THE FIRM
Corporate Law in India

M&A Norms For General Insurers

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Corporate India is seeing a wave of regulations being introduced to streamline inorganic corporate growth in the country. This momentum is not limited to central legislations governing corporate transactions. Industry specific regulations governing such transactions are also on the rise. The insurance industry has witnessed the first of such regulations with the Insurance Regulatory and Development Authority ("**IRDA**") having unveiled the regulations to govern the mergers and amalgamations in the general insurance space in the form of IRDA (Scheme for Amalgamation and Transfer of General Insurance Business) Regulations 2011 ("**Regulations**") which came into force from May 31, 2011. 'General Insurance Business' is defined under the Insurance Act, 1938 ("**Act**") to mean fire, marine or miscellaneous insurance business, whether carried on singly or in combination with one or more of them.

The Regulations have been introduced after a period of 10 years since the insurance sector opened up for the private sector in August 2000 and have been made applicable specifically for insurance companies in the private sector. The two-step approval process of the IRDA has not been made a substitute for other statutory approvals. Any merger and amalgamation of insurance companies is still governed by the provisions of the Companies Act, 1956 ("**Companies Act**") and requires the sanction of the relevant Courts to become effective. The Regulations lay out an elaborate process for seeking approval of the regulator in the event of merger or an amalgamation of insurance companies but are not devoid of certain lacunae especially given the plethora of new laws governing such corporate transactions. This article summarizes some of the key aspects of the Regulations and highlights certain areas that may need to be addressed by the regulator.

<u>Position prior to the Regulations</u>

Prior to the enactment of the Regulations, mergers and amalgamations of insurance companies were regulated under Section 35 to 37 of the Act. In essence, even before the Regulations, every merger, amalgamation and transfer of business needed the nod of the IRDA prior to it becoming effective. The approval process under the Act was a onetime approval that required the IRDA to approve the scheme of amalgamation. A post facto filing with the IRDA was also required after the amalgamation was completed.

<u>Requirements of the Regulations</u>

The Regulations prescribe a comprehensive process for obtaining the two-fold approval of the IRDA:

• *<u>Notice of Intention:</u>* The Regulations continue to stipulate a 'notice of intention' to be filed with the IRDA prior to application for the implementation of the scheme. The documents to be filed along with the notice of intention now include a report on the manner in which the interest of the policyholders will be protected and a report on compliance with applicable laws including the Competition Act, 2002. This addition is in furtherance of the spirit of the Regulations namely to safeguard the interests of the insurance policyholders.

• *<u>In-principle approval:</u>* The first of the two staged process is the in-principle approval to be

accorded by the IRDA prior to the insurance companies making an application in this regard to the Courts and other regulatory authorities for their approvals. The in-principle approval could stipulate and be subject to certain conditions or changes as the IRDA may deem necessary. Upon receipt of the in-principle approval, the nature and terms of the scheme are required to be published in at least one national daily and one vernacular newspaper. Thereafter approvals from the other regulators and Courts need to be sought.

• *Final Approval:* Pursuant to scheme being approved by the various regulatory authorities, the transacting parties are required to approach the IRDA for a final approval of the scheme. As per the Regulations, the amalgamations and transfer of the general insurance business will be effective from the date as specified y the IRDA while granting the final approval.

The Regulations also prescribe a filing fee payable to the IRDA for processing the in-principle approval being 1/10th of 1% of the total gross premium writing direct in India by the transacting entities during the financial year preceding the financial year in which the application was filed subject to a minimum of INR 5,000,000 and a maximum of INR 50,000,000.

Analysis

The following paragraphs examine the issues that may arise and require clarity pursuant to the Regulations:

Scheme of Amalgamation v/s a transfer of assets

The Regulations, although titled "Scheme of Amalgamation and Transfer of General Insurance Business", appear to govern only schemes of amalgamations formulated under Sections 391-394 of the Companies Act since the definition of the term 'scheme' has been limited to the ones formulated thereunder. What needs to be clarified is whether other transfers by way slump sale or acquisition of the insurance business would also be subject to procedures under the Regulations or whether such transfers would be subject to the provisions of the Act. Section 35 of the Act that previously governed such transactions includes within its scope all forms of agreements relating to transfer of the insurance business and is not restricted to a scheme formulated under Sections 391-394 of the Companies Act.

Shareholders and Creditor Meetings

Under the Companies Act, every scheme under Sections 391-394 thereof is required to be approved by the shareholders and creditors of both the transferee and the transferor companies. These meetings are called for pursuant to the directions of the Courts. Whilst the Regulations require the scheme to be approved in-principle prior to the same being sanctioned by the Courts, it is not clear as to whether the in-principle approval needs to be sought prior or post the shareholders/creditors meeting approving the scheme. Should the in-principle approval be obtained prior to the shareholders and creditors approving the same, a change that may be requested by the shareholders and creditors may again require the approval of the IRDA. In the alternative, obtaining the shareholders'/creditors approval prior to seeking an in-principle approval may also result in the transferor and transferee companies going back to shareholders to approve any change that the IRDA may propose. Further, the requirement to publish the terms of the scheme in newspapers after receipt of in-principle approval may also have a bearing on when the shareholders and creditors meeting need to be held.

Overlap of jurisdictions

A merger of two insurance companies may also attract the filing requirements of the Competition Act, 2002 ("**Competition Act**") relating to combinations under which the Competition Commission of India ("**CCI**") is required to look into whether such mergers would have an appreciable adverse effect on competition in India. Although there are no objective criteria to determine 'appreciable adverse effect on competition', the CCI is bound to look into the following factors in arriving at a determination on the appreciable adverse effect on competition like (a) whether the arrangements creates barriers to new entrants in the market; (b) whether the arrangements will drive existing competitors out of the market; (c) whether the arrangements will foreclosure competition by hindering entry into the market; (d) whether the arrangements accrue benefits to consumers; grant improvements in production or distribution of goods or provision of services etc. The objective of the Competition Act is to

promote competition and to protect the interests of the markets. The aim of the Regulations is to regulate the growth of the insurance sector and also to protect the interests of policyholders and consequently, it would appear that the objective of the Regulations and the Competition Act overlap to a substantial extent. Since both regulations need to view a transaction on a holistic basis and given the similarity of the objectives of the regulations, a single window clearance from both regulators may prove beneficial for such transactions from a consumer and industry perspective. Further, both regulators are empowered to require the transacting parties to make changes to the scheme if the regulators so deem necessary. These changes may also require to be reconciled by both regulators to sustain the commercial viability of the transaction.

Timelines

Since the IRDA has not stipulated any particular timeline for the grant of both, in-principle approval as well as the final approval, the total time frame for the consummation of the scheme cannot be ascertained and the process could be long drawn especially since the sanction of a scheme may be subject to the approvals of various other regulators.

Costs

Extended costs would have to be incurred in seeking approval from the IRDA for a merger, given that the filing fees are a minimum of INR 5,000,000 and a maximum of INR 50,000,000. This along with the filing fees payable to other regulators would make the cost of entering into a scheme of arrangement exponential. Such additions to the Regulations could be viewed as a disincentive for transacting parties to use the route of court approved mergers for purposes other than genuine commercial and business purposes.

Effective Date

The Regulations vest with the IRDA, the authority to stipulate when the scheme of amalgamation becomes effective. These powers of the IRDA may have to be reconciled with the provisions of the Companies Act, which requires every scheme of arrangement approved by the Courts to be filed with the Registrar of Companies within 30 days of an order being passed for the scheme to become effective.

Conclusion

While the Regulations appear to lay down elaborate procedures to be undertaken in the event of a merger and amalgamation of general insurance companies including a two-step approval from the IRDA, the Regulations are definitely a step toward balancing the interests of the policyholders and liberalization and consolidation of the insurance sector in India. It’s a question of time to see how the Regulations will unfold and how the issues arising out of the implementation of these Regulations will be tackled. The IRDA should address the concerns of the industry to ensure that the benefits of the Regulations are not overshadowed by the procedural difficulties. While the Regulations are only applicable to general insurance companies, the industry now awaits the IRDA to unshackle regulations for mergers and amalgamations of companies engaged in other streams of business in the insurance sector.

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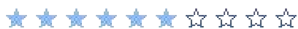

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