the investment under the Insurance Act, 1938 and IRDAI Act, 1999 and others as well as the challenges it is facing.

Concerning this, much less is known about the potential of investment in the insurance sector, and this paper attempts to fill this gap by following objectives:

1. To study the Insurance sector for Investments.
2. To find out the Benefits of investing in the Insurance sector.
3. To analyze the regulatory framework of investment in the insurance sector
4. To know and highlight the issues in investing in the insurance sector.

II. INSURANCE COMPANY AND INVESTMENT MARKET

The insurance business in this paper consists of life and general including health and re-insurance insurers. An insurer is defined under section 2(9) of the Insurance Act, 1938 as those individuals or unincorporated bodies of individuals or body corporate of individuals incorporated under the law of any other country carrying on the business of the insurance in India.⁴ In laymen's terms, the one doing the business of the insurance is called insurers. For understanding the players of the investment market, the investors here are the public for raising

²Piljan Ivan, Cogoljević Dušan, Piljan Tatjana, ROLE OF INSURANCE COMPANIES IN FINANCIAL MARKET, FACULTY OF BUSINESS ECONOMICS AND ENTREPRENEURSHIP, *International Review* 2015.

³ Ray, Saon & Thakur, Vasundhara & Bandyopadhyay, Kuntala, INDIA'S INSURANCE SECTOR: CHALLENGES AND OPPORTUNITIES, (July,2020).

⁴ Section 2(9), The Insurance Act, 1938.

capital and insurance companies for further investment, the insurance company is the insurance company, the insurance intermediaries are brokers, agents, surveyors, administrators, and the investment categories are listed in the following sections.

A) Insurance Company: It is defined under section 8 of the Insurance Act, 1938, which provides that it is an insurer being a company, association, or partnership. Further, an Indian Insurance Company is defined under section 7A of the same act, which means a company which is formed and registered under the Companies Act, 1956, which has aggregate holdings of equity shares less than 49% paid-up capital by a foreign company or by its subsidiary company and whose sole purpose is to conduct the life insurance, general insurance, and reinsurance business. These insurance companies through the constituted contract with the policyholders c.⁵ Thus, the overall profitability of these companies depends on the premiums they receive but the premium cannot operate the business of serving the policy, so they also make investments.⁶

B) Investment Market: It is a market that makes it possible to raise capital and funds for the operation of a business and enables those who have excessive funds to earn more by investing.⁷ It mobilizes domestic savings and enables successful companies to take over companies that perform poorly. It also enables external financing for the development and expansion of the company.⁸ Concerning the insurance sector, insurance is the transaction of giving insurance coverage when it is claimed and taking premiums in return, due to time lag between when the premium collected and paid out in the forms of claims, operating expenses, and taxes, these companies invest the money collected from premium and receive the investment income with high returns.⁹ Thus, the financial market comes into play where the insurance companies either raise more funds from it or invest in the stock market, and consequently, there is a relationship of the volatility of the stock market with the income of the insurance companies.¹⁰

C) Insurance Intermediaries: It is defined under section 2(f) of the Insurance Regulatory and Authority of India Act, 1999, these are individuals who are brokers, reinsurance brokers,

⁵ W. S. Holdsworth, *Early History of the Contract of Insurance*, 17 COLUM. L. REV. 85(1917).

⁶ Irem Hussaine, Prof. Bashir Ahmad Joo, DETERMINANTS OF PROFITABILITY OF LIFE INSURERS IN INDIA- PANEL EVIDENCE, *International Journal of Management Studies*, 6(7), pp.58-65.

⁷ Supra note 1.

⁸ Ibid.

⁹ Sunder Ram Korivi and Monita Joshi-Khamkar, INVESTMENT PRACTICES OF LIFE INSURANCE COMPANIES IN INDIA: THE QUEST FOR A COMPLIANT PORTFOLIO. INSURANCE MARKETS AND COMPANIES, 5(1), *Journal of Insurance markets and Companies*, (August 19, 2014).

¹⁰ Wani, Arif Ahmad, and Ahmad, Showket, RELATIONSHIP BETWEEN FINANCIAL RISK AND FINANCIAL PERFORMANCE: AN INSIGHT OF INDIAN INSURANCE INDUSTRY, (November 1, 2015).

insurance consultants, surveyors, and loss assessors. These individuals assist insurance companies in selling their insurance products to the customers without holding policyholder's monies. However, surveyors and third-party administrators are not involved in marketing the business, surveyors assess the loss and administrators provide services in health insurance respectively but not in marketing the business.¹¹

They act as a link between insurance firms and their customers. They have a distinct role to play in the servicing of the policy, both in selling it and claiming it. They make the necessary disclosures and keep the two parties in the loop to maintain transparency.¹² They are licensed and regulated by the IRDAI under different regulations enacted according to their functions.¹³

D) Investment categories: According to the Investment-master circular of IRDAI (Investment) Regulations, 2016, the investment categories are as follows:¹⁴

Equity shares through IPO, Reverse Repo in Government Securities and Bonds, Mutual funds including exchange-traded funds, Assets backed securities, Alternative investment fund, Debt securities, other specific bonds/ Non-convertible Debentures, and Derivatives.

III. INVESTMENT IN INSURANCE SECTOR

Investment in the insurance sector or business is concerned with raising funds to run and operate the business. The application of insurance funds is intended for expenditure or payment of claims. The business requires to generate more funds and profit to cover the total expenditure and expand the business.¹⁵

The standpoint of this paper is not to confuse that an insurance policy is an investment. Insurance is one pillar of personal finance along with banks and investments. Insurance policy is to be purchased to protect from unforeseeable risks to mitigate such uncertainty and it cannot offer a return to the policyholder during the tenure.¹⁶ Investment, on the other hand, is described

¹¹Handbook of Insurance Intermediaries, IRDAI. Available at <https://www.policyholder.gov.in/uploads/CEDocuments/Intermediaries%20Handbook.pdf>

¹² Ibid.

¹³ Insurance Regulatory and Development Authority (Insurance Brokers) Regulations, 2002, Insurance Regulatory and Development Authority (Licensing of Individual Insurance Agents) Regulations, 2000 and the Insurance Regulatory and Development Authority (Licensing of Corporate Agents) Regulations, 2002, IRDAI (Third Party Administrators-Health Services) Regulations, 2016, IRDAI (Insurance surveyors and loss assessors) Regulations, 2015.

¹⁴ Master Circular-Investment, IRDAI(Investment) Regulations, 2016, (May 2017). Available at [http://www.dhc.co.in/uploadedfile/1/2/-1/IRDAI%20-%20INVESTMENTS%20-%20MASTER%20CIRCULAR%20-IRDAI%20\(INVESTMENT\)%20REGULATIONS,%202016.pdf](http://www.dhc.co.in/uploadedfile/1/2/-1/IRDAI%20-%20INVESTMENTS%20-%20MASTER%20CIRCULAR%20-IRDAI%20(INVESTMENT)%20REGULATIONS,%202016.pdf)

¹⁵ Perpetua, Ehiogu & Theophilus, Aguguom. (2018). CONTRIBUTION OF INSURANCE INVESTMENT TO THE OVERALL GROWTH OF INSURANCE INDUSTRY IN NIGERIA, (August 2018).

¹⁶ EXPLAINED: WHY INSURANCE IS NOT AN INVESTMENT. (February 9, 2021) Available at <https://www.financialexpress.com/money/insurance/explained-why-insurance-is-not-an-investment/2190807/>

as raising funds for capital and from the point of view of insurance managers, converting the funds of premiums into income in the normal course of business, with a return anticipated either immediately or later.¹⁷

The robust growth of the life insurance business is the explanation of the underlying market performance of the insurance companies.¹⁸ One of such insurance products is in the life insurance business called unit-linked insurance products. It has a combination of a Term insurance policy and investments. The insurance coverage is on the death and the investment is made by the company on behalf of the policyholder.¹⁹ However, the risk of the investment is born by the policyholder.²⁰ Thus, the emerging market of insurance-cum-investments such as endowment plans, and moneyback-plans creates a new opportunity for the investors seeking to benefit from the growth in the financial sector.

Hence, in today's time with the growing size of insurance companies due to buying insurance products, investing in the insurance business by the investors has a lot to benefit from adding this business to their portfolio.

Benefits of investing:

- Insurance companies receive funds from policyholders for further investment. Thus, insurance companies should be used by the investors as an institution to invest most of the savings.
- Insurance companies are also financial intermediaries as they take sources from one sector and invest the source in another sector. They place invested assets of the policyholder into series of investments to raise more funds.
- These companies also generate certain profits from the premium due to the time lag between the collected premium and paid out claims and taxes. Thus, chances of affecting with current losses are less.
- The insurance products offered by the insurance companies are long-term in nature with defined maturity. Thus, the investors seeking long-term growth in investments can invest in companies that have captured the potential growth.

¹⁷ Ibid.

¹⁸ WHY INVESTING IN INSURANCE BUSINESS MAKES SENSE, (18 November 2019). Available at <https://www.newindianexpress.com/business/2019/nov/18/why-investing-in-insurance-biz-makes-sense-2063232.html>

¹⁹ John Varghese, UNIT LINKED INSURANCE PRODUCTS AND REGULATORY TANGLE, ((2011), SCC Online. Available at <http://www.sconline.com/DocumentLink/483YVou7>

²⁰ Ibid.

- Investment of funds from the collected premiums by the insurers has two major impacts: Increases profits and helps companies in lowering the premium amounts, making the policy more attractive.
- Investment by insurers in government securities and bonds yields a higher return in the long term and ensures governments in paying the interest and principal.²¹

IV. REGULATORY FRAMEWORK OF INVESTMENTS IN INSURANCE SECTOR

1. Raising capital through Capital Market: According to section 6 of the Insurance Act, 1938, the company can issue capital of 100 crores in life and non-life insurance business under the provisions of the companies Act, 2013 and the securities exchange board of India Act, 1992.

Further in the exercise of the powers conferred by Section 114A read with Section 6A of the Insurance Act, 1938 and sections 14 and 26 of the IRDAI 1999, the issuance of capital by life insurance companies is regulated by the IRDAI (Issuance of Capital by Indian Insurance Companies transacting Life Insurance Business) Regulations, 2015, and section 3 mandates that written prior approval from IRDAI.

The same is mandated for general insurance, health insurance, and re-insurance under section 3 of the IRDAI (Issuance of Capital by Indian Insurance Companies transacting other than Life Insurance Business) Regulations, 2015.

This also implies that the securities such as shares, bonds, debentures, derivatives, and other marketable securities defined under section 2(h) of the SEBI Act and approved securities under section 3 of the Insurance Act, 1938 are permitted to be issued as instruments for investments in insurance products after the approval of the authority.²² Further, in 2015, the IRDAI amended section 6A of the Insurance Act, 1938 which permitted insurance companies to issue other forms of capital and notified the new regulation called IRDAI (other forms of Capital) Regulations, 2015, which lay down the other forms of capital as preference share capital and subordinated debts.

2. Investments by insurers: According to section 114(2)(i) read with section 27A, 27B, 27C, 27D, and 28 of the Insurance Act, 1938 and IRDAI Master Circular of Investments²³, the

²¹ Frequently Asked Questions, Government securities market in India. Available at <https://m.rbi.org.in/Script/s/FAQView.aspx?Id=79#2>

²² Section 6, The Insurance Act, 1938.

²³ Supra note 13.

IRDAI exercised its power and enacted IRDAI(Investment) Regulations, 2016 which highlights the investment criteria for the insurers.

According to regulation 5 of the IRDAI(Investment) Regulation, the investment criteria for life insurance business are:

Sr. no	Type of Investment	% to funds as under Regulation 4(a)
1.	Central Government securities	≥25%
	Central and state government securities	≥50%
2.	Approved Investments	≥50%
	Other investments approved by the directors and ratified by IRDAI	≥15%
3.	Household Finance and infrastructure	≥15%

According to regulation 8 of the IRDAI(Investment) Regulation, the investment criteria for general insurance business are:

Sr. no	Type of Investment	% to funds as under Regulation 4(a)
1.	Central Government securities	≥20%
	Central and state government securities	≥30%
2.	Approved Investments	≥70%
	Other investments approved by the directors and ratified by IRDAI	≥15%
3.	Household Finance and infrastructure	≥15%

3. Investment by foreign companies: The 2015 Amendment in the insurance sector was a move to liberalize the insurance sector as it increased the foreign direct investment in

insurance companies from 26% to 49%.²⁴ Due to unfair parity between the Insurance companies and insurance intermediaries as the latter does not have the policyholder's monies, the stakeholders represented that FDI in intermediaries under Rule 9 of the Indian Insurance Companies (Foreign Investment Rules), 2019 should not be capped with 49%.²⁵ Thus, in 2019, the amendment to rule 9 was made which provided that the FDI in Insurance intermediaries is 100% under automatic route subject to the verification by IRDAI.²⁶ Further, The IRDAI also clarified that they do not have to comply with the Indian owned and control norms under the IRDAI (Guidelines on Indian owned and controlled), 2015 which necessarily required the insurance companies and intermediaries to maintain the ownership and control of Indian Residents.²⁷

V. PROBLEMS IN INVESTMENT

1. **Obscure Regulatory authority of insurance-cum-Investment products:** In 2010, the regulatory battle between SEBI and IRDA over the jurisdiction of ULIPS has obscured the regulation of insurance-cum-investment products. The order of SEBI's of banning the 14 companies for not registering ULIPS was overlooked by the introduction of the Joint committee through the Securities and Insurance Laws (Amendment and Validation) Ordinance, 2010.²⁸ It provided all the issues relating to the jurisdiction of all the regulators (SEBI, IRDAI, Reserve Bank of India, Pension Fund Regulatory and Development Authority) will be reconciled by the administrative body comprised of the Minister of Finance, Secretary to the Ministry, and the Chairman of the respective regulatory bodies.²⁹

This mechanism had an impact on investors that would make every investor in today's emerging market take a step back from investing in the insurance business. The Board for the protection of investors' interests is the SEBI, which also gives investors the right to educate in terms of financial product and transparency,³⁰ while the objective of the IRDAI is to protect

²⁴ The Insurance Law (Amendment) Act, 2015.

²⁵ Subhangi Pathak, Priya Misra, 100% FDI IN INSURANCE INTERMEDIARIES: A WELCOME CHANGE, (October 3, 2019). Available at https://www.mondaq.com/india/insurance-laws-and-products/850494/100-fdi-in-insurance-intermediaries-a-welcome-change#_ftn1

²⁶ Indian Insurance Companies (Foreign investment) Amendment Rules, 2015.

²⁷ Guidelines on Indian owned and controlled, (October 19, 2019). Available at https://www.irdai.gov.in/ADMINCMS/cms/frmGeneral_Layout.aspx?page=PageNo2644&flag=1

²⁸ John Varghese, UNIT LINKED INSURANCE PRODUCTS AND REGULATORY TANGLE, ((2011), SCC Online. Available at <http://www.sconline.com/DocumentLink/483YVou7>

²⁹ The Securities and Insurance Laws (Amendment and Validation) Ordinance, 2010. Available at [https://www.prsindia.org/billtrack/the-securities-and-insurance-laws-amendment-and-validation-bill-2010-1221#:~:text=The%20Securities%20and%20Insurance%20Laws%20\(Amendment%20and%20Validation\)%20Bill%2C%202010,Ministry%3A&text=This%20Bill%20clarifies%20that%20Unit,regulate%20other%20such%20hybrid%20products.](https://www.prsindia.org/billtrack/the-securities-and-insurance-laws-amendment-and-validation-bill-2010-1221#:~:text=The%20Securities%20and%20Insurance%20Laws%20(Amendment%20and%20Validation)%20Bill%2C%202010,Ministry%3A&text=This%20Bill%20clarifies%20that%20Unit,regulate%20other%20such%20hybrid%20products.)

³⁰ Preamble, Section 11(f), The Securities Exchange Board of India Act, 1992.

policyholders and insurance companies.³¹ The effectiveness of this order is still not prevalent, as investors feel that SEBI's involvement in such products would have ensured the interests of investors. The order is therefore not justified because ULIPS or insurance-cum-investments are regulated by IRDAI and not by SEBI.

Therefore, the ordinance is not justified in why ULIPS or insurance-cum-investments are regulated by IRDAI and not SEBI.

2. **Insurance-cum-investments products are securities or not:** The same ordinance also amended the definition of life insurance products and extended to include ULIPS in it and simultaneously excluded it from the definition of securities under SEBI Act.³² This also creates problems with the regulation under IRDAI as the nature of ULIPS or any coming innovative insurance-cum-investment cannot be ignored on the fact that they are more than insurance, it involves the nature of marketable and investing the hard monies of various investors into various assets classes which pose risks to the investors.³³ Thus, the ordinance is still not justified in why ULIPS or insurance-cum-investments are not considered as a collective investment scheme under section 2(b) read with section 11-AA of SEBI Act, 1992 and comes under the definition of securities.

3. **Less investment by insurers in bonds and mortgage-backed securities:** The large amount of investment made by the insurers is directed towards the central and state government's securities. Investment in corporate bonds, however, increases the rate of return and in mortgage-backed securities, there are longer maturity liabilities to invest in mortgage loans, which are less penetrated by Indian Insurers.³⁴

4. **Excessive norms for Foreign Investors:** The regulatory structure for foreign investors is moving in the right direction to encourage the participation of investors in the insurance business. However, the control of the companies should be in the hands of the Indian residents has left investors subjective, as they must adhere to Indian owned and controlled guidelines and change the existing joint ventures agreements to ensure adherence to guidelines.³⁵ Furthermore, in Insurance Intermediaries, the additional requirement of the key management

³¹ Preamble, Insurance Regulatory and Development Authority of India Act, 1999.

³² Supra note 28.

³³ Legislative brief, The Securities and Insurance Laws (Amendment and Validation) Ordinance, 2010. Available at <https://www.prsindia.org/uploads/media/Securities/ulip%20ordinance-2.pdf>

³⁴ Rishabh Sharma, Abhinav Harlalka & Simone Reis, IRDAI: WALKING THE TALK?, (December 24, 2015). Available at https://www.nishithdesai.com/information/research-and-articles/nda-hotline/nda-hotline-single-view/article/irdai-walking-the-talk.html?no_cache=1&cHash=2d293c993b98eea6b087553f86da33d4.

³⁵ Ray, Saon & Thakur, Vasundhara & Bandyopadhyay, Kuntala, INDIA'S INSURANCE SECTOR: CHALLENGES AND OPPORTUNITIES, (July, 2020).

personnel and directors of an insurance company with a majority shareholding of foreign investors must be Indian residents. As a result of the strict adherence to numerous obligations, foreign investors lose interest, which can be a deciding factor in whether to invest.³⁶

VI. CONCLUSION

Investment in the insurance business is a cash-to-cash cycle, from premium collection to investment to claim settlement. The development and growth of the industry depend on the management of this cycle, where the investment remains an interchangeable tool to facilitate settlement of the claim. With the increasing purchase of insurance products by the public, this industry has developed and grown in the coming years, and every investor seeking to get a high return should add this business into their portfolio. Further, the emerging market with innovation in products like Insurance-cum-Investment products in the life insurance industry will lead to more changes in the way the industry operates and engages its customers.

The regulatory framework of raising capital, investment by insurers and foreign investors are reformed according to the changes the industry is adapting. The 2015 amendment has liberalized the industry for investment, in addition to equity shares the step of introducing the other forms of capital has permitted avenues of raising funds by insurance companies, and the guidelines of India owned and controlled have well balanced the interest of the domestic residents in the move of the liberalization.

With regards to the problems in the regulatory reforms of the investment in the insurance business, the nature of marketable of the insurance-cum-investments products cannot be ignored and it should fall under the definition of the securities so that they are tradeable in the capital market. The regulatory authority must be both SEBI and IRDAI would regulate the portion falling within their domain. The investment component of these products must seek registration from SEBI and the insurance component was to be governed by the IRDAI. It also suggests that the excessive norms on foreign investors are a determining factor for investment in India, so lack of certainty and ambiguity in the norms needs more clarification and improvement. The sole premium from the customers cannot operate the industry for a long period. Hence, the investment market of the insurance industry needs attention in the capital market, protection of insurance investors should also be recognized like other companies, more participation of investors for raising funds and participation of the insurers to invest the funds further to operate the industry and contribute to the economy. Therefore, the investment by the insurers should also go beyond the government securities and focus on the bonds and

³⁶ Ibid.

mortgaged securities. With the changes in the regulatory reforms and participation of investors in the industry, this business has full potential to contribute to the investment market of India.
