

Competition law and the Indian insurance sector¹

The structure of the insurance market in India where close to two third of the market share is with the public sector insurers, anti-competitive behaviour is perhaps not something of immediate concern. Although a number of private sector insurers have or will be completing their first ten years of business, the Indian insurance industry is yet to reach the level of growth where issues of competition assume practical importance. On the other hand, competition law in India is still in a nascent state of development. The Competition Act of 2002 prohibits anti competitive agreements, abuse of dominant position and combinations. Although the provisions pertaining to combinations are yet to come into force, the Competition Commission of India (CCI) is reportedly working on finalising the merger control regulations.

There are views that the insurance sector should be exempted from the purview of the Competition Act. Although the recent recommendations of the Committee of Secretaries on merger and acquisitions in the banking sector makes it less likely that sectoral exemptions will find favour with the policy makers, there are examples such as the European Union (EU) where special treatment is extended to the insurance sector by exempting it from the purview of competition rules. The burgeoning number of private sector life and general insurers in the Indian market and the competition amongst them to capture larger market share does not seem conducive of anti-competitive combinations or abuse of dominant position. However, the Indian insurance sector has vast potential for growth and continues to attract investors from within and outside India. It may change the market conditions prevailing today. At the same time, competition rules in India are still developing and calls for consideration of issues and developments in other jurisdictions regarding sector specific exemptions.

In this regard it may be useful to look at some issues effecting the application of competition rules to the insurance sector in the EU. The European Commission's Block Exemption regulations for the insurance sector [Commission Regulation (EC) No 358/2003; hereinafter referred to as BER 1] provided general exemption to certain agreements in the insurance sector from the EU's general prohibition of practices restrictive of competition. The exemptions were mainly for (i) Joint calculations and studies; (ii) Joint establishment and distribution of non-binding standard policy conditions; (iii) The setting up of insurance pools for the joint coverage of new risks; and (iv) The establishment, recognition and distribution of technical specifications, rules and codes of practice on security devices.

The BER1 expired on 31 March 2010 and the European Commission press release IP/10/359 of 24 March 2010 declared adoption of a new Block Exemption Regulations (BER2) to be effective from 1 April 2010 till 31 March 2017. The BER2, however, has reduced the scope of exemption to the sector. Exemption for agreements on standard

¹ Views are personal.

policy conditions and agreements on security devices are no longer available under BER2.

The main arguments in favour of insurer co-operation are that (i) sharing of information that enables premium calculation; (ii) co-operation in developing policy terms enhances consumer welfare; and (iii) pooling arrangements are essential to enable insurers to insure large risks;

The business of insurance naturally deals with uncertainty and relies upon the law of averages, so that larger the database of information better is possibility of proper risk rating. An insurance company's own loss statistics may be inadequate for the purpose and co-operation among insurers in sharing their loss experience provides access to a sufficiently large collection of data. It may also provide an incentive for insurance companies to merge. The BER2 exempts agreements with respect to the joint compilation and distribution of calculations of the average cost of covering a specified risk in the past, but subject it to a number of conditions including the requirement of such compilations being made available to other insurance undertakings and consumer organizations on reasonable terms.

The emphasis on making the calculations and tables available to any insurer indicates the European Commissions concern over preventing joint studies, calculations or tables from leading to market power in the hands of incumbent insurers and creation of entry barriers to new entrants.

The argument for insurer co-operation in pooling arrangements has prevailed in favor of insurers under the BER2. The BER2 acknowledges that co-insurance pools can be necessary to allow participating undertakings to provide insurance for risks for which they might only offer insufficient offer in the absence of the pool. However neither BER1 had provided nor BER2 provide absolute exemptions to pooling arrangements. In recognition of the possibility that pooling arrangements may lead to restrictions on competition such as standardization of policy conditions, amounts of cover and premiums, the BER2 restricts the scope of the exemption. Under the BER2 the exemptions apply (i) where the co-insurance pool is created exclusively for covering 'new risks', then for three years from the date of establishment of the pool irrespective of market share of the pool; and (ii) for all other co-insurance pools, till the BER2 remains in force, if the market share of the co-insurance pools does not exceed 20% (25% for reinsurance pool). The period of applicability of the exemption would be limited to a maximum of two years where the co-insurance pool's market share exceeds 20% subsequently. 'New risks' essentially refers to those risks for which it is not possible to know in advance what subscription capacity is necessary to cover the risk. It could be risks that did not exit previously as well as existing risks for which objective analysis indicate material change in their nature.

The argument for insurer cooperation in developing standard policy conditions is based on the premise that the supply of insurance services lacks transparency and consumers are not in a position to compare the terms and conditions of various policies available in the market. However the EC is of the view that agreements for standard policy conditions or agreements on security devices are not specific to the insurance sector and the BER2 no longer exempts such agreements.

The BER2 underwrites the fact that the economics behind the business of insurance sector distinguishes it from other businesses. However exemptions under the BER2 are limited to certain types of agreements and it may be wrong to read it as a blanket exemption of the insurance sector from the competition rules. As India is in the process of shaping up the regulatory regime to support the broad provisions of the Competition Act, it may be an opportune time to consider the various arguments for and against sector specific exemptions. It is interesting to note that during the consultation process conducted by the EC for review of the BER1, a number of the industry representatives cited legal certainty as the reason why the BER should be renewed. A legislative decision regarding exemption should also take this aspect into account. A blanket exemption based on the current market situation may pose difficulties for policy changes in the future.

DRAFT