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NATIONALIZATION AND PRIVATIZATION OF THE INSURANCE BUSINESS IN INDIA

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ABSTRACT

After the Indian insurance Companies Act, 1938 was passed, there was mushroom growth of insurance companies in India. In spite of mushrooming of many insurance companies per capita insurance in India was merely Rs. 8 in 1944 as against Rs. 2000 and Rs. 600 in US and UK respectively. Even this limited growth is marked by many malpractices, deficiencies and frequent liquidations of insurance companies shaking public confidence and depriving policyholders of their savings and security. It is reported that in those days insurance and banking was in the control of big industry houses resulting in interlocking of funds between banks and insurance companies. These irregularities were mainly of two types. Firstly, malpractices that had crept into management of insurance companies especially during 1940s such acquisition of insurance companies by financiers and use of life insurance to serve other enterprises in which the financier was interested or for speculation, payment of large emoluments to nominees of the controlling interests and interlocking of funds between banks and insurance companies. Secondly, factors which have operated for years towards disruption of Indian insurance such as excessive costs, rebating and unsatisfactory standards of management of business.

KEY WORDS : Insurance, Nationalization Etc

INTRODUCTION

These dark deeds of dishonest insurance men helped to intensify the public chauvinism and invited public demand for nationalization. As a consequence Government of India nationalized life insurance by amalgamating all the private companies under one corporation, i.e. Life Insurance Corporation of India. At the time of nationalization of life insurance in 1956, one hundred and fifty four Indian insurers, sixteen Non-Indian insurers and seventy-five provident societies were carrying on the life insurance business in India. Despite of this broad-based rganization of life insurance, the insurance business was mainly restricted to cities and towns at that time. With this background the chapter seeks to discuss the nationalization and privatization of insurance business in India. It examines the rationale for nationalization and privatization of life and general insurance business in India. The process and impact of nationalization, privatization of insurance business are also explained

RATIONALE FOR NATIONALIZATION

After India became independent in 1947, the then Prime Minister Jawaharlal Nehru‟s vision was to have key industries under direct government control to facilitate the implementation of National Planning. Insurance business (or for that matter, any financial service) was not seen to be of strategic importance. The nationalization of life insurance is an important step in our march towards a socialist society. Its objective was to serve the individual as well as the State. We require life insurance to spread rapidly all over the country and to bring a measure of security to our people3.

RATIONAL FOR NATIONALIZATION OF LIFE INSURANCE BUSINESS

The rationale for nationalization of life insurance business and LIC as outlined by the then by Finance Minister, Shri C.D. Deshmukh, while piloting the Bill for nationalization thus: Firstly, to conduct the business with the utmost economy, in a spirit of trusteeship; Secondly, to charge premium no higher than warranted by strict actuarial considerations; Thirdly, to invest the funds for obtaining maximum yield for the policy-holders consistent with safety of the capital; and lastly, to render prompt and efficient service to policy-holders, thereby making insurance widely popular he genesis of nationalization of life insurance came from a document produced by Mr. H. D. Malaviya called "Insurance Business in India" on behalf of the Indian National Congress. In that document, he made four important claims to justify nationalization. First, he argued that insurance is a "cooperative enterprise," under a socialist form of government, therefore, it is more suited for government to be in insurance business on behalf of the "people". Second, he claimed that Indian companies are excessively expensive. Third, he argued that private competition has not improved services to the "public" or to the policyholders. Preventive activities such as better public health, medical check-up, hazard prevention activities did not improve. Fourth, lapse ratios of life policies were very high leading to "national waste." The Preamble of LIC Act, 1956 provides the objective of nationalization of LIC business in India in the following words: An Act provide for a nationalization of Life Insurance Business in India by transferring all such business to a corporation established for the purpose and provide for the regulation and controls of the business of the corporation and for matter connected therewith or incidental death. Thus, the nationalization was justified based on three distinct arguments. First, the government wanted to use the resources for its own purpose. Clearly that meant that the government was not willing to pay market rate of return for the assets (otherwise, they could have raised the capital whether insurance companies were private or public); Second, it sought to increase market penetration by nationalization. How could nationalization possibly deepen the market that private insurance companies cannot? There are two possibilities.

(1) Nationalization would create a monopoly. If there are economies of scale in the market, it would thus become possible for government to cut the cost of operation per policy sold below what private companies could.

(2) Through nationalization government could take life insurance in rural areas where it was not profitable for private businesses to sell insurance; Thirdly, the government found the number of failures of insurance companies to be unacceptable. The government claimed that the failures were the result of mismanagement4.

RATIONALE FOR NATIONALIZATION OF GENERAL INSURANCE BUSINESS

The rationale for nationalization of general insurance business and the objective behind the established GIC as summarized under The General Insurance Business (Nationalization)Act 1972 to provide for the acquisition and transfer of shares of Indian Insurance companies and undertaking of other existing insurer in order to serve better the needs of the economic by the securing the development of general insurance business in the best interest of the community and to insure that the operation of the economic system does not result in the concentration of the wealth to the common detriment and control of such business. Prior to 1973, general insurance was urban- centric, catering mainly to the needs of organized trade and Industry. One hundred and seven insurers including branches of foreign companies operating in the country were amalgamated. These were grouped into four companies, viz. the National Insurance Company Ltd., the Oriental Insurance Company Ltd., the New India Assurance Company Ltd., and the United India Insurance Company Ltd. with head offices at Calcutta, New Delhi, Bombay and Madras respectively. GIC was incorporated as a company in 1972 and it commenced business on January 1st 1973. Before November 1972, a number of Indian and many foreign companies did general insurance business in India and this business was linked with their branches abroad. In addition, LIC, some mutual companies and cooperative societies also offered this product. In fact, on the eve of nationalisation, Indian (including LIC) and non-Indian entities carried out insurance business in India. Nationalisation saw the business of all these organisations absorbed by the General Insurance Corporation (GIC) with its four subsidiaries5.

PROCESS OF NATIONALIZATION OF LIFE INSURANCE BUSINESS

Political independence under the stewardship of our first beloved Prime Minister JawaharLal Nehru, the people of India moved to achieve their economic independence by the five year plan. The agrarian society was to be industrialised by government activity and planning. The level of education was also rising as a consequence of which the insurance consciousness in people of country increased. There was increased confidence in domestic companies. The leading insurers also indulged in vigorous developmental programmes. All these contributed to a boom in the insurance business an in particular in life business. Huge amount of capital were available with the insurer and the government found it handy to utilise there funds for its developmental plan and also to insure the investing public a better security.

The life insurance business was first nationalized in 1956 by the passing of Life Insurance Corporation Act 1956. The controlled business of all insurers whose business was nationalized was taken over by the corporation along with their assets and liabilities. The original capital of the Corporation was Rs. 5 crores which was provided by the Central Government under the Act. The creation, control and extension of the Corporation is in the hands of the Central Government. Along with the life, fire and marine, other insurance like motor vehicles, aviation, burglary and other liability insurance also developed. In the beginning this business was monopolized by British firms. The Indian insurer got into this business during the present century. All reinsurance business was in the hands of the foreign firms and the first Indian reinsurance concern, namely, the Reinsurance Corporation of India was formed in 1957 with a view to stop the heavy drain on our foreign exchange. After the nationalization of the life business, The Insurance Act 1938 applied mainly to the general insurance by a drastic amendment in 1968 to the act, more effective control and supervision was provided over the general insurance companies requiring increased deposits from them, giving the controller of insurance more power to inspect and issue direction to the insurer in all matters including the appointment and removal of their directors, constituting a tarrif advisory committee to fix control and regulate the rates of premiums, conditions of policies etc. The function of tariff advisory committee infixing and revising the rate of tariff was held as a legislative power and not an administrative one and so binding on the insured in the same manner as any other provisions of Insurance Act in spite of such control there was persistent public demand for the nationalisation of general insurance business on which an ordinance was promulgated by the president of India on 13 may 1971 which was replaced by the General Insurance (Emergency Provisions) Act 1971. Finally in 1972 the general insurance business also nationalised by setting up our government corporation called the General Insurance Corporation with four subsidiary companies for caring on the general insurance business. The nationalised insurance companies were expected not to confine themselves to the present activities but would cover new field in due course. In this way by the end of the year 1972 both life and general insurance business were nationalized. The rationale behind nationalization is summarized as under6.

PROCESS OF NATIONALIZATION OF GENERAL INSURANCE BUSINESS

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companies for carrying on the general insurance business.
The nationalisedinsirance companies were expected not to confine themselves to the present activities but would cover new fields in due course. The object of the Act to provide for the acquisition and transfer of shares of Indian insurance companies and undertaking of other existing insurer in order to serve better the needs of the economic by the securing the development of general insurance business in the best interests of the community and to insure that the operation of the economic system doesn"t result in the concentration of the wealth to the common detriment and control of such business. Section 4 of the GIC (Nationalisation) Act, 1972 deals with the effect of nationalisation of general insurance business by transferring the share of the existed insurer to GIC. On the appointed day all the share in capital of every Indian Insurance Company shall stand transferred to and vested the central government in the central government free of all trusts, liabilities and encumbrances affecting them. The Central Government shall by Notification provide for the transfer of not less than 10 share of every such company such persons as may be specified in the notification to enable the Indian insurance company to function as a government company. Every Notification made under sub-section (2) shall specify the names and description of the person to whom the shares are transferred and the particulars of shares which are transferred to each such person. A copy of every Notification made under subsection (2) shall, as soon as may be after it is made, be sent by the Central Government to the concerned Indian Insurance Company, who shall, on receipt of such copy, and notwithstanding anything contained in the Companies Act of r in its articles of association, forthwith rectify its register of members by including therein the persons mentioned in the notification as the holders of the shares specified therein. For the removal of doubts it is hereby declared that the transfer and vesting of shares effected under sub-section
(1) shall not be deemed to affect any right of the Indian Insurance Company subsisting immediately before the appointed day against any share holder to recover from him any sum of money on the ground that share holder has not paid or credited to the insurer the whole or any part of the value of the shares held by him or on any other ground whatsoever7.

MALHOTRA COMMITTEE THE ARCHITECTURE OF PRIVATIZATION OF INSURANCE BUSINESS

The Committee recommends as follows:
(i) The private sector should be allowed to enter insurance business. No single company should be allowed to transact both life and general insurance business. The number of new entrants should be controlled;
(ii) The minimum paid-up capital for a new entrant should be Rs 100 crore. However, a lower capital requirement can be prescribed for state level cooperative institutions taking up life insurance business;
(iii) The promoters' holding in a private insurance company should not exceed 40% of the total. However, if the promoters wish to start with a higher holding, they should be permitted to do so provided their holding is brought down to 40% within a specified period of time through public offering. No person other than the promoters should be allowed to hold more than 1% of the equity. Promoters should at no time hold less than 26% of the paid-up capital;
(iv) If and when entry of foreign insurance companies is permitted, it should be done on selective basis. They should be required to float an Indian company for the purpose, preferably in joint venture with Indian partner;
(v) Before the private sector is allowed to enter the insurance field, the Controller of Insurance should start functioning effectively;
(vi) Regulatory and prudential norms as well as conditions for ensuring level playing fields among insurers should be finalised early so that intending entrants into the insurance business would be aware of the stipulations they would have to comply with. These conditions should aim to ensure that life insurers do not neglect the small man or the rural business and that the general insurers have balanced portfolios;
(vii) Though nationalised insurance companies are in a position to face competition, it is essential

that they quickly upgrade their technology, reorganise themselves on more efficient lines and are enabled to operate as board-run enterprises.

LIBERALIZATION OF INSURANCE BUSINESS

(a) A majority of areas previously reserved for the public sector have been thrown open to the private sector to strengthen the forces of competition. Competition is growing in the banking sector which already includes numerous public sector banks as well as private sector banks, both Indian and foreign. A similar trend is also evident among non-banking financial institutions, including leasing companies, mutual funds, merchant banks, and other intermediaries dealing with securities business. In contrast, life and general insurance companies remain state monopolies. LIC is a moonlit. There is very little competition among subsidiary companies of G1C. The question arises as to why the consumer of insurance services should not be provided a wider choice so that he can get the benefits of competition in terms of range of insurance products, lower price of insurance covers, and better customer service8;

(b) The Committee further observed: part of government share holding in selected public sector enterprises, including profitable public sector banks, is being offered to the public. Should a similar policy be adopted for the insurance industry? If so, how far should disinvestment go in order to make the insurance companies operationally autonomous, efficient and competitive;

(c) The Committee added: Regulation over the capital market as well as the banking sector has been considerably strengthened. On the other hand, thanks to nationalisation, regulation of the insurance industry has atrophied. Reestablishment of effective regulation over the insurance business is a crucial issue which would become all the more urgent if the sector was to be liberalized;

(d) The Committee also observed “There is very high pre-emption of insurance industry's funds through government mandated investments. This affects the financial results of insurance companies and has implications for rates of insurance premia and returns on savings invested in life insurance. Preemption of commercial banks61 resources is being reduced. What changes should be made in regard to mandated investments of the insurance industry. The rapid growth of the capital market and likely development of government and corporate bond markets should offer greater investment opportunities and challenges to insurance companies”;

CONSEQUENCE OF PRIVATISATION OF INSURANCE SECTOR

1. Privatization if Insurance was eliminated the monopolistic business of Life Insurance Corporation of India. It may help to cover the wide range of risk in general insurance and also in life insurance. It helps to introduce new range of products;
2. It would also result in better customer services and help improve the variety and price of insurance products;
3. The entry of new player would speed up the spread of both life and general insurance. It will increase the insurance penetration and measure of density;
4. Entry of private players will ensure the mobilization of funds that can be utilized for the purpose of infrastructure development;
5. Allowing of commercial banks into insurance business will help to mobilization of funds from the rural areas because of the availability of vast branches of the banks;
6. Most important not the least tremendous employment opportunities will be created in the field of insurance which is a burning problem of the presence day today issues; and lastly after opening up of insurance in private sector, various leading private companies including joint ventures have entered the fields of insurance both life and non-life business. Tata AIG, Birla Sun life, HDFC standard life Insurance, Reliance General Insurance, Royal Sundaram Alliance Insurance, Bajaj Auto Alliance, IFFCO Tokio General Insurance, INA Vysya Life Insurance, SBI Life Insurance, Dabur CJU Life Insurance and Max New York Life. SBI Life insurance has launched three products Sanjeevan, Sukhjeevan and Young Sanjeevan so far and it has already sold 320 policies under its plan9.

CONCLUSION

Therefore it gave without saying that an appropriate life insurance policy within the paying capacity of the insured is one of the social security measure, which is envisaged under Indian Constitution, as held in LIC v. Consumer Education and Research Centre, social security is a facet of socio-economic justice to the people in particular to the middle class and lower middle class. Hence, in Sukh Dev Singh v. Bhagat Ram Sardar Singh Raghwanshi, the Supreme Court held that LIC is a „State‟ within the meaning of Article 12 of the Indian Constitution and it is charged with a duty to carry on life insurance business within and outside India to secure that the life nsurance business to be developed to the best advantage of the community. Therefore the LIC must function to the best interest of the community. Insurance law in our country is spread through a number of legislation, regulations, judicial decisions and orders of quasi-judicial bodies like consumer fora. Some legislations deal with the formation of contract of insurance like Indian Contract Act, 1872 and Insurance Act, 1938. Some lays down the provisions regarding regulation and control of insurance business like Insurance Act 1938 and Insurance Regulatory and Development Authority of India Act, 1999. Some legislations aims to deal with specific categories of insurance like Life Insurance Corporation Act, 1956, General Insurance Business (Nationalization) Act, 1972 and Marine Insurance Act, 1963 while other deal with liability insurance like Public Liability Insurance Act, 1991 and Motor Vehicle Act, 1988. Apart from this, IRDAI has framed various regulations since its inception to regulate various aspect of insurance. The existence of wide array of legislations on insurance reveals a segmented rather than an integrated and holistic approach towards the regulations of insurance business in India. The presence of repetition, replications, contradictions, confusion, multiple legislations have made the things difficult to understand and implement.

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