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Bancassurance : Can you Bank on it?

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ABSTRACT

Bancassurance is defined as the insurance distribution model where insurance products are sold through bank branch network. The presence of several banking groups as promoters of insurance companies is of great significance to this model. With a network of over 80,000 branches, spread across the length and breadth of the country banks are having the necessary potential to make bancassurance the most efficient way to achieve financial inclusion in insurance sector. The bank customers with higher average premium per-capita provide quicker means to grow for insurers. The complementary nature of insurance products towards the bank advances (e.g. credit life) provide synergies in operations to the entire financial sector. The ease of access to bank customers reduces servicing costs, contributes to lower lapsation of insurance policies and hence lower costs to the economy.

Banks see value in insurance business due to complementarity of products, fee income derived from the distribution of insurance and ease of recovery of advances in case of death of the borrower or destruction of properties. Several banks being promoters of the insurance companies also gain when valuation of those companies goes up due to synergies derived from bancassurance. Life insurance is a contract between an insurance policy holder and an insurer, where the insurer promises to pay a designated beneficiary a sum of money (the "benefits") upon the death of the insured person. Depending on the contract, other events such as terminal illness or critical illness may also trigger payment.

The need for increasing the reach of life insurance in India is pretty obvious. To increase penetration level to a higher level than the present one will require more efforts. Banks can play an effective role in this context. The untapped potential can be used with proper training of involved human resource.

Keywords - Bancassurance, Life Insurance, Privatisation, Product innovation

I. INTRODUCTION

The most comprehensive definition of a service has been given by Philip Kotler, who defines a service as an act or performance that one party can offer to another that is essentially intangible and does not result in the ownership of anything. (Kotler, 2007)Its production may or may not be tied up to a physical product.

Services are economic activities that bring about a desired change in, or on behalf of the service recipient, thereby creating value and providing benefits for the customer. Thus, the focus remains on customer satisfaction, just as ingoods, but in services, emphasis is on the personal reception of these benefits.

From the predominantly agricultural economy in the earlier times, the country has come a long ay in its development since its independence in 1947. In advanced economies such as USA, France or Germany, services is the largest sector in the economy. In these countries, almost three quarters of the GDP is accounted for by the tertiary sector. In third world countries such as China and India, the tertiary sector is not yet so important. China seems to have made strong gains in manufacturing sector and is a very low-cost producer for many industrialised countries. India and China both are moving towards dominance of services. If we consider global economic trends, it is clear that national economic advancement is led by services sector.

II. PRIVATISATION

The process of privatisation of many sectors have created opportunities for private players. Monopoly of public sector is replaced by competition and that has ushered a new era of customer orientation. The importance of services delivery is well understood by private investors. They make great efforts to be customer friendly and effective to ensure customer loyalty. Not only external customers are important, but internal customers are the backbone of any successful organisation. The effectiveness of employee would determine the customer perception of service delivery. (Kulkarni, 2008)

Life Insurance

Life insurance is a contract between an insurance policy holder and an insurer, where the insurer promises to pay a designated beneficiary a sum of money (the "benefits") upon the death of the insured person. Depending on the contract, other events such as terminal illness or critical illness may also trigger payment. The policy holder typically pays a premium, either regularly or as a lump sum. Other expenses (such as funeral expenses) are also sometimes included in the premium; however, in Australia the predominant form simply specifies a lump sum to be paid on the policy holder's death. The advantage for the policy owner is "peace of mind", in knowing that the death of the insured person will not result in financial hardship for loved ones.

Life policies are legal contracts and the terms of the contract describe the limitations of the insured events. Specific exclusions are often written into the contract to limit the liability of the insurer; common examples are claims relating to suicide, fraud, war, riot and civil commotion. Life basedcontracts tend to fall into two major categories:

- Protection policies–designed to provide a benefit in the event of specified event, typically a lump sum payment. A common form of this design is term insurance.
- Investment policies–where the main objective is to facilitate the growth of capital by regular or single premiums. Common forms (in the US) are whole life, universal life and variable life policies. (Wikipedia, 2012)

INSURANCE VS ASSURANCE

The specific uses of the terms "insurance" and "assurance" are sometimes confused. In general, in jurisdictions where both terms are used, "insurance" refers to providing coverage for an event that might happen (fire, theft, flood, etc.), while "assurance" is the provision of coverage for an event that is certain to happen. In the United States both forms of coverage are called "insurance", for reasons of simplicity in companies selling both products (Wikipedia, 19Jan 2012)

Life Insurance Distribution

It is an acknowledged fact that Insurance, especially in India, is more sold than bought. Since life insurance is meant to cover potential losses in future and not to cater to immediate consumption needs, there is always a tendency to postpone or avoid the purchase of life insurance. The low awareness levels in the society further add to the difficulty in selling life insurance. Distribution, therefore, becomes the key link in the chain of activities in the business of Insurance. In a country like India distribution, which essentially means carrying the message of insurance through the last but toughest mile, acquires even greater preeminence.

In view of the sensitive nature of the business by virtue of its being in the financial domain and the key role played by distribution, insurance selling, worldwide, is a tightly regulated activity. Coming to India, the Insurance Act, 1938 has laid out clear cut provisions on the following issues pertaining to distribution of insurance:

- Licensing of Insurance Agents
- Conditions/ceilings on payment of commission
- Privileges of Agents
- Code of conduct for agents

There was no change in the above provisions so long as the insurance industry was a monopoly during which distribution of insurance was largely confined to the tied agency channel.

III. CHANGING SCENARIO

With the notification of the IRDA Act, 1999 and the pursuant opening up of the sector to private players, distribution of insurance has witnessed a flurry of activities shown below:

- Specification of minimum educational qualification for agents and intermediaries
- Mandatory pre-license training and examination
- Issue of License by IRDA
- Elaborate regulation prescribing the code of conduct for all intermediaries
- Issue of regulations allowing/regulating corporate agencies, brokers and referrals

The above initiatives have completely changed the complexion of insurance distribution in the country. The raised level of qualifications at entry, pre-license training, qualifying examination and tightening of the code of conduct for the intermediaries over the last few years have all contributed to improvement in the quality of distribution in the insurance sector. The advent of new channels such as Corporate Agents including, Bancassurances, Brokers and Referrals has helped in the massive expansion that the insurance sector witnessed in India in the recent past. These channels have not only helped the sector to leverage on the clientele/network of the corporate who enrolled as insurance intermediaries but also facilitated institutionalization of the distribution of insurance.

The entry of the new players, the consequent expansion of offices, new channels of distribution, increase in number of tied agents along with the increasing awareness and acceptance of insurance have all contributed to the massive expansion of the insurance sector in the last seven years. The unprecedented buoyancy in the economy during this period has no doubt supported this splendid performance. The magnitude of the business expansion of the life insurance sector can be gauged from the fact that the CAGR stood at over 37% over the last seven years. The penetration and density of the life sector had also gone up from 1.2% to 4.1% and Rs.280 to Rs.1510 respectively between the years 2000 & 2006.

Despite the emergence of new channels of distribution, tied (individual) agency channel remains the mainstay of the sector, still contributing a lion's share of the business being generated by the insurers.

On the life insurance side, the new business premium procured by the tied agency channel amounts to 89% of the total in the year 2006-07. The number of life insurance agents has increased from around 8 lakhs in the year 2000-01 when the sector was opened up to private insurers, to roughly 20 lakhs by the end of the year 2006-07. Out of this the number recruited by the new private insurers is around 9 lakhs, the remaining 11 lakhs being with the public insurer LIC.

Among the new channels the corporate agencies had performed particularly well with a prominent share coming from the bancassurances. In the year 2006-07, corporate agents had procured 7.3% of the total new business premium mobilized, two-thirds of which had come from the bancassurances.

It has however been the experience in the sector that while the new channels have contributed to the business expansion, the expected decline in the distribution costs which was one of the objectives of allowing them to operate did not materialize to the desired extent. On the contrary, the widespread perception in the sector points to an increase in overall distribution costs, though the first year commissions have seen a steady decline.

IV. GROWTH OF BANCASSURANCE

The growth of Bancassurance was phenomenal in initial years of opening. The premium collected through Bancassurance has gone up to Rs 21947 crore in the financial year 2009-10 which is 7.31% of the total premium income of life and non-life insurance sectors. In the year 2009-10, the total compensation received by banks is approximately Rs 2744 crore. There are 17 banks with shareholding in insurance companies. The total paid up capital infused by the banks as on 31.03.2009 was Rs 3328.36 crore and as on31.03.2010, it was Rs 3735.31 crore. However the premium growth seems to have reached a plateau due to the inability of both banker & Insurance companies in exploiting full potential of bank customer profile. Not even 10% of the housing advances are covered either by credit life or mortgage insurance. This is of concern when we consider the low levels of insurance penetration in the country.

V. CAUSE FOR CONCERN

The reason for the low utilization of potential of bancassurance are manifold, principal ones being the monopolistic relations, low levels of training, lack of operational coordination, unequal relationship, short duration of tie-ups, lack of specially designed products, non utilisation of technology platform and poor servicing standards prevailing in bancassurance channel. The banking regulator has set up enviable standards in customer servicing, redressal of grievances, transparency in charges apart from stringent control over operational procedures. It is necessary to providesimilar set of standards in bancassurance business also. For achieving the higher insurance penetration, and density, higher levels of policy holder servicing and for providing a proper regulating framework the committee made the following recommendations:

1. The Bancassurance channel may be allowed to operate on principles of tied agency preserving the current legal status of the bank as an agent of the insurer.
2. Banks may be allowed to have tie-up with any two sets of insurer:
   - Two in life insurance sector
   - Two in non-life insurance sector excluding health
   - Two in health insurance sector
   - ECGC and AIC.
3. Constitution: A 'Bank' defined as per Banking Regulation Act 1949, and any subsidiary of a bank constituted as a special purpose vehicle for insurance distribution exclusively with RBI's approval and NBFC's including HFCs, accepting deposits and branches of foreign banks operating in India may be permitted to conduct insurance business in India under the 'Bancassurance'. Each banking group may be permitted to tie up with the same set of insurers irrespective of the number of corporate agent licenses the group has.
4. Compensation to Banks:

i. The banks shall not be eligible for any compensation other than the commission payable for distribution of insurance products. The current stipulation in Corporate Agency Regulations, barring all other payments shall be applicable to the banks also The CEO and CFO of the bank shall certify the sum total of all payments or reimbursements received by bank and its affiliates from the insurers and their affiliates on annual basis.

ii. Discount in valuation of Equity share given by insurers to bank distribution partners and all other types of payments in cash or kind shall be valued as per accounting standards, at arms length and treated as advance commission and amortised in a period not extending beyond three years.

iii. The Bancassurance regulations shall provide for recovery of any compensation received in excess of the permitted commission, from banks and their affiliates.

5. Accounts and certification:

   i. The bancassurers shall have to maintain an appropriate form of auditable accounts. A Compliance Certificate from CEO and CFO shall be prescribed.

   ii. They shall furnish the periodical returns to the Authority in the formats a prescribed by the Authority.

   iii. Provisioning for operational risk by bancassurers for the insurance distribution may be prescribed by RBI.

   iv. Insurance vertical of the bank/SPV shall be headed by an officer who reports directly to Board of Directors of the Bank.

   v. Corporate governance norms regarding disclosure shall have to be complied by the banks treating Bancassurance as integral part of bank's business operations.

6. Training:

   i. Regulations shall mandate that the bank staff be fully trained in handling insurance products so that the sale process is transparent and the policyholder gets full disclosure of the features of the product. One-time rigorous training may be given to the sales personnel of the bank, with added stress on complex products along with stricter certification at renewal.

   ii. The bancassurers shall market insurance products only in those branches where specified person is posted.

7. Code of Conduct:

   i. Mis-selling of Insurance Products: Any malfeasance, misfeasance or nonfeasance by the bank staff shall be strictly dealt with by RBI. Banking Ombudsmen may be mandated by RBI to accept complaints from policyholder, whenever the bank or its staff is found in default. However, the Insurer is always answerable to the policy holder, as long as 64VB of Insurance Act is satisfied

   ii. Claim settlement: The agreement between the banker and the insurer may provide for banker to assist the policyholder in making the claim and processing the claim as per the procedures prescribed by the insurance company.

   iii. Policy Servicing: The insurers and bancassurers shall enter into a detailed Service Level Agreement (SLA) regarding the policy servicing activities to be undertaken by the insurer.

   iv. The insurer may be allowed to rely on the due diligence and KYC carried out by the bank for its existing relationships

   v. The sale of insurance products by bank staff shall compulsorily be preceded by Needs Analysis.

8. Inspection and Supervisory terms:

   i. The Bancassurance regulation may provide for IRDA and RBI to inspect any of the Bancassurance partners.

   ii. IRDA shall strengthen the inspection and off site monitoring of distribution partners as they account for the largest component of expenses.

9. Agreement between the banker and the insurer: i) The tenure of the agreement between the banker and the insurer shall not be less than five years.

10. Referral System: It is observed that the referral model is costlier than the corporate agency model. Inequitable relationship between the banker and the insurer has resulted in higher premium on the policyholder. The referral system shall not be available to bancassurers

11. IT and other Infrastructure: Technology platform built by banks is of immense use for them in Bancassurance business. Efforts shall be made to leverage the technology to improve efficiency of distribution.

12. The permission to tie up with multiple insurers as per these recommendations shall be contingent upon banks fulfilling all the conditions specified in these recommendations.

It is expected that the above recommendations, when implemented will result in a vibrant bancassurance channel, benefiting the policy holders, banker and insurer.

Life Insurance Direct Marketing Association

Direct response selling of life insurance is the fastest growing segment of the life insurance industry today. Each year a higher percentage of overall life insurance sales can be attributed to some type of direct marketing effort.

More than $300 million in life insurance premium is initiated each year from direct response efforts and direct sales of life insurance represents as much as 10% of all policy sales on an annual basis. According to Pat Wedeking, president of the Life Insurance Direct Marketing Association (LIDMA), what was once considered a “non-traditional” form of life insurance sales is now becoming a major source of new business.

“Our industry has embraced a shift in customer behavior and preference in how they want to address their life insurance needs. Some want to feel more ‘in control’ of their insurance decisions, many want to save their time and others simply want their insurance protection in force in a more timely fashion.”

LIDMA was formed as a catalyst for the growth for life insurance professionals involved in direct marketing and those looking to expand their new business efforts into direct response sales. The organization will serve as a source for industry research and will monitor the interest of its members on a legislative level. The Association also serves as the industry’s primary forum for the exchange of ideas, a champion for the development of advanced marketing and operations technology and an advocate for industry ethics and professional standards.

Since its inception as a not-for-profit organization in 2005, LIDMA has grown quickly and its membership now includes many of the life insurance industry’s top carriers, agencies, producers, exam companies and technology vendors.

“We have made tremendous strides in bringing together the major players in the life insurance direct response industry and together we have already made some real progress,” said Shervin Eftekhari, vice president of LIDMA. “LIDMA’s ultimate objective is to help get more life insurance in force more efficiently. The support that LIDMA has received in these early days shows there are many in our industry that see the same opportunity we do regarding the growth of this sales segment.”

The growth of the direct sales niche can largely be attributed to a void direct marketers are filling, especially with middle income earners. Statistics from the American Council of Life Insurance 2004 Fact Book reported 12,581,000 individual permanent and term life polices were purchased, virtually the identical number purchased almost 30 years before. Over the same time period there was a 38% increase in the U.S population base of 293.7 million in 2004, as compared to 212.6 million in 1975-yet the number of policies sold remained consistent.

According to LIMRA, the Life Insurance Market Research Association, in 2004, one-third of adults in the U.S. carry no life insurance at all. Although there has been an increase in group insurance with ownership rising from 25% in 1976 to 37% in 2004, there is still a large and growing segment of the population which is not being served and life insurance direct marketers are ideally positioned to occupy this niche.

“The direct response industry has adapted to a continued change in customer behavior towards more remote, direct buying,” says Wedeking. “While there continues to be strong demand for traditional face to face advice for consumers, the growth of direct response sales in our industry shows that there is an incredible opportunity for the life insurance industry to serve the otherwise underserved middle market.”

Some of LIDMA’s early successes involve working with carriers to incorporate new processes and operations enhancements to better service the volume of direct sales policies. The Association also serves as a consolidated voice to technology companies that have improved customer interaction and policy processing through the Internet and those that look to upgrade the customer service levels in nationwide call centers.

LIDMA is also becoming active in nationwide marketing campaigns to educate consumers on their need for life insurance and the direct response avenues available to them to address their specific life insurance objectives.

While LIDMA’s goal is to support and enhance the success of its members, the Association never looses sight of its true mission.

“As life insurance professionals we can never loose sight of the fact that our products are a vital part of the security of the consumers we serve around the world,” says Wedeking. “We want to help our members get more policies in force because we know that by doing so we are helping to protect more individuals and families.”

There are distinct advantages to buying a one size-fits-all life insurance policy. In a nutshell, the benefits of direct life insurance are:

- It's much simpler to apply for this type of policy
- Download the application form from the internet, or apply on the phone or at your bank or insurance company branch
- The questions are easy
- Minimal medical to no medical information required
- Fast answer–you know straight away if your application has been successful
- Immediate death cover–you are covered straight away, upon acceptance of your application

These products appeal to people who know what they want and like the idea of having a straight forward life insurance policy in place to protect their family and assets, should the worst happen unexpectedly. Direct life insurance is also a good quick-fix for someone who wants to put a policy into place straight away but plans to review their complete asset protection and investment strategy with a licensed financial planner a bit later on.

VI. CONCLUSION

The need for increasing the reach of life insurance in India is pretty obvious. To increase penetration level to a higher level than the present one will require more efforts. Banks can play an effective role in this context. The untapped potential can be used with proper training of involved human resource. New generation welcomes changes with open arms and organizations should be able to offer something different than before to attract and retain them. Insurance companies have to realize that bancassurance is the way to sell insurance in the future as it is the most cost-effective and effective way to reach the customer, while banks will have to take a cue from successful peers in bancassurance to realize that it will only contribute to their growth and not stymie it.

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