ALLEN & OVERY

India in focus

India opens its insurance market to further foreign investment

Key take-aways

Earlier this year, the Insurance (Amendment) Act 2021 (the **Act**) came into force in India, allowing non-Indian investors to hold majority control in Indian insurance companies for the first time (subject to certain conditions). Foreign ownership of up to 74% in an Indian insurance company is now permitted via the 'automatic route' – ie without prior approval from the Indian government (subject to verification by the Insurance Regulatory and Development Authority of India (**IRDAI**)). The requirement that Indian insurance companies must be "Indian owned and controlled" has also been removed.

The Act signals the continuing liberalisation of the Indian insurance sector and follows the legislative change in 2015 when the cap on foreign ownership in Indian insurance companies was increased from 26% to 49%.

Since 2015, the sector has seen a significant rise in foreign investment, including an influx of private equity funds interested in growing their presence in the Indian insurance market.

It is expected that the liberalisation of foreign investment in the Indian insurance sector brought about by the Act will lead to similar increased inflows of foreign capital, as well as stimulate growth and innovation in the Indian insurance sector. International investors who were previously reluctant to invest in Indian insurance companies because of being unable to exercise "control" (owing to both the 49% cap and the requirement of "Indian ownership and control") are revisiting potential investment opportunities.

Conditions for foreign investment in the Indian insurance market

When the Act was passed earlier this year, the Government of India had alluded to certain "conditions" continuing to apply. Some commentators suggested that these "conditions" would retain the requirement of "Indian ownership and control" over Indian insurance companies introduced in 2015 (which effectively restricted foreign investors' control over and veto rights in relation to significant polices of Indian insurance companies including in relation to business plans, products and audit/tax/accounting policies).

Fortunately, that has not been the case. Instead, the conditions (prescribed in the Insurance Companies (Foreign Investment) Amendment Rules 2021 (the **Rules**)) effectively require Indian residency for a majority of directors and key management – with additional conditions for insurers with more than 49% foreign investment. The "Indian owned and controlled" requirement has therefore been removed by the Act – in addition to increasing the aggregate foreign investment limit from 49% to 74%. This change will enable foreign investors to negotiate stronger management rights and control over significant policy decisions.

The current conditions for foreign investment in the Indian insurance sector are set out below.

Indian insurers having any amount of foreign investment:

- The majority of directors, the majority of key management persons, and at least one of the company's chairperson, managing director and chief executive officer, must be resident Indian citizens.
- Compliance with this requirement must be achieved within one year of the commencement date of the Rules (ie by 19 May 2022).

Additional conditions for Indian insurers with more than 49% foreign investment:

- At least 50% of the directors must be independent directors unless the chairperson is an independent director (in which case at least one third of the board must be made up of independent directors).
- A specified percentage of profits are required to be retained by the insurance company as general reserves. Specifically, in respect of a financial year for which a dividend is paid by the insurance company on equity shares and for which at any time its solvency margin is less than 1.2 times the prescribed control level of solvency, no less than 50% of net profits of that financial year must be retained in general reserve.

Commentary

This increase in the permitted threshold of foreign direct investment in the Indian insurance sector represents an opportunity for international investors. Existing investors can look to exercise their change of law call options and new investors can look to invest in majority stakes in the Indian insurance market.

It is expected that this easing of foreign direct investment limits will help Indian insurers attract much needed capital to deepen insurance penetration and lead to increased inflows of foreign capital.

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