



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

IRDA/F&A/GDL/LSTD/1547/08/2016

August 05, 2016

To

All Private sectors Insurers

Sub: Guidelines on Remuneration of Non-executive Directors and Managing Director /Chief Executive Officer / Whole-time Directors of Insurers

Financial institutions like insurance companies are an important part of the financial system. Any risk that adversely affects the insurers also gets transmitted to the other constituents, and through them, to the financial system. The global financial crisis in the recent past was a result of such phenomenon.

The remuneration packages and bonuses & incentives to the employees of financial institutions have often been based on high short-term profits without adequate regard to the long-term risks emanating from their decisions/ actions. The incentives have encouraged excessive risk taking behavior by employees, which threatened the global financial system and left firms with fewer financial resources to absorb losses in cases where the risks materialized. The compensation or remuneration practices at financial institutions are now broadly believed to have been one of the major factors that contributed to the crisis.

The issue has been widely discussed and debated in various international forums and a set of principles has been brought out by the Financial Stability Board (FSB) for implementation of sound remuneration practices by financial institutions. These are:

1. Effective governance of compensation – active Board oversight
2. Effective alignment of compensation to prudent risk-taking
3. Effective supervisory oversight and engagement by stakeholders.

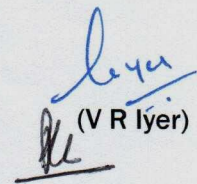
The Insurance Core Principle (ICP) – 7 of the International Association of Insurance Supervisors (IAIS) also endorses the implementation of a remuneration policy covering the members of the Board of insurers, senior management and Key management

persons in control functions and other employees whose actions may have material impact on the risk, and supervisory oversight over the same.

The principles of fair and equitable remuneration packages to top executives of financial firms has also been endorsed by the G-20 nations and the Basel Committee on Banking Supervision (BCBS) and have already been implemented in various jurisdictions, including the European Union.

In this background, the Authority, in exercise of its powers under Section 14 of the IRDA Act, 1999 prescribes the guidelines annexed with this circular on remuneration for Non-Executive Directors and Managing Director / Chief Executive Officer / Whole-time Directors of Insurers.

The guidelines shall be effective from 1st October, 2016 or from the date of appointment / re-appointment of MD / CEO / WTDs and Non-executive Directors, whichever is later.


(V R Iyer)

Insurance Regulatory and Development Authority of India (Remuneration of Non-executive Directors of Private Sector Insurers) Guidelines, 2016

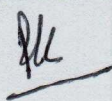
The need to bring in professionalism to the boards of insurers cannot be overemphasized. In order to enable Insurers to attract and retain professional directors it is essential that such directors are appropriately compensated. Accordingly, the Authority has finalised the guidelines on remuneration for non-executive Directors, as under for implementation by the private sector insurers.

1. Remuneration Policy

- a. The Board of Directors, in consultation with its Nomination and Remuneration Committee, should formulate and adopt a comprehensive remuneration policy for the non-executive Directors. While formulating the Policy, the Board shall ensure compliance with the provisions of the Companies Act, 2013.
- b. The Board may, at its discretion, provide for, in the Policy, payment of remuneration in the form of profit related commission to the non-executive directors, subject to the insurer making profits. Such remuneration, however, shall not exceed Rs. Ten lakh per annum for each such director excluding Chairman. For the Chairman of the Board, the remuneration may be decided by the Board of Directors of the respective company.

2. Sitting fees and reimbursement of expenses

In addition to the directors' remuneration mentioned in para 1.b above, the Insurer may pay sitting fees to the non-executive directors and reimburse their expenses for participation in the Board and other meetings, subject to compliance with the provisions of the Companies Act, 2013.



3. Disclosure

Insurers are required to make disclosure on remuneration paid to such directors on an annual basis at the minimum, in their Annual Financial Statements.

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Insurance Regulatory and Development Authority of India (Remuneration of Chief Executive Officer / Whole-time Director/ Managing Director of Insurers) Guidelines, 2016

The remuneration payable to Chief Executive Officer / Whole-Time Director / Managing Director is governed by the provisions of Section 34A of the Insurance Act, 1938. The Section 34A provides as under

34A. (1) In the case of an insurer,—

- (a) *no amendment made after the commencement of the Insurance (Amendment) Act, 1968, of any provision relating to the appointment, reappointment, termination of appointment or remuneration of a managing or whole-time director, or of a manager or a chief executive officer, by whatever name called, whether that provision be contained in the insurer's memorandum or articles of association, or in an agreement entered into by him, or in any resolution passed by the insurer in general meeting or by his Board of directors shall have effect unless approved by the Authority;*
- (b) *no appointment, re-appointment or termination of appointment, made after the commencement of the Insurance (Amendment) Act, 1968, of a managing or whole-time director, or a manager or a chief executive officer, by whatever name called, shall have effect unless such appointment, reappointment or termination of appointment is made with the previous approval of the 2[Authority].*

Explanation.—For the purposes of this sub-section, any provision conferring any benefit or providing any amenity or perquisite, in whatever form, whether during or after the termination of the term of office of the manager or the chief executive officer, by whatever name called, or a managing or whole-time director, shall be deemed to be a provision relating to his remuneration.

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(2) Nothing contained in sections 268 and 269, the proviso to sub-section (3) of section 309, sections 310 and 311, the proviso to sections 387, and section 388 (in so far as section 388 makes the provisions of sections 310 and 311 apply in relation to the manager of a company) of the Companies Act, 1956 (1 of 1956), shall apply to any matter in respect of which the approval of the 1[Authority] has to be obtained under sub-section (1).

(3) No act done by a person as a managing or whole-time director or a director not liable to retire by rotation or a manager or a chief executive officer, by whatever name called, shall be deemed to be invalid on the ground that it is subsequently discovered that his appointment or re-appointment had not taken effect by reason of any of the provisions of this Act; but nothing in this sub-section shall be construed as rendering valid any act done by such person after his appointment or re-appointment has been shown to the insurer not to have had effect.

As is evident from the above, any provisions relating to remuneration of Managing Director /Chief Executive Officer / Whole-Time Director requires prior approval of the Authority. The Authority in order to streamline the process of the approval had issued circular no. 031 /IRDA /CIR/ COMPLIANCE/ AUG-2007. The circular prescribes the manner of seeking approval for the appointment and remuneration of the MD/ CEO/ WTDs, by what so ever name called. The form C of the circular covers the break-up of remuneration payable to MD /CEO/ WTDs.

The Authority has not laid down any prescription/guidelines to the insurers on remuneration of MD/ CEO/ WTDs. In effect, there are no limits imposed by IRDAI on the remuneration structure barring the fact that remuneration beyond Rs. 1.50 crore should be debited to the Shareholders' Fund.

In the light of the above, it is felt that there is an immediate need to lay down guidelines on remuneration of the MD / CEO / WTDs which needs to be kept in view while processing the remuneration application. In view of the above, the Authority hereby lays down the following framework on remuneration of the MD

/CEO / WTDs. The framework enunciated below draws the global best practice as also the framework in place in the financial sector in the domestic market.

1. The guidelines shall be applicable for remuneration payable to MD / CEO / WTDs of Private sector Insurers.
2. Insurers should formulate and adopt a comprehensive remuneration policy covering the MD/CEO/ WTDs. The said policy should also be reviewed annually. The policy should cover all aspects of the remuneration structure such as fixed pay, perquisites, bonus, guaranteed pay, severance package, stock, pension plan, gratuity, etc. taking into account these guidelines.

The process of framing / review the policy should be completed within 3 months of the issue of the Guidelines.

3. Insurers should ensure that for the MD/ CEO/WTDs :
 - i. Remuneration is adjusted for all types of risk,
 - ii. Remuneration outcomes are symmetric with risk outcomes, and
 - iii. Remuneration payouts are sensitive to the time horizon of the risk.
 - iv. The mix of cash, equity and other forms of remuneration must be consistent with risk alignment.
4. A wide variety of measures of credit, market and liquidity risks may be used by the Insurers in implementation of risk adjustment. The risk adjusted methods should preferably have both quantitative and judgmental elements. The following are the minimum parameters which needs to be taken into account the following
 - i. Persistency
 - ii. Solvency
 - iii. Grievance Redressal
 - iv. Expenses of Management
 - v. Claim settlement
 - vi. Claim repudiations
 - vii. Overall Compliance status

- viii. Overall financial position such as Net-Worth Position of Insurer, Asset under Management (AUM) etc.

The above parameters are only indicative; Insurers may formulate their own parameters which should be in line with the Business Plan of the Insurer.

- 5. **Fixed pay:** Insurers are required to ensure that the fixed portion of remuneration is reasonable taking into account all relevant factors.

6. Variable pay composition and deferral

- i. While designing the remuneration arrangements it should be ensured that there is a proper balance between fixed pay and variable pay. At higher levels of responsibility, the proportion of variable pay may be higher.
- ii. The variable pay could be in cash, stock linked instruments or mix of both. However, Employees Stock Option Plan (ESOP) may be excluded from components of variable pay.
- iii. The deterioration in the financial performance of the Insurer and the other parameters specified at para 4 should generally lead to a contraction in the total amount of variable remuneration paid.
- iv. The Insurer may define what is "substantial" in its remuneration policy. Where the variable pay constitutes a substantial portion of the total pay, [say 50% or more], an appropriate portion of such variable pay, [such as 40 % to 60 % of such variable pay] must be deferred over a period of not less than of 3 years.
- v. There should be proper balance between the cash and stock / share components (other than ESOP) in the variable pay in case the variable remuneration contains stock or equity share linked instruments (other than ESOP).

7. ESOP

ESOP is kept outside the computation of the total remuneration but the extent of ESOP should be reasonable. The details of ESOP granted should also be disclosed in terms of the disclosure requirements stipulated for the financial statements of the Insurers.

In case the shares of the insurance company are offered as ESOPs to Managing Director / Chief Executive Officer / Whole Time Directors , then:

- i. If the CEO/MD/WTDs is one of the promoters / investors or directly related to the promoters, then the same will be governed by the provisions of SEBI (Issue of Sweat Equity) Regulations, 2002 as amended from time to time except those relating to pricing of shares. The manner of pricing of shares shall be disclosed upfront to the Authority.
- ii. In other cases, the same will be governed by the SEBI's ESOP guidelines.

8. Sweat Equity: In case the shares of the insurance company are issued as Sweat Equity, then the same will be governed by the provisions of the Sweat Equity Regulations issued by SEBI.

9. Variable pay –timing

In case of deferral arrangements of variable pay, the deferral period should not be less than three years. Remuneration payable under deferral arrangements should vest no faster than on pro rata basis.

10. Clawback

- i. In case of deferral remuneration, in the event of any negative trend in the parameters specified in para 4 and/or the relevant line of business in any year during the vesting period, any unvested / unpaid portions are to be clawed back. However, while exercising such provisions due consideration may be given to the actual / realized performance of the insurer.

- ii. For legal enforceability, the claw back system shall be driven by observable and verifiable measures of risk outcomes. Insurers may put in place appropriate mechanism to incorporate claw back mechanism in respect of variable pay, linked to such parameters as are defined at para 4 above.

11. Guaranteed bonus

- i. Guaranteed bonuses are not consistent with sound risk management or the pay-for performance principles and should not be part of remuneration plan. Therefore, joining / sign on bonus should only occur in the context of hiring new staff and be limited to first year. However, payment of such bonus may be made beyond the year of joining.
- ii. However, in case such guarantees are built in, payment thereof should be in the form of ESOPs only since payments in cash upfront would create perverse incentives and promote undue risk taking.
- iii. Insurers should not grant severance pay other than accrued benefits (gratuity, pension, etc.) to MD/ CEO/WTDs without the prior approval of the Board. It is clarified that severance pay does not include notice period pay.

12. Disclosure and engagement by stakeholders: The following disclosures are mandated in the Annual Report.

- **Qualitative**


- Information relating to the design and structure of remuneration processes and the key features and objective of remuneration policy
- Description of the ways in which current and future risks are taken into account in the remuneration processes.
- Description of the ways in which the insurer seeks to link performance during a performance measurement period with levels of remuneration.

- **Quantitative disclosure :**

- Number of MD/ CEO/ WTDs having received a variable remuneration award during the financial year
- Number and total amount of sign on awards made during the financial year
- Details of guaranteed bonus, if any , paid as joining / signing bonus
- Total amount of outstanding deferred remuneration, split into cash, shares and share linked instruments and other forms.
- Total amount of deferred remuneration paid out in the financial year
- Breakup of amount of remuneration awarded for the financial year to show fixed and variable, deferred and non-deferred.

Accounting and renewal of remuneration:

- No revision in remuneration shall be permitted till the expiry of one year from the date of earlier approval.
- In case the annual remuneration of the MD/ CEO/ WTDs exceeds Rs.1.50crore (including all perquisites plus bonuses etc., by whatsoever names), such excess shall be borne by the Shareholders' account.
- No remuneration shall be paid to MD/CEO/WTDs by any of the promoter / investor or by the group companies of the promoters'/ investors' companies.



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