

Unit Linked Insurance Products- Whose Territory Is It Anyway?

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Background

The war between the two regulators of India- IRDA and SEBI began on April 9 of this year when SEBI banned 14 Insurance companies from selling ULIPs, citing the case with its logic that basically ULIPs are nothing but substantially a mutual fund product and hence falls under the jurisdiction of capital market watchdog, SEBI and not IRDA. Reacting to the development IRDA refused to go by the unilateral act of SEBI and took legal route to settle its claim over the ULIPs. In between personal egos of both heads of respective regulatory bodies, C. B. Bhavde of SEBI and J. Hari Narayan of IRDA clashed and became a staple diet of those in media to relish upon.

The controversy became personalized ego battle and what was lost in the process was the most important consideration- the interests of the common investors and the market at large. If any person buys an insurance product he/she has some long to very long time horizon in mind which goes on to insure him for the future contingencies. But when someone buys a mutual fund product he has some other purpose like making an investment with comparatively small amounts of money and taking advantage of economies of scale and expert services with huge investible fund at the disposal of AMC's due to pooling of investments and presence of professional portfolio management. The nature of both the products is very differing in the very purpose of their existence so their bundling into one was expected to draw flak in near future. Also common persons used to buy insurance products for its heavy benefits in the event of casualty or death (Life insurance or mediclaim in particular). But once ULIPs came this very purpose got blurred in the minds of customers. They started opting to sell their ULIP units in the middle of their term for short term benefits and profit booking as they treated it like a mutual fund unit losing their cover of life and accidents. In a country like India where still a large number of population is uninsured or under insured this was certainly not a welcome sign. But this very fact hardly got publicized in any of the news bites. Also in substance ULIPs are mutual fund products but since they were issued by insurance companies they easily bypassed the compliance and disclosure requirements of SEBI. It became a common trend of Indian market that every insurance company had an AMC business and vice versa.

Recent Developments

Since the germane of battle was in the statutory premises of the country it had to be fixed by amending them. What came as the surprise was the speed with which a proposed amendment and a new ordinance were put in place after repeated backtracking in the initial phase when FM himself advised both the parties to get their disputed sorted through legal procedure. There were basically four statutes which were making the jurisdiction of ULIPs debatable between insurance regulator and market regulator. These were Securities Contracts (Regulations) Act, 1956, Reserve Bank of India (RBI) Act, 1934, the Insurance Act, 1938 and SEBI Act, 1992.

The Securities and Insurance Laws (Amendment and Validation) Ordinance 2010 inserted an explanation to section 2 of the Securities Contract (Regulation) Act, 1956 declaring 'securities shall not include any unit linked insurance policy or scrips or any such instrument or unit, by whatever name called, which provides a combined benefit risk on life of the persons and investment by such persons and issued by an insurer referred to in clause (9) of section 2 of the Insurance Act 1938'.

In the SEBI Act, an explanation to section 12 has been inserted to the effect that collective investment scheme or mutual fund shall not include any ULIP or scrips or any such instrument or unit, by whatever name called, which provides a component of investment besides the component of insurance issued by an insurer.

To give insurance companies a conclusive claim over the issues of ULIP business in general and IRDA to monitor them in particular the Ordinance seeks to amend the Insurance Act, 1938 by inserting an explanation to section 2 "life insurance business shall include any unit linked insurance policy or scrips or any such instrument or unit, by whatever name called, which provides a component of investment and a component of insurance issued by an insurer...'

The Ordinance is expected to be passed in the monsoon session of the Parliament and soon it may become a law. Another development is regarding formation of a high level Committee in the chairmanship of Finance Minister to sort out the jurisdictional issues of the regulatory bodies in the country especially in cases of hybrid products and overlapping territories. If this Committee forms a well structured guideline in the context of dispute redressal mechanism which every now and then brews up between regulatory bodies, it shall be a milestone in resolving the disputes in case of ambiguity in the legal framework defining the jurisdiction of regulators. It would be equally interesting to watch out for a regulation to regulate the regulators especially for our country where there is a case of abundance or sometimes multiplicity of regulatory bodies.

Conclusion

The clash between the two regulators is over for the time being but does that guarantee the non occurrence of same in the future? Getting something resolved by putting an end to the claim of one party has never been a fruitful and long lasting proposition. For the time being SEBI might be silenced for it has become toothless but the question remains to be settled about the validity of the ULIP itself leave its jurisdictional validity. There is a group of experts who are voicing against the ULIPs since long but their points are suppressed in the high powered clash of the two regulators. Also IRDA under whose jurisdiction the ULIP business will finally be defined needs to have some stringent provisions governing the disclosure and compliance requirements. It should also tighten the noose over the insurance companies with clearly defined stringent provisions for them to submit periodical disclosures and accordingly frame investor friendly guidelines. Being master is one thing and handling the responsibility with that power is an altogether different ballgame. We need to see whether IRDA is able to justify its newly acquired power or not?

Also the outcomes of the high level Committee to resolve the dispute between regulatory bodies will be keenly followed event. This may go a long way in defining the roles of regulatory bodies in a country where we have a case of multiplicity of them.