

Turf Wars II: Moving Towards a Super-regulator

May 25 2010

The initial expectation of a behind-the-scenes resolution of the dispute between the Securities Exchange Board of India (SEBI) and the Insurance Regulatory and Development Authority (IRDA) over which of them has jurisdiction over unit-linked insurance products (ULIPs) appears to have been overly optimistic. Public interest litigation has been commenced in the Mumbai and Allahabad High Courts, naming a number of life insurers as respondents. A reference has also been made to the Supreme Court.

SEBI had written to a number of life insurers effectively questioning the basis on which they had been selling ULIPs to the public in circumstances where they were not registered with SEBI (for further details please see "Turf wars: who regulates unit-linked products?"). The IRDA and the 14 life insurers in SEBI's notice had responded to the notice and it was felt that the issue would be resolved through private discussions between SEBI and the IRDA, with the involvement of the Ministry of Finance if necessary. This was proved wrong when on April 9 2010 SEBI issued an order to the 14 life insurers named in its initial notice in which it ruled that the ULIPs offered by them were in fact a combination of investment and insurance, and that the investment element was in the nature of mutual funds and accordingly could be offered for sale only after registration with SEBI.

SEBI directed the 14 life insurers not to:

"issue any offer document, advertisement, brochure soliciting money from investors or raise money from investors by way of new and/or additional subscription for any product (including ULIPs) having an investment component in the nature of mutual funds, till they obtain the requisite certificate of registration from SEBI."

On April 10 2010 the IRDA responded with a circular to all life insurers, which said that SEBI's action would "seriously jeopardise and adversely effect the interests of the policyholders and the interests of the insurers". The IRDA was concerned that SEBI's order would bring disruption to the insurance industry and concluded that compliance with SEBI's order would not be in the public interest. Therefore, the IRDA directed all 14 life insurers to continue as usual, including offering, marketing and servicing ULIPs, notwithstanding the SEBI order of the previous day. The IRDA simultaneously issued a press release to policyholders assuring them that the ULIPs that they hold are both safe and secure, and that the matters arising out of SEBI's orders would be addressed as quickly as possible.

On April 12 2010 the government finally intervened and announced that SEBI and the IRDA had agreed to restore and maintain the prior state of affairs until a court could decide which of them had jurisdiction over ULIPs. SEBI then issued a press release stating that its April 9 2010 order would be effective as of that date for all new ULIPs issued, but that it would not apply to ULIPs that were in existence before April 9 2010.

A flurry of petitions followed, with public interest litigation being filed in two Indian high courts and a SEBI petition being filed with the Supreme Court seeking to club together all public interest litigation on the ULIP issue. The Supreme Court accepted the petition and on April 28 2010 issued notice to the IRDA and the 14 life insurers. The Supreme Court has scheduled a hearing for July 8 2010.

The nine life insurers that were not the subject of either of SEBI's notices remain spectators. Among those nine life insurers is the Life Insurance Corporation (LIC) - the government-owned largest life insurer in the Indian market. In 2008/09, nearly a decade after the liberalisation of the Indian insurance market, LIC's market share was 61% measured by first-year premium income and 70% measured by the number of policies sold. Accepting that these percentages do not differentiate between ULIP and other product premiums, it is fair to say that the bulk of the market is not subject to SEBI's ban on new ULIPs from April 9 2010, even though the products sold by these nine life insurers are in substance little different from the ULIPs sold by the 14 life insurers that were the subject of SEBI's order.

In the meantime, the IRDA appears to be positioning itself for the Supreme Court hearing on July 8 2010. SEBI had made the point that certain life products were pure investment plans in that they offered no life cover. In an IRDA Circular of May 3 2010 it barred life insurers from selling pension plans that do not include life cover. There are several such products in the market and, because all products need to be agreed by the IRDA in advance, these products have been sold with the IRDA's approval.

In terms of what the Supreme Court might decide, one of the judges reportedly made an interesting aside to the effect that what may be needed is a "super-regulator". That sentiment has been expressed by others - for example, the finance minister in his 2010 Budget Speech. If there is to be a super-regulator, there will be reorganisation at both the SEBI and the IRDA, as well as other regulatory bodies, such as the Pension Fund Regulatory Authority.

Yet, where is the consumer in all of this? Figures on the sale of ULIPs as a result of the tussle between the IRDA and SEBI are not yet out, but it is feared that the negative publicity surrounding the amount of commission paid on ULIP sales may have a negative impact on sales growth.

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