

ulips



# The road

THE IRDA-SEBI TUSSLE OVER  
HAVE A BIG IMPACT ON THE

By **Monika Shinghal**

**U**niversally, consumer buying behaviour is governed by their need to buy rather than the shopkeeper's urge to sell. Simply put, buying precedes selling. But a quick glance at the common investment habits of people in developing countries like India indicates that there are some exceptions to this universal principle. Most people in such

countries, for want of even basic knowledge of finance and money management, seek expert aid and rely on their financial planners to manage their savings and returns. Thanks to their limited knowledge of finance, they are sold investment solutions. They do not actively go out and buy investment products.

In such a scenario, the ongoing tussle between insurance watchdog Insurance Regulatory and Development Authority (IRDA) and financial market regulator

Securities and Exchange Board of India (SEBI) over regulation of unit-linked insurance products (ULIPs) could, at best, have a minimal impact.

Explained Sanjiv Bajaj, joint managing director, Bajaj Capital, which distributes insurance products of the group's insurance arm, Bajaj Allianz: "In India, financial solutions are not bought, they are sold. Although people understand the importance of investment, they don't actively look for the right

# ahead

## ULIPS MIGHT NOT MARKET



the total premium received from ULIPs recorded a phenomenal growth of 82 per cent as against the same period last year.

When compared with February, the month on month rate of growth comes to 170 per cent. While life insurance companies' ULIP business grew in February, it dipped substantially in January due to significant modifications in regulations by way of putting a cap on all charges levied on policyholders. It came about in the second half of the last calendar year. But, experts label such ups and downs as temporary jolts which are inevitable in the history of all products.

Overall, data available so far for this calendar year indicates growth of ULIP business. It has been in line with their performance last year. In 2009-10, while the life insurance business grew 25.83 per cent, the growth rate of unit linked business was 35.33 per cent. In terms of the volume of first year premium, it increased from Rs 44,332.40 crore to Rs 59,996.46 crore in 2009-10.

However, it is the April numbers which are keenly awaited. Said Alpesh Patel, principal consultant, Cedar Consulting: "While the growth registered in ULIPs so far is good, it is not entirely unexpected around this time of the year. April numbers would be interesting, as they would reveal whether the current controversy has had any impact on the product or it's just psychological." As the January to March period is the last quarter of financial year and indicates year end, any investment product witnesses good volumes with everyone rushing to make investments, specially in tax saving instruments. So while most investment products attract volumes in last quarter of the financial year, first quarter (April-June) of the year usually wit-

**Overall data for this calendar year shows growth of ULIP business. In 2009-10, while the life insurance business grew 25.83 per cent, the ULIP business grew by 35.33 per cent. Volume of first year premiums increased from Rs 44,332.40 crore to Rs 59,996.46 crore in 2009-10.**

nesses a dip. ULIP is no exception. Said Patel: "It would be interesting to see if the drop is more acute this year. If it is, it could be attributed to the regulatory clash."

Meanwhile, IRDA has proposed significant changes in the regulatory guidelines for ULIPs in the last few months. The first big change came about in July last year when the regulator proposed a cap on all charges levied on customers under various heads. In order to encourage people to buy ULIPs for long-term and not look at it as short-term investment instrument, the regulator insisted that the difference between gross profit and net profit should not exceed 300 basis points and 225 basis points (100 basis points is equivalent to 1 per cent) for ULIPs less than or up to 10 years and ULIPs more than 10 years respectively. Of this, fund management charges should not exceed 135 basis points irrespective of the policy tenure. Until now, while their method of allocation was pre-defined, there wasn't any cap.

Therefore, often the total cost of investing in ULIPs would exceed

products. Instead, they rely on financial planners. So, if one's agent convinces him of the product's utility, he is less likely to contest. Given this, what impact can such regulations have on the product and business of life insurance companies?"

It would be difficult to predict if the ongoing turf war has had any bearing on ULIPs, as IRDA is yet to announce the April numbers. The war started in April, and data available so far indicates an upward trend. For instance, in March 2010,

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returns or leave very little on the table for customers. The underlying idea of this step, therefore, was to make the cost structure rational and simple and enable better returns to customers. It came amidst widespread criticism of ULIPs which were widely perceived to be high-cost-low-return insurance instruments.

In another big change proposed in August 2009, the regulator provided for scrapping surrender charges if the customer was exiting from his policy after five years, ensuring him full fund value on such exits.

Further in October, the regulator emphasised on the necessity of public disclosures by insurance companies to their customers. It came out with a detailed exposure draft which laid the format in which insurance companies were supposed to make public disclosures to their policyholders and investors. It made it mandatory for insurers to provide such data to their customers for at least a period of five years. It also proposed guidelines for public disclosures by insurance companies inviting comments from stakeholders.

The aim of this step was also to enable prospective and existing customers understand the insurance company better before buying its products or investing in its stock. In January this year, guidelines pertaining to public disclosures by insurance companies were finalised. The regulator made it mandatory for insurers to provide all such information and also host the same on their websites for a minimum period of five years latest by April 15.

Adding to the series of modifications made in ULIP guidelines in the last one year is the latest circular issued by the regulator this month. Through this, it aims to make way

for standardisation of terms and conditions of all unit linked insurance products being offered by insurance companies presently.

To protect the interests of policyholders, the regulator also proposes to bring about a standardisation of insurers' approach in the event of lapsation, revival and surrender of linked policies. Under this, the biggest change has been a proposal to put a cap on surrender charges instead of leaving it to the discretion of insurers. Reiterating that no surrender charges would be levied if the customer exits his policy after five years (six years if the term of the policy is more than 10 years),

the regulator has provided for a ceiling of 12.5 per cent for policies less than 10 years and 15 per cent for policies more than that period.

This hasn't gone down well with the industry and has sparked a debate between the regulator and industry. The industry is of the view that if this proposal goes through, the business of ULIPs would become 'unviable' for them.

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Said Bajaj: "A cap on surrender charges would not serve any purpose. On the contrary, it would defeat the regulator's goal of making ULIPs long-term products. By imposing such caps, such products are being made very investment-oriented. ULIP is a long-term solution. Such caps would only encourage people to exit from their unit linked funds whenever they want without thinking much about the charges."

Besides, the industry is largely of the view that the regulator has already done quite a lot in this direction by scrapping surren-

der charges after five years. "This cap would make it a short-term investment product when it should be looked at as a long-term protection and investment solution," added Bajaj.

Another big proposal by the regulator is the requirement on part of every insurance agent and broker to make it clear to the customer the amount he would be paying upfront as commission to him at the time of buying the unit linked policy. The underlying objective is to enhance transparency for customers and help him understand the cost he incurs in buying such products.

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This has unleashed panic in the industry, particularly in the agent and insurance broking community. Experts are of the view that if the proposal has its way, it would drastically dent the ULIP market. This, in turn, might have a bearing on the growth of life insurance industry in the short-term.

Said Ravi Trivedi, executive director, KPMG: "From a long-term perspective, this kind of transparency is great. But in a market as nascent as India, where investment solutions are sold and not bought, such rules would only discourage the selling community. Unless you give enough incentives to people selling the product on ground, they would not take interest in promoting it to customers."

The general view is that unless the

Indian financial market reaches a certain stage of maturity, such rules would not work. "If such are rules are applied at the current stage, it would create a mess in the present state of maturity," says Trivedi.

Has the current mess diverted people's attention to other investment options like New Pension Scheme (NPS)? Experts offer divergent views. While most experts think that instruments like NPS have always been popular with people but have not made much headway on account of their limited distribution, some think that it is obvious for less popular products to gain currency during such periods of disturbance.

Said Trivedi: "NPS is a great product, but one needs to see how many people are selling it. It has major distribution issues although it is an excellent investment option for people who want to invest for long-term. The cost is as low as 0.006 per cent of ULIPs."

Lovaii Navlakhi of International Money Matters agreed with Trivedi: "NPS is a far better product than ULIP but it has distribution issues." Adding an interesting dimension to the issue, he further said: "It is natural for other products to gain people's attention during such times. Besides, no single product can fulfill one's investment needs. Everyone needs to put his money in a basket of products."

All in all, experts are of the view that ULIPs, under their new structure, would in all probability, work in favour of customers in the long run but might cause mayhem at the current stage of maturity of India's financial markets. "They should have been brought over a period," said Trivedi.

As for the emerging scenario, buzz on the street is that SEBI will have its way. ●

