Client Update

Indian Insurance Reforms — New Guidelines on the "Control" Conundrum

NEW YORK
David Grosgold
dgrosgold@debevoise.com

Nicholas F. Potter
nfpotter@debevoise.com

John M. Vasily
jmvasily@debevoise.com

LONDON
Geoffrey P. Burgess
gpburgess@debevoise.com

Shashwat Patel
spatel@debevoise.com

HONG KONG
E. Drew Dutton
eddutton@debevoise.com

Parveet Singh Gandoak
psgandoak@debevoise.com

As discussed in our previous client update,[1] the Insurance Laws (Amendment) Act, 2015 (the "Act") increased the foreign ownership cap in Indian insurance companies from 26% to 49%. One of the key requirements of the Act and the related regulations was that "ownership" and "control"[2] of the jointly held company must remain with resident Indian citizens or Indian companies owned and controlled by resident Indian citizens. There was no such requirement under the previous insurance regime prior to the Act and the related regulations.

The Indian insurance regulator, the Insurance Regulatory and Development Authority ("IRDA"), does not have any existing body of jurisprudence on the meaning of "Indian control" and has recently issued long-awaited guidelines[3] (the "Guidelines") to clarify the concept. However, while these Guidelines are helpful, there remains considerable uncertainty as to how they will be applied.

---

[1] Available here.

[2] The term "control" has been defined to include:

- the right to appoint a majority of the directors; or
- to control the management or policy decisions, including by virtue of shareholding or management rights or shareholders agreements or voting agreements.

A similar definition of control and the scope of rights constituting control has been examined and interpreted by various Indian regulators, including the Foreign Investment Promotion Board ("FIPB"), the Securities and Exchange Board of India, and the Competition Commission of India in various decisions in different sectors. However, the regulatory approach to its interpretation has not been consistent.

[3] Guidelines on "Indian owned and controlled," Ref No. IRDA/F&A/GDL/GLD/190/10/2015, October 19, 2015. Available here.

KEY POINTS

Following are some of the key highlights of the Guidelines:

- For an Indian insurance company to ensure that "control" remains with Indians, the Guidelines require that:
  - a majority of directors (excluding independent directors) should be nominated by Indian promoters/Indian investors;
  - key management persons (including CEO, Managing Director, Principal Officer) should be appointed either (a) through the company's board of directors or (b) by the Indian promoters/Indian investors;
  - the Company's board of directors must control significant policies;
  - if the chairman of the board of directors has a casting vote, such chairman should be nominated by the Indian promoters/Indian investors; and
  - a quorum should include the presence of a majority of the Indian directors irrespective of the presence of a foreign investor's nominee (which can also be required as a protective right).
- Foreign partners will be allowed to nominate senior management personnel (other than the CEO) subject to the board's approval.
- Existing companies have been given until January 18, 2016 to comply with the Guidelines, while new companies are required to be in compliance from inception.
- Existing companies are also required to submit an undertaking signed by their CEO and Chief Compliance Officer confirming compliance with the Guidelines. Such an undertaking is to be accompanied with a board resolution certifying compliance and, where applicable, a copy of the joint venture agreement where amendments have been made to bring it in line with these Guidelines.

CONCLUSION

In view of the Act and the Guidelines, Indian parties will need to be able to demonstrate control of Indian insurance companies through their boards of directors. It will not be sufficient to argue that no party is in control or that there is joint control. The IRDA has not indicated whether "independent directors" can be appointed jointly by the foreign partner and the Indian investor. Practitioners are taking the view that the IRDA may permit independent directors to be

nominated jointly by the parties, which should give significant comfort to foreign investors on the neutrality of the board in taking key decisions.

Notably, the term “management and policy decisions” has also not been defined in either the Act or the Guidelines. We believe “management and policy decisions” will be construed to mean decisions regarding the day-to-day functioning and management of the company, its business and its operations. These decisions should be different from strategic or structural decisions, which may require approval of foreign/minority investors with a view to protect their investment. In our view, consent rights with respect to the latter category of decisions should pass regulatory scrutiny.

Although the Guidelines are a step in the right direction to bring some much-needed clarity around what constitutes “Indian control,” it seems likely that the IRDA will review each transaction on a case-by-case basis. The first few IRDA approvals[4] are expected in the next few weeks and should shed further light on how foreign insurers will be able to structure customary minority protections and veto rights without running afoul of the new “Indian control” requirements.

* * *

Please note that Debevoise & Plimpton is not licensed to advise on Indian law. This update is based on information that has been published in the press and from other sources in the public domain.

Please do not hesitate to contact us with any questions.

---

[4] Many insurance companies have filed applications to raise their foreign partner’s stake with both the FIPB and the IRDA. So far, Bharti AXA Life Insurance, Edelwiess Tokio Life and Aegon Religare Life Insurance have received FIPB approvals.