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Government of India
Ministry of Finance
Department of Financial Services
(Insurance Division)
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2nd floor, Jeevan Deep Building,
Parliament Street, New Delhi.
Dated: 1st August, 2012

To
Shri G. Srinivasan, CMD, United India, Chennai
Shri A. K. Saxena , CMD, Oriental Insurance, New Delhi
Shri A. R. Sekar, Current In-Charge, New India, Mumbai
Shri N.S.R. Chandra Prasad, CMD, National Insurance, Kolkata

Subject: <u>Strategy to be adapted by companies for Fire Insurance-reg</u>

Dear Sir,

As we are all aware, Fire Portfolio has always, in the past, generated underwriting surplus and had, in fact, provided cushion to subsidize the losses being incurred in other portfolios. Of late, however, it is observed that some of the PSUs have been incurring losses in Fire Portfolio too with consistent regularity. The main reason seems to be de-tariffing of premium rates in 2007, which has resulted in a very unhealthy competition amongst the four PSUs, so much so that the sanctity of the basic concept of ‘prudent underwriting’ is lost. In view of the factual position as above, the PSUs are advised to be more cautious and prudent in underwriting Fire business by devising a proper underwriting / marketing strategy to maintain its age old status of a profitable segment of non-life insurance business. The Advisory is, accordingly, issued as under:-

1) Pricing of Fire cover is required to be made more realistic, so that the combined ratio including Claims, ME and Commission remains below 100% . As a matter of rule,' Burning Cost' analysis should be the basis for working out the commercial rate of premium after providing for ME, Commission, contribution towards catastrophes & other necessary provisions along with a reasonable margin of profit.

2) Since the companies do not have adequate data product-wise for calculation of burning cost, it is recommended that on an ad-hoc basis, the price level which is as on date, uneconomical and unsustainable needs to be worked out in a manner to arrest losses. Keeping expansive nature of fire business in term of number of policies, type of risks being covered, process of manufacturing, property value, geographical spread etc., it is imperative that the proper and judicious calibration in premium in all type of risks and size of

exposure, is affected immediately. Any upward revision of premium only in class rated / small policies i.e. policies of smaller sum insured will prove to be detrimental to the policy holder of small sum insured and ultimately defeat the project of Financial Inclusion. Under no circumstances the policies with smaller sum insured should be used to compensate for the loss of premium due to the highly discounted rates given to the corporate industries. (Policies with high sum insured). It is suggested that average premium per policy in different sum insured bands (<50 crore, 50-100 crore, 100-500 crore, 500 crore and above) shall be enhanced in such a manner that the combined ratio of the portfolio does not exceed 100% and an increase of 20% of total annual premium is achieved for each band of sum insured separately and also overall for the portfolio.

The performance should be monitored at HO level on monthly basis. The data shall be compiled in a structured format and each RO shall be responsible to ensure that their operating offices achieve the desired premium rate correction.

It will be mandatory for the company to place a quarterly report before the Board on Region wise & Sum insured band wise, average premium per policy vis-a-vis corresponding figures last year along with the violations of understanding on renewal retentions, procuration protocol, sharing of data on underwriting and claims etc.

3) The four PSU companies, especially since de-tariffing, have been resorting to huge under cutting while quoting premium, in order to get business in their anxiety to maximize the growth domestic premium income (GDPI). A stage has come when companies are offering a ridiculous level of 100% discount on the standard fire policies by not charging premium at all for the basic policy but only for add-on covers. It is also observed that in the name of increasing their premium and thus market share, companies are trying to procure business from other PSU companies by offering such high levels of discounts. Since most of these are big discounts, the fall out of such discounts is on individual retail policies where the premiums have been hiked up continuously. As a result of which there is a huge price distortion where individuals and retail policyholders who are otherwise not in a position to bargain are made to pay disproportionately higher level of premium per policy, compared to what it should be vis-à-vis such corporate account holders who have the bargaining power and are able to get such windfall discounts. Accordingly, the price discovery in fire sector is not based on the market factor because of the deliberate dampening of the natural premium which could be market determined. It is well established that the PSU companies cannot procure business in the name of increasing premium while ignoring the bottom-line knowingly well that this is a loss-making proposition. Such kind of

extremely negative business procuring tendency, especially by continuously underwriting of premium by PSUs pricing cannot be allowed to continue, and, therefore, all the four insurance companies shall ensure that the companies desist from snatching renewals of business (irrespective of value) of other PSU companies except for specific NOC from the CMD of the company which had issued the expiring policy after due consideration of the ICR for the previous years and the underwriting in all such cases must be in conformity of the laid down policy and the guidelines.

4) Further, accordingly, it must be ensured that the premium charged would be lower than the guide rates filed with IRDA, only in those cases where the ICR of the Regional Office and the Sum Insured band is less than 70%. The pricing is to be done by underwriters at various levels based on risk features as laid down in file and use procedure of each insurer filed with the IRDA. Any deviations of this will be considered only by the Head Office and also Where ICR is above 70%, the risk shall be rated only by Head Office. The risk management committee shall analyse on a quarterly basis the performance of the portfolio and seek such details as necessary from the management and guide management about the rates of premium to be charged in the following quarter and onwards.

5) It is further advised that the 4 PSU companies must have coordination amongst themselves in regard to various aspects of fire insurance business such as growth, profitability, procuration etc. and discourage any unhealthy competition of pricing or otherwise resulting into unnecessary strain on Company's resources or reserves by causing loss. Thus the existing systems of joint consultation before underwriting any big risk shall continue. No PSU should under-quote for the account held by another PSU irrespective of the sum insured and pricing should not be used to snatch renewal at a loss. And efforts will be made to ensure that any transfer of accounts is with due concurrence of the existing insurer and the insured based on policy of merit ratings.

6) The companies shall set up Underwriting Cells both at HO and RO levels by segmenting the risks as under:-

   i) Above Rs. 1000 crores

   ii) Rs. 500 to Rs.1000 crores

   iii) Rs.100 crores to Rs.500 crores

   iv) Below Rs.100 crores

   The level of authority for underwriting and monitoring of price of segmented risks would be as under:-

i. Head Office – all policies above Rs. 500 crores
ii. RO – Rs.100 crores to Rs.500 crores for MD & BI together
iii. DO - below Rs.100 crores

Head office of the respective company to decide the mechanism for delegation of authority and also the guidelines for underwriting by the operating offices. It is proposed that like HO, there will be similar coordination committee at RO centres to work in coordination for compliance of the guidelines. The proposed committee at RO level shall examine all proposals for sum insured in the band of Rs.100 to Rs.500 crores to determine the correct price.

7) In order to ensure uniform underwriting approach, the Companies need to evolve Common Underwriting Manual / Internal Guidelines/policies to be approved by the respective Board of the Company after getting it approved first by the RMC. The Companies to evolve common underwriting guidelines by 17th August, 2012.

8) Source-wise/channel-wise analysis of business underwritten and the losses emanating there-from should be made to identify loss making accounts so as to exercise extra underwriting precautions while accepting/renewing any such business.

9) The companies may ensure formation of investigation teams at the level of underwriting offices as well as at ROs level to visit the site of accident immediately after the loss is reported. This must be strictly be monitored at least in big losses, (say of more than 20 lakh), in order to avoid exaggeration of claims and frauds etc.

10) The companies should ensure collaboration at the industry level and with Police Authorities and judiciary for prevention of frauds. They should consider filing of criminal cases against those entities found to be indulging / conniving in filing of fraudulent claims.

11) Further, quarterly report in respect of such cases where the combined ratio is more than 100% may be placed before the Board of Directors for their information and guidance within one month of the end of each quarter, with all relevant details, through the RMC and the Chair of RMC shall brief the Board on these cases and shall make available all details as sought for.

12) It is proposed that in respect of business coming through intermediaries with special reference to brokers, such offices only will release quotes where the plant or the client’s corporate office is located. No quote shall be given for RFQs for clients assets/corporate office located outside the jurisdiction of the

branch. This measure is intended to reduce the possibility of the Companies' various offices giving different quotes for the same risk.

13) In order to ensure that pricing policy is a bench mark against burning cost plus management expenses, the Companies should be called upon to generate integrated data of the four companies for each class of product / risk separately. The exercise is to be completed by the end of December, 2012 so that the pricing policy can be determined more scientifically for the next financial year.

14) It is suggested that at Head Office level the companies must hold a high level discussion immediately to document the understanding amongst themselves on various aspect such as retention of renewals, quotation, procuration etc. The outcome of this meeting should be conveyed to us within a week's time.

Please acknowledge receipt and confirm the action taken.

This has the approval of Secy (FS).

Thanking you,

Yours faithfully

(Arun K Misra)
Under-Secretary to the Govt. of India

Copy to:-
CE, GIPSA