

IRDAI issues guidelines on 'Indian owned and controlled'

November 10 2015 | Contributed by [Tuli & Co](#)

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Background

The insurance sector has witnessed sweeping changes in its regulatory regime since the beginning of 2015. These changes commenced with the passage of the Insurance Laws (Amendment) Ordinance in December 2014, which was later enacted as the Insurance Laws (Amendment) Act 2015. Arguably, the most significant change introduced by the amendment act was the increase in the permissible foreign investment limit in Indian insurers from 26% of the paid-up capital of such companies to 49%, provided that the Indian insurers were 'Indian owned and controlled'.

As a first step to providing a framework for implementation of the increased foreign investment limit, the Ministry of Finance issued the Indian Insurance Companies (Foreign Investment) Rules 2015 on February 19 2015. The rules provide that the Foreign Investment Promotion Board must approve any foreign investment beyond 26%, up to the new limit of 49%. The rules also clarify that the increased foreign direct investment limit applies to insurance intermediaries, in accordance with the terms and conditions set out therein. In addition, the Department of Industrial Policy and Promotion issued Press Note 3/2015 on March 2 2015, which amended the Consolidated Foreign Direct Investment Policy in order to ensure that it was uniform with the rules.

Guidelines

The most recent addition to the regulatory regime governing foreign investment in Indian insurers are the guidelines on 'Indian owned and controlled' issued by the Insurance Regulatory and Development Authority (IRDAI) by way of an October 19 2015 circular. The guidelines apply to Indian insurers and insurance intermediaries. The salient features of the guidelines are as follows:

- The guidelines have provided some much-needed clarity on the meaning of 'Indian control'. The term 'control' has been defined (in the amendment act) to include the right to appoint a majority of the directors or control management or policy decisions, including by virtue of shareholding or management rights or shareholders' agreements or voting agreements. In this regard, the guidelines reiterate that control can be exercised by virtue of any of the following:
 - shareholding;
 - management rights;
 - shareholders' agreements;
 - voting agreements; or
 - any other manner outlined in the applicable laws.
- The majority of the board of directors – excluding independent directors – must be nominated by the Indian promoters and investors.
- Key management personnel – including the chief executive officer (CEO) and the principal officer – must be appointed by the board of directors or by the Indian promoters and investors. Foreign investors may nominate a key management person (excluding the CEO), but the board of directors must approve the nominee.

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- Control over significant policies should be exercised by an appropriately constituted board of directors.
- If the chair of the board of directors has a casting vote, he or she must be nominated by the Indian promoters and investors.
- A valid quorum for a board meeting will be constituted with the presence of a majority of the Indian directors.
- The CEO and chief compliance officer must file an undertaking with the IRDAI confirming compliance with the 'Indian owned and controlled' criteria set out in the guidelines.

Comment

While the guidelines have provided some much-needed clarity on the interpretation of the term 'Indian controlled', substantial subjectivity in this regard still exists. It is clear that the IRDAI requires Indian promoters and investors to exercise control over the composition of the board of directors of Indian insurers and insurance intermediaries. However, the nature of shareholders' agreements, management rights and voting agreements which will be considered as exercising 'control' remains to be seen. Whether typical joint venture agreements – which provide foreign investors with a range of veto rights in relation to the operation and management of companies – will need to be revisited, renegotiated and amended is unclear.

Another aspect which requires the IRDAI's clarification is exactly how the 49% foreign investment limit will be calculated. The insurance industry is waiting for the amendments to the IRDAI (Registration of Indian Insurance Companies) Regulations 2000 to be approved and come into force.

Thus, while the guidelines shed some light on certain grey areas surrounding the recent regulatory changes in the insurance sector, further regulatory clarity is needed. Further, certain aspects may be clarified only through practice and the regulator may need to adopt these practices in the future.

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