INSURANCE - INDIA

New guidelines on investment by private equity funds in insurers

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Introduction

By way of a June 10 2016 order, the Insurance Regulatory and Development Authority of India (IRDAI) set up a committee to evaluate the risk-based capital approach and market-consistent valuation of liabilities of Indian insurance business. The committee's report, released on July 17 2017, noted that after almost 15 years of promoter-run business (almost all existing entities are joint ventures with foreign companies), the Indian insurance industry is still dominated by government-owned public sector companies, and private insurance players in India are largely owned by well-established businesses.

However, the IRDAI has recently been receiving requests to allow private equity funds to acquire majority stake in Indian insurers. In response to such requests from private equity funds, venture funds and alternate investment funds, the IRDAI released the IRDAI (Investment by Private Equity Funds in Indian Insurers) Guidelines 2017 on December 5 2017, to facilitate and regulate private equity funds' investment in insurers as investors and promoters.

Highlights and takeaways

The guidelines apply to unlisted Indian insurers and private equity funds that have invested in unlisted insurers.

The guidelines allow for private equity funds to invest either directly in Indian insurers in the capacity of an investor or to invest through a special purpose vehicle (SPV) in the capacity of a promoter in the insurer.

A 'private equity fund' has been defined under the guidelines to include an alternate investment fund as registered with the Securities and Exchange Board of India or a fund specifically formed for investment in one or more entities by one or more persons. An 'SPV' is defined as a company registered under the Companies Act 2013 or a limited liability partnership formed under the Limited Liability Partnership Act 2008 the purpose of investment in an insurer as an investor, a promoter or both.

Foreign investment in such private equity funds will be determined in accordance with the guidelines issued by the Department of Industrial Policy and Promotion from time to time.

The guidelines stipulate that the minimum shareholding by promoters or the promoter group must be maintained – at all times – at 50% of the paid-up equity capital of the insurer. However, this requirement will not apply to a company where the present holding of the promoters is less than 50%. In such cases, the present holding of the promoters will be considered as the minimum holding.

The investment by a private equity fund in an insurer must meet the fit and proper criteria prescribed by the IRDAI.

Where a private equity fund invests directly in the insurer, the fund cannot hold more than 10% of the paid-up equity share capital in the insurer. Further, in such a scenario, all Indian investors, including private equity funds, cannot jointly hold more than 25% of the paid-up equity share capital of the insurer.

Where a private equity fund invests in an insurer through an SPV in the capacity of a promoter, it cannot leave at will. The guidelines stipulate a five-year lock-in period for an SPV which invests in the insurer and the investors of the SPV. However, the lock-in period will not apply to shareholders of the SPV which hold less than 10% of the SPV's capital.

Induction of new shareholders into the SPV by issue of fresh shares beyond 25% will require prior approval from the IRDAI.

A private equity fund through an SPV cannot be a promoter for more than one life insurer, general insurer, health insurer and reinsurer. Further, the SPV must provide an undertaking to subscribe to the rights issue of the insurer. The post-lock-in period divestment plan, preferably made through an initial public offering in accordance with the relevant regulation applicable for such divestment, must be submitted by the SPV.

In addition to the requirements set out under the guidelines, it has been expressly clarified that private equity funds must continue to comply with the applicable provisions of, among other things, the IRDAI (Transfer of Equity Shares of Insurers) Regulations 2015 – which govern the transfer of equity shares in insurers – and the guidelines on Indian owned and controlled, as issued by the IRDAI.

Comment

The guidelines have opened more avenues for Indian insurers to obtain capital and are therefore a step in the right direction to augment private equity investment in the insurance sector. The move appears to have been welcomed by the industry, as it allows private equity funds to act not only as financial and strategic investors in insurers, but also to take charge of the insurer in the capacity of a promoter and hence contribute to the further development of the Indian insurance industry. Apart from increasing the avenue for funding, the Indian insurance industry is also likely to benefit from the expertise and experience which private equity funds bring to the table.

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