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Implication of IRDAI Circular on Motor Third Party

Institute of Actuaries of India

Radhika Bijlani
Param Dharamshi
Arpit Bhagat

Mentor: R Arunachalam

Introduction

The genesis of IRDAI Circular
The New Motor Third Party Directions

Introduction

The genesis of IRDAI Circular

- Triggered by the petition filed by Dr. S Rajaseekaran for enforcement of road safety norms and appropriate treatment of accident victims, was borne the new third party regulation.
- The guidelines were introduced following a Supreme Court order on July 20 this year on a plea seeking relief for victims of road accidents who could not get compensation as owners did not have third-party cover.
- The recommendation was suggested by the SC's Road Safety Committee in a meeting on March 26 where it stated that 66% vehicles running on roads across the country were without any third-party insurance cover.
- The committee recorded that of the approximately 18 crore vehicles plying on city roads, only six crore have third-party cover and that victims of road accidents, in particular fatal accidents, are not getting compensation because the vehicles are not insured.

Introduction

The New Motor Third Party Directions

- In line with the decision of the Supreme Court, all general insurers (barring the stand-alone health insurers and the specialised insurers) need to carry out the following in respect of Motor Third Party Insurance covers for new cars and new two-wheelers with effect from 1st September, 2018:

Offer only three year Motor Third party cover for new cars

Offer only five year Motor Third party cover for new two wheelers

Impact on Motor Business

What doesn't change?
What changes?
Impact on package policies

Impact on Motor Business

What doesn’t change?

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No impact while renewing old policies
The new rule applies only for new private cars and two-wheelers purchased on or after September 1, 2018. The registration date will be considered as the date of purchase.

Only third-party outflow goes up:
The upfront premium for 3 or 5 years has to be paid only on the third-party liability and not on the own-damage (OD) section.

No Impact on IDV
The new rules will not impact the insured's declared value (IDV) of the vehicle.

Impact on no-claim bonus
The NCB is applicable only on the OD portion and not on the TP part.

Impact on Motor Business

What changes?

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Impact on premium outflow: Instead of making annual premium payments, the TP premium will have to be paid as an upfront-lumpsum payment.

TP Tariff has gone up: For new cars, except for below 1000 cc segment, premium for all other car owners will be more. While for two wheelers, except for below 150 cc segment, premium would be more.

	Pre Sep '18 Tariff		Post Sep '18 Tariff	Diff
	Annual Rate	Total Outflow	Total Outflow	
<= 1000 cc	1850	5,550	5,286	(264)
>1000cc, <=1500cc	2863	8,589	9,534	945
>1500 cc	7890	23,670	24,305	635

Impact on Motor Business

Impact on package policies

- Impact on Comprehensive covers:

Long Term Cover: Both TP and OD cover for 3/5 years

Bundled Cover: 3/5 years for TP, but annual cover for OD

Add on covers may be offered on an annual basis or on a 3/5 year basis as well

For long term covers, insurers would need to file the new rates for these covers. Existing rates to be used for annual covers.

Impact on Product Design

Impact on Product Design

- Mandatory for GI companies to provide Long term cover for new cars and two wheelers.

- Type of Products introduced
  - Option 1. Long-Term Package Cover: (TP=3 Years Plus OD=3 Years)
  - Option 2. Bundled Cover: (TP=3 Years Plus OD=1 Years)
  - Option 3. Standalone Third-Party Only cover: (TP=3 Years without OD)
  - Option 4. Standalone OD Only Cover (Necessitates the need to introduce this option)

- Concept of Deposit Premium
  - The recognition of future premium as "Premium Received in Advance" rather than as a part of company's GWP
  - This will be inconsistent with other long term products (e.g. Health)

Impact on Product Design

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- Coverage and Terms and Conditions of the policy.
  - Identical cover, terms and conditions to current annual Private Car and Two Wheeler Package Policy
  - Add on covers being offered.
  - On cancellation return entire deposit premium, the remaining premium to be refund on short scale basis.

- Premium Recognition
  - For Motor TP, premium can be recognized basis 1/no of years.
  - For OD cover there is no clear guideline for recognition of premium.
  - Inconsistency in recognition of premium across companies.

Impact on Product Design

- Commission Payout.
  - Based on premium recognition, the commission payout will be determined.
  - Chances of inconsistency in commission payout between the companies.

- Distribution Channel.
  - Viability of agency and online channels to be challenged.
  - Greater sourcing from OEM tie-ups.

- Administration Systems.
  - Whether the current systems are capable enough to handle the new product variants.

- Marketing.
  - New marketing literature to be published.

Impact on Pricing

Impact on Pricing

- Plausible change in consumer behaviour (changes in claim frequency).
- Allowance for NCB
  - This can vary as compared to annual product.
  - Also there can be inconsistency between the companies.
- Pricing for Add On covers needs to be revisited.
- Investment Income and Claims Inflation
  - The burning cost has to be adjusted for the future investment income that will be earned as well as for claims inflation.
  - There are chances that since TP premium gets locked for long term, the superimposed inflation can lead to higher ultimate loss ratios than expected.

Impact on Pricing

- Deferring the commission payment, based on recognition of the premium which can help company in earning more investment income.

- Insured Declared Value (IDV) reduces year on year and the same has to be accounted for in pricing the premium.

- Administration Expenses
  - Renewal expenses to reduce.

- Margin for Adverse Deviation may be included since this a new product being introduced.

Implication for Insurer, Customer and Intermediaries

Implication for Insurer

- Only General Insurers will be impacted. Standalone Health Insurers or Specialized Insurers will not be impacted

- New products will have to be registered and repriced in accordance with their general pricing philosophy/approach

- Overall Motor Third Party Premium and exposure is likely to increase in the duration of the new long term policies.

- Adverse impact on Motor Own Damage and other add on covers business may be observed.

- Cancellation of long term Motor Third Party Cover policies will only be allowed on the following grounds:
  - ➢ Double Insurance
  - ➢ Vehicle not in use anymore because of Total Loss or Constructive Total Loss
  - ➢ In the event the vehicle is sold and/or transferred

Implication for Insurer

IMPACT ON RESERVING AND CAPITAL MODELLING

- Any Premium from the long term TP cover that is yet to be recognised will contribute to the Deposit Premium and will not be accounted for in reserves.
- The ideology for reserving of OD and other add on covers is likely to remain unchanged.
- TP exposure to increase in the subsequent years. Exposure will need to be adjusted accordingly
- Since there is a concept of Deposit premium, there would not be impact on the capital requirement of the company.

Implication for Insurer

Reinsurance

Increased TP Exposure

Multi Year Reinsurance Contracts

Investments

Long Term Investment Options

Higher Returns on Deposit Premium

FDI Insurer

Making FDI Insurers aware of the new products

Capital Requirement of FDI Insurers

Implication for Customers

Lack of awareness

Covers available

What is compulsory?

Upfront Premium Payment

Large initial outflow

Protection against adverse premium movement

No Claim Bonus

How would it work with the new products?

When does NCB apply?

Insurer Portability

Different covers from different insurers

Move from one insurer to another

Implication for Intermediaries

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Commissions

Likely to benefit from additional Commission from the long term product.

Awareness for agents and dealers

New products

Making the customer aware of changes

Making online systems consistent with the new contracts

Online direct Channels

Impact on OD business

OD And other Add On covers may suffer due to increased upfront TP Premium

Appendix

Appendix

For car owners, the one-time outgo will be high

TYPE OF VEHICLE AND ENGINE CAPACITY	ANNUAL THIRD PARTY RATES BEFORE (₹)	LONG-TERM THIRD PARTY RATES NOW* (₹)
PRIVATE CARS		
Not exceeding 1,000 cc	1,850	5,286
Exceeding 1,000 cc but not exceeding 1.500 cc	2,863	9,534
Exceeding 1,500 cc	7,890	24,305
TWO-WHEELERS		
Not exeeding 75 cc	427	1,045
Exceeding 75 cc but not exceeding 150 cc	720	3,285
Exceeding 150 cc but not exceeding 350 cc	985	5,453
Exceeding 350 cc	2,323	13,034

**Three years for cars and five years for two-wheelers. Source: Irdai*