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Insurance brokerages & IRDA Regulations Current Scenario & Emerging Challenges

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ABSTRACT

Brokers are insurance intermediaries, who represent their clients, unlike the insurance agents, who represent their insurance company. In many markets, insurance brokerages have played significant role in bringing sophistication in the industry and some of the large transnational brokers are as big as many insurers, in terms of their operational breadth and size. Internationally, insurance brokerages operate in the non-life segment, especially the corporate sector. Insurance companies (PSU as well as Private Banks) have learnt to manage the channel conflict between brokers and their agency force and they usually reward their loyal agents by giving them higher commission. Till now, around 35 medium and large insurance brokerages have been given licenses by the regulator, Insurance Regulatory and Development Authority of India (IRDAI), to start insurance broking indirect, reinsurance and composite segments. Top three international brokers control around 80 percent of brokerage business procured by top 20 brokers in India. IRDAI has recently opened the Indian insurance market for insurance brokers in its attempt to create a level playing ground between insurance brokers and insurance web aggregators, to encourage competition, promote efficiency in operations & Client service. While increasing the compliance requirements by way of the new IRDAI norms of adherence, distinct focus has been made on building better controls and corporate governance.

This research paper opens with current scenario of Insurance Industry where insurance brokerage firms operate significantly in the non-life segment. Second part deals with the IRDAI's role in regulating the industry. Third part discusses the competition between the various distribution channels with business for non life business. The paper concludes with emerging challenges for IRDAI in bringing out a harmonious opportunity for large players as well as small insurance brokerage firms and product innovation.

Keywords: Insurance Brokerages, Non –Life, Insurance Regulatory & Development Authority of India (IRDA), distribution channels, Product innovation.

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INTRODUCTION

Insurers conceptualise, design, obtain approvals and offer their products. But in order that the product reaches the intended beneficiary and the beneficiary is convinced to buy, an effective intermediary – who acts as a bridge between the seller and the buyer – is utmost essential. That is where the industry gives scope for Agents, Brokers, Banks, and Insurance Marketing Firms etc. to play an important role. In many markets, insurance brokerages have played significant role in bringing sophistication in the industry and some of the large transnational brokers are as big as many insurers, in terms of their operational breadth and size. Internationally, insurance brokerages operate in the non-life segment, especially the corporate sector. Insurance companies (PSU as well as Private Banks) have learnt to manage the channel conflict between brokers and their agency force and they usually reward their loyal agents by giving them higher commission. From being a matchmaker between insurance companies and business firms earlier, the scope of the broker has expanded to providing various value-added services. Apart from structuring and placement of insurance cover, these include claims management, risk management, alternative risk transfer mechanisms, employee-benefit solutions, captive management, actuarial services, personnel outsourcing, political and environment risk advice, pre-emergency planning and evacuation, business continuity planning etc.

This research paper opens with current scenario of Insurance Industry where insurance brokerage firms operate significantly in the non-life segment. Second part presents discussion of the major distribution channels for non – life insurance industry and IRDA's role in regulating the industry. Third part discusses the factors responsible for low penetration of non-life business. The paper concludes with emerging challenges for product innovation and in ushering a harmonious opportunity for large players as well as small insurance brokerage firms.

I. Indian Scenario

India has been a rather late starter. The Insurance Regulatory & Development Authority (IRDA) brought out its first set of regulations, permitting brokers to operate, as recently as October 2002. The first set of Licenses was issued only in January 2003 (India Insure being the first to have been granted the License). In India, Brokers are different from other Insurance service providers in several ways. Unlike an Agent (or a corporate agent), who represents a specific Insurer only, a broker represents the client, and not the insurer. He can approach all Insurers for a competitive quote. A Bancassurance outfit (commercial banks), is normally an Agent and not a broker. A Third Party Administrator (TPA, sometimes confused with a Broker) is a service provider for Insurance companies, providing services related to health insurance only.

IRDA has permitted 3 types of Brokers to operate in India:

(1) The Direct Broker (between end-users and primary insurers only),

(2) Re-insurance Brokers (between primary insurers and re-insurers only) and He can approach all Insurers for a competitive quote.

(3) Composite Brokers (both the above). Brokers

The Indian insurance industry has experienced various challenges and major structural changes since the 1990s. Indian insurance industry, for a long period, relied heavily on traditional agency distribution channels. Since the insurance industry was completely under the monopoly of the public sector organizations for decades, there was a slow and rugged growth in the insurance business due to lack of competitive pressures. The Government of India, in 1994, appointed a Committee under the Chairmanship of R. N. Malhotra, former Governor of RBI, to study the need for private participation in the insurance industry. The committee reported that only 22 per cent of the Indian population was insured. Based on the committee report, the Government of India took necessary initiatives to improve the operational efficiency of insurance companies and insurance penetration as well. The year 1999 brought a remarkable change in the Indian insurance sector, as a result of major structural changes like ending of Government monopoly and passing of the Insurance Regulatory and Development Authority (IRDA) bill, relaxing all entry restrictions for private and foreign players to enter into the Indian market. Innovative products, smart marketing and aggressive distribution have enabled fledgling private insurance companies to sign up Indian customers faster than anyone expected. The Insurance industry in India experienced substantial growth in terms of numbers, life insurance premium, number of policies and distribution network, after the opening up of the industry to the private sector. Today, there are totally 44 registered players penetrating into insurance business with 22 in life and 21 in general insurance businesses and one national re-insurer (IRDA Report). Distribution channels function as arteries in a marketing network that delivers goods and services to consumers. Today distribution is increasingly seen as one of the key marketing variables (Devlin, 1995; Thornton and White, 2001), capable of providing significant competitive advantage, particularly in the service sector where consumer, technological, and regulatory trends have increased competitive pressures markedly. The new era of insurance development in India has seen the entry of international insurers, the proliferation of innovative products and distribution channels, and the raising of supervision standards. Intensified competition, rising agent costs, and product transformation have driven insurers to seek more efficient approaches to operate in the market. Many insurers in India changed their distribution strategies from direct writers to a coexistence of agent-led, broker-led, bank-led and other forms of distribution systems.

II. Main Objectives

1) To examine the major insurance distribution channels for insurance products in India,
2) To propose innovative non-conventional channels of distribution which benefit insurers and policy holders. As part of our discussion on overview of Indian insurance distribution channels, including a SWOT analysis for the major channels is also made.
3) As part of the analysis, the distribution strategies of various insurance companies are discussed. Further , customer channel alignment and comparison of various channel attributes, and policy contributions have been presented .Non-conventional distribution channels inclusive of digital , common service centres , point of sale centres are also explored. The Indian insurance industry was chosen for the study, since multiple

channels are common in the distribution retailers, distributors and even the internet. When multiple channels are used by the consumers, it will be appropriate to evaluate the Channels by an analysis of their strengths, weaknesses, opportunities and threats (SWOT).

Insurance Distribution Channels operating in India

Traditional Channels	Modern Channels	Alternative Channels
✓ Individual Agents ✓ Corporate Agent ✓ Broker ✓ Work Site Marketing	✓ Bancassurance ✓ Micro-Insurance	✓ Direct Internet Marketing ✓ Telcassurance ✓ Shopassurance

(i)Individual Agents: Traditionally, individual agents have been the primary channels for insurance distribution in the Indian market; the public sector insurance companies have their branches in almost all parts of the country and have attracted local people to become their agents. The agents are from various segments in society and collectively cover the entire spectrum of society. The profile of the people who acted as agents suggests they may not have been sufficiently knowledgeable about the different products offered, and may not have sold the best possible product to the client. However, the customer trusted the agent and company. This arrangement worked adequately in the absence of competition.

SWOT Analysis of Direct Agency Distribution Channel

Strengths	Weaknesses
• Well trained staff. • In-depth knowledge of the industry. • Comprehensive customer insight.	• A limited number of people inhabiting small towns/rural areas. • The high costs of switching current insurance • Consumers(policy holders) from a competing firm are large . • The struggle to stay ahead on the technological adoption curve in a small / rural communities which are marginalized /handicapped in terms of income and awareness
Opportunities	**Threats**
• Participation within a growth industry. • Increased sales through an expansion of the current service offerings. • As the company continues to grow, the ability to decrease fixed costs over a growing customer base.	• Competition from local brokerages that respond to high superior offerings of the insurance. • A significant slump in the economy that will likely have a correlated effect on the industry.

	• A single of series of huge, unexpected, distressing events that put significant strain on the financial health of the insurance industry as a whole.

(ii) Corporate agents: Independent Financial advisors (IFA) are authorized agents of insurance companies having tie –ups with more than one company. They are qualified professionals who can provide on a variety of products. IFA assembles different financial products in accordance with the customer needs and provide value-added products by creating customized insurance structure. Today, IFA show a significant presence as a distribution channel in both life and non –life business.

(**iii) Work site marketing:** Under this strategy, insurers send a team to a target group and explain the products , either individual or group, that are suitable at their place of work, on a voluntary pay –roll deduction basis. The target group may be employees of a particular company, educational institution or any kind of organization. Insurance companies will be able to sell insurance products, particularly pension and health plans, through this channel. One possible reason for insufficient development of this channel in India is that employers generally expect some kind of incentive to provide the facilities to the life insurers for making presentations and making arrangements for deduction of premium from salaries.

(iv)Brokers: Insurance Brokers are professionals who assess risk on behalf of a client, advice on mitigation of that risk, identify the optional insurance policy structure, bring together the insurer and the insured and carry out the work preparatory to the contract. Brokers represent the customer and will sell the products of more than one company. They seek to determine the best fit for the client and effectively address the mind block faced by the public about the various companies. This channel of brokers is best suited to high end corporate clientele.

(v) Bancassurance : In India , a bank can tie up with one general insurance and one life insurance as mandated by IRDA regulation. It is general experience that bank personnel handling insurance products do not know much about the products and once they make customers, they are not much bothered about their queries. Moreover, it will be useful for selling certain types of products only.

SWOT Analysis of Bancassurance

Strengths	**Weaknesses**
• Most suitable for personal line products &Householders' Comprehensive Insurance • Huge pool of skilled professionals • Customization effort required at the outset	• Internet essential for operating offices • Inflexibility of the products • Middle Class overburdened-no money left after tax • Tax Exemption for all bancassurance • products required • Lack of goodwill by banks as well as insurance companies

	• Tariffs-inflexible • Ratings not based on sound actuarial principle
Opportunities	**Threats**
• Bank's enormous database • Homogeneous groups can be churned out of the database to develop and market products • Almost all companies have done just distribution of insurance products for nearly 5-10 years before going into risk carrying business • RBI & IRDA should have no hesitation in allowing the merger of banks and insurance companies	• Security Threats on database of Banks • Potential entry of new insurance companies which are promoted by banks. • High competition

(vi) **Micro Insurance:** The huge untapped market for insurance is the rural and social sector. Micro insurance is defined as the protection of low income households against specific perils, in exchange for premium payments proportionate to the likelihood and cost of the risk involved. It provides an opportunity to the insurance companies to meet their social responsibility as well as secure a strong footing in the rural market. The active distribution channels for micro insurance in India are NGOs, MFIs, and SHGs (self-help groups), Micro

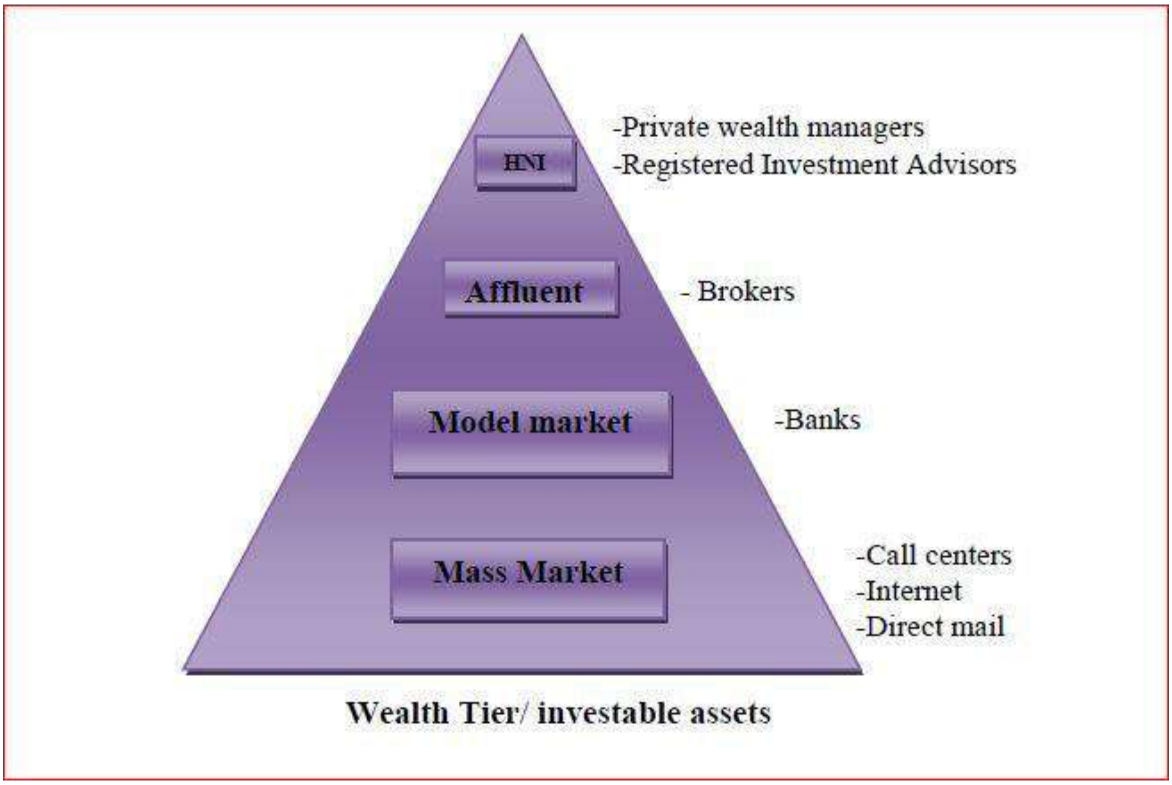
agents, Cooperative Banks and RRBs (regional rural banks), and Post Offices. The MFIs/NGOs have been identified as main delivery channels by most of the insurance companies. These have a large network, catering to a huge number of clients. However, most of the MFIs have limited ability to process the insurance claims as such they try to customize the insurance product in order to simplify the operational process involved.

(vii) Alternative Channel of Distribution: The new alternative channels of distribution are yet to be utilized in full swing. Till now, nearly 86% insurance policies are sold through traditional channels. Exploitation of retailing and other forms of modern channels will definitely bring life insurance business to new heights. The success of marketing insurance depends on understanding the social and cultural needs of the target population, and matching the market segment with the suitable intermediary segment. Further, all intermediaries can't sell all lines of business profitably in all markets. There should be a clear demarcation in the marketing strategies of the company from this perspective. It is observed that determining the value of alternative distribution channels is a delicate balance.

Benefits of Alternate Distribution Channels to Customers and Insurance Companies

Benefits to Insurers	Benefits to Customers
• Lesser procurement cost • Easy access of customer base • Known customer and easy risk assessment • Channel diversification • Increase in market penetration • Increase in volume of business • Extensive customer reach	• Low premium because of reduced distribution cost • Convenient in payment • Conveniently getting all financial needs under one roof • Double assurance/credibility • Easy and automatic renewal • Enabling better service • Refined quality products

Distribution Channels Aligned to Target the Various Customer Segments in Indian Insurance Sector



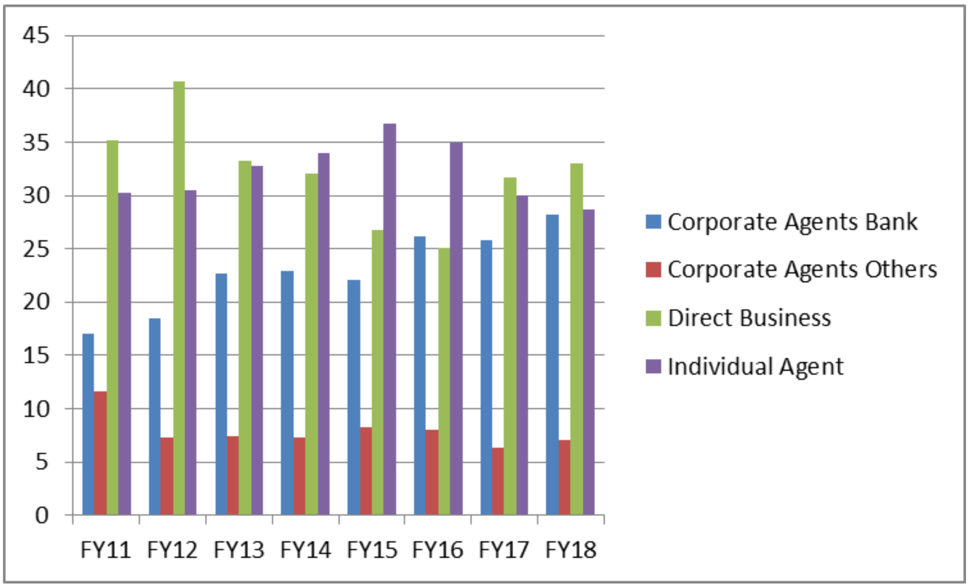
A Summary of Key attributes of various distribution channels in India

Type of channel	Cost	Accessibility	Profitability	Efficiency	Reach	Security	Performance
Agency	Medium	High	Medium	Average	Medium	Medium	High
Work Site Marketing	High	Low	Medium	Average	Low	High	Low
Micro-Insurance	Low	High	High	Average	High	Average	Average
Bancassurance	Medium	Medium	Medium	Medium	Low	High	Average
Direct Sales/Marketing	Low	Medium	High	Average	Low	Average	Average
Virtual sales (internet)	Very low	Very high	Very high	High	High	Medium	High
Shoppassurance	Medium	Low	High	High	High	High	High
Telcassurance	Low	High	High	High	High	Low	High

Source: Insurance Institute of India

The measure of insurance penetration and density reflects the level of development of the sector. While insurance penetration is measured as the percentage of the insurance premium to GDP, insurance density is calculated as the ratio of premium (in US $) to the total population (per capita premium). Over the last ten years, the penetration of non-life sector in the country. Its density has gone up from US $ 2.4 in 2001 to US $ 13.2 in 2016.Recent data on Channel wise GDPI share of Non-Life business is presented below:

Diagram I: Channel wise GDPI Share – Non Life Insurance



Note: *Totals of percentages would not add to 100 % due to under insurance and low insurance penetration inIndia .*

Source *: IRDA Annual Reports & statistics .*

III. Factors responsible for low penetration of Non-life Business:

(i)Generally , increased competition , rising cost inflation, changing customer loyalty and preferences as well as complex emerging risks are all pushing the insurance industry to look for ways to break the shackles of tradition to innovate and to device new products. It is evident that what was relevant yesterday is not completely applicable today. This can be attributed to the current predicament of 'soft' underwriting cycle and broader economic weakness. Inadequate product innovation and design inhibits the writing of profitable business and the realisation of the full potential of the Indian insurance market. Despite such large societal impact the current tend shows that risk carriers focus on the optimization of products and processes and accept incremental changes as if they were innovation. However, the power of innovation lies in trying something different rather than merely using a specific technology to overcome a problem. There is a dire need to embrace a new approach or new technology to address persist operational challenges.

(ii) De-tarrification - mere price war

The Year 2007 ushered in de-tarrification and with this the rules of the games changed and changed forever. When introducing its de-tarrifing policy in the general insurance market, the Insurance Regulatory and Development Authority (IRDA) intended to benefit consumes by allowing risk carriers to independently price products for each line of business and develop innovative practices and customer – friendly options for policy holders. It was hoped that this would in turn mean an improved market with better penetration and correct pricing.

The basic ideology behind detarrification was to allow risk carriers to price as per the risk profile but instead many risk carriers have been resorting to merely reducing price without considering the risk in its entirety, leading to a price deflation. This is definitely not sustainable in the long run. After liberalization of the industry in 1999 – 2000, the Indian general insurance industry, in terms of gross direct premium, had grown from Rs.11,446 crores in FY2002 to Rs.57,964 crores in FY2012, which corresponds to a CAGR of 17.6% during the period FY 2011-17 . Although the above CAGR figures projects a rosy picture, it is just a mirage as most of the insurance companies are yet to generate underwriting profits.

(iii) Traditional channels undergoing a change

The way insurance was sold itself has undergone a radical change. 10 years ago none of the insurance companies would have imagined insurance being sold through internal or in the by lanes of crowded malls. For a very long time agents and brokers were the only dominant channels for risk carriers. As a result the business side within insurance companies developed there channels specific views. When products were conceived and formulated, they necessarily were formed around the existing channels, and thus today's silo approach to product was born. With the advent of new channels, the changing face of distribution demands to move away from traditional products and to innovate and devise products apposite to the new channels. This need is evident not only in terms of the change in the channel but also in terms of different demography to which the product needs to cater to E.g. Internet as a tool for purchasing insurance has a very different set of customers as compared to a traditional agency channel. Web itself has been continuously evolving as a medium.

Customers are the key to transforming markets. They provide the revenues and profit to the companies which focus on their requirements. Current insurance market traditionally has been a product centric market and while insurers were maintaining their product centricity, consumers changed in other ways. Insurance companies inadvertently ignored this important transformation. Breathing in a liberalised world executive the complex contracts, clients' requirements have undergone a sea change. From traditional standard fire & special peril policy to contractor's pollution legal liability policy, a drift can be observed from a simple overseas travel policy to mobile benefit solution.

(iv) Unravelling the mystery behind Innovation.

Innovation is the cornerstone on which a new product is evolved. Many a times it is misconstrued that innovation is limited to product only. The fact of the matter is that innovation has many avatars like process innovation, distribution innovation, customer experience innovation each contributing in breaking the shackles of trading and helping in devising new products. To mass produce an innovative product at a price that the market will accept requires complimentary organisational and marketing innovations. The most generic form of innovation is "product innovation" and insurers should focus most on the same. Rather than taking a traditional view of the product, restricting it to only functional benefits, insurance product should be viewed as an end to end solution incepting from product selling buying experience and the service experience by way of claim or otherwise. Starting from the traditional definition of the product, in terms of the policy, the best way, to innovate is to listen deeply to customers and to non – customers.

(v) Product Innovation: Direct Insurer vs. Reinsurer

Product innovation traits are broadly similar indirect insurance and reinsurance markets. However, there will be subtle differences in the way they approach product innovation. Direct insurers works in close proximity with the end customers are hence understand their requirements better moulding the product accordingly. On the other hand more organized reinsurance sector simulates and perhaps facilitates innovation. In particular, reinsurers have had to look beyond the conventional and embrace capital market solutions due to the practical limits on their risk absorbing capacity.

(vi)Banks and Distributors

For all the insurance companies one of the most lucrative channels of bank. It already has a large base of clients who can be offered insurance policies. Insurance companies realise the importance of this channel and are increasingly trying to make inroads in to this channel. Unfortunately even today sales volume generated through this channel is no commensurate to the potential it has. For banks insurance is always a transaction oriented ancillary function. Insurance companies need to make this channel graduate to the level that they own up the process and the client and thus raising the effectiveness for all the stakeholders.

(vii)Operational Innovation

Al the insurance companies have built huge systems to cater to their functional requirements. But the way there systems are build they work more in silo rather than interacting with each other. There is a lot of overlapping in the functions. This in effect ensures that inefficiency creeps in system and the dependence on individuals is very high. Similarly each company interacts with huge number of suppliers. Insurers should begin by consolidating vendors and then by consolidating systems. The lesser the numbers, the more seamless operation will become.

(viii)Changes in regulations by IRDA

The regulatory environment can have a dual influence o product innovation in insurance, both in terms of stimulating new product ideas or prohibiting certain activities. This applies both in terms of the oversight of the activities of the insurance companies themselves as well as the regulatory constraints facing their customers. As an example of the former, changes to financial sector regulation in a number of emerging economies have been influential in stimulating micro-insurance. Similarly Solvency II norms of IRDA which are yet to be implemented are encouraging insurers to review insurance products in a bid to optimise regulatory capital.

(ix)Selling Insurance to Downtrodden by Government sponsored programmes:

The evidence from the any recent attempts to sell various kinds of insurance to the poor in India and other less developed countries confirms that there are major concerns for the buyers. They are not insurmountable but demand imaginative solutions For example, the pensions out to be indexed – after all, the poor, quite justifiably, do not want to bear the inflation risk, and indeed why would we want them to be the victims of the government's caprice. Government – sponsored pensions and insurance schemes have of course been there for many years. What is striking is the fact that this government has decided to make them the centrepiece of its anti-poverty efforts, rather than something that gets announced during a budget speech as a sop to a particular constituency and then largely forgotten.

Limitations: The study has covered a formidable array of distribution channels of Nonlife insurance business right from traditional to emerging modes. Since the penetration of non-life business insurance business has been low, awareness of the products has been facing severe challenges. The discussion has relied on secondary data as available from IRDA, Insurance Institute of India and other industry sources.

Conclusion: Emerging Challenges

- Innovating as it turns out means taking controlled risks – which are a primary function of an insurance company. Still projects or activities such as the array of product Innovation is seldom seen in the insurance industry – surprising as the risk involved is very low and the insights gained quite high.
- Insurance will have to overcome its sluggishness, if there is to be a culture of new product development within the industry. It is imperative that this culture of innovation is built in the organization. It is evident that Risk carriers who anticipate and plan for change will be able to create their own future. Such players acknowledge **product innovation as a culture, not as a department**. This means all the organisations should look forward to imbibing a culture of experimentation of allowing for mistakes and of everybody with a stake or an interest in the organization, participating in idea generation for product innovation.

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