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Insurance 2.0 | 100% FDI in Indian Insurers

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Introduction

On 1 February 2025, the Honourable Finance Minister of India as part of her budget speech announced the much-awaited increase in the foreign direct investment (**FDI**) limit for the Indian insurance sector from 74% to 100% as part of the budget speech for 2025 (**Budget Speech**).

This announcement follows the public consultation initiated by the Ministry of Finance in November 2024 for amending the Insurance Act, 1938 (**Insurance Act**) to *inter alia* provide for: (a) increase in FDI limit to 100%; (b) a composite license regime for life and non-life insurance business under a single license (as opposed to standalone licenses for life, general and health insurance); and (c) regulatory framework for managing general agents. Our update with respect to this is available here.

This is the latest step in the liberalisation of the insurance sector and is a welcome development for international insurers and foreign financial sponsors looking at the Indian market.

Key aspects of the announced changes

- In addition to announcing the intended increase in the FDI limit, the Honourable Finance Minister's speech referred to the following key conditions:

  - **Premium investment in India**: The announcement refers to the increased limit of 100% being available only with respect to insurers that invest the entire premium in India. Under the current regulations, premiums collected by insurers are classified as 'policyholder funds', and the law already explicitly prohibits insurers from investing policyholder funds outside India, either directly or indirectly. Once profits are realized, they are transferred to 'shareholder funds', from which dividends can be declared. While current regulations do not impose specific investment restrictions on shareholder funds, it remains to be seen whether additional conditions or clarifications will be introduced to align with the Honourable Finance Minister's statement.

  - **Simplification of conditionalities**: The Honourable Finance Minister also mentioned that the "*current guardrails and conditionalities associated with foreign investment will be reviewed and simplified.*" The Insurance Regulatory and Development Authority of India (**IRDAI**) has been consistently making significant progress in this area by consolidating operational regulations and issuing master circulars. While any further simplification will be welcomed by the market, the specifics of these changes remain unclear.

- **No explicit mention of "*composite insurance*"**: While the Honourable Finance Minister did not specifically refer to "composite insurance" licenses (i.e., a unified license covering multiple lines of insurance businesses instead of requiring separate licenses and entities), in our view, this does not imply that the proposal to introduce "composite insurance" licenses is off the table. It remains to be seen how developments unfold in this regard.

Next steps to implement the announced changes

The change in FDI limit will be effective only after a number of steps are completed:

- *Amendments to the Insurance Act*: The Insurance Act will require amendments to formally implement the increase in FDI limits. This will be done through a bill that must be approved by both houses of the Indian Parliament. Following parliamentary approval, the bill will require the President of India's assent. Once the bill receives Presidential approval, it must be published in the Official Gazette of the Government of India and dates will have to be notified when the amendment shall take effect.

  Current status and historic timing: As of now, the bill to amend the Insurance Act has not yet been tabled in Parliament. However, given that the draft amendments have already undergone public consultation, and with the budget session extending until April (including recesses in February and March), there is a possibility that the bill may be introduced during this session. That said, the exact timeline remains uncertain. Once tabled, the passage of these amendments is expected to be smooth, given the clear parliamentary majority of the current government. In 2021 when the increase in FDI limits from 49% to 74% was announced on 1 February 2021 as part of the Union Budget, the Insurance Amendment Bill, 2021 was tabled before the Rajya Sabha (the upper house of Indian Parliament) on 15 March 2021 and adopted by both houses on 22 March 2021. The Bill received Presidential assent on 25 March 2021.

- *Amendments to operational rules*: After the necessary amendments to the Insurance Act are carried out, the IRDAI will need to amend its operational rules limiting FDI in insurers at 74% such as the Indian Insurance Companies (Foreign Investment) Rules, 2015 and the IRDAI (Registration, Capital Structure, Transfer of Shares and Amalgamation of Insurers) Regulations, 2024. In this regard, the following aspects will need to be closely watched:

  - Currently, an Indian insurer with FDI must have: (a) a majority of its directors; (b) a majority of its Key Management Personnel (as defined in IRDAI regulations); and (c) at least one amongst the Chairperson of its board of directors, managing director and chief executive officer; to all be resident Indian citizens.

  - Similarly, in insurers with FDI exceeding 49%:

    - Majority of the board of directors has to comprise independent directors; and

    - For any financial year in which dividends are paid on equity shares and the solvency margin falls below 1.2 times the control level of solvency, the insurer must retain at least 50% of its profits in its general reserve.

  - These requirements will likely be carried forward under the new regime. Given the nature of an insurer's operations, insurers should not find it difficult to comply with these requirements.

  Current status and historical timing: IRDAI is yet to initiate public consultation or issue draft guidelines with respect to the proposed increase in FDI limits. In 2021, IRDAI notified amendments and new operational guidelines with respect to the increase only in July 2021, the time period from announcement to implementation of changes to all the operational rules was approximately six months.

- *Amendments to the foreign exchange regime*: Government of India will have to amend the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 to increase FDI limits in the sector to 100%.

  Current status and historical timing: The changes are yet to be notified. In 2021, when the FDI limits were increased from 49% to 74%, the time period from announcement of the change as part of the Union Budget 2021-22 (1 February 2021) to implementation of amendments to the foreign exchange regime (19 August 2021) was approximately six and a half months.

Comments

The proposed increase in FDI limits to 100% will likely be a game-changer for the Indian insurance sector, injecting much-needed capital and presumably an increased transfer of knowledge, expertise and technology. The Indian insurance market remains under-penetrated and the easing of the FDI limits is a significant step forward in encouraging greater investment in the sector. While coverage has gradually been increasing, to increase this momentum, the government must fast-track the implementation of the increased FDI limits and other reforms proposed in the November 2024 public consultations, aligning with its broader vision of achieving 'Insurance for All' by 2047.

Against the backdrop of the positive impact this is likely to have on the sector as a whole, there are three specific implications of note at this stage.

- The removal of the compulsion to have a local partner may encourage market-entry by new carriers as one of the key challenges new entrants have faced in the past is finding the right local partners.

- Foreign private equity investors looking to back a CEO and management team faced significant hurdles due to the requirement of having a local partner hold a 26% stake. The regulator has traditionally been reluctant to allow professional management teams without substantial independent financial backing to become shareholders and Indian partners in respect of the Indian shareholding requirements. With the approval of 100% FDI, private equity investors will now hopefully have a more straightforward pathway to enter the sector, eliminating the dependency on a domestic partner and facilitating greater investment flexibility.

- Finally, existing investors in current joint ventures may consider their strategic options going forward. This does not necessarily mean that all international insurers will buy-out their local partners (and the terms of existing shareholders' agreements will have to be analysed), but conversations around strategic realignment are likely to begin. Local partners with robust distribution channels are expected to see heightened interest from foreign insurers seeking collaborative ventures and partnerships.

Much depends on the nature of the changes that are introduced, so watch this space.

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