INSURANCE - INDIA

New corporate governance guidelines for insurers

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Introduction

The focus on corporate governance has increased significantly since Satyam Computer Services Limited's corporate fraud and internal governance failure came to light. Post Satyam, the legislature has taken steps to incorporate certain basic principles of corporate governance in the revamped Companies Act 2013. These steps include provisions relating to:

- the constitution of boards of directors;
- the appointment of independent directors;
- the constitution of certain mandatory board committees; and
- directors' duties.

For listed companies, corporate governance norms are even more stringent due to the need to protect the interests of multiple minority investors.

These general corporate governance norms apply in addition to the specific norms and regulations which may apply to an entity by virtue of the sector in which it operates. In this regard, it is important to consider that the Indian insurance sector is highly regulated in terms of the nature of business undertaken by insurance entities and the duty owned by these entities to their policyholders. In light of this, the Insurance Regulatory and Development Authority of India (IRDAI) first introduced corporate governance guidelines for all Indian insurers on August 5 2009 (the 2009 guidelines).

2016 guidelines

The IRDAI recently replaced the 2009 guidelines with the Guidelines for Corporate Governance for Insurers in India of May 18 2016. The 2016 guidelines seek to incorporate relevant changes introduced by the Companies Act and consider other relevant changes in the insurance sector since 2009 in order to provide an appropriate corporate governance regime for Indian insurers. The 2016 guidelines also supersede the Guidelines on Reporting of Key Persons of October 9 2013 and stipulations regarding the appointment of statutory auditors issued through circulars of July 25 2005 and April 22 2009.

The 2016 guidelines specify the system of controls which Indian insurers must put in place and, among other things, set out norms for:

- the appointment of key managerial persons and statutory auditors;
- the constitution and functions of boards of directors; and
- the delegation of board functions.

They also provide for disclosure requirements and whistleblowing provisions. The key features of the 2016 guidelines are summarised below.

Provisions in consonance with Companies Act
Under the 2016 guidelines, the boards of Indian insurers must appoint independent directors and at least one female director, in compliance with Section 149 of the Companies Act. The independent directors must meet and evaluate the performance of the insurer's board in accordance with the Companies Act.

Further, the 2016 guidelines provide norms for preventing conflicts of interest and mandate that insurers comply with the provisions regarding related-party transactions under Section 188 of the Companies Act.

Disclosures with respect to related-party transactions and remuneration paid to key managerial personnel must now be made in the annual accounts in compliance with the Companies Act. In addition, disclosures with respect to the persistency ratio must be made by insurers transacting life insurance business.

Finally, as per the Companies Act, insurers must maintain corporate social responsibility in order to perform their prescribed functions.

Constitution of board committees
The 2016 guidelines have extensively revamped the norms with respect to the constitution of board committees and their responsibilities with regard to managing insurers. The key changes are as follows:

- Under the 2009 guidelines, the nomination committee and remuneration committee were separate and their constitution was voluntary. Under the 2016 guidelines, these committees have now been integrated into a single committee and are mandatory.
- Life insurers need no longer establish an asset liability management (ALM) committee. Where insurers do not constitute an ALM committee, the functions of the ALM committee – as stipulated under the guidelines – must be performed by the risk management committee.
- Insurers transacting life insurance business must constitute a with-profits committee, as envisaged under the Insurance Regulatory and Development Authority (Non-linked Insurance Products) Regulations 2013, which set out the framework for, among other things:
  - the share of assets attributable to policyholders;
  - the investment income attributable to the participating fund of policyholders; and
  - the expenses allocated to policyholders.
- Insurers must constitute an audit committee to perform the prescribed functions.

Outsourcing arrangements
All outsourcing arrangements must be approved by the committee of key management persons and should comply with the insurer's board-approved outsourcing policy. Further, the insurer's management must monitor and review the performance of agencies to which operations have been outsourced annually. Finally, the provision stipulating that outsourcing arrangements should be for a fixed three-year period has been deleted. The 2016 guidelines also reiterate that insurers are prohibited from outsourcing their core functions.

Compliance requirements
Insurers must file a certificate of compliance signed by the compliance officer. In addition, insurers must file a compliance report stating their compliance status with the 2016 guidelines.

The 2016 guidelines also apply to reinsurers and branches of foreign reinsurers set up in India (excluding certain specified provisions, such as the requirement to have a policyholders' protection committee (for reinsurers) and the constitution of a board and mandatory committees (for branches of reinsurers)).

Comment

By incorporating the changes introduced by the Companies Act into the 2016 guidelines, it appears that the IRDAI is seeking to place more responsibility on the management of insurers and reinsurers. Specifically, non-compliance with the provisions regarding independent directors and related-party transactions will not only make insurers liable under the Companies Act, but also the 2016 guidelines. Hence, the highly regulated nature of the insurance sector and the close scrutiny of insurer and reinsurer business operations remain significant factors for players in the Indian insurance industry.

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