Insurance & Reinsurance

## Standardisation of ULIP Charges: Proposed Reforms

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The Insurance Regulatory and Development Authority has taken recent steps towards standardising the various charges applicable to unit-linked insurance policies (ULIPs). This update focuses on the authority's establishment of a panel of actuaries and the recommendations made by this panel for standardising and reducing the number of charges on ULIPs. ULIPs are structured to provide both life insurance protection and the option for policyholders to participate in capital and debt markets in a manner consistent with their risk appetite.

However, general market trends indicate that ULIPs are portrayed and pitched to prospective customers as investment products, rather than insurance products. Arguably, ULIPs are seen as a viable alternative to mutual funds for investment purposes. Despite criticism of these products (eg, the high charges involved), ULIPs reportedly continue to contribute to up to 60% of new life insurance premiums in the private sector. Reports suggest that even in light of the recent stock market meltdown, renewal premium has grown by 35%, owing primarily to a threefold increase in renewal premium on ULIPs.

In view of the penetration and popularity of ULIPs, as well as the level of complaints about the misselling of ULIPs and ambiguous charges, the authority has been issuing various guidance for regulating the design and sale of ULIPs. Initial guidance came by way of its ULIP Guidelines of December 21 2005, wherein it was specified that ULIPs must conform to the medium and long-term investment characteristics of ULIPs, and that one of the basic features of a ULIP should be a long-term nature (for further details please see "Unit-Linked Insurance Product Guidelines").

The ULIP guidelines also specified that insurers must use a uniform definition of policy charges under all their ULIPs in order to give customers a better and clearer understanding of the product. Further, upper limits must be specified for all charges other than premium allocation and mortality charges.
The authority has also issued further guidance, which is indicative of the changes it envisaged in response to, among other things, complaints about the misselling of ULIPs and ambiguous charges.

For example, in a circular of August 18 2007 insurers were told to phase out all their actuarial-funded ULIPs. The objective of this exercise was to allow customers to compare the ULIPs of different insurers. Further, in a circular of January 1 2008 insurers were told that the policy documents of all ULIPs issued to customers must provide information in the prescribed format on all charges to be paid and the amount available for investment in each policy year.

Despite this guidance, charges deducted from the premium collected from policyholders remain an area of uncertainty for customers. Further, in the absence of a standard structure for levying charges, the comparison of different ULIPs requires financial expertise. Multiplicity of costs and uncertain limits on charges make the comparison of ULIPs difficult even for financial experts. Uncertainty over charge structure often leads to confusion and, when compared with mutual funds which need not be long-term investments, may lead to the impression that ULIPs are very expensive. Given that the authority's regulations do not allow insurers to project a rate of return on ULIPs beyond 10%, an ambiguous cost structure may reflect poorly on the benefits of investing in ULIPs.

In order to standardise ULIP charges, in July 2008 the authority established a panel comprising the actuaries of various life insurers with the mandate to reduce the number of charges, create single standard definitions for each charge and standardise the expression of charges. According to press reports, this panel has recommended six specific categories of charge and has also specified that insurers cannot levy any other charges. These six categories are as follows:

- premium-related charge;
- withdrawal load;
- insurance charge;
- fund-related charge;
- policy administration charge (this charge is further segmented into three categories, of which an insurer can choose only one); and
- specific service charge.

At present, the authority is reviewing these recommendations. However, in the meantime it has also stated in press reports that it does not wish to get into micromanagement, and that it will instead recommend ceilings on individual charges and collective ceilings on all charges. Insurers will be free to determine the various charges within these limits.

The authority is also believed to be considering the issue of misselling ULIPs. Possible measures include mandating that the policyholder and agent sign a table of charges alongside the proposal form.
At present, it is not clear when the authority will issue its guidance on these issues or whether this guidance is likely to be implemented for existing customers as well. However, given the committee's recommendations, which suggest significant changes, and the complaints concerning misselling, it will be interesting to see how the authority plans to take this lucrative product forward.

***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***

**www.tuli.biz**