

CORPORATE GOVERNANCE GUIDELINES **FOR INSURANCE COMPANIES**

1. General

- 1.1 Corporate Governance is understood as a system of financial and other controls in a corporate entity and broadly defines the relationship between the Board of Directors, senior management and shareholders. In case of the financial sector, where the entities accept public liabilities for fulfillment of certain contracts, the relationship is fiduciary with enhanced responsibility to protect the interests of all stakeholders. The Corporate Governance framework should clearly define the roles and responsibilities and accountability within an organization with built-in checks and balances. The importance of Corporate Governance has received emphasis in recent times since poor governance and weak internal controls have been associated with major corporate failures. It has also been appreciated that the financial sector needs to have a more intensive governance structure in view of its role in the economic development and since the safety and financial strength of the institutions are critical for the overall strength of the financial sector on which the economic growth is built upon. As regards the insurance sector, the regulatory responsibility to protect the interests of the policyholders demands that the insurers have in place, good governance practices for maintenance of solvency, sound long term investment policy and assumption of underwriting risks on a prudential basis. The emergence of insurance companies as a part of financial conglomerates has added a further dimension to sound Corporate Governance in the insurance sector with emphasis on overall risk management across the structure and to prevent any contagion.
- 1.2 The Insurance Regulatory and Development Authority (IRDA) has outlined in general terms, governance responsibilities of the Board in the management of the insurance functions under various Regulations notified by it covering different operational areas. It has now been decided to put them together and to issue the following comprehensive guidelines for adoption by Indian insurance companies. These guidelines are in addition to provisions of the Companies Act, 1956, Insurance Act, 1938 and requirement of any other laws or regulations framed thereunder. Where any provisions of these guidelines appear to be in conflict with the provisions contained in any law or regulations, the legal provisions will prevail. However, where the

requirements of these guidelines are more rigorous than the provisions of any law, these guidelines shall be followed.

2. Objectives

2.1 The objective of the guidelines is to ensure that the structure, responsibilities and functions of Board of Directors and the senior management of the company fully recognize the expectations of all stakeholders as well as those of the regulator. The structure should take steps required to adopt sound and prudent principles and practices for the governance of the company and should have the ability to quickly address issues of non-compliance or weak oversight and controls. These guidelines therefore amplify on certain issues which are covered in the Insurance Act, 1938 and the regulations framed thereunder and include measures which are additionally considered essential by IRDA for adoption by insurance companies.

2.2 The guidelines accordingly address the various requirements broadly covering the following major structural elements of Corporate Governance in insurance companies:-

- Governance structure
- Board of Directors
- Control functions
- Senior management:
 - CEO & other senior functionaries
 - Role of Appointed Actuaries
 - External audit – Appointment of Statutory Auditors
- Disclosures
- Outsourcing
- Relationship with stakeholders
- Interaction with the Supervisor
- Whistle blowing policy

2.3 In these guidelines, the reference to the “Board” would apply to the “Board of Directors” and “Senior Management” to the team of personnel of the company with core management functions. Normally, this would include officials at one level below the Executive Director (including Functional Heads). In regards to insurers, the Appointed Actuary has a special executive and statutory role.

3. Significant Owners, Controlling Shareholders and Conflict of Interest – Role of Board

- 3.1 IRDA prescribes a minimum lock-in period of 5 years from the date of certificate of commencement of business of an insurer (R3) for the promoters of the insurance company and no transfer of shares of the promoters would be permitted within this period.
- 3.2 Section 2 (7A) of the Insurance Act, 1938 has prescribed the ceiling of FDI in Indian Insurance Companies at 26%. It could be capped at such percentage as may be notified by the Government of India¹ in future. The manner of computation of FDI to satisfy this requirement is detailed at Regulation 11 of the IRDA (Registration of Insurance Companies) Regulations, 2000.
- 3.3 The Insurance Act stipulates prior approval of the IRDA for registration/transfer of shares, exceeding one per cent and /or which involve holding of share capital, after such transfer, in excess of 5 per cent of the paid-up capital of the company (2.5 per cent for banking or Investment Company). The Board of Directors of the company shall ensure that the registration of shares is in compliance with the above provisions of the Act and Circular No.022/IRDA/F&A/Aug-05 dated 25th August, 2005 on regulatory framework on (i) issue of shares in any form other than equity and (ii) transfer of shares.
- 3.4 Sections 297 & 299, of the Companies Act 1956, *inter-alia*, deal with the potential areas of conflicts of interest and the obligation of the Directors and the disclosures thereof. Primarily, the conflicts of interest in insurance companies arise whenever there are conflicting interests of shareholders, policyholders and management, and there is therefore a duty on the Board to act in the interest of policyholders or prospective policyholders. The Authority may in due course also define significant ownership that could attract potential conflicts of interest. AS 18 of ICAI also casts obligations for the disclosures of transactions involving related parties. There should be adequate systems, policies and procedures to address potential conflicts of interest, compliance with AS 18. These include Board level review of key transactions, disclosures of any conflicts of interest to manage and control such issues.

¹ Presently the ceiling is 26 per cent.

- 3.5 Auditors, Actuaries, Directors and Senior Managers shall not simultaneously hold two positions in the insurance company that could lead to conflict or potential conflicts of interest.
- 3.6 The Board should ensure ongoing compliance with the statutory requirements on capital structure while planning or examining options for capital augmentation of the Company.

4. Governance Structure

4.1 General

Currently, the private insurers in India are yet to go public and get their shares listed on the stock exchanges. The composition of the Boards of the Public Sector Undertakings in the insurance sector is also laid down by the Government of India. It is relevant to observe here that the Corporate Governance requirements of companies listed in the Stock Exchanges have evolved over time and are outlined in Clause 49 of the Listing Agreement of the Stock Exchanges. As the listing requirements are available in public domain they are not being repeated. However, since the Indian insurance companies are as yet unlisted the Authority advises all insurers to familiarize themselves with Corporate Governance structures and requirements appropriate to listed entities. The companies are also well advised to initiate necessary steps to address the extant “gaps” that are so identified to facilitate smooth transition at the time of their eventual listing in course of time.

4.2 Varying structures of the Board

Subject to the above, the insurance companies presently could have different structures with the Board of Directors headed by a Full-Time or Part-Time Chairman with distinct executive and oversight responsibilities among the other Directors and Senior Management. It is expected that whatever form is taken, the broader elements of good Corporate Governance are present.

4.3 Groups and Conglomerates

The governance structure of the insurer could also be influenced by its association with an insurance group or a larger financial/ non-financial conglomerate. Insurers who are a part of a financial group could also be subject to the regulatory requirements on governance policies and practices established for the group level and implemented uniformly across the group.

However, these practices should be reoriented at the level of the insurer taking into account its specific business and risk profile. Such insurers should nevertheless strive to maintain consistency in policies and practices in order to reinforce controls across the group.

5. **Board of Directors**

5.1 **Composition**

- The Insurance Act stipulates that the insurance companies in India would be **public companies** and hence, would require a properly constituted Board.
- Insurers should ensure that the Board comprises of competent and qualified Directors to drive the strategies in a manner that would sustain growth and protect the interests of the stakeholders in general and policyholders in particular.
- The size of the Board in addition to being compliant with legal requirements (where applicable), should be consistent with scale, nature and complexity of business. The size and composition should ensure that they collectively provide knowledge, skills experience and commitment along with independence. Further, the Board Members should be in a position to dedicate sufficient time and commitment to fulfilling their responsibilities.
- It is expected that the shareholders of the companies elect or nominate Directors from various areas of financial and management expertise such as accountancy, banking, insurance, finance, economics etc., with qualifications and experience that is appropriate to the company.
- It is essential that the Directors possess the knowledge of group structure, organizational structure, process and products of the insurer and the Board generally complies with the following requirements:-
 - The Board of Directors and Senior Management understand the operational structure of the insurer and have a general understanding of the lines of business and products of the insurer, more particularly as the insurer grows in size and complexity.
 - The Board of Directors of an insurer belonging to a larger group structure/ conglomerate should understand the material risks and issues that could affect the group entities, with attendant implication on the insurer.

- The Board of Directors is required to have a significant number of “Independent Directors” (as laid down in the Listing Agreement). The optimum contribution of Independent and Non-Executive Directors enhances the quality of business judgment and benefits the shareholders and policyholders. This is especially important in respect of insurance companies under conglomerate structure and where there is potential scope for transfer of risks and conflicts of interests that affect the group entities. At a minimum, where the company has a non-executive Chairman, at least one third of the directors should be independent and in other cases at least fifty percent of the directors should be independent. While the above intention is desirable and would facilitate smooth transition on the listing of the companies, the companies should have a minimum of two independent directors so long as they are unlisted.
- Similarly, where the Chairman of the Board is non-executive, the Chief Executive Officer should be a whole time director of the Board.
- As a matter of prudence, not more than one member of a family or a close relative as defined in the Companies Act or an associate (partner, director etc) should be on the Board of an Insurer.

5.2 **The Role and responsibility of the Board and their Discharge**

The specific areas of responsibilities of the Boards of the insurance companies are detailed in the *Annexure 1*. The Board would primarily concentrate on the direction, control and governance of the insurer and in particular should articulate and commit to a corporate philosophy and governance that will shape the level of risk adoption, standards of business conduct and ethical behaviour of the company at the macro levels. The Board should also set clear and transparent policy framework for translation of the corporate objectives. The Board can delegate its authority to the Board Committees in the discharge of this responsibility but such delegation does not absolve the Board from its primary responsibilities. In this regard, the Board should seek detailed and transparent information flow from the senior management through well documented agenda notes and also devise appropriate systems to serve as effective monitoring arrangements. As the Boards generally do not meet at frequent intervals, it is imperative that the senior management is clearly made accountable for the two way information flow.

The structure of the Board of Directors should be oriented to setting-up of objectives to meet the expectations of various stakeholders, strategies for their

fulfillment and for monitoring the achievements. The insurers need to consider interests of all stakeholders, and especially their policyholders as a specific group. Further, since there could arise a conflict of interest amongst the various stakeholders, a key board function is to establish strategies and policies that define ethical individual and corporate behaviour and ongoing, effective processes that ensure adherence to these strategies and policies.

Thus, with a view to being effective, the Board in active consultation with the Management should set strategies and policies to address, at the minimum, a broad range of areas, as indicated below. There should concurrently be arrangements to review the policies from time to time to ensure that they are dynamic.

- Overall direction of the business of the insurer, including projections on the capital requirements, revenue streams, expenses and the profitability. While laying down the projections, the Board must address the expectations of the shareholders and the policyholders.
- obligation to fully comply with the Insurance Act and the regulations framed thereunder, and other statutory requirements applicable to it;
- addressing conflicts of interest;
- ensuring fair treatment of policyholders and employees;
- ensuring information sharing with and disclosures to stakeholders, including investors, policyholders, employees, the regulators, consumers, financial analysts and/or rating agencies.
- establishing channels for encouraging and facilitating employees raising concerns or reporting a possible breach of law or regulations, with appropriate measures to protect against retaliation against reporting employees;
- developing a corporate culture that recognizes and rewards adherence to ethical standards.

5.3 Fit and Proper Criteria

In line with the international and domestic norms, the Directors of insurance companies have to meet the “fit and proper” criteria. The criteria to be satisfied, at a minimum, would relate to integrity demonstrated in personal behaviour and business conduct, soundness of judgment and financial soundness. The Insurance Act prohibits (i) a life insurance agent to be the Director of the life insurance company; and (ii) the common directorship among life insurance companies. Currently, the fit and proper requirements seek to ensure that the Director should not have been convicted or come

under adverse notice of the laws and regulations involving moral turpitude or of any professional body. With a view to ensuring that the Directors comply with the above requirement, a due diligence enquiry should be undertaken on the person to be appointed as Director or for the continuance of the existing Directors only after obtaining a declaration from the proposed/existing Directors in the format given in *Annexure 2*, at the time of their appointment/re-appointment.

It is desirable that the Boards constitute a Nomination Committee to scrutinize the declarations of intending applicants before the appointment/reappointment/election of directors by the shareholders at the General Meetings. The Nomination Committee could also make independent/discreet references, where necessary, well in time to verify the accuracy of the information furnished by the applicant. The insurance companies are further advised that they should obtain an annual declaration from the Directors that the information provided in the declaration at the time of appointment/re-appointment has not undergone any change subsequently and the changes, if any, are apprised by the concerned Director to the Board.

The Directors are also required to enter into a Deed of Covenant as per the format placed at Annexure 3, with the insurance company, duly approved by the Board, pursuant to their terms of appointment to ensure that there is a clear understanding of the mutual role of the company, the Directors and the Board in Corporate Governance.

5.4 Conduct of Meetings

The Board should also lay down systems that would make the Company Secretary responsible for proper conduct of the Board meetings and with adequate time to deliberate on the major issues in detail. The Minutes should be recorded as soon as possible after the meeting and get circulated. There should be a system of familiarizing new Directors with the background of the company's governance philosophy, duties and responsibilities of the Directors, etc. Well structured arrangements should be in place for ongoing briefing of Directors on dynamic changes in the financial sector in general and in the insurance in particular for updating the Directors through formal and informal programmes covering regulatory systems, market growth trends, future strategic plans/operations etc.

6. Control Functions

Given the risks that an insurer takes in carrying out its operations, and the potential impact it has on its business, it is important that the Board lays down the policy framework to put in place:

- robust and efficient mechanisms for the identification, assessment, quantification, control, mitigation and monitoring of the risks;
- appropriate processes for ensuring compliance with the Board approved policy, and applicable laws and regulations;
- appropriate internal controls to ensure that the risk management and compliance policies are observed;
- an internal audit function capable of reviewing and assessing the adequacy and effectiveness of, and the insurer's adherence to its internal controls as well as reporting on its strategies, policies and procedures; and
- Independence of the control functions, including the risk management function, from business operations demonstrated by a credible reporting arrangement.

6.1 The responsibility for the oversight of control functions of an insurer should be entrusted to Directors possessing the appropriate integrity, competence, experience and qualifications.

6.2 For insurers within a group, appropriate and effective group-wide risk control systems should be in place in addition to the control systems at the level of the insurer. It is essential to manage risks appropriately on a group-wide basis as well as at the level of the insurer. The Boards of the respective insurers are required to lay down requisite policy framework to ensure that such risks are adequately addressed.

7. **Delegation of Functions**

With a view to providing adequate Board time for discharge of the significant corporate responsibilities, the Board can consider setting up of various Committees of Directors by delegating the overall monitoring responsibilities after laying down the roles and responsibilities of these Committees to the Board. In particular, the following aspects need to be defined in respect of the role and functions of the Committees:

- Constitution
- Objectives
- Responsibilities
- Frequency of meeting / quorum requirements

- Appointment and removal of members
- Reporting to the Board

The company can establish several Committees to undertake specific functions depending on the size and level of the complexity of the operations. Typically, the Committees that assist the Board are Audit Committee, Risk Management Committee, Nominations Committee, Remuneration Committee, Investment Committee and Asset-Liability Management Committee. However, the Authority advises insurers that it is mandatory to establish Audit; Investment; Risk Management; Policyholder Protection; and Asset Liability Management (in case of life insurers) Committees that have a critical role in strengthening the control environment in the company. Establishment of the other Committees is left to the option of the insurer. The role and responsibilities of the Committees would generally be as detailed below:-

7.1 **Audit Committee (mandatory)**

- The Audit Committee shall oversee the financial statements, financial reporting, statement of cash flow and disclosure processes both on an annual and quarterly basis. It shall set-up procedures and processes to address all concerns relating to adequacy of checks and control mechanisms.
- The Chairman of the Audit Committee should be an independent Director of the Board and should ideally be a professional Chartered Accountant or a person with strong financial analysis background. The association of the CEO in the Audit Committee should be limited to eliciting any specific information concerning audit findings.
- The Audit Committee will oversee the efficient functioning of the internal audit department and review its reports. The Committee will additionally monitor the progress made in rectification of irregularities and changes in processes wherever deficiencies have come to notice.
- The Audit Committee shall be directly responsible for the recommendation of the appointment, remuneration, performance and oversight of the work of the auditors (internal/statutory/Concurrent). In case of statutory audit, the independence of the external auditors shall be ensured (although the approval of appointment, remuneration and removal of the statutory auditors shall be done by the shareholders at the general body meeting).
- The Audit Committee shall have the oversight on the procedures and processes established to attend to issues relating to maintenance of

books of account, administration procedures, transactions and other matters having a bearing on the financial position of the insurer, whether raised by the auditors or by any other person.

- The Audit Committee shall discuss with the statutory auditors before the audit commences, about the nature and scope of audit as well as have post-audit discussions to address areas of concern.
- Any additional work other than statutory/internal audit that is entrusted to the auditor or any of its associated persons or companies shall be specifically approved by the Board keeping in mind the necessity to maintain the independence and integrity of the audit relationship. All such other work entrusted to the auditor or its associates shall be specifically disclosed in the Notes to Accounts forming part of the annual accounts of the insurer.

7.2 Investment Committee (mandatory)

- The Board of every Insurer shall set up an Investment Committee comprising of at least two Non Executive Directors, the Chief Executive Officer, Chief of Finance, Chief of Investment Division and wherever an appointed actuary is employed, the Appointed Actuary.
- The Committee's role in managing the investments out of the policyholders' funds is crucial and hence the constitution of the Investment Committee should be approved by the Board of Directors and any new appointment or removal of any member of the Investment Committee shall also be approved by the Board and be communicated to the Authority within 30 days.
- The Committee shall be responsible for laying down an overall investment policy and operational framework for the investment operations of the insurer. The policy should focus on a prudential Asset Liability Management (ALM) supported by robust internal control systems. The investment policy and operational framework should, inter alia, encompass aspects concerning liquidity for smooth operations, compliance with prudential regulatory norms on investments, risk management / mitigation strategies to ensure commensurate yield on investments and above all protection of policyholders' funds. It is also responsible for a periodic review of the Investment policy based on the performance of investments and the evaluation of dynamic market condition.
- Members of the Committee should be fully conversant with the various responsibilities cast on them by the IRDA (Investment) Regulations

2000 as amended from time to time as well as the guidelines issued on the system of risk management.

- The members of the Committee should not be solely influenced by the credit rating agencies. The committee should independently review their investment decisions duly supported by the due diligence process required to be carried out by the Investment Team.
- It shall also put in place an effective reporting system to ensure compliance with the policy set out by it apart from Internal / Concurrent Audit mechanisms for a sustained and on-going monitoring of Investment Operations.
- The IC shall atleast meet once in a quarter and look into various aspects of investment operations and monitor them.
- The IC shall furnish a report to the Board on the performance of Investments atleast on a quarterly basis and provide analysis of its Investment portfolio and on the future outlook to enable the Board to look at possible policy changes and strategies.

7.3 Risk Management Committee (mandatory)

It is now well recognized that the sound management of an insurer as in the case of other financial sector entities, is dependent on how well the various risks are managed across the organization. In pursuit of development of a strong risk management system and mitigation strategies, insurers shall set up a separate Risk Management Committee to lay down the company's Risk Management Strategy. The risk management function shall be organized in such a way that it is able to monitor all the risks across the various lines of business of the company and the operating head has direct access to the Board. Conventionally this function is under the overall guidance and supervision of the Chief Risk Officer (CRO) with a clearly defined role. The insurers can, however, presently organize the function appropriately to the size, nature and complexity of their business keeping in view the need for operative independence of the Head of the risk management function.

Broadly, the Risk Management Committee shall:

- assist the Board in effective operation of the risk management system by performing specialised analyses and quality reviews;
- maintaining a group-wide and aggregated view on the risk profile of the insurer in addition to the solo and individual risk profile;
- report to the Board details on the risk exposures and the actions taken to manage the exposures;

- advise the Board with regard to risk management decisions in relation to strategic and operational matters such as corporate strategy, mergers and acquisitions and related matters.

7.4 Asset Liability Management Committee (mandatory for life insurers)

ALM is an ongoing process of formulating, implementing, monitoring and revising strategies related to assets and liabilities to achieve an organization's financial objectives, given the organization's risk appetite, risk tolerances and business profile. The need for ALM cannot be over-emphasized as it lays down the framework to ensure that the insurer invests in a manner which would enable it to meet its cash flow needs and capital requirements at a future date.

The responsibilities of the ALM Committee shall include:

- Setting the insurer's risk/reward objectives and assess policyholder expectations.
- Quantifying the level of risk exposure and assessing the expected rewards and costs associated with the risk exposure.
- Formulating and implementing optimal ALM strategies and meeting risk/reward objectives. The strategies must be laid down both at product level and enterprise level.
- Laying down the risk tolerance limits.
- Monitoring risk exposures at periodic intervals and revising ALM strategies where required.
- Placing the ALM information before the Board at periodic intervals.

7.5 Policyholder Protection Committee (mandatory)

The Authority places significant emphasis on the protection of policyholder's interests and on the adoption of sound and healthy market conduct practices by insurers. Towards meeting these objectives, IRDA has notified the (i) Protection of Policyholders' Interests Regulations, 2002 and (ii) Insurance Advertisements and Disclosure Regulations, 2002. The Authority has also put in place the Guidelines on Advertisements, Promotion & Publicity of Insurance Companies and Insurance Intermediaries in January 2006. Insurers are also required to report on the number and nature of complaints to the IRDA at monthly intervals to enable IRDA to assess the governance and market conduct issues with respect to each insurer. With a view to addressing the various compliance issues relating to protection of the interests of

policyholders, as also relating to keeping the policyholders well informed of and educated about insurance products and complaint-handling procedures, each insurer shall set up a Policyholder Protection Committee which shall directly report to the Board.

The Committee should put in place systems to ensure that policyholders have access to redressal mechanisms and shall establish policies and procedures, for the creation of a dedicated unit to deal with customer complaints and resolve disputes expeditiously.

Thus, the responsibilities of the Policyholder Protection Committee shall include:

- Putting in place proper procedures and effective mechanism to address complaints and grievances of policyholders including misselling by intermediaries.
- Ensure compliance with the statutory requirements as laid down in the regulatory framework.
- Review of the mechanism at periodic intervals.
- Ensure adequacy of disclosure of “material information” to the policyholders. These disclosures shall, for the present, comply with the requirements laid down by the Authority both at the point of sale and at periodic intervals.
- Review the status of complaints at periodic intervals to the policyholders.
- Provide the details of grievances at periodic intervals in such formats as may be prescribed by the Authority.
- Provide details of insurance ombudsmen to the policyholders

7.6 Other Committees

The other Committees which are optional, which can be set up by the Board, include the Remuneration Committee, Nomination Committee and the Ethics Committee. In cases where Board decides not to constitute such Committees, their functions and responsibilities can be addressed in such manner as the Board may deem fit.

7.6.1 Remuneration Committee (not mandatory)

It is pertinent to draw attention to the provisions of Section 34 (A) (1) of the Insurance Act, 1938 which stipulates that the remuneration of CEOs/Whole-time Directors of Indian insurance companies is subject to statutory approval

of the IRDA. Further, the overall management costs of the insurer are also additionally governed by the limits prescribed statutorily in the Insurance Act and Rules framed there under in order to protect the interests of the policyholders.

The setting up of a Remuneration Committee should keep the above requirements in view. Further, the envisaged role of the Committee includes the following aspects:

- The Remuneration Committee is required to determine on behalf of the Board and on behalf of the shareholders with agreed terms of reference, the insurer's policy on specific remuneration packages and any compensation payment, for the CEO and the Executive Directors of the company.
- The remuneration package shall be closely connected with the performance objectives laid down for the senior management.
- To avoid conflicts of interest, the Remuneration Committee, which would determine the remuneration packages of the executive directors may comprise of at least three directors, all of whom should be non-executive directors, with the Chairman of the Committee being an independent director.
- The Chairman of the Remuneration Committee could be present at the Annual General Meeting, to answer the shareholders' queries. However, it would be up to the Chairman to decide who should answer the queries.

7.6.2 Nomination Committee (not mandatory)

The role of the Nomination Committee has been discussed in para 5.3.

7.6.3 Ethics Committee (not mandatory)

Responsibilities of the Ethics Committee typically include:

- monitoring the compliance function and the insurer's risk profile in respect of compliance with external laws and regulations and internal policies, including the insurer's code of ethics or conduct
- receiving reports on the above and on proactive compliance activities aimed at increasing the insurer's ability to meet its legal and ethical obligations, on identified weaknesses, lapses, breaches or violations and the controls and other measures in place to help detect and address the same

- supervising and monitoring matters reported using the insurer's whistle blowing or other confidential mechanisms for employees and others to report ethical and compliance concerns or potential breaches or violations
- advising the board on the effect of the above on the insurer's conduct of business and helping the board set the correct "tone at the top" by communicating, or supporting the communication, throughout the insurer of the importance of ethics and compliance
- approving compliance programmes, reviewing their effectiveness on a regular basis and signing off on any material compliance issues or matters.

8. Senior Management

8.1 CEO & Other Senior Functionaries

The Chief Executive Officer of the company and other key functionaries are responsible for the operations and day to day management of the company in line with the directions of the Board and the Committees set up by the Board. Section 34A of the Insurance Act, 1938 requires prior approval of the Authority for appointment, re-appointment or termination of the Chief Executive Officer and the Whole Time Directors. The Authority expects the CEO to be responsible for the conduct of the company's affair in a manner which is not detrimental to the interests of the policyholders and is consistent with the policies and directions of the Board. The Board should, therefore, carry out effective due diligence to establish that the new incumbent is 'fit and proper' before recommending the name for Authority's approval. In case the CEO resigns, the Authority should be kept informed of such resignation and the reasons therefor. The Insurance Act also prohibits the CEO of a **life insurance company** from being a Director on the Board of any other Indian insurance company/bank/investment company.

As the appointment of the CEO is made with the prior approval of the IRDA the Board should take proactive steps to decide on the continuance of CEO well in time before the expiry of his tenure or to identify the new incumbent. The Authority requires the proposal to be submitted with the approval of the Board at least a month before the completion of the tenure of the incumbent. As a corollary, the Board should also have practices in place for succession planning for the key senior functionaries through a process of proper

identification and nurturing of individuals for taking over senior management positions.

8.2 Role of Appointed Actuaries

IRDA has brought out detailed Regulations on Appointed Actuary vide IRDA (Appointed Actuary) Regulations, 2000, detailing the procedure for his appointment, qualifications, powers along with his duties and obligations. The Regulations also stipulate that prior approval of the Authority shall be taken for the appointment of the Appointed Actuary. The Board should ensure that the requirements are scrupulously complied with. In brief, it is reiterated that

- A procedure for appointment of Appointed Actuary should be put in place.
- The Appointed Actuary should qualify and satisfy the 'Fit & Proper' criteria.
- The insurer shall clearly set forth the Actuary's responsibilities and any advisory role vis-à-vis the Board or the management as well as his/her rights and obligations. These shall be in addition to the duties of the Appointed Actuaries as specified in the IRDA Regulations and any other directions of IRDA in the matter.
- As soon as the Appointed Actuary realizes that the entity does not comply or is likely to fail in complying with the requirements of solvency and other parameters of sound operations, he/she shall inform the Board of the management. If no viable/acceptable solution is taken, then he/she has to inform IRDA.
- The Board shall interact directly with the Appointed Actuary wherever it considers it expedient to secure his advice, it may do so in such manner as it may deem fit.

The Appointed Actuary shall provide professional advice or certification to the board with regard to:

- estimation of technical provisions in accordance with the valuation framework set up by the insurer
- identification and estimation of material risks and appropriate management of the risks
- financial condition testing
- solvency margin requirements
- appropriateness of premiums (and surrender value)
- allocation of bonuses to with-profit insurance contracts

- management of participating funds (including analysis of material effects caused by strategies and policies)
- product design, risk mitigation (including reinsurance) and other related risk management roles.

While the areas of advice/certification listed above are with specific reference to life companies, the appointed actuaries in case of non life insurance companies shall provide such advice/certification to the extent applicable.

In order to facilitate the Appointed Actuary in discharge his responsibilities, he shall at all times be provided access to the information as required.

8.3 External Audit - Appointment of Statutory Auditors

The IRDA (Preparation of Financial Statements and Auditors' Report of Insurance Companies) Regulations, 2002 empower the Authority to issue directions/guidelines on appointment, continuance or removal of auditors of an insurance company. These guidelines/directions may include prescriptions on qualifications and experience of auditors, their rotation, period of appointment, etc., as may be deemed necessary by the Authority.

8.3.1 Appointment

The statutory auditors recommended by the Audit Committee are required to be appointed at a general body meeting of the shareholders of the insurer. For the present, the statutory auditors of insurers are required to certify the insurer's accounts on an annual basis. The Board should therefore ensure that the statutory auditors are compliant with the regulatory requirements and there are no conflicts of interest in their appointment.

The auditors should possess the competence and integrity to alert the appropriate authorities promptly of any event that could seriously affect the insurer's financial position or the organization of its administration or its accounting and of any criminal violations or material irregularities that come to his notice.

8.3.2 Guidelines on eligibility Conditions/Qualifications

The Authority, vide Circular No: 36/7/F&A/EMPL/74/July/05 dated 25th July 2005, while discontinuing maintenance of the panel of auditors, has laid down the requirements to be complied with for a firm to be eligible to be appointed as statutory auditor of an insurance company. The guidelines

provide for joint audit of each insurance company by two statutory Auditors. In order for an audit firm to be eligible to be appointed as statutory auditors the following conditions must be complied with:

- Be in continuous practice for a period of fifteen years;
- Minimum number of partners, their qualification and experience in the audit firm as employee/partner;
- At least one partner/employee should have CISA/ISA or equivalent qualification.
- One of the joint auditors may have a term of 5 years and the other 4 years in the first instance. Thereafter, the maximum duration for which an auditor can be retained is a period of five years.
- In appointment of the statutory auditors, the insurer must ensure compliance with the requirements on 'cooling off' period of two years on completion of the tenure of 4/5 years as the case may be.
- No Audit Firm shall carry out more than two statutory audits of Insurance Companies (Life /Non-Life/Reinsurance).

8.3.3 Access to Board and Audit Committee

The Audit Committee should have discussions with the statutory auditors periodically about internal control systems, the scope of audit including the observations of the auditors (where applicable) and review the quarterly/half yearly and annual financial statements as the case may be before submission to the Board of Directors and also ensure compliance with the internal control systems.

The statutory auditors should also have access to the Board of Directors through the Audit Committee.

9. Disclosure Requirements

The IRDA (Preparations of Financial Statements) Regulations, 2002, have prescribed certain disclosures in the financial statements and the Authority is in the process of finalizing additional disclosures to be made by insurers at periodical intervals. In the meantime it may be ensured by the Board that the information on the following, including the basis, methods and assumptions on which the information is prepared and the impact of any changes therein are also disclosed in the annual accounts:-

- Quantitative and qualitative information on the insurer's financial and operating ratios, namely, incurred claim, commission and expenses ratios.

- Actual solvency margin details vis-à-vis the required margin.
- Life insurers shall disclose policy lapse ratio.
- Financial performance including growth rate and current financial position of the insurer
- A description of the risk management architecture
- Details of number of claims intimated, disposed of and pending with details of duration
- All pecuniary relationships or transactions of the Non-Executive Directors vis-à-vis the insurer shall be disclosed in the Annual Report.
- Any other matters, which have material impact on the insurer's financial position.

10. Outsourcing

- 10.1 The IRDA (Registration of Insurance Companies) Regulations, 2000 requires that the insurer should be able to carry on all functions in respect of insurance business including management of investments within its own organizations. An insurer shall not, therefore, outsource any of the company's substantive functions other than those that have been explicitly permitted. Each proposal to outsource any function of the insurer as permitted by the Authority (e.g., as in the case calculation of NAV of Investments) shall be reported to IRDA before entering into the arrangement. Where the IRDA issues any guidance in the matter, it shall be complied with. All outsourcing arrangements of the company shall have the approval of the Board. Every outsourcing contract shall contain explicit safeguards regarding confidentiality of data and all outputs from the data, continuing ownership of the data with the insurer and orderly handing over of the data and all related software programmes on termination of the outsourcing arrangement. The arrangement shall be for a defined duration of not more than 3 years and should have provision for premature cancellation without attracting penalties. The Authority would issue in due course guidelines on functions that cannot be outsourced.
- 10.2 The Company shall monitor and review the performance of agencies to whom operations have been outsourced at least annually and report findings to the Board.
- 10.3 The Authority reserves the right to access the operations of the outsourced entity to the extent these are relevant to the insurance company and for the protection of policyholder.

11. Relationship with Stakeholders

A stakeholder is any person, group or organization that has a direct or indirect stake in an insurer. The stakeholder can affect or be affected by the insurer's actions, objectives and policies.

11.1 The key stakeholders in case of an insurer include shareholders, employees, policyholders and supervisors. Other stakeholders could include creditors, service providers, unions, rating agencies, equity analysts and the community at large.

11.2 The stakeholders are interested in the operations of the insurers in terms of:

- its profitability and thus its capacity to provide a return on capital to shareholders, hire employees, expand its operations and contribute to economic and social activity
- its ability to meet its obligations to the various stakeholders as they come due, thereby also promoting trust and confidence in the financial system

11.3 Towards protecting the interests of the various stakeholders the insurer must ensure complete transparency in operations and make periodic disclosures. The disclosures stipulations must at the minimum address the following:

- financial statements accurately and fairly represent the financial condition of the insurer; and
- the insurer is running its business soundly and will be viable over the long term.

In particular, the disclosure requirements of the participating policyholders and the unit linked policyholders must be duly addressed.

12. Interaction with the Supervisor

12.1 Effective corporate governance practices in the office of the insurer will enable IRDA to have greater confidence in the work and judgement of an insurer's board, senior management and control functions.

12.2 In assessing the governance practices in place, the IRDA would:

- Seek confirmation that the insurer has adopted and effectively implemented sound corporate governance policies and practices;

- assess the fitness and propriety of board members;
- monitor the performance of boards;
- assess the quality of insurers' internal reporting, risk management, audit and control functions;
- evaluate the effects of the insurer's group structure on the governance strategies;
- assess the adequacy of governance processes in the area of crisis management and business continuity.

12.3 The IRDA would at periodic intervals bring to the attention of the Board and senior management, concerns which have been detected through supervisory activities.

12.4 ***Reporting to IRDA***

12.4.1 Insurers should examine to what extent they are currently complying with these guidelines and initiate immediate action to achieve compliance (where not already in compliance) within a period of six months from the date of these guidelines. It is expected that all the arrangements would be in place to ensure full compliance with the guidelines from the financial year 2010-2011. Where such compliance is not possible for any specific reason, the insurer should write to the IRDA for further guidance.

12.4.2 Each insurer should designate an officer as the Compliance officer whose duty will be to monitor continuing compliance with these guidelines.

13. **Whistle Blowing Policy**

13.1 The insurers are well advised to put in place a "whistle blowing" policy, where by mechanisms exist for employees to raise concerns internally about possible irregularities, governance weaknesses, financial reporting issues or other such matters. These could include employee reporting in confidence directly to the Chairman of the Board or of a Committee of the Board or to the external auditor.

The Policy illustratively covers the following aspects:

- awareness of the employees that such channels are available, how to use them and how their report will be handled

- handling of the reports received confidentially, for independent assessment, investigation and where necessary for taking appropriate follow-up actions
- a robust anti-retaliation policy to protect employees who make reports in good faith
- Briefing of the board of directors.

13.2 The appointed actuary and the statutory/internal auditors have the duty to 'whistle blow', i.e., to report in a timely manner to the IRDA if they are aware that the insurer has failed to take appropriate steps to rectify a matter which has a material adverse effect on its financial condition. This would enable the IRDA to take prompt action before policyholders' interests are undermined.

Responsibilities of the Board of Directors

- 1) The Board should ensure that the Governance principles set for the insurer comply with all relevant laws, regulations and other applicable codes of conduct.
- 2) The Board should set the following policies in consultation with the Management of the Company as indicated.
 - a) Define and periodically review the corporate business policy.
 - b) Define the underwriting policy of the insurer.
 - c) Determine the retention and reinsurance policy and in particular, the levels of retentions of risk by the insurer and the nature and extent of reinsurance protection to be maintained by the insurer.
 - d) Define the policy of the insurer in investment of its assets consistent with an appropriate asset liability management structure.
 - e) Define the insurer's policy on appointments and qualification requirements for staff at all levels and for fixing their remuneration and benefits; the remuneration policy should not include incentives that encourage imprudent behaviour.
- 3) The Board should define and set the following standards:-
 - a) Define the standards of business conduct and ethical behaviour for directors and senior management.
 - b) Define the standards to be maintained in policyholder servicing and in redressal of grievances of policyholders.
- 4) The Board would be responsible to provide strategic guidance for implementation of business policy and structure a management information system for review and course correction.
- 5) As an integral part of the proper implementation of the guidelines of the business and other policies, the Board should take action as under:-
 - a) Establish appropriate systems to regulate the risk appetite and risk profile of the Company. It will also enable identification and measurement of significant risks to which the company is exposed in order to develop an effective risk management system.
 - b) Ensure that all supervisory/regulatory directions are submitted to the Board and the supervisor's recommendations are utilized in the assessment of the performance of the senior management in implementation of Board philosophy.

- c) Define the role of the Appointed Actuary and the degree of his involvement in the designing and pricing of products and in determination of liabilities.
 - d) Ensure that the Appointed Actuary has direct access to the Board and reports on important matters to the Board in a timely manner.
 - e) Ensure that the IT systems in the company are appropriate and have built-in checks and balances to produce data with integrity.
 - f) Ensure that the company has in place a robust compliance system for all applicable laws and regulations.
 - g) Prescribe the forms and frequency of reporting to the Board in respect of each of the above areas of responsibility.
- 6) In the discharge of the above and other Governance functions, the Board should delegate the responsibilities to mandated/ other recommended Empowered Committees of Directors while retaining its primary accountability.
- 7) The Board should ensure that the insurer is compliant with its directions and all statutory provisions and regulations framed thereunder through:
- a) A sound system of internal controls and audit in respect of all aspects of the insurer's activities and accounts, including financial, operational and compliance controls and such systems should be annually reviewed by the Board for their effectiveness.
 - b) The Internal Audit function should perform in an objective, independent and risk oriented manner, with timely feedback to the Board.
 - c) Prescribing and reviewing all delegations of authority to various levels of management, especially in underwriting, claims, reinsurance, investments and financial transactions. Ensure that critical decisions are taken under the 'four eyes' principle.

Name of the Insurance Company:

Declaration and Undertaking by Director (with enclosures as appropriate as on)		
I.	Personal details of director	
a.	Full Name	
b.	Date of Birth	
c.	Educational qualifications	
d.	Relevant Background, Knowledge and Experience	
e.	Permanent Address	
f.	Present Address	
g.	E-mail Address/Telephone Number	
h.	Permanent Account Number under the Income Tax Act and name and address of Income Tax circle	
i.	Any other information relevant to Directorship of the Insurance Company	
II.	Relevant relationships of Director	
a.	List of relatives if any who are connected with the insurer (Refer Section 6 and Schedule 1 A of the Companies Act, 1956)	
b.	List of entities, if any, in which he/she is considered as being interested(Refer Section 299(3)(a) and Section 300 of the Companies Act, 1956)	
III.	Records of professional achievements	
a.	Relevant professional achievements	

IV	Proceedings, if any, against the director	
a.	If the director is a member of a professional association/body, details of disciplinary action, if any, pending or commenced or resulting in conviction in the past against him/her or whether he/she has been banned from entry of at any profession/occupation at any time.	
b.	Details of prosecution, if any, pending or commenced or resulting in conviction in the past against the director and/or against any of the entries listed II(b) and (c) above for violation of economic laws and regulations.	
c.	Details of criminal prosecution, if any, pending or commenced or resulting in conviction in the last five years against the director	
d.	Whether the director attracts any of the disqualifications envisaged under Section 274 of the Company's Act, 1956?	
e.	Has the director or any of the entities at II (b) and (c) above been subject to any investigation at the instance of Government department or agency?	
f.	Has the director at any time been found guilty of violation of rules/regulations/legislative requirements by customs/excise/income tax/foreign exchange/other revenue authorities, if so give particulars	
g.	Whether the director at any time came to the adverse notice of a regulator such as SEBI, RBI, MCA	
h.	Whether the director was associated as director or officer with any entity that was wound up or that was penalized for violation of any law.	

i.	Any other explanation/information in regard to items I to III and other information considered relevant for judging his/ her fit and proper compliance.	
V	Other directorships or senior executive positions held by the director	

Undertaking

I confirm that the above information is, to the best of my knowledge and belief, true and complete. I undertake to keep the insurer fully informed, as soon as possible, of all events which take place subsequent to my appointment which are relevant to the information provided above.

I also undertake to execute the deed of covenant required to be executed by all directors of the insurance company.

Place:
Date:

Signature of the Director

VII. Remarks of Board of Directors of Insurer

Place:
Date:

Signature

FORM OF DEED OF COVENANTS WITH A DIRECTOR

THIS DEED OF COVENANTS is made this _____ day of _____ Two thousand _____ BETWEEN _____, having its registered office at _____ (hereinafter called the 'Insurance Company ') of the one part and Mr/Ms _____ of _____ (hereinafter called the 'Director') of the other part.

WHEREAS

A. The Director has been appointed as a Director on the Board of the Insurance Company (hereinafter called 'the Board') and is required as a term of his/her appointment to enter into a Deed of Covenants with the Insurance Company.

B. The Director has agreed to enter into this Deed of Covenants, which has been approved by the Board, pursuant to his said terms of appointment.

NOW IT IS HEREBY AGREED AND THIS DEED OF COVENANTS WITNESSETH AS FOLLOWS:

- 1)** The Director acknowledges that his/her appointment as Director on the Board of the Insurance Company is subject to applicable laws and regulations including the Memorandum and Articles of Association of the Insurance Company and the provisions of this Deed of Covenants.
- 2)** The Director covenants with the Insurance Company that:
 - i) The Director shall disclose to the Board the nature of his/her interest, direct or indirect, if he/she has any interest in or is concerned with a contract or arrangement or any proposed contract or arrangement entered into or to be entered into between the Insurance Company and any other person, immediately upon becoming aware of the same or at meeting of the Board at which the question of entering into such contract or arrangement is taken into consideration or if the Director was not at the date of that meeting concerned or interested in such proposed contract or arrangement, then at the first meeting of the Board held after he/she becomes so concerned or interested and in case of any other contract or arrangement, the required disclosure shall be made at the first meeting of

the Board held after the Director becomes concerned or interested in the contract or arrangement.

- ii) The Director shall disclose by general notice to the Board his/her other Directorships, his/her memberships of bodies corporate, his/her interest in other entities and his/her interest as a partner or proprietor of firms and shall keep the Board apprised of all changes therein.
- iii) The Director shall provide to the Insurance Company a list of his/her relatives as defined in the Companies Act, 1956 and to the extent the Director is aware of Directorships and interests of such relatives in other bodies corporate, firms and other entities.
- iv) The Director shall in carrying on his/her duties as Director of the Insurance Company:
 - a) use such degree of skill as may be reasonable to expect from a person with his/her knowledge or experience;
 - b) in the performance of his/her duties take such care as he/she might be reasonably expected to take on his/her own behalf and exercise any power vested in him/her in good faith and in the interests of the Insurance Company;
 - c) shall keep himself/herself informed about the business, activities and financial status of the Insurance Company to the extent disclosed to him/her;
 - d) attend meetings of the Board and Committees thereof (collectively for the sake of brevity hereinafter referred to as ' Board ') with fair regularity and conscientiously fulfil his/her obligations as Director of the Insurance Company;
 - e) shall not seek to influence any decision of the Board for any consideration other than in the interests of the Insurance Company;
 - f) shall bring independent judgment to bear on all matters affecting the Insurance Company brought before the Board including but not limited to statutory compliances, performance reviews, compliances with internal control systems and procedures, key executive appointments and standards of conduct;
 - g) shall in exercise of his/her judgment in matters brought before the Board or entrusted to him/her by the Board be free from any business or other relationship which could materially interfere with the exercise of his/her independent judgment; and
 - h) shall express his/her views and opinions at Board meetings without any fear or favour and without any influence on exercise of his/her independent judgment;

- v) The Director shall have:
 - a) fiduciary duty to act in good faith and in the interests of the Insurance Company and not for any collateral purpose;
 - b) duty to act only within the powers as laid down by the Insurance Company's Memorandum and Articles of Association and by applicable laws and regulations; and
 - c) duty to acquire proper understanding of the business of the Insurance Company.
 - vi) The Director shall:
 - a) not evade responsibility in regard to matters entrusted to him/her by the Board;
 - b) not interfere in the performance of their duties by the whole-time Directors and other officers of the Insurance Company and wherever the Director has reasons to believe otherwise, he/she shall forthwith disclose his/her concerns to the Board; and
 - c) not make improper use of information disclosed to him/her as a member of the Board for his/her or someone else's advantage or benefit and shall use the information disclosed to him/her by the Insurance Company in his/her capacity as Director of the Insurance Company only for the purposes of performance of his/her duties as a Director and not for any other purpose.
- 3) The Insurance Company covenants with the Director that:**
- i) the Insurance Company shall apprise the Director about:
 - a) Board procedures including identification of legal and other duties of Director and required compliances with statutory obligations;
 - b) control systems and procedures;
 - c) voting rights at Board meetings including matters in which Director should not participate because of his/her interest, direct or indirect therein;
 - d) qualification requirements and provide copies of Memorandum and Articles of Association;
 - e) corporate policies and procedures;
 - f) insider dealing restrictions;
 - g) constitution of, delegation of authority to and terms of reference of various committees constituted by the Board;
 - h) appointments of Senior Executives and their authority;
 - i) remuneration policy,
 - j) deliberations of committees of the Board, and

- k) communicate any changes in policies, procedures, control systems, applicable regulations including Memorandum and Articles of Association of the Insurance Company, delegation of authority, Senior Executives, etc. and appoint the compliance officer who shall be responsible for all statutory and legal compliance.
 - ii) the Insurance Company shall disclose and provide to the Board including the Director all information which is reasonably required for them to carry out their functions and duties as a Directors of the Insurance Company and to take informed decisions in respect of matters brought before the Board for its consideration or entrusted to the Director by the Board or any committee thereof;

The insurance company shall provide training on an on-going basis to enable the directors to discharge their role effectively.
 - iii) the disclosures to be made by the Insurance Company to the Directors shall include but not be limited to the following:
 - a) all relevant information for taking informed decisions in respect of matters brought before the Board;
 - b) Insurance Company's strategic and business plans and forecasts;
 - c) organisational structure of the Insurance Company and delegation of authority,
 - d) corporate and management controls and systems including procedures;
 - e) economic features and marketing environment,
 - f) information and updates as appropriate on Insurance Company's products;
 - g) information and updates on major expenditure;
 - h) periodic reviews of performance of the Insurance Company; and
 - i) report periodically about implementation of strategic initiatives and plans;
 - iv) the Insurance Company shall communicate outcome of Board deliberations to Directors and concerned personnel and prepare and circulate minutes of the meeting of Board to Directors in a timely manner and to the extent possible within two business days of the date of conclusion of the Board meeting; and
 - v) advise the Director about the levels of authority delegated in matters placed before the Board.
- 4) The Insurance Company shall provide to the Director periodic reports on the functioning of internal control system including effectiveness thereof.**

- 5) The Insurance Company shall appoint a compliance officer who shall be a Senior Executive for reporting to the Board/respective Committees of the Board and be responsible for setting forth a framework on compliance responsibility and for implementation thereof. He/she shall also monitor adherence to the applicable laws and regulations and policies and procedures including but not limited to directions of Insurance Regulatory and Development Authority and other concerned statutory and governmental authorities.
- 6) The Director shall not assign, transfer, sublet or encumber his/her office and his/her rights and obligations as Director of the Insurance Company to any third party provided that nothing herein contained shall be construed to prohibit delegation of any authority, power, function or delegation by the Board or any committee thereof subject to applicable laws and regulations including Memorandum and Articles of Association of the Insurance Company.
- 7) The failure on the part of either party hereto to perform, discharge, observe or comply with any obligation or duty shall not be deemed to be a waiver thereof nor shall it operate as a bar to the performance, observance, discharge or compliance thereof at any time or times thereafter.
- 8) Any and all amendments and/or supplements and/or alterations to this Deed of Covenants shall be valid and effectual only if in writing and signed by the Director and the duly authorized representative of the Insurance Company.
- 9) This Deed of Covenants has been executed in duplicate and both the copies shall be deemed to be originals.

IN WITNESS WHEREOF THE PARTIES HAVE DULY EXECUTED THIS AGREEMENT ON THE DAY, MONTH AND YEAR FIRST ABOVE WRITTEN.

For the Insurance Company	Director
By
Name:	Name:
Title:	
In the presence of:	
1.... ..	2.... ..
