

PRIVATE EQUITY INVESTMENTS IN INDIAN INSURANCE COMPANIES

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On October 13, 2022, the Insurance Regulatory and Development Authority of India (the “IRDAI”) published an exposure draft of the IRDA (Registration of Indian Insurance Companies) Regulations, 2022 (the “**Draft Registration Regulations**”), under which it is proposed to permit private equity funds (“**PE Funds**”) to act as promoters of Indian insurance companies.

Conditions for Investment

Investments may be made in two distinct capacities: (i) as an investor; and (ii) as a promoter.

Investment as an investor is subject to a cap of 25% (twenty-five percent) of the paid-up equity share capital of insurer. This investment is restricted to no more than two (2) life insurers, two (2) general insurers, two (2) health insurers and two (2) reinsurers, if (i) the investment exceeds 10% (ten percent) of the paid-up equity capital of the insurer; and (ii) if the investor has the authority to appoint/nominate a director on the board of the insurer(s).

Investment as a promoter is restricted to one (1) life insurer, one (1) general insurer, one (1) health insurer and one (1) reinsurer. The minimum shareholding of the PE Fund promoter must be maintained above 50% (fifty per cent) of the paid-up equity capital of the insurer. This stake may be diluted, subject to the insurer maintaining a track record of solvency ratio above the control level during the five (5) years immediately preceding the stake dilution by the promoter(s) and the shares of the insurer being listed on a stock exchange in India. However, the diluted shareholding of the promoter(s) must never be less than 26% (twenty-six percent) of the paid-up equity capital of the insurer.

Regardless of the capacity under which the investment is being made, the investment must be made entirely out of own funds and not from borrowed funds.

Investments by PE Funds are subject to certain additional requirements under the Draft Registration Regulations. The investment must be as per the PE Fund’s strategy reflected in its placement memorandum to its investors or its charter documents. In addition, for a PE Fund to invest as a promoter:

- (i) the PE Fund or its parent fund must have completed ten (10) years of operation;
- (ii) the funds raised by the PE Fund including its group entities must be at least US\$500 million (or its equivalent in INR);
- (iii) the investible funds available with the PE Fund must be at least US\$100 million; and
- (iv) the PE Fund must have invested in the financial sector in India or other jurisdictions.

In addition, in respect of all new insurance applications, insurers as well their promoter(s) and investor(s) will have to comply with the lock-in period as below, which varies based on the timeline of investment.

Particulars	Investment in the capacity of	Lock-in Period
At the time of or before grant of R3 (i.e., Certificate of Registration)	Promoter or Investor	5 years
Investment within 5 years post grant of R3 (in case of change in shareholding pattern)	Promoter or Investor	Earlier of the following: a) 5 years or b) 8 years from the grant of R3
Investment after 5 years but before 10 years post grant of R3 (in case of change in shareholding pattern)	Promoter	Earlier of the following: a) 3 years or b) 12 years from the grant of R3
	Investor	Earlier of the following: a) 2 years or b) 11 years from the grant of R3
Investment after 10 years post grant of R3 (in case of change in shareholding pattern)	Promoter	2 years
	Investor	1 year

Further, the shareholders of the insurer cannot create any encumbrance whatsoever on the equity shares of the insurance company during the lock-in period. After the lock-in period, an encumbrance can be created, but only with the prior written approval of the IRDAI. The insurer, its promoter(s) and investor(s) must also fulfill the “Fit and Proper” criteria on a continuous basis.

Fit and Proper Criteria

Any investment by an investor or a promoter will be subject to compliance of the “Fit and Proper” criteria, an illustrative list of which has been provided in the Draft Registration Regulations. The criteria include aspects such as:

1. The applicant’s integrity, reputation, track record:
 - a. The financial strength of the promoter/investor.
 - b. Ability to infuse capital to meet business, solvency and regulatory requirements.
 - c. Compliance with laws in India, including foreign investment and tax laws.

- d. Ability to access capital or financial markets to source funds that may be needed for any future capital infusion.
 - e. Business record and experience of the applicant.
2. Due diligence
 - a. Approval/NOC by other regulatory bodies in India and/or outside India, as applicable;
 - b. Insider trading, fraudulent or unfair trade practices or market manipulation by the PE Fund or any of its promoters/group entities.
 - c. Proceedings including convictions against the entity or any of its promoter/group entities or any of its KMPs, by any regulatory/statutory/judicial bodies in India or abroad.
 3. Interest of policyholders and the public at large.
 4. Impact on the management and governance structure of the insurer.
 5. Agreement between shareholders and impact on control/management of the insurer.
 6. Capital structure of the promoter/investor.
 7. Source of funds for investment.

Other Changes in the Regime

Investments by PE Funds into Indian insurance companies are also governed by the IRDAI (Investment by Private Equity Fund or Alternate Investment Fund in Indian Insurance Companies) Guidelines, 2017 (the “**PE Investment Guidelines**”). In order to harmonize the regime governing PE Funds’ investments in Indian insurance companies and prevent contradictions between the Draft Registration Regulations and the PE Investment Guidelines, some of the below listed changes will be necessitated to the PE Investment Guidelines.

The PE Investment Guidelines explicitly prohibit direct investment by PE Funds into Indian insurance companies in the capacity of promoter. This restriction will need to be removed. Further, there is a cap on direct investment by PE Funds into Indian insurance companies in the capacity as an investor of 10% (ten percent) of the paid-up equity share capital of the insurance company. However, the Draft Registration Regulations do not make a distinction between PE Fund investors and other investors while prescribing a cap on investment in the capacity as an investor of 25% (twenty-five percent) of the paid-up equity share capital of insurer. This cap must be harmonized.