The Dynamics of an Evolving Environment: Role of a Chartered Accountant

Insurance industry has shown a vibrant growth over the last decade – that is, during the period after it was opened up for private participation. The privatisation introduced during the last decade of 20th century has added a new dimension to the very aspect of insurance business in India. This astounding growth process in the post-liberalisation period has got transparent and stronger with several regulatory developments under the Insurance Regulatory Development Authority. The Institute of Chartered Accountants of India (ICAI) in particular and Chartered Accountants in general have been playing a crucial role in the systematic and accountable growth of Insurance industry in the country. The insurance sector has thrown open challenging jobs for the Chartered Accountants in Finance, Risk Management, Planning and Operations functions in insurance companies. In this article the author analyses the dynamics of evolving insurance environment and the role and responsibilities of the Chartered Accountants in this regard.

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Insurance industry has shown a vibrant growth over the last decade – that is, during the period after it was opened up for private participation. Although the growth had been steady even during the earlier period with the four subsidiaries competing with each other in the non-life arena, and the lone player in the life sector consolidating by leaps and bounds; it was always felt that the

flavour of competition has been conspicuous by its absence. The privatisation introduced during the late last decade of the twentieth century has brought in a new sense of competitive spirit in the players; apart from the introduction of some world-class players into the Indian domain. All this has certainly added a new dimension to the very aspect of insurance business in India.

A cursory look at some of the statistics will certainly add credence to the type of growth achieved over the last ten years. There are currently nearly two dozen players each in the life and non-life domains; and the number has been growing steadily over the last few years. It goes to show the keenness of the players to tap the immense potential that is available in the country. The total first year premium of life insurers (during the financial year 2010-2011) which reflects the new business secured during the year stood at ₹1,25,826 crore, registering a growth of nearly 15 per cent over that of the previous year. The non-life insurers, apart from the stand-alone health insurers, underwrote a total premium of ₹42,569 crore as against the previous year's figures of ₹35,816 crore registering a healthy growth of nearly 16 per cent. Apart from the tremendous business growth, the investments of the insurance companies have attained significantly large volumes which play a major role in the overall economic development of the country. For example, the investment portfolio of life insurers as at the end of the financial year 2009-2010 showed a whopping figure of ₹12,05,155 crore and that of non-life insurers stood at ₹66,372 crore.

The three specialists in health insurance mustered a total business of ₹1,529 crore during the year which is more than 44 per cent higher than the previous year's performance. Even among the regular non-life insurance companies, health insurance as a class has grown tremendously which is a very positive trend in a domain where the total coverage – including the government sponsored schemes – of the population under any arrangement for health-related coverage does not go beyond 10 per cent to 12 per cent. While there are a few problems associated with this class mainly owing to the low awareness levels, we have been addressing the issues progressively on an on-going basis; and it is expected that this class of insurance will demonstrate even greater purpose-oriented growth during the years to come. Portability of Health insurance, issues pertaining to the Third Party Administrators, standard treatment protocols, etc. are some of the top priorities for us and we are confident that there will be a lot of ground gained in the near future.

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There have been several regulatory developments that have been very significant for the growth of the industry in the post-liberalisation period. To quote some of the important ones, detariffing of the non-life arena has been a very important milestone. It was being felt that despite the opening-up of the industry, an administered pricing stifled the freedom of the players. After a series of checks for assessing the maturity of the players to handle the freedom, it was eventually felt that the Indian insurance market is mature enough for the pricing freedom. It is gratifying to note that the confidence reposed in the players has not been belied and we have not had an occasion to intervene in the day-to-day affairs of any player. However, we have been exhorting the players of the importance of their achieving operational surpluses and not depending unduly on their investment incomes to offset their underwriting losses. In a scenario that typically demonstrates a high volatility in the interest rates, it is common knowledge that undue dependence on investment incomes would be highly risky.

The Indian insurance market has been exclusively agency-driven, historically. While several milestones have been achieved with the 'agent' being the centre of all activity, the professionalism associated with intermediation was felt to be greatly limited – especially in designing the vital risk management function of corporate entities. Accordingly, several distribution channels like brokers, corporate agents, bancassurance, etc. have been introduced in the liberalised regime; and have been operating successfully along with the ubiquitous agent. It was

often expressed by the clientele as also by the media that there is an element of mis-selling by the intermediaries. We have taken several measures to ensure that this trend is arrested; and subsequent results have indicated that there is vast improvement in this regard.

In a domain that is typically representative of low awareness levels, there is need for identifying all areas that need to be consolidated in empowering the client. One way of achieving this is by ensuring that the distribution channels are thoroughly professional; and that they fulfill their role of need-identification, followed by a need-based selling. We have taken several measures to achieve this and a constant review of the training needs of the distributor is a step in this direction. Further, there should be ways of ensuring that the awareness levels of the insuring public itself improve over a period of time. This would go a long way in setting at rest most problems associated with mis-selling, problems of adverse selection, doing away with litigation that leads to a no-win situation, controlling frauds, etc. We have been actively taking several measures to improve the understanding levels of the average policyholder through conduct of seminars, press releases, sponsorship of educational programs in the radio and visual media etc. Besides, the players themselves are encouraged to promote healthy campaigns that contribute towards a steady rise in the awareness levels of the policyholders and prospects.

Despite all the measures being taken by the regulator and the players, there is a huge role for every stakeholder to participate in a campaign of such an importance. The basics of the operation of the insurance contracts need to be understood even by the policyholder belonging to the lowest stratum of the society in order that the growth of the insurance industry itself is based on sound business ethics. Only such a regime will ensure that several misconceptions associated with the industry are set at naught; and the industry makes steady progress with the average buyer volunteering to buy insurance rather than being driven to do it.

Apart from the average rise in the awareness levels of the general populace through various methods, specific professionals like the Chartered Accountants have a huge role to play – especially in the corporate sector. With their vast understanding of the financial services, CAs are typically positioned to be excellent ambassadors of the cause of spreading the importance of risk management that would eventually lead to protection of invaluable assets. Further, being an important component of some of the professional roles like surveyors and loss assessors, Chartered Accountants can be very effective mediators between the insurers and the insured in reducing avoidable controversies and insurance related litigation.

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Above all, there is growing importance of attaining uniform standards of reporting in financial services, globally. While the task is stupendous, the Chartered Accountant can contribute a lot towards proper interpretation of the standards; and their adoption by the Indian corporate domain so that in the end we move towards attaining global standards in terms of business achievements as also a proper reporting.

IRDA & ICAI

Apart from the very generalised role play for CAs mentioned above,

there is a lot that CAs can do for the betterment of the Indian insurance industry; and in pursuit of this, IRDA, from the very beginning, had a close association with ICAI. IRDA was of the view that it should retain its inherent powers to decide the way the insurance business is to be regulated but involve ICAI and take its suggestions/recommendations in policy matters relating to accounting, audit and investments. It was thus in 1999 that IRDA constituted Accounting Committee and approached ICAI to nominate Chartered Accountants of repute and stature to lay down standards in framing IRDA's Accounting and Investment Regulations. IRDA felt that it would be appropriate that the accounting committee be made as a Standing Committee on Accounting Issues (SCAI) and have members primarily drawn from the CA profession with merit and stature to advice the IRDA on matters within their domain. Today the vice president in the office of the ICAI represents the profession in the SCAI. The SCAI is headed by a past President of ICAI, and has practicing members from ICAI,

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Actuarial Society of India, CAs from the industry (representing Life and Non-Life Business both from PSUs and private sector), and CAs who specialise on security systems, to advise IRDA on policy matters relating to:

1. Specific needs of accounting, auditing and investments of the insurance industry covering both Life and Non-Life Business
2. IFRS-4 on insurance contracts, IFRS-7 on financial instruments and to suggest a roadmap to implement the recommendations of IFRS committee of IRDA
3. Adoption of accounting and auditing standards for both Life and Non Life business
4. Insurance industry specific standards, valuation procedure, disclosure norms under accounting regulations
5. Norms for revenue recognition, provisioning and assets classification
6. Regulations of investments of Life and Non-Life insurers
7. Best practices under investment risk management systems and process
8. Periodical reporting and formats for such reporting under accounting and investment regulations
9. Other policy issues relating to accounting, investment and audits as may be referred to the committee

International Standards on Investments

As the Indian economy is growing at a fast pace, it is important that it has strong and robust systems that meet the minimum international standards that are mandated by International Association of Insurance Supervisors (IAIS). It may be seen that insurance investments grew from around ₹1 lakh crore in the year 2000, when the sector was opened for private players, to a staggering ₹14 lakh crore in 2010. As the investments represent the policyholders' money which requires to be protected, IRDA felt the need for tighter controls which at least meet the minimum standards of IAIS in respect of:

a. Investment Asset Mix
b. Diversification (Spread) of investment risk
c. Classification of investments
d. Investment management structure
e. Risk management systems
f. Systems to prompt the regulator of any systemic issues
g. Other Regulations:
   1. Safe keeping of assets
   2. Preventing insider trading
   3. Asset-Liability Management
   4. Standard Operating Procedure (SOP)
   5. Contingency plans to mitigate effects of deterio-rating condition

Need for a Different Approach

The humongous insurance investments with demanding international standards mandated by IAIS; and business needs along with technology development in the financial market required a robust system to be put in place. To address these fast paced developments, IRDA, in 2008 amended the investment regulations to address the growing complexity of insurance investments, both under traditional and unit linked platform. Such amendments should take into consideration the following, which are very specific to insurance:

a. The insurance liabilities represent the present value of future liability. Hence the regulations, apart from addressing the liabilities, should also address 'Solvency' needs.
b. As the Insurance Act does not permit liabilities to be funded through borrowings, a few more safe avenues should

be permitted to generate investment income.

c. As payouts depends on 'contingent' event, and is a 'process', liquidity needs are factored in investment policy, and should be enabled through regulations

d. As insurers are 'Risk Carriers', insurance investments are to be held in 'safe' assets. Hence, regulations limit the exhaustive category of investments. The audit mechanism put in place should ensure that investments are not made beyond the categories and limits permitted under the regulations.

e. Standards mandated should be same for both state-owned and private players – providing a level-playing ground; and the best available technology for a 'dynamic' monitoring/ reporting should be put in place.

f. Investment operation, being dynamic, for an effective control should be based on 'Exception' reporting

Monitoring Systems – IRDA's Methodology

The total insurance industry investments, as at 31st March, 2011 are around ₹14 lakh crore. Regulators globally usually do not have the adequate numbers of and/or adequately trained staff to fully and effectively carry out the supervision mandate. As such, to rely on professional bodies is inevitable. As ICAI is a regulator of Chartered Accountants who play a key role in certifying and attesting the various activities in an insurance company, IRDA had engaged ICAI in laying down the standards in the area of accounting and investments; and systems relating to these functions. Hence, the model that is in place engages CAs to carry out the audits as per the procedures laid down by ICAI. To put it differently, the chartered accountant is the regulator at the insurer's office. But the key is to lay down standards for such audits, so that the regulator's control requirements (both systems and transaction) are fully addressed.

Toward the above, IRDA introduced the systems audit to be certified through CAs; and the transactions process through such systems to be audited through concurrent audit by CAs so that IRDA secures a good hold on an extremely huge portfolio in a country which has the second highest population in the world. Thus by engaging CAs through ICAI, the monitoring mechanism of IRDA will have a clear institutional backup. While implementing the institutional model IRDA had:

1. Retained the business controls within IRDA's Board, where ICAI is also a member, represented by its President in office.
2. Decided on the various controls to be checked, and periodicity in which such checking should be done. As checking and re-porting are essentially an audit function, the same had been kept under the control of ICAI.
3. In this connection, IRDA, through ICAI had issued the following 'Technical Guides':
   a. Technical guide on Re-view and Certification of Invest-ment Risk Mana-gement Systems and Processes of insurance companies.
   b. Technical guide on inter-nal/ concurrent audit of invest-ment functions of insurance companies.
4. The audit is done on 100 per cent of transactions to report 'exceptions' to the Board of insurer, with the comments of audit committee of the board.
5. The insurer is required to file with IRDA, the audit report, with the feedback of the audit committee and along with Board's response to such exceptions on a quarterly periodicity.
6. The audit is aimed at provi-ding IRDA the focus to look at systemic impact such exce-ptions would bring out.

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RESPONSIBILITIES OF CAs

1. Internal/Concurrent Audit should:

a. Cover 100 per cent of trans-actions and report exceptions.

b. Examine Investment Policy (IP), Standard Operating Procedure (SOP), its implementation, and review.

c. Compliance to regulations, cir-culars and guidelines.

d. Fund accounting process lead-ing to computation of NAV in the case of ULIP funds.

e. Report on systems and pro-cess supporting investment operations covering Front, Mid and Back Office.

2. Confirmation on:
a. Implementation of audit committee recommendations.
b. All investments made follow SOP issued by Investment Committee (IC).
c. Classification of investment risk by IC for ranking (risk based monitoring/reporting).
d. Implementation of dealing employee guidelines.
e. Implementation status of systems and process – Phase 1.
f. Segregation of shareholder/ policyholder funds, its accounting and identification at custodian level.
g. Reporting of Chief Investment Officer (CIO) and Chief Financial Officer (CFO) – for segregation of investing and its accounting.
h. Compliance to exposure norms and certification of NAV and its declaration.
i. Reporting of fund performance and regulatory compliance to insurer's Board.

Opportunities for CAs

The insurance sector has thrown open challenging jobs for the Chartered Accountants in Finance, Risk Management, Planning and Operations functions in insurance companies. CAs are known for their keen analytical ability, excellent technical skills and meticulous working style; and with their effective communication and interpersonal skills, can emerge as insurance specialists.

In this scenario, CAs are thrust with responsibility to authenticate various types of information submitted to the regulator by an insurance company. Thus CAs have a dual role to play. While within the insurance company, they play a crucial role in providing the management the analysis of business and also project the way forward, the practicing CAs who do the audit have their commitment towards the public and other stakeholders including the regulator.

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Thus, CAs can play the following roles:

1. As employees in insurance companies can take up the following:
   a. Chief Investment Officer
   b. Equity Research
   c. Dealer in Debt/Equity Market
   d. Compliance Officer
   e. Fund Manager
   f. Risk Manager
   g. Fund Accounting & NAV Calculation
   h. Framing Standard Operating Procedure
2. External support services in the following areas:
   a. Statutory Audit
   b. Internal Audit
   c. Concurrent Audit
   d. Information Systems Audit
   e. Risk Assessment
   f. Risk Advisory
   g. Framing Standard Operating Procedure
   h. Framing Investment Policy
3. Apart from the above, CAs can undertake the following:
   a. Insurance management,
   b. Insurance marketing,
   c. Underwriting management,
   d. Claims management,
   e. Product development,

Way Forward

As the insurance sector is growing at a rapid pace, the need for CAs, who are equipped with the needs of the industry will be in acute demand. Towards this demand ICAI should be in a position to supply Chartered Accountants to bridge the gap that exists now. In this connection, ICAI may like to take a look at the following:

1. Review the historical patterns of specialisations that the CAs take to - and based on this study revamp the CA course curriculum to channelise the CAs into their preferred areas of specialisations.
2. On the same count, integrate the Diploma in Insurance Risk Management (DIRM) and Diploma in Information Systems Audit (DISA) courses with the CA course. The content of these courses needs to be revamped with a bias for more practical training in the respective fields.
3. Collaborate with sector regulators for carrying out the above.
4. Integrating Information Security and Systems study into the CA curriculum.
5. Making it mandatory for CAs to have a six months industrial training in their area of specialisation.
6. Revisit the terms of reference of the Committee on Information Technology and the Committee on Insurance and Pension; and enlarge the scope of these committees with larger representation from industry so that the industry needs are well addressed. ■