



भारतीय बीमा विनियामक और विकास प्राधिकरण
INSURANCE REGULATORY AND
DEVELOPMENT AUTHORITY OF INDIA

Ref. IRDA/ENF/MISC/ONS/259/11/2017

Final Order in the matter of
M/s. Future Generali India Life Insurance Company Limited

Based on reply to Show Cause Notice dated 22nd June, 2017 and submissions made during Personal Hearing chaired by Mr. P.J. Joseph, Member (Non-Life), Insurance Regulatory and Development Authority of India (hereinafter referred as IRDAI/the Authority) on 23rd August, 2017 at 11:00 a.m. at the office of the Insurance Regulatory and Development Authority of India, 3rd Floor, Parishrama Bhavanam, Basheerbagh, Hyderabad.

Background

The Insurance Regulatory and Development Authority of India (IRDAI/the Authority) had conducted an onsite inspection of M/s. Future Generali India Life Insurance Company Limited (Hereinafter referred to as "the Life Insurer/Company") during 5th October 2015 to 16th October, 2015 at the Head Office of the Life Insurer situated in Mumbai, India.

The inspection was intended to check the compliance of the Life Insurer to Insurance Act, 1938, IRDA Act, 1999, Rules, Regulations, Circulars, Guidelines and other directions issued there under by the Authority. The inspection covered the activities of the Life Insurer for the financial years 2012-13, 2013-14 and 2014-15.

The Authority forwarded a copy of the report to the Life Insurer on 9th August, 2016 and the reply was received at the Authority vide letter dated 12th September, 2016. Post scrutiny of the first compliance, the Authority had sought further clarifications on some of the observations for which the Life Insurer responded to vide emails dated 30.03.2017, 08.05.2017, 17.05.2017, 24.05.2017 and 06.06.2017. Upon examining the submissions made by the Life Insurer vide the communications referred herein, the Authority issued a Show Cause Notice on 22nd June, 2017 which was responded to by the Life Insurer vide letter dated 13th July, 2017. As requested therein, a personal hearing was given to the Life Insurer on 23rd August, 2017. Mr. Munish Sharda, MD&CEO, Mr. Goraknath Agarwal, Advisory Actuary, Mr. Bikash Choudhary, Appointed Actuary & CRO, Mr. S. Mahesh, EVP & Head-Operations, Mr. Madangopal Jalan, EVP-Legal & Compliance & CS and Mr. Amol Apte, AVP-Legal & Compliance were present in the hearing on behalf of the Life Insurer. On behalf of the Authority, Mr. A. Ramana Rao, GM & HoD(F&A-Life), Mr. Prabhat Kumar Maiti, GM(Enforcement), Mr. Gautam Kumar, DGM(Life), Mr. C.S. Kumar, DGM (Actuarial), Ms. B. Padmaja, DGM(F&A-Life) and Mr. K. Sridhar Rao, AGM(Enforcement) were present in the hearing.

The submissions made by the Life Insurer in their written reply to Show Cause Notice, the documents submitted by the Life Insurer in evidence of their submissions in reply and also those made during and post personal hearing have been considered by the Authority and accordingly the decisions thereon are detailed below.

Charge No.1

On examination of Form A relating to outsourcing Activities of the insurer for the year 2013-14 and 2014-15, it was observed that the Life Insurer has not reported the outsourcing activities with one of the Outsourced entities.

Violation of Clause 11.2 of Outsourcing Guidelines, IRDA/LIFE/CIR/GLD/013/02/2011 dated 01/02/2011.

Submission by the Life Insurer

The Company has engaged 177 vendors and 83 vendors for outsourcing activities during 2013-14 and 2014-15 respectively. All the activities and payouts to these vendors have been reported except only one entity observed by the Authority. Non-reporting of single entity was an inadvertent omission on the part of the Company. Thus, the Company wants to submit that there was no intention not to report the accurate information. Further the Company has over a period of past 2-3 years tightened its vendor evaluation process for outsourcing vendors; and the company has carried out the required due diligence for the vendor whose name was inadvertently not included in the Outsourcing Report as mentioned above.

It is confirm that the Company had terminated the arrangement with that entity w.e.f. 31/05/2015. Since the company had terminated the arrangement, it was not reflecting in outsourcing returns filed from March, 2016. The Company also confirms that all outsourced vendors were reported in the outsourcing returns filed during the March, 2016 to March, 2017.

Decision

There shall not be any scope for inadvertent errors while reporting to the Authority. Reporting is a mandatory requirement and the Life Insurer should have ensured reporting, even about the entity missed out. Hence the Life Insurer has violated the above mentioned provisions of Outsourcing Guidelines. The Life Insurer is warned for the violation committed. The Life Insurer is directed to ensure continuous compliance with Regulation 21 of IRDAI (Outsourcing of Activities by Indian Insurers) Regulations, 2017 hereinafter.

Charge No.2

- a) ULIP policies were issued under Employer-Employee (EE) relationship.
- b) Further, policies were issued under Employer-Employee relationship even where the Lives assured were not employees.

Violation of IRDAI Circular No.036/IRDA/LIFE/JAN-06 dated 30th January, 2006.

Submission by the Life Insurer

a) *The policies were not issued under key man/partnership insurance. They were issued only under Employer-employees schemes. Another circular No.37/Irda/life/mar06 dated 22/03/2006 clarified that the products sold under Employer-employee schemes could be other than term insurance.*

b) *Reasonable due diligence has been carried out by the Company to establish employer-employee relationship (not amounting to key man) as is required for issuance of policies under EE schemes. As per the documents procured along with the proposal forms of the said policies, the relationship of employer-employee could be established which is consistent with Underwriting manual (prevailing at the time of underwriting the referred policies). Copy of the underwriting manual is submitted to the Authority, post personal hearing.*



Decision

Considering the submissions made, **charge is not pressed.**

Charge No.3

a) Ageing analysis of death claims for the years 2013-14 and 2014-15 revealed that there were delays in settlement of death claims.

b) Further for the claim cases viz., Death Claims, Foreclosure, Maturity and Surrenders payout, where the decision to settle the claim has been taken by the company but the claims have not actually been paid due to some requirement like discharge voucher or bank details of the claimant for NEFT payment is moved to Life Premium Policy Suspense Account (LPPS) and all these cases were reported to have been paid in the public disclosures and to the Authority. From the details of Outstanding LPPS account summary (as on 30.09.15) As on 30.09.2015, the insurer was having Rs 18.18 Crore in the liability suspense account, which was shown as settled but was not actually paid.

Violation of Regulation 8 of IRDAI (Protection of Policyholders' Interests) Regulations, 2002 and violation of Clause 6 of Annexure II of Corporate Governance Guidelines, IRDA/F&I/CIR/025/2009-10 dated 05/08/2009

Submission by the Life Insurer

a) All the claims shown in the observation were pending for payment on account of receipt of bank details of the claimants, discharge voucher and due to dispute among the claimants. The company has done away with the process of asking for advance discharge voucher from the claimants. The company has shown significant improvement in claim settlement over the past 3 years and has automated the claims management process. The company has also paid penal interest wherever claim payment was delayed at 2% above the bank rate. Claims statistics for the past three years as under to establish the improvements.

Parameter	2013-14	2014-15	2015-16	2016-17
Claims Settled (%)	74.88%	83.70%	90.26%	89.53%
Repudiation Percentage	14.76%	14.54%	8.63%	9.22%
Claims Pending at the end of the year (% of total claims)	10.36%	1.76%	1.11%	1.24%
Turn Around Time for claims (in no of days)	43.01	51.33	29.97	22.31

Further the following age-wise analysis of claims paid as on 30/06/2017 indicates further improvements in TATs.

Sl.No.	Types of Claims	No. of claims paid						Total No. of claims paid
		On or before maturity	1 month	1 - 3 months	3 - 6 months	6 months - 1 year	> 1 year	
1	Death Claims	13	146	15	0	0	0	174



b) LPPS is used to park the monies before the actual payout is made to the policyholder. The Company uses the said LPPS Account for death claims where decision to make payment of the claim has been taken by the company, maturity/survival, surrenders, and foreclosures. The Company reports this amount in the LPPS account as liability and also reports the same as unclaimed amounts and uploaded on the Company's website as per Regulatory guidelines. The amounts available in LPPS pool are available at a policy level and can be classified into different categories viz., Death, Maturity, Survival Benefit, Surrender and Foreclosure etc.

It is to submit that the balance outstanding under LPPS has been reduced to Rs.1.19 Crores from Rs.18.18 Crores (as at the time of inspection). Now, the Company has changed the practice and treats the claims as settled only when the claim is actually paid as against the previous practice of treating them as paid based on Company's decision to pay. Further the amounts are transferred to unclaimed funds as per the Regulations in place as on date.

It is to further submit to the Authority that the control environment of the company including claims payments and reporting have been subjected to the ICFR process in March 2016 and March 2017. The auditors of the company have found the control environment to be satisfactory and there is no adverse report as such on the control failures on this aspect of operation of the company. Therefore it is to humbly submit to the Authority that the control and corporate framework expected of a life insurer as laid down in the corporate governance guidelines is in place and it's always been company's endeavour to continue to strengthen the control environment.

Decision

a) Ageing analysis at the time of inspection by the Authority indicates that the Life Insurer has not ensured compliance with regulatory norms on settlement of claims. A considerable number of claims were outstanding beyond prescribed time period. However considering the submissions that they have shown improvements in settlements, charge is not pressed. The Life Insurer is advised to ensure continuous compliance to Regulation 14 of IRDAI (protection of policyholders' Interests) Regulations, 2017.

b) The Claims can be shown as paid only when those are actually paid. Until such time they shall be shown as outstanding in the books of account. Further the claims which are settled but not claimed by the claimant/policy holder shall be transferred to unclaimed accounts as per circulars/guidelines issued in this regard. Hence the practice adopted by the life Insurer is not acceptable. However, considering the submissions that they have changed the practice and that the amounts are transferred to unclaimed funds as per the Regulations in place as on date, charge is not pressed. The Life Insurer is advised to adopt practices, within the purview of extant regulatory norms, with regard to claims processing and settlement.

Charge No.4

Under an insurance policy, the Life insurer had repudiated the critical illness claims on the ground of medical non-disclosure and the decision of the life insurer was challenged by the claimant at Insurance Ombudsman office, which refuted the ground of the life insurer on the basis of non-availability of the evidences and directed the Life Insurer to pay the claim. The Life Insurer honoured the decision of the ombudsman and paid the claim under critical illness but cancelled the base policy from inception (on the same ground which was refuted by the ombudsman) and refunded the premium to the claimant.

Violation of Section 45 of Insurance Act, 1938 and violation of File and Use guidelines.



Submission by the Life Insurer

With reference to the policy in question, the Customer had opted for Future Care Plus plan with Accidental Death Rider and Accelerated Critical Illness (CI) Benefit Rider. The proposal was logged in on July 05, 2011 and policy was issued on July 20, 2011. Policyholder intimated the CI rider claim on July 24, 2013 and since the claim had occurred within 2 years from risk commencement date an investigation was carried out. The claim investigation revealed that Life Assured was suffering from Chronic Rheumatic Heart Disease (CHRD). As per the Chief Medical Officer (CMO) note dated December 13, 2014, CHRD is an infection of heart valves since childhood. This note from CMO was based on Hospital Discharge Summary (HDS) document dated May 13, 2013. The health history stated in this HDS revealed that the Life Assured was suffering from 'chest pain with shortness of breath since 2 years' and it also stated that Life Assured had 'weight loss since 2 years'. The Company had repudiated the critical illness rider claim and voided the policy on the grounds of Medical Non-Disclosure as mentioned above. The Policyholder was an employee of the Company and was well aware of his rights as a policyholder and was well informed about the terms and conditions governing the policy contract;

The Complainant in his complaint before the Hon'ble Office of Ombudsman had only disputed the Company's decision to repudiate his Critical Illness Rider and no challenge was made by him to Company's decision to void the policy. The Company has refunded excess premiums paid by the Policyholder and the same has duly been accepted by him; Since the limited question before the Office of Ombudsman was to decide on the Company's stand to repudiate the Critical Illness Rider, the same was adjudicated and decided by the Office of Insurance Ombudsman; As stipulated in the then prevailing Redressal of Public Grievance Rules, 1998, the Company was in receipt of a due written consent from the Policyholder, indicating his agreement with the award passed by the Office of Insurance Ombudsman i.e. payment of Critical Illness Claim. The Company in accordance with the award had made payment of Critical Illness Rider Benefit to the policyholder; the policyholder did not approach the company with any request to reinstate the base policy;

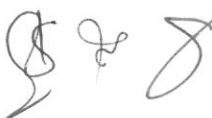
It is further submitted that any decision as to whether the said provisions of Section 45 have been followed by the Company or not would be purely the subject matter of any challenge that the policyholder may raise against the decision of the Company and the adjudication of such dispute/challenge by the judicial/quasi-judicial ombudsman before whom the decision is challenged, if any.

In the present case calling of base policy in question was not disputed/challenged by the Policyholder and as such the Company is not in violation of the provisions of Section 45 of the Insurance Act, 1938 as were in force on the date of issuance of the policy in as much as it has duly complied with the directions of the adjudicating authority on the limited question presented before the said authority by the policyholder. It is to submit that since the matter at hand is a one off case with peculiar facts and since the same deals with whether the policyholder had any dispute against the decisions of the Company, one for repudiation of Critical Illness Rider and the other for voiding the base policy, the same may kindly not be considered as a violation of File and Use (F&U) Regulations.

Copy of the documentary evidence of the company having approached the life assured for reinstatement of the policy is submitted to the Authority.

Decision

Considering the above submissions of the life insurer, charge is not pressed.



Charge No.5

The Life Insurer had not paid the surrender value under ULIP policies to be auto foreclosed after the revival period/lock in period for many years. However, the same were paid in 2015 along with the penal interest.

Violation of Clause 6 of Annexure II of Corporate Governance Guidelines, IRDA/F&I/CIR/025/2009-10 dated 05/08/2009 and File and Use guidelines.

Submission by the Life Insurer

The cases highlighted in the said charge pertains to the period which is prior to September 2014 i.e. these cases were foreclosed prior to September 2014. The Company had started automating the Foreclosure Process in Life Asia in the year 2013-14. It would be pertinent to mention here that any technology change in Life Asia is a time consuming process. The Company had identified the absence of Foreclosure and other day 2 processes in Life Asia and had begun the process of enhancing Life Asia in the year 2013-14. This enhancement was completed in the year 2014-15. Since at the relevant point in time, the foreclosure process in the Company was a manual process, there were delays in settlement of the foreclosure amounts in favour of the policyholders.

It is further confirmed that the Company had cleared all the legacy foreclosure cases and had made a payment of interest at the rate of Bank Rate + 2% (11% as the bank rate was 9% for that particular year) to all the policyholders whose foreclosure payments were delayed. No cases are pending as on the date.

It is to submit that now the Company has due process in place to ensure that all the day 2 functionalities (system requirements for post issuance transactions) are duly in place. And the product is launched after obtaining due approvals of the Risk Management Committee and the Board of Directors of the Company thereby eliminating chances of any file and use non-compliance arising out of the said product regulations. The Company now has an automated system to process foreclosure cases. The said system has been put in place since August 2014 and as such the matter highlighted in the charge has been duly addressed and rectified by the Company.

The company also wish to state that the Company now has a highly effective system to communicate with the customer 90 days prior to the foreclosure date in any given policy, through different communication modes including SMS, e-mail and physical letters giving last chance to the policyholder to revive the policy. In case if the policy finally moves to foreclosure, the money is released to the customer on the date of foreclosure falling due.

During the FY 2016-17, 13532 cases were foreclosed and all the payments have been duly processed. In case of delay, the Company has a policy of paying interest at Bank Rate + 2%.

The control environment has been tightened since Sept 2014 with automation put in place. The concern of the Authority regarding violation of Clause 6 of the Corporate Governance guidelines has been addressed. This is validated by the fact that the controls were subjected to the ICFR process in March 2016 and March 2017 and the statutory auditors have found the control environment satisfactory. Hence the Company is of the opinion that the control framework expected of a life insurer as laid down in the Corporate Governance Guidelines is in place.



Decision

The Life insurer must note that there shall be every system in place to ensure that all the servicing aspects are taken care of. There is a lapse and that was occurred due to absence of systems at the point of time. The issue is a contractual obligation and the Life Insurer should have ensured the timely payouts pertaining to the auto foreclosed policies. However, considering the submissions that currently they have placed proper automated systems, that they paid all the legacy payouts along with penal interest as on date and that there are no such cases pending as on date, charge is not pressed. However, the life insurer shall ensure compliance with the Regulation 46 of IRDAI (Linked Insurance Products) Regulations, 2013 continuously.

Charge No.6

There is no automatic process to pay annuity to the annuitants. List of annuity payments is sent to finance team which is not updated into the policy administration system and policy administration system has no information on details about the annuity payouts. The details of annuity invoice raised to finance department is entered manually into a separate excel sheet which has no information about the dates on which the invoice to finance regarding annuity payments was raised and the date on which the payment was done by the finance system. This weak control system resulted into undue delay in annuity payments.

Violation of Clause 6 of Annexure II of Corporate Governance Guidelines, IRDA/F&I/CIR/025/2009-10 dated 05/08/2009.

Submission by the Life Insurer

A consolidated log of all the annuity payments is maintained by the User Department. In the last week of previous month, a consolidated payment voucher is raised to the Finance team for payment falling due in next month. The finance team cross verifies the data for payments. Post verification of the said date the annuities are credited to the respective customer account on the respective dates. Hence, though the process is manual in nature, the same is being managed through a maker-checker process. This is done to ensure that the policyholder's interest is protected. It is further submitted that the number of annuities issued by the Company is very low and thus the same can effectively be managed manually. Further it is our humble submission that the existence of a manual payment system with adequate compensating controls cannot be construed as violation of clause 6 of the Annexure II of the Corporate Governance Guidelines.

It is to submit that the Company as on date automated the annuity calculation process. It is further submitted that the Company has already initiated automation of annuity payouts work flow and the same will go live by end of financial year 2017-18. The annuity amount payable to the policyholder is calculated through the policy administration system without any manual intervention. The said system has the capability of capturing the annuities' data to ensure timely payment.

The said automated system is supplemented by an effective manual system which includes communication to the policyholder, (triggered as early as 180 days in advance before the maturity date to follow up with the policyholder for timely submission of documents required for issuance of annuity policy). Further SMS, e-mail, letters, calls and field visits, etc. which are utilized to ensure the relevant documents are received from the policyholder well in time. Hence, the Company has due control mechanism in place to ensure timely payment of annuities.



It is to submit that with reference to the 10 policies highlighted by the Authority where delays were there, the Company has provided annuity retrospectively from the date of respective proposals and all due annuity payouts have been made to the policy holders. It is further to confirm that interest has been paid by the company for all the 10 cases from the due date of annuities till the dates of actual payouts.

The Companies Act now requires the Board of Directors of the Company to comment on the adequacy of the internal control environment for financial reporting (ICFR) which has to be certified by the statutory auditors. These controls have been subjected to the ICFR Process in March 2016 and March 2017. The statutory auditors have found the control environment satisfactory. Hence the company is of the opinion that the control framework expected of a life insurer as laid down in the Corporate Governance guidelines are in place.

As on 31/07/2017 the company has only 699 annuity policies of which survival certificates are awaited for 173 cases and annuity is yet to fall due for another 153 cases. For the remaining 373 cases annuity payouts are being made on due dates and that the timely payouts will be made for annuities falling due on future dates. It is further to confirm that during the current calendar year, the company has received only one complaint pertaining to annuity payment and the same has been resolved to the satisfaction of the policy holder.

Decision

On examination of data brought out by the Inspection team of the Authority, it is found that there were delays in commencement of annuity from the date of vesting of annuity. The delays observed range from two months to eleven months. Lack of automated system for payouts of annuities may be the cause of the delays. Hence the submission of the Life Insurer, that “there is maker checker process, though the process is manual” cannot be accepted. The Life Insurer is warned for not ensuring the timely commencement of annuities payout. While noting the submissions that they have paid the annuities retrospectively along with interest for the cases observed by the Authority, the Life Insurer is directed to complete the process of automation of annuity payouts (as submitted by them) at the earliest to curb delays in settlements.

Charge No.7

In Variable Insurance Products (VIP), Group Gratuity (UIN 133N045V01) Group Leave Encashment plan (UIN 133N044V01), the investment return declaration on quarterly basis by the Appointed Actuary was not in line with the File and Use approved by the Authority. In File and Use, the formula for additional investment return was as follows:

Additional interest rate = (Investment return- Minimum Floor rate- 1.10% towards expenses)
However, the investment return provided by the investment Department and declared by the Appointed Actuary has not used the above formula in any of the quarter. Email communications between appointed actuary and other user Departments revealed the same.

Violation of File and Use Guidelines.

Submission by the Life Insurer

As per File and Use for product Group Gratuity (UIN 133N045V01) and Group Leave Encashment plan (UIN 133N044V01), the additional interest rate is to be determined as follows:



"Additional Interest Rate = (Investment return- Minimum Floor Rate-1.10% towards expenses)

Where investment return will be arrived at as under:

Non-Zero positive additional interest rate will be decided considering the prevailing interest rate for the current quarter and expected investment return in the following quarter based on the average investment return earned on the fund in the 12 months preceding the quarter, in which the interest rate will be credited."

In the above formula, the investment return expected to be earned in the next quarter (for which interest is being declared) is worked out by the investment department and it includes the expected fund to be received by the Company under new as well as existing schemes for which information is taken based on business projections. It also considers the expected outgo under such policies. It further considers and the investment return earned by the Company on such fund during last 12 months and a weighted yield is derived.

The additional interest rate for the next quarter is determined by the Appointed Actuary based on above formula taking expected return provided by investment team as the effective investment returns. The effective investment yield of minimum floor rate is subtracted, the expense loading is subtracted thereafter, which is generally less than 1.10% p.a. and hence the additional interest rate declared is favourable to the clients.

Hence, the additional interest rate has been declared using the equation given in the File & Use approved by the Authority. It is to confirm that the Company has not taken charge more than allowed as per File & Use approved by the Authority, which is 1.10%, towards expenses. Further, the deduction towards expenses has been different for different fund sizes till 31st December 2016. The basis for it was that many of the expenses incurred by the company are fixed and so as a percentage of fund size, the deductions towards expenses should differ.

The 2013 regulation on products provided a cap on commission for group fund based products. Similarly, the recent 2016 regulations on commission continue to cap the commission on group fund based products.

According to the Company's interpretation, the intent of regulation is that whenever there is a group with large fund amount or premium, the expenses do not move in line with size of the fund and hence, commission is capped to a certain fixed amount so as to not penalize policyholder with large fund size. This is done in individual policies as well where there is a large sum assured discount on premiums.

Thus, to not penalize policyholders which have higher fund size or larger scheme size, the returns were declared taking into the effect the size of the fund to allow for savings in expenses and commission which becomes fixed after a certain point in time.

However, the Company has been declaring single rate for all fund sizes just after onsite inspection by the Authority in the month of December 2015 i.e. post declaring in September 2015 for quarter October – December 2015.

Following will make clear of our approaches before and after 31st December 2016 –



Financial Year	Quarter	Fund Size	Investment Return (1)	Minimum Floor Rate (2)	Expense s (3)	Declared Interest Rate (4)=1-2-3
2015-16	Q3	Fund < 5 Cr	8.5%	1.0%	0.3%	7.2%
		Fund >= 5 Cr & < 10 Cr	8.5%	1.0%	0.2%	7.3%
		Fund >= 10 Crores	8.5%	1.0%	0.0%	7.5%
	Q4	All Fund Sizes	8.3%	1.0%	0.2%	7.1%
2016-17	Q1	All Fund Sizes	8.5%	1.0%	0.3%	7.2%
	Q2	All Fund Sizes	8.6%	1.0%	0.4%	7.2%
	Q3	All Fund Sizes	8.5%	1.0%	0.3%	7.2%
	Q4	All Fund Sizes	8.3%	1.0%	0.3%	7.0%

Decision

The formula, for calculation of “Additional Interest Rate”, as approved in the File & Use, provides for a fixed percentage of 1.1% towards expense. Hence as per File & Use, as filed and approved by the Authority, there is no scope for using a different rate. The Life Insurer’s attempt to justify their action of File & Use violation, by submitting that the same is in the interest of policyholder, undermines the very objective of File and Use procedure. The Life Insurer is expected to protect the interest of policyholders subject to compliance of all regulatory requirements. In the documentary evidences collected during the onsite inspection, there is no explicit mention of allowance for expenses. Hence it is clear that the said expense was allowed implicitly without suitable disclosure. The Life Insurer’s submission of allowing for a lower percentage towards expense has the potential to be treated as afterthought as can be observed from the expenses allocated to the funds with more than Rs.10 crores (0.0%) for the 2015-16 Q3. Besides, by agreeing that they have applied lower rate towards the expense, than that approved in the File and Use, the Life Insurer accepted the violation of File and Use. The Life insurer is warned for the violation committed. The Life Insurer is hereby directed to apply for modification of File and Use, if they intend to change the approved features of these products. The Life Insurer shall take approval for modifications under File and Use procedure.

Charge No.8

The Authority vide Ref: IRDA/ENF/ORD/ONS/115/06/2015 dated 11th June, 2015, charge no.5, with regard to incorrect classification of a lease agreement as finance lease instead of operating lease, advised the Life Insurer to ensure compliance with regulatory prescriptions in classification of lease agreements. (The observation was classification of lease as operating lease instead of financial lease). However, the Life Insurer has continued to show the lease as operating lease only. Further the Life Insurer has also been showing another lease as operating lease instead of financial lease. In case if the lease is classified as ‘finance lease’ the same would result in recognition of additional asset and liability to the extent of Rs. 26 Crore in the year 2013-14 and Rs. 8 Crore in the year 2014-15. However, such asset would not have been considered for the purpose of ‘available solvency margin’.

Non-Compliance with the Authority’s directions given vide final order referred herein and violation of Violation of Regulation 2(e) of IRDA (Assets Liabilities and Solvency

Margin of Insurers) Regulations, 2000 and Violation of Regulation 3(1) read with Clause 1 of Schedule A (Part 1) of IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002 (Accounting Standard 19 prescribed by ICAI).

Submission by the Life Insurer

The Company had noted the concern regarding non-compliance of the order issued by the Authority. In accordance to the concerns raised, the Company has stopped entering into any further lease transactions. As per our understanding of the referred order, the Authority had not pressed any charges since the classification of lease as a financial lease had no impact on the solvency of the company. The Authority had directed us to adhere to the requirements stipulated in the extant regulatory framework.

It is to humbly submit to the Authority that the Company's interpretation of the order was that the company should not enter into any such leases going forward and show the new leases, if any, as finance leases. Hence the Company has not entered into any such lease arrangement post the referred order of the Authority.

It is also to submit that post the issuance of the order, the Company's senior officials met with the Authority and highlighted the following:

1. That these are contracts already entered into and therefore difficult to change
2. That the contracts will run off in the FY 2018-19
3. That the company is not entering into any fresh leasing arrangements.
4. That the reclassification of the leasing arrangements into Financial Lease had negligible impact on the solvency of the company
5. That our Statutory Auditors have approved these accounts without any qualifications

This was followed up with a formal letter to the Authority on January 14, 2016. It is therefore to submit to the Authority that the company had no intention of not following the Honourable Authority's direction. This act of following up on the order with a visit and a formal letter to the Authority should be viewed as company's intention to follow the Authority's direction and not be in violation in future.

Impact on solvency

The impact on solvency in case the operating leases had to be accounted as finance leases for the last four financial years is as follows:

Solvency Ratio	31st March 15	31st March 16	31st March 17
As operating lease (existing)	2.91	2.03	1.61
As finance lease	2.78	1.96	1.59

The above table indicates that the change in the classification has minimal impact on the solvency ratio workings as explained in the table above and the Company would continue to be above the regulatory minimum solvency of 1.50.

The Statutory Auditors of the Company comment on whether the interpretation of the Accounting standards by the Company is in order. The Company has entered into leases from FY 2008-09 and since then the statutory auditors past and current have reviewed these leases and found the accounting treatment in order.

The Company wish to submit that since these leases are contractual arrangements and the Lessor has considered the same as Operating Leases in their records, it would not be possible for the company to unilaterally reclassify the Leases as Finance Lease in its books.

Hence, the Company is of the view that compliance with Clause 1 Schedule A of the IRDA (Preparation of Financial Statements and Auditors Report of Insurance Companies) Regulations, 2002 is evidenced by an unqualified report from the Auditors.

To alter the accounting treatment from operating leases to finance leases would result in the Company running the risk of its accounts being qualified since the auditors have already agreed that these transactions are operating leases in nature. Further considering that the Company has treated the leases as operating leases, no assets have been recorded in the books of accounts for these transactions and thus violation of Regulation 2 (e) of IRDA (Assets Liabilities and Solvency Margin of Insurers) Regulations, 2000 may not arise.

During the personal hearing on 23rd August, 2017, while noting the above submissions, the Authority suggested the Company to explore the option for prior period error correction if any to give effect to the directions given in the order. The Company submitted letter no. FG/FIN/MM/17-18/065 dated 21/09/2017 for consideration of the Authority. The summary of the letter is as below:-

The company would like to confirm that the Company will cumulatively change the method of treatment of leased assets from "Operating Lease" to "Finance Lease" and necessary entries will be passed in the books of account to cumulatively change the treatment to Finance Lease. It is to confirm that all lease transactions during the financial year 2017-18 will be recorded only on "Finance Lease" basis. Appropriate disclosure would be made in the Notes to accounts to the financial statements.

It is to further submit that Net impact on account of re-classification of lease in the books of account from Operating Lease to Finance Lease from inception till 30 September 2017, would be increase in deficit in Revenue account by Rs.0.66 crores. Even during the period when the lease transactions were treated as "Operating Lease" (which will be reversed), there was a minor impact on the solvency ratio which was maintained above the required solvency rate as per IRDAI Regulations at all times.

Decision

The Authority through its final order Ref: IRDA/ENF/ORD/ONS/115/06/2015 dated 11th June, 2015, charge no.5, has given its decision on this issue as 'The Life Insurer is hereby directed to adhere to the requirements stipulated in the extant regulatory framework.' It was categorically indicated at that time that the lease was to be classified as "financial lease" and that post issuance of the said order, the Company shall take steps to ensure correct classification of lease in question, any other such leases and also similar leases going forward. However, the Life insurer has interpreted the direction of the Authority resulting in their adhering to the Authority's order only in part.

The Life Insurer submitted that they have discussed/filed a formal letter with the Authority mentioning therein about the details of their compliance of the Authority's direction.

The life insurer must note that unless there is an explicit approval from the Authority for exemption of the lease in question from being classified as "financial lease", the Life Insurer is under an obligation to adhere to the directions. But the Life insurer has not ensured the same. The Life Insurer is warned for not ensuring adherence to

the directions of the Authority in full. The submissions that the impact on solvency margin requirements is not significant and that they have not entered into any such leases post the Authority's order are noted. However, such violations, if any, noticed again in future will be viewed very seriously.

With regard to the letter dated 21/09/2017 submitted in respect of exploration of the option for prior period error correction, if any to give effect to the directions given in the order, the Authority accepts the requests made in the said letter of the Life insurer. The Company can proceed as proposed in the said letter in regard to the leases under question.

The Authority hereby categorically reiterates that the Life insurer shall not classify such leases as operating leases hereinafter.

Summary of Decisions

The following is the summary of decisions in this order:

Charge No.	Brief Title of Charge and the provisions violated	Decision
1	Activities outsourced were not reported to the Authority. <i>Violation of Clause 11.2 of Outsourcing Guidelines, IRDA/LIFE/CIR/GLD/013/02/2011 dated 01/02/2011</i>	Warning & Direction
2	Policies were issued under Employer-Employee scheme though the Life Assured was not Employees. Further the scope of cover should term assurance but ULIP policy was given. <i>Violation of IRDAI Circular No.036/IRDA/LIFE/JAN-06 dated 30th January, 2006.</i>	Charge not pressed
3	Delays observed in settlement of death claims and claims under death, foreclosures, maturity and surrender though actually not paid were shown as paid. <i>Regulation 8 of IRDA (Protection of Policyholders' Interests) Regulations, 2002.</i>	Charge not pressed & Advisory
4	Under a policy, critical illness rider claim was repudiated which was appealed to Ombudsman who subsequently directed the Life insurer to pay the claim. However, the Life Insurer at the time of rejection of the claim under rider also cancelled the base policy and not reinstated even after Ombudsman order. <i>Violation of Section 45 of Insurance Act, 1938.</i>	Charge not pressed
5	No systems were in place to pay surrender value in case of auto foreclosures. <i>Violation of clause 6 of Annexure II of Corporate Governance Guidelines, 2009 and File and Use guidelines.</i>	Charge not pressed & Advisory
6	No automated process for annuities payments was in place. <i>Violation of Clause 6 of Annexure II of Corporate</i>	Warning & Direction

	<i>Governance Guidelines, 2009.</i>	
7	Investment declaration in VIP products not as per File and Use. <i>Violation of File and Use guidelines.</i>	Warning & Direction
8	Even after the Authority's direction to classify a particular lease as financial lease, the Life Insurer has been continuing the classification as Operating lease. <i>Non-Compliance with the Authority's directions given vide final order referred herein and violation of Violation of Regulation 2(e) of IRDA (Assets Liabilities and Solvency Margin of Insurers) Regulations, 2000 and Violation of Regulation 3(1) read with Clause 1 of Schedule A (Part 1) of IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002 (Accounting Standard 19 prescribed by ICAI).</i>	Warning and Direction

Conclusion

- i) The Life Insurer shall confirm compliance in respect of all the directions referred to in this Order, within 21 days from the date of issuance of this order. Timelines, if any as applicable shall also be communicated to the Authority.
- ii) The Order shall be placed before the Audit committee of the Life Insurer and also in the next immediate Board meeting and a copy of the minutes of the discussions shall be provided to the Authority.
- iii) If the Life Insurer feels aggrieved by any of the decisions in this order, an appeal may be preferred to the Securities Appellate Tribunal as per Section 110 of the Insurance Act, 1938.

Place: Hyderabad

Date: 29th November, 2017



(P.J. Joseph)

Member (Non-Life)

