Free Look Cancellations of Health Insurance Policies

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On May 27 2009 the Insurance Regulatory and Development Authority (IRDA) issued a circular on free look periods, which are applicable to health insurance policies and other policies issued by life insurers that have a deferred coverage of risk. The circular mandates that health insurance policies must also provide a free look period and directs life insurers not to deduct a proportionate risk premium in cases where the policy is cancelled during this period.

A free look period is a recognised concept both in India and other parts of the world. It is regarded as a consumer-friendly provision that gives policyholders the chance to go through the fine print of the policy documents - something which they might not have considered doing at the time of signing the proposal form. Usually, customers can cancel policies only if they disagree with the terms and conditions of the contract. For long-term financial commitments (eg, life insurance policies), a free look period also gives the policyholder the time to assess the viability of his or her commitment. The rationale of a free look period lies in the fact that the majority of individual customers of these products are lay persons who might be unable to understand all the terms and conditions at a glance.

Regulation 6(2) of the IRDA (Protection of Policyholders' Interest) Regulations 2002 specifies that in respect of policies issued by a life insurer, the letter forwarding the policy to the insured must specify that he or she has 15 days from the date of receipt of the policy document to return the policy. Upon cancellation, the insured is entitled to a refund of the premium paid, but is subject to:

"*a deduction of a proportionate risk premium for the period on cover and the expenses incurred by the insurer on medical examination of the proposer and stamp duty charges*."

The May 27 2009 circular modified the applicability of this provision for "health insurance policies and other such policies issued by life insurance companies" where there is a "deferred coverage of risk". In such cases, since there is an "absence of risk cover" during the free look period, life insurers cannot deduct a proportionate risk premium if the policy is returned during the free look period. Failure to comply with this modification will make life insurers liable for action under the insurance rules and regulations.

Despite the circular preventing life insurers from deducting a proportionate risk premium, it is likely that medical examination expenses and stamp duty charges may still be deducted, as these aspects of Regulation 6(2) have not been made expressly inapplicable.

The circular does not define the kind of health insurance policy or the 'other such policies' to which it applies. However, the terms of the circular appear to apply to any policy issued by a life insurer in which there is a waiting period.

More interestingly, there is another direct indication from the IRDA that a life insurer may sell a pure health cover. This follows the IRDA's earlier guidance of April 2 2008, wherein it stated that:
"*Insurers are aware that a number of life insurance companies are offering health insurance products in a significant way. The premium underwritten towards some of the products could partially include benefits under section 80D of the Income Tax Act 1961 based on the approvals granted by the Authority.*"

Although the IRDA has, as a matter of practice, approved the pure health covers of various life insurers and has also made ancillary references to health covers issued by life insurers (eg, through the April 2 2008 circular), there has been no express guidance on the sale of health products by life insurers. In the overall context, particularly given the reluctance of insurers to cancel policies where the insured wishes to cancel for pure pricing issues, it would be interesting to ascertain the market's reaction to the circular going forward (ie, whether the terms of the circular need further clarification).

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