

Impact Of Foreign Direct Investment In Insurance Sector In India- A Legal Study

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ABSTRACT

For a developing country like India, Foreign Direct Investment (FDI) is considered as new striking features of development during the last two decades to accelerate the spectacular growth and economic activities in Indian context. The 21st century has made the world as one of the most extraordinary, transparent, vibrant, liberal and interdependent world economic order where FDI insurance are used to bridge the gap between domestic savings and investments among the emerging and developing economies. The role of FDI in present insurance context is noteworthy to mobilize national savings and channelize them into investment into different sectors of economy. FDI in insurance would increase the transmission of insurance to meet India's long term capital requirements to finance and building of infrastructures. Despite many years of parliamentary debate, the present NDA Government getting a green signal to pass the Insurance Laws (Amendment) Act, 2015 seek to increase the cap on FDI in the insurance sector from 26% to 49% but the regulations have still lots of restrictions and plethora of uncertainties. This research paper's objectives are to explore the cost of FDI in insurance, know the reasons behind the urgent needs to attract more FDI, major reforms and overview of the policy and regulatory environment. This study tries to conclude that increase of FDI is no doubt an optimistic move for the future development and hence this sector need huge amount of capital investment which can be done effectively in present scenario.

Key Words: Foreign Direct Investment, India, Foreign Investment, Insurance Sector, Economy, Capital.

INTRODUCTION**Indian Dependence On Foreign Direct Investment And Insurance**

In present Indian economic front, the insurance sector keeps pace with the neo-liberalizing international trend due to the recent Balance of Payment and economic crisis in the 90th decade which probably the major cause to bring a favorable breakthrough in the insurance market in India. The world has witnessed that the Indian economy has been dependent on the insurance sector for many years. But this dependence has caused numerous problems and rarely made it apparent those alternative sources of financing for diversifying the economy, providing new employment opportunities, transferring technology and globalization which were considered as the burning topic of debate for Liberalization-Privatization and Globalization (LPG) of Foreign Direct investment (FDI) and trade policies. During the advent of the New Industrial Economic Policy in 1991 in Indian context, FDI plays a vital role and the Multinational Corporations (MNCs) have come out as a major actor where globalization offers a parallel opportunity for developing countries like India to attain a quicker economic growth through trade and investment. The scenario depicts that during the time of the 1970s, the international trade grew more rapidly than FDI, so far that international trade was most significant for international economic collaborations. Due to some administrative lacuna in country wise, the situation changed fundamentally in the middle of the 1980s.

When FDI started to increase sharply, the government attempted to address the situation in various successive plans which were designed to improve and modernize the economy through transferring technologies and establishing marketing and procuring network for efficient productions and sales internationally.¹ At this present juncture, due to lack of control over the national economy and failed to adequate solution to generate employment, there is no way to attract FDI which is considered as an urgent need of hour.

The need for FDI is not only developing or under developed countries but also in the developing world. The poor countries may require the FDI mostly for developmental purpose. It helps the developing countries to developed transparent broad and effective policy environment for investment issues as well as builds human and institutional capacity to execute the same high on agenda. There is hardly a facet of human psyche that the 21st century has shrunk the world into a small village where no nation can live in isolation. Even the international organizations like the UN agencies also highlight the urgent needs to shed protectionism in the trade policies by all the countries. FDI has helped the Indian

¹ Kumar, Sarwan;(2016); Impact of FDI on Economic Growth of India; (Unpublished); PhD. Thesis; Himachal Pradesh University,; Shimla; p.1

economy grow and government continues to encourage more investment. So, FDI are used to bridge the gap between domestic savings and investments.² Foreign direct investment is important not only for the growth of the national economy but also the source of income as well as forced saving helps latest advancement of the technology transfer, new techniques, management know-how, infrastructure facilities and increased productive capacity from developed economies to developed one.

FDI has become an instrumental factor and this kind of paradigm shift in attitude led the Indian government to subscribe the general international trend towards encouraging foreign direct investment. The ultimate result is that it provides considerable changes in the existing legal and regulatory framework. In this research study, it will examine the nature, scope and significance of the legal framework for FDI in Indian insurance sector in the light of the challenges because at present, India is a flourishing industry with both national and international players competing and growing at rapid rate. In India, insurance sector consists of 52 insurance companies where 24 are in life insurance and 28 are non-life insurers. Life Insurance Corporation of India (LIC) is the sole public sector company with six non-life insurers, re-insurers, and other stakeholders like agents, brokers, surveyors and third party administrators servicing health insurance claims.³

PURPOSE OF THE STUDY

Laws are formulated only for the better application of FDI that created to provide a favourable condition which will attract foreign investors to a host country. There is a possibility that FDI can provide significant benefits to the host country, but problems may arise in the areas of the bureaucratic inefficiency, protection of property rights, ability to repatriate profits, liberated market for currency exchange, erosion of the traditional values, and consequences arising from foreign competition and ownership. In the process of accelerating the growth of FDI in the developing country like India, the government of India has make the regulatory framework lot more flexible to striking the balance between the legal and political dimensions while attempting to safeguard the inherent nature of the country. Regarding legal and regulatory framework, it is equally important to note down that foreign investors get different advantages of tax holiday, tax exemptions, exemptions of service and central taxes. Sometimes time's political instability creates negative impact upon the firms where FDI is imposed. The government so far as committed to reduce political instability and opened few Special

² Talwar, Ms. Reena; and Ali, Dr. Saiyed Wajid; (2015); Foreign Direct Investment in Insurance Sector in India: A Critique; *BVIMSR's Journal of Management Research*; India; Vol. 7 Issue-1. p.68

³ Hasan, Aamir; (2015); Impact Analysis of FDI on insurance Sector in India; *SMS*; India; Vol. XI, No. 1; June 2015; p.3

Economic Zones (SEZs)⁴ to get benefits by investing money. Apart from that there are number of laws has been passed and executed for making the investment safe, secure, transparent and easily comprehensive for the foreign investors.

In this study, it will examine the significance of the FDI in Insurance sector in India and its legal and regulatory framework within the ambit of the public and private enterprise.

RESEARCH METHODOLOGY

For this study, the researcher has been adopting doctrinal method of research based on the literature review and exploratory in nature. Due to the limited sources, the researcher has used only the secondary sources which are procured from the public domain such as government reports, websites, research reports, Department of Industrial Policy and Promotion (DIPP) reports, Reserve Bank of India (RBI) reports, reports of Planning Commission/NITI Aayog, IRDA Reports and various research articles published in different journals and collect all kinds' necessary information keeping the above significance in the mind. During analysis and interpretation of data, explorative research has been carried out according to the depth of the study.

REVIEW OF LITERATURE

This study has a good impact on the basis of the previous studies. During the last two decades Foreign Direct Investment has gained a considerable attention of most of the researchers around the globe. A remarkable development has been made by the researchers, insurance analysts and economists in the field of FDI. In today's modern competitive world, FDI has been considered as one of the most fascinating and interesting topic among the researchers. The collected review of literature on FDI reveals that though the rest of the world used the mechanisms of the FDI in insurance sector but still, it is a matter of discussion. FDI in insurance has some merits, limitations and its barriers. For its theoretical perspectives, many research scholars argue about the possibilities of the economic development with the help of FDI. It is true that the fundamental objectives of the FDI are to earn the profit at any cost by ignoring the overall social and economic development of the host nation. So, the present investigation is to examine and a clear attempt to reduce the illusion and verify the thoughts about the implication of FDI in India.

⁴ Kannan, S. and Geetha, V; (2014); FDI in India: Law, Policy and Procedure; 2nd edition; Thomson Reuters; P.102

S.Kannan and V. Geetha (2014) in their book “FDI in India: Law, Policy and Procedure” in their book revealed that insurance sector, specifically the life insurance dominate the overall sector in India, accounting for 87% of total premiums generated in the country. After the entry of the FDI in private participation in 2000, a large number of foreign firms are entering into India despite certain restrictions over the ownership, business functions and allocations of the raw materials.

Manoj Pant with Deepika Srivastava (2015) in their book ‘*FDI in India- History, Policy and the Asian Perspective*’ reported about foreign direct investment in insurance industry in India and tracing the evolution and development of India’s foreign investment policy in the 1980s to 2000s.

Swati Mahajan (2016) in her book “*Contemporary Economy (Including Banking & International Economic Issues)*” revealed that FDI and in insurance are used to bridge the gap between domestic savings and investments, especially in developing and under developed countries. FDI is equally important for the long term growth of the economy of a country.

Suman Kalyan Choudhury and Sukanta Sarkar in their book “*Foreign Direct Investment Indian Perspective*” reported that FDI has played an important role in the process of globalization. The rapid expansion in FDI by the multinational enterprises since the mid 1980s may be attributed to significant changes in technologies, greater liberalization of trade and investment regimes including developing countries like India.

NEED OF THE STUDY

In the history of Indian trade, the 1990th decade is considered as landmark for the speedy development after the regime of the Balance of Payment. It typically introduced the LPG to boost the economic development and at the same time it was the urgent need of hour to open up the Indian insurance sector for foreign direct investment to accelerate the growth engine of the country’s economy. As per the provision of United Nations Declaration of Human Rights, 1948, it provides that “everyone has a right to a standard of living adequate for the health and well being of himself and his family, including food, sheltering, clothing and medical care and necessary social service along with the right to security in the event of unemployment, sickness, disability, widowhood or other lack of livelihood in circumstances beyond his control. Apart from the law and directions of the Insurance Regulatory and Development Authority of India (IRDA), Insurance companies in India are obliged to extend insurance benefits to economically weaker sections of the society in the unorganized sector with flexibility in discharging its functions in a way which will improve consumer confidence in the law and also generate employment at a highest and wider level in India. To raise the investment flow in India,

insurance is necessary. Without insurance, trade commerce will find it difficult to face the impact of major perils like fire, earthquake etc.⁵

The insurance sector in India is a flourishing industry with a considerable importance to bring a developing economy where both national and international players competing and growing at a high and rapid style. In this study, it tries to concentrate on insurance that FDI is necessary and it is a major tool of globalization for economic implication for future development. It requires a detailed analysis of FDI into requires an examination of the trend and the impact of FDI in the insurance sector.

MAIN AREA OF THE STUDY

This study relies on the legal and regulatory framework of FDI in insurance sector in India. It primarily analyse the law, legal procedure, history and eventually the necessity of the FDI in Indian perspective. It examines the hurdles connected with the administrative as well as the political obstacles within the legal framework of FDI. Therefore, it tries to prevent the administrative barriers for successful integration of FDI, including the permissible zone of activities which are open for the foreign investment, the role of privatization in the light of the promotion of FDI in the insurance sector in India.

OBJECTIVE OF THE STUDY

After the independence, it sustain several advantages like the superior information technology, well developed industrial base, large insurance and commercial market, lots of skilled and trained workers who can speak English like the other nations citizen to reduced he brain drain at a low wage rate.⁶ Yet India is relatively low in FDI flow in comparison to the other developed countries and ready to attract FDI for faster economic growth. In this context, the study has followed two distinct objectives:

- (i) To study the current scenario of FDI and the reasons behind the urgent needs to attract more FDI in insurance sector in India.
- (ii) To analyse the major reforms in the light of the Insurance Laws (Amendment) Act, 2015.

⁵ Bhattacharyya, Sunil Kr. (ed.); (2017); Emerging Issues of Foreign Direct Investment (FDI) in India with Special Reference to NE Region; First Edition; Jagaran Sahitya Prakash; Dhing, Nagaon; P.46

⁶ Bedi, Priyanka; and Kharbanda, Ekta; (2014); Analysis of Inflows of Foreign Direct Investment in India- Problems and Challenges; Global Journal of Finance and Management, India; Vol. 6; Number 7; P.676

STATEMENT OF THE PROBLEMS

The government's intention from the very beginning of the nationalization of the insurance industry was to create a monopoly state and protect the policyholders from the private and foreign competition. Insurance industry faced lot more problems like technology gap, poor infrastructure, inadequate capital and poor product quality. The major problems are-

- (i) There is a lack of insurance education and mass awareness among the common people.
- (ii) The infrastructure is very poor in the rural area, because due to lack of bank account, low income, expensive and luxurious schemes cannot attract them.

FOREIGN DIRECT INVESTMENT AND INSURANCE SECTOR IN INDIA

A healthy and developing insurance sector is of vital importance to every modern economy. Because insurance encourages the savings habit, provides a safety net to rural and urban enterprises and individuals and generates the long term funds for infrastructure development. During the 19th century, there was no any proper rules and regulation regarding insurance in Indian history. But after independence FDI is simultaneously considered as an important instrument to achieve the long term economic development not only as a source of income, extra capital but also through transfer of developed technology together with the fast moving global management practice. Because after liberalization of the insurance industry in India taking the suggestions from the Malhotra committee, it has emerged as the acid test for the ability and willingness of the central government to implement the market friendly economic reform and policy making regulatory environment.

DEFINITION OF FOREIGN DIRECT INVESTMENT

In today's economic scenario, the concept of FDI is adopted by many developing countries for speedy economic growth. Though, there is no sophisticated definition, but the International Monetary Fund (IMF), United Nations Conference on Trade and Development (UNCTAD)'s World Investment Report has defined FDI is "an investment that is made to acquire a lasting interest in an enterprise operating in an economy other than that of the investor" and also FDI as "an international investment that reflects the objectives of a resident entity in one economy (Foreign Direct investment or Parent Enterprise) or obtaining a "Lasting Interest" an control in an enterprise resident in an economy other

that of the Foreign Direct Investor. In this context, the Government of India is also not exceptional relating to the adoption of FDI in Insurance.⁷

GROWTH OF FDI AND A GLOBAL OVER VIEW IN INSURANCE INDUSTRY

Growing and impetus competition will work together within the ambit of wider variety of products which results into a more suitable, flexible and valued insurance sector in India. It attributes the reap of future benefit and the new government's stress on the economic reform, several steps taken by the IRDA to make insurance industry more consumer friendly and India's favourable demographic, the future of India's insurance industry looks very good. Due to this increasing immense competition, the global insurance industry put pressure spontaneously on the existing companies to become more effective and efficient to enhance their advancement of technology related process and alter their business models. In common parlance, it is noteworthy that, most insurance companies are demanding to improve the effectiveness of their underwriting process, cut their expenses and reduce claims leakage since returns from investments are decrease.

SOURCES OF FDI REGULATION IN INDIA

To provide an elementary picture about the smooth functioning of the government machinery, there must have some prominent and contemporary sources for the regulation of FDI in insurance. It may be the national laws, bilateral investment treaties, multilateral and regional agreements, local customary laws and state control etc.

In National Perspective

In a nation building process, a proper drafted and implementation of the FDI law is fruitful for regulating and monitoring the inflow of FDI. India is also not exceptional; hence, it paves the way for maximizing the benefits received from such foreign investment. So, local and national laws pay attention and are viewed as "Quid Pro Quo for the right to invest" with two sophisticated purpose like Entry Route and Operational Existence.⁸

Entry Route and Operational Existence for Receiving FDI

For the safest and secured implication of FDI laws, India has maintained the timeliest regulated insurance regulation in the world where increased investment and intense competition will be beneficial

⁷ *ibid*; 1, pp.1-2

⁸ Sewilem, Mohammed Al; (2012); *The Legal Framework for Foreign Direct Investment in the Kingdom of Saudi Arabia: The Theory and Practice*; (Unpublished); PhD. Thesis; School of Law; School of Oriental and African Studies; University of London; P.65

for the both insurer and insured. There is a common psychology that the concept of 'foreign' element has not permitted but the admission of FDI in a certain host country has some objectives and conditions. Many developed and developing countries imposed some FDI restriction directly or indirectly in the name of the licensing and citizenship requirements. After liberalizing the insurance sector, the Central Government had opened up the insurance sector for private participation in 1999 and also allowing the private companies to have foreign equity up to 26%.

In order to boost the capital intensive insurance sector, the government raised the FDI cap in insurance to 49% from 26% through a notification issued by the Department of Industrial Policy and Promotion (DIPP).⁹

Though FDI in India has been largely export oriented, but an Indian company may have received FDI under two routes, which are given as below-

- i) Automatic Route (RBI Route)
- ii) Government Route (SIA/ FIPB route)

In general, the application of FDI is not covered under the automatic route, but simply requires prior approval of the central government of India, which is considered as the Foreign Investment Promotion Board (FIPB), Department of Economic Affairs, and Ministry of Finance.¹⁰

Favourable Legislation in Indian Scenario

After closely witnessing the rapid economic growth in China and Asian players, it has undergone a process to adopt national laws that attract foreign investors by creating an investment climate in India. In Indian scenario, FDI is governed and distribution by a number of laws. FDI in insurance sector, as prescribed in the Insurance Act, 1938 is allowed under the automatic route. The Reserve Bank of India issued a set of regulation which outlined and 'automatic route' through which foreign investors may be granted automatic approval for investment. So, these are some key legislations that could have a potential impact on foreign investors setting up in India, are as follows-

- i) Insurance Act, 1938
- ii) Life Insurance Corporation Act, 1956
- iii) General Insurance Business (Nationalization) Act, 1972
- iv) Insurance Regulatory and Development Authority Act, 1999 (IRDA)
- v) Insurance Laws (Amendment) Act, 2015

⁹ Mahajan, Swati (ed.); (2016); *Contemporary Economy*; 4th ed.; Knowracle Publication; jammu; p.70

¹⁰ Choudhury, Dr. Suman Kalyan; and Sarkar, Dr. Sukanta;(ed.); (2014); *Foreign Direct Investment: Indian Perspective*; 1st ed.; S. K. Book Agency; New Delhi; p. 69

SETTING FOR WTO NEGOTIATIONS UPON FDI IN INSURANCE SECTOR

Generally, there is a close relationship between the regulation of the FDI and the labour markets in the host country to achieve the greater benefits. As per the provisions of the North American Free Trade Agreement, Mexico showed the best example of getting highest FDI benefit; Agreements among the ASEAN (1987) Member countries are also successful example relating to the promotion and protection of the foreign benefits. In this current WTO legal framework, the General Agreement on Trade Services (GATs), the Agreement on Trade-Related Investment Measures (TRIMs), the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), Uruguay Round Understanding on Rules and Procedure governing the dispute settlement. Hence, in 1998, a significant development came to limelight in the field of the multilateral investment treaty through OECD namely it was Multilateral Agreement on Investment (MAI).¹¹

POLICY AND REGULATORY ENVIRONMENT OF FDI IN INSURANCE

In order to remove the ambiguity prevails regarding the confusion of FDI and Foreign Institutional Investment (FII), a committee has already been constituted under the chairmanship of Dr. Arvind Mayaram, Secretary, DEA, Ministry of Finance and which recommends for creating more jobs, creating more sources of revenue, technology transfer and reduce the country's dependence on agriculture, industry and insurance related sector. In this way, the government of India was highly required to open the Indian market for the world community at large as pre requisite criteria of joining the World Trade Organization. Under the purview of WTO and its accession to the globalization; it helps the transition from dual economic structure in to a highly integrated economy and it paves the way to changes the rules of investment.

- i) Foreign investment of 10% or more through eligible instruments, made in an Indian listed company would be treated as FDI.
- ii) An investor may be allowed to invest to below the 10% threshold and this can be treated as FDI subject to condition that FDI stake is raised to 10% or beyond within 1 year from the date of first purchase.
- iii) In peculiar company, an investor can hold the investment either under the FDI route or under the FII route.¹²

¹¹ *ibid*, 8; p.78

¹² Sikhare, Yogesh; (2015, 29-30 January); Foreign Direct Investment in Insurance in India; Business and Management Review; Vol. 5; No.4; Kalyan, India: ICIEE. p.33

TRANSPARENCY, PREDICTABILITY AND LEGAL SECURITY OF FDI IN INSURANCE SECTOR

In the days of the Corporate Social Responsibility (CSR), transparency is considered as the highest degree of the social cohesion and stability of the host countries affair. The absence of the cohesion and social stability it may create possible damage to the reputation and risk perception among the foreign enterprises. A non transparent host-country business environment raises information costs, divert corporate energies and a bucket of corruption. The entry of FDI paves the way to a more transparent, vibrant, corruption less and international cooperation friendly environment which is very important. Without any sound, effective and arguably regulated policy framework foreign investors may have facing some problem to take risk perception. The continuous wave of economic liberalization and globalization sweeping across the world has opened many national markets for international players. But the foreign investors need transparent and predictable rules on which they can operate with the help of legal security. In most of the cases, risk and consequent rewards would be unreasonable for the host countries. So, a powerful attributes in favour of Multilateral Agreements on Investment (MAI) under the direct guidance of World Trade Organization (WTO) is necessary and hence, it will provide the basic needed transparency, predictability and legal security. Because the opposite views regarding the lack of transparency, predictability and legal security is precisely what is often the origin of difficulties for countries to attract the FDI.¹³

MAJOR HIGHLIGHTS OF THE INSURANCE LAW (AMENDMENT) ACT, 2015

Due to changing scenario in the society, lot of changes have been made by the successive government and took vigorous steps to amend the Insurance act 1938 for various reasons. The recently amended insurance laws aims at empowering the Insurance Regulatory and Development Authority of India (IRDAI) with the intention to bring more flexibility and profound efficiency in discharging its functions in a way which will improve the consumer friendly confidence in the legal side and also generate employment at a wider level.

The Bill was passed with major reforms in the Insurance Act, 1938, the General Insurance Business (Nationalization) Act, 1972 and the Insurance Regulatory and Development Authority (IRDA) Act, 1999. The Insurance Laws (Amendment) Act, 2015 to be so enacted will replace the old Insurance Laws (Amendment) Ordinance, 2014 which came into force in 26th December, 2014. The main highlights of this Act-

¹³ Drabek, Zdenek. (1998, June). A Multilateral Agreement on Investment, Convincing the Sceptics. *Staff Working Paper. ERAD-98-05*. Economic Research and Analysis Division: World Trade Organization. p. 5

- i.** The new law raises the FDI limit for insurance from 26% to 49% with the safeguard of Indian partnership and control.
- ii.** Promoting Reinsurance business in India.
- iii.** Promotion of health insurance as a separate segment.

FINDINGS AND CONCLUSION

By evaluating the relevant data of the selected working of Life and Non-life Insurance Companies in India and especially to the north eastern states, it can be said that there is need of FDI to strengthen the Insurance Companies for business expansion and also the Insurance Councils, by way of inclusion of local self help groups and insurance co-operative societies. But still, there is a long way ahead. Selected private life insurance companies are improving business within the ambit of the urban and semi urban areas. Though, Foreign Direct Investment has no reverse impact on the business procedure but the researcher has found that FDI assists in infrastructural growth and better facilities and promoting the business management in a planned way. So, there is a need to take special care as compared to other business, understanding its reliability and potentiality to re-engineer the business model within the ambit of Make in India and present working schemes like Start-up India. The present image of long pending Act has opened a new vistas and probably will help to deepen the insurance market in the country which is the second most populous in the world. There is a possibility in the hands of the foreign investors to have a healthy and sound arbitral system to monitoring the litigation for quick disposal. Because due to the lack of knowledge and lack of trust on judicial system, the foreign investors they generally relied on the host country's sound arbitration mechanism.