Chapter 3

Reinsurance

3.1 Regulatory framework

Sec. 101A of the Insurance Act 1938 stipulates that every insurer shall re-insure with Indian reinsurers such percentage of the sum assured on each policy as may be specified by IRDA. The IRDA has prescribed 15 *per cent* of the sum insured of every policy from 1 April 2007. It was earlier 20 *per cent*. This is called obligatory cession. The Insurance companies draw up reinsurance programmes for various classes of risks in order to fix retention limit of risks commensurate with their financial strength.

IRDA (General Insurance-Reinsurance) Regulations, 2000 govern the reinsurance arrangements. Regulation 3(1) stipulates that the reinsurance programmes of insurance companies should be guided by the following objectives:

- maximise retention within the country,
- develop adequate capacity,
- secure the best possible protection for the reinsurance cost incurred and
- simplify the administration of business.

3.2 Corporate governance

IRDA in its circular of 3 November 2004 to all general insurers advised the introduction of internal procedures necessary to ensure compliance with the guidelines for good corporate governance, with immediate effect.

The guidelines, require the Board of Directors of insurance companies to:

- prescribe clear policies and procedures for implementing the reinsurance strategy, including setting underwriting guidelines, policy terms and conditions, aggregate exposure, establishing limits on the amount to be automatically covered by reinsurance and procedures of acceptance of risk exceeding the automatic capacity,
- fix the retention level, based on well researched recommendations about net retention per risk and per event for each class of business,
- maintain an up to date list of approved reinsurers, which carry the minimum rating together with the approved level of exposure,
- determine the automatic insurance capacity and catastrophe cover along with the workings for the manner in which it was determined,

- be informed of the exposure to the net account, in case of retention of risk at a level higher than permitted by the reinsurance programme,
- accord prior written approval where reinsurance terms are different from the terms of original insurance and obtain reports on the additional exposure arising out of it,
- ensure that there is a management information system in place conforming to the requirement on reporting frequency and level of detail of every claim,
- ensure that there is an adequate internal control system for reporting the claims to the appropriate reinsurer.

The guidelines also emphasised the need for regular audit and examination of claim recovery.

BOX 3.1

Glossary of Reinsurance terms

Facultative means the reinsurance of a part or all of a single policy, in which cession is negotiated separately. The reinsurer and the insurer have the option of accepting or declining each individual submission.

Pool means any joint underwriting operation of insurance or reinsurance in which the participants assume a predetermined and fixed interest in all business underwritten.

Retrocession means the transaction whereby a reinsurer cedes to another insurer or reinsurer all or part of the reinsurance it has previously assumed.

Retention means the amount which an insurer assumes for his own account. In proportional contracts, the retention may be a percentage of the policy limit. In 'Excess of loss' contracts, the retention is an amount of loss.

Treaty means a reinsurance arrangement between the insurer and the reinsurer, usually for one year or longer, which stipulates the technical particulars and financial terms applicable to the reinsurance of some class or classes of business.

Excess of loss (XL) cover This is a reinsurance arrangement to protect a company's net account against claims beyond normal ranges as well as against catastrophe losses.

Probable Maximum Loss (PML) This is an estimation of 'Probable Maximum Loss' that can occur. Reinsurance cessions are done on the basis of the PML to effect savings in reinsurance premium.

Surplus treaty A company cedes those amounts which it cannot or does not want to retain on its net account. Such a contract is known as surplus treaty.

Inward Acceptance When a company participates in the treaty of another insurer, it is called inward acceptance.

GNPI Gross Net Premium Income (GNPI) means gross premium income less reinsurance cessions.

Capacity It refers to insurer's capability to accept the level of risk as proposed in the Reinsurance Programme.

3.3 Audit objectives

The performance audit aimed to assess the performance of the reinsurance programmes and to ascertain that :

- reinsurance programmes of the companies were designed to maximise retention of insurance premium within the country;
- the regulatory framework was complied with;
- the process of selection of brokers and reinsurers was transparent and objective;
- the existing Management Information System was effective; and
- internal audit in relation to reinsurance was regular and adequate.

3.4 Results of Reinsurance Department Operations

The performance of reinsurance operations of the four PSUs for the past three years is given in Table 3.1:

Table 3.1: Performance of reinsurance operations by PSUs

(Rs. in crore)

	Cessions				Acceptances				
YEAR	**Premium**	**Claims**	**Add: Commission**	**Profit/ Loss (-)**	**Premium**	**Claims**	**Less: Commission**	**Profit/ Loss (-)**	**Net Profit/ Loss**
	New India Assurance Company								
2004-05	1522.64	862.08	263.37	-397.19	314.58	98.12	65.61	150.85	**-246.34**
2005-06	1665.02	1659.64	285.94	280.56	332.13	310.56	51.60	-30.03	**250.53**
2006-07	1653.54	1288.81	296.74	-67.99	468.53	155.27	81.00	232.26	**164.27**
	National Insurance Company								
2004-05	1073.88	809.15	214.90	-49.83	95.38	43.92	19.30	32.16	**-17.67**
2005-06	953.62	977.57	174.63	198.58	100.28	54.23	19.30	26.75	**225.33**
2006-07	1024.92	882.10	214.19	71.37	53.15	24.18	13.55	15.42	**86.79**
	United India Insurance Company								
2004-05	871.00	539.00	198.00	-134.00	101.00	40.00	15.00	46.00	**-88.00**
2005-06	991.02	1729.88	197.72	936.58	62.08	51.62	17.31	-6.85	**929.73**
2006-07	1043.39	634.47	214.85	-194.07	74.15	35.29	16.17	22.69	**-171.38**
	Oriental Insurance Company								
2004-05	977.80	602.18	172.20	-203.42	105.26	35.77	28.34	41.15	**-162.27**
2005-06	1190.83	1497.37	199.68	506.22	81.52	47.52	22.58	11.42	**517.64**
2006-07	1247.26	922.85	231.98	-92.43	106.78	61.16	29.56	16.06	**-76.37**

(Details compiled from Annual Accounts of the concerned Reinsurance Departments)

The profits in reinsurance operations arise when recoveries from reinsurers towards claim paid exceed the premiums ceded. Loss in reinsurance indicates that cessions made were more than the loss recovered from the reinsurers.

The operating results of GIC, the national reinsurer, are given in Table 3.2

Table 3.2: Operating results of GIC

(Rs. in crore)

	2004-05	2005-06	2006-07
Gross premium	5121.55	4880.77	7404.17
Net premium	4613.87	4234.88	6420.87
Commission/ brokerage	1207.49	1102.93	1670.12
Operating expenses	40.60	45.33	48.11
Claims, increase in unexpired risks reserve and other outgoes	3942.99	4349.12	4779.78
Operating profit/loss (excluding investment income)	-577.21	-1262.50	-77.14

The increase in loss in 2005-2006 was mainly due to a change in the accounting policy resulting in deferring of revenue of the fourth quarter of the year to the following year.

3.5 Retention of adequate capacity within the country

Table 3.3: Details of total foreign and Indian cessions

(Rs. in crore)

Year/Company→		NIA	NIC	UIIC	OIC
2004-05	Total cessions	1522.64	1073.88	871.00	977.80
	Foreign cessions	216.18	175.37	142.90	294.37
	Indian cessions	1306.46	898.51	728.10	683.43
	Percentage of Indian cessions	85.80	83.67	83.59	69.90
2005-06	Total cessions	1665.02	953.62	991.02	1190.83
	Foreign cessions	233.49	74.42	98.41	384.74
	Indian cessions	1431.53	879.20	892.61	806.09
	Percentage of Indian cessions	85.98	92.20	90.07	67.69
2006-07	Total cessions	1653.54	1024.92	1043.39	1247.26
	Foreign cessions	223.56	3.20	171.27	343.39
	Indian cessions	1429.98	1021.72	872.12	903.87
	Percentage of Indian cessions	86.48	99.69	83.59	72.47

(The figures relating to total cessions are compiled from the books of the Reinsurance department)

Table 3.3 would show that the broad objective of maximum retention within the country has largely been achieved. However, GIC stated that there was further scope to improve retention levels within the country and that its capacity to underwrite and accept risk should be fully utilised by the companies. In NIC, foreign cessions during 2006-07 were abnormally low due to booking of cessions to foreign reinsurers through Indian brokers as Indian cession.

3.6 Reinsurance strategy

IRDA by its circular of 3 November 2004 advised that every insurer should document clear policies and procedures for implementing the reinsurance strategy set by its Board of Directors. However, it was noticed that though the circular was placed before the respective Boards (except NIC), no separate document detailing policies and procedures as envisaged by the circular was prepared by any of the companies.

The companies stated that their annual Reinsurance Programmes were comprehensive documents which were approved by their respective Boards and filed with the IRDA. Reinsurance Programmes were, by nature, dynamic and could be modified depending on market conditions. Such modifications/deviations were authorised by the CMDs of the companies under powers delegated to them by the Boards.

While it is agreed that the annual Reinsurance Programmes were comprehensive, they do not address all the issues mentioned in the IRDA circular of 3 November 2004. Essentially, the IRDA circular contemplates the framing of an over-arching strategic document under which annual Reinsurance Programmes are to be prepared.

3.7 Non-utilisation of capacity of terrorism pool

A market terrorism pool was created with effect from 1 April 2002, to be managed by GIC. All insurance companies in India are members of the pool. The pool commenced with a capacity to cover up to Rs.200 crore which was revised up to Rs.600 crore per location with the pool rate fixed by the Tariff Advisory Committee (TAC)/Pool Manager from time to time. The Tariff Advisory Committee directed (April 2002) that all terrorism risk up to the prescribed limits was required to be underwritten in the country and charged pool rate.

In respect of Mega risks (risks exceeding the pool capacity) separate terrorism risk policies were issued (2004-07) covering the risks beyond the pool capacity by the companies. The rate applied was as per the Reinsurer's quote and the complete reinsurance arrangement was made on facultative basis, outside the country, instead of availing the pool capacity.

The above underwriting of the terrorism risk was not in compliance with the TAC circular and resulted in the non-utilisation of national capacity created. The amount of premium thus not ceded to pool was Rs.6.51 crore (Rs.4.33 crore - NIA, Rs.1.05 crore - UIIC and Rs.1.13 crore - NIC).

UIIC replied (September 2007) that cessions to the pool would not be feasible as the rates obtained from the market were lower than the pool rates. However this reply has to be viewed in the context of TAC's specific directions to underwrite the risks at the pool rate up to the capacity of the pool.

The companies stated that it was not feasible to split the cessions in case of Mega Risks exceeding Rs.600 crore. While Audit's suggestion was noted, the Pool Manager viz. GIC stated that the Underwriting Committee of the pool was seized of the matter and the issue was expected to be soon resolved.

3.8 Facultative placement

Regulation 3(10) of IRDA (General Insurance-Reinsurance) Regulations, 2000 stipulates that every insurer shall offer an opportunity to other Indian insurers including the Indian reinsurer, to participate in its facultative and treaty surpluses before placement of such cessions outside India. It was observed that NIA has a retention capacity of Rs.75 crore, Rs.100 crore and Rs.200 crore in the fire department in 2004-05, 2005-06 and 2006-07, respectively. UIIC, while making facultative cessions in respect of 11 policies, did not consider the retention capacity of NIA. This resulted in underutilisation of capacity and consequent outgo of facultative premium of Rs.8.45 crore, in respect of 11 policies test checked in audit.

While the companies (NIC, UIIC and OIC) expressed certain difficulties in obtaining inter-company facultative reinsurance support, it would be desirable to address this issue in Inter-Company meetings. This would facilitate achieving the objective of maximising retention of premium within the country.

3.9 Delay in collection of Reinsurance Premium in GIC

Premia in respect of inward treaties were to be collected quarterly or half-yearly according to the terms of treaties. During the period 2004-07, it was noticed there were delays in collecting reinsurance premia in GIC with respect to both proportional and non-proportional treaties. Details are in Table 3.4.

Table 3.4: Delay in receipt of premium

Description	Non-proportional	Proportional
Number of treaties where delay was noticed	219	51
Amount of premium delayed (Rs. in crore)	19.84	14.62
Period of delay		
Upto 30 days	77	71
31 - 90 days	264	93
91 - 180 days	147	49
181 - 365 days	58	29
Above 365 days	5	Nil
Total number of Instances	**551**	**242**

The delayed receipt of premium affected the cash flow of the company.

While agreeing that there had been delays in receipt of premium in some acceptances, GIC stated that it had recently activated a Credit Control Department to follow up on such recoveries.

3.10 Delay in receipt of adjustment premium

GIC accepts non proportional treaties from Indian insurance companies collecting Minimum Deposit Premium (MDP) based on the Estimated Gross Net Premium Income (EGNPI) indicated in the Treaty. As soon as practicable after the expiration of the treaty agreement, the reinsured (insurance companies) render a statement of their actual Gross Net Premium Income to GIC. It was however, seen that receipt of adjustment premium of Rs.93 lakh was delayed as detailed in Table 3.5.

Table 3.5: Delay in receipt of adjustment premium

(Rs. in crore)

No of cases delayed					
No of treaties	**Upto 90 days**	**91 to 180 days**	**181 to 365 days**	**Total**	**Amount**
12 out of 24 treaties checked	5	8	5	**18**	0.83
7 out of 28 treaties checked	3	3	2	**8**	0.10
Total				**26**	**0.93**

GIC stated that it would control such delays in future through its Credit Control Department.

3.11 Additional exposure due to difference in terms of reinsurance

In terms of the IRDA guidelines on good corporate governance, Reinsurance departments will not have the authority to increase the net retention of the insurer either through failure to place reinsurance or through placement of reinsurance on terms different from terms of original risk, without prior approval of the Board.

UIIC issued 10 policies and accepted co-insurance share in respect of six policies on terms which were at variance with the terms agreed with the reinsurers. This involved an additional exposure of Rs.511.66 crore to the company during 2004-07. This additional exposure arose due to difference in deductibles as per the terms of the reinsurance and terms of insurance policy.

In one specific case (Tata Motors) it was noticed that the company's share of the claim was Rs.58.46 crore and only an amount of Rs.24.02 crore was recoverable from reinsurers. The balance of Rs.34.44 crore was borne by the company. This exceeded the per loss limit of Rs.15 crore as per Reinsurance Programme.

Similarly in OIC, 39 reinsurance policies were issued during the period 2004-07 on terms which were at variance with the terms agreed with the reinsurers. This resulted in an additional exposure of Rs.303.31 crore to the company.

While the cases were subsequently brought before the Board for ratification, no prior approval was taken as contemplated in the IRDA guidelines. Moreover, it was noticed that only the individual cases involving additional risk exposure were being brought before the Boards for ratification. The overall, cumulative exposure arising out of such cases needs to be placed before the respective Boards to facilitate a complete and proper appreciation of risk exposure of the companies.

The companies stated that owing to competition in the market, some risks needed to be underwritten on terms which were different from the original terms agreed with the reinsurers. Owing to the spreading of risk, it was unlikely that total additional net exposure would be affected by any single accident/event. In all such cases, approval of the respective Boards was being obtained. However, these replies do not address the issue raised by Audit, i.e. the overall, cumulative exposure arising out of all such cases should be placed before the respective Boards to facilitate a comprehensive appreciation of risk exposure.

3.12 Cessions based on Probable Maximum Loss

Probable Maximum Loss (PML) will always be lower than the sum insured. In 500 out of 1653 cessions in UIIC during the period 2004-07, Probable Maximum Loss was higher than the sum insured for individual small policies. The company had made cessions in respect of those policies based on PML. As the maximum loss in those policies would not exceed the sum insured, the adoption of PML for making cessions was inappropriate. This resulted in excess cession of premium amounting to Rs.3.32 crore in Fire Department.

UIIC stated (September 2007) that there had been an error. The company was attempting to have a system in place for underwriting such policies and cessions thereon, so that such errors did not recur in future.

Similarly in 183 out of 1653 cessions reviewed in audit, UIIC adopted the entire PML instead of only their share of PML for making cessions. This resulted in additional exposure to the Company’s account. UIIC agreed (October 2007) that, in future, risks would be classified appropriately based on their share of the risk.

3.13 Empanelment of brokers

The Government of India, Ministry of Finance in its circular of September 2002 to insurance companies on corporate governance had instructed that there should be a credible system of empanelment of brokers. It was further stated that managements should develop detailed guidelines for empanelment and usage of these intermediaries. These guidelines were to be submitted to the respective Boards for approval.

However, the companies did not develop detailed guidelines for empanelment of brokers. It was noticed that UIIC and NIA approached certain brokers for obtaining quotes from reinsurers merely indicating the geographical area from which they had to obtain quotes. In UIIC, three brokers obtained 45 and 51 *per cent* of the total business placed through brokers in 2005-06 and 2006-07, respectively. UIIC stated (September 2007) that the audit observations were duly taken note of and that the utilisation of intermediaries was being progressively broad-based, to the extent possible.

In NIC, it was noticed that an amount of Rs.5.23 crore was ceded to certain reinsurers through brokers even though the company was also directly placing business with the same reinsurers.

The companies responded that they were following specific criteria while selecting brokers including reputation in the international reinsurance market, past experience of the companies with the brokers, advice on Reinsurance Programmes, etc. However, the intention of the Ministry's circular of September 2002 is that the companies should develop detailed guidelines which should underpin a credible system of empanelment of brokers. These guidelines are also required to be approved by the respective Boards.

3.14 Rates of reinsurance commission on outward cession

In terms of the Government of India, Ministry of Finance Circular dated 18 September 2002, in the absence of any policy guidelines from the Board, companies were not to resort to reducing commission receivable on reinsurance ceded, thereby reducing quotations to client. Reinsurance commission was meant to take care of the cost of procurement, cost of funding claims till recovery was made from the reinsurers and to account for any non-recovery in the event of their going insolvent. The companies were advised not to reduce reinsurance commission indiscriminately. A proper policy was to be framed by each company and any deviation was to be made only by Chairman cum Managing Director on basis of a reasoned order. A summary of such decisions would be reported to Board immediately.

However it was noticed that the companies had not developed policies as contemplated in the circular of Ministry of Finance except OIC. As had been agreed earlier (March 2002) by the General Insurers' (Public Sector) Association (GIPSA), a minimum percentage of 10 would be collected as reinsurance commission. OIC, had however stipulated a range of 5 to 20 *per cent* commission for different classes of business.

It was noticed that, during the period 2004-07, the four companies collected commission at rates less than 10 *per cent*/rates approved by the company. This resulted in foregoing income of Rs.29.34 crore as detailed in Table 3.6.

Table 3.6: Income foregone

(Rs. in crore)

Company	No. of cessions	Income foregone
NIA	84	14.38
NIC	22	1.90
UIIC	441	10.76
OIC	36	2.30
Total	**583**	**29.34**

Out of the 583 cessions mentioned in Table 3.6, no commission was collected in 206 cessions.

In reply, the companies (NIC, UIIC and OIC) stated that such deviations from the agreed rate of 10 *per cent* were necessitated by the competitive environment. OIC periodically reports such deviations to its Board. It is suggested that the other companies could consider reporting such deviations to their respective Boards.

3.15 Placement of business with reinsurers

Regulation 3(7) of IRDA (General Insurance- Reinsurance) Regulations, 2000 stipulates that insurers have to place business only with those reinsurers enjoying, for at least five years, a credit rating of at least BBB (Standard & Poor) or equivalent rating of any other international rating agency.

A review of selected treaties in the five general insurance companies during the period 2004-07 revealed the following:

(a) In UIIC, an amount of Rs.7.91 crore during 2005-06 and Rs.9.96 crore during 2006-07 was ceded to five reinsurers with rating below ‘BBB’. The company replied (August/September 2007) that they had business relationships on reciprocal basis with some of the insurers for a long period of time even before constitution of IRDA. However, this was not acceptable since it was in violation of the IRDA’s Regulations.

(b) In GIC, during 2004 and 2005, two reinsurers and during 2006, three reinsurers with rating below ‘BBB’ were given business. In respect of 21, 48 and 46 reinsurers in 2004, 2005 and 2006, respectively, even data about the ratings was not maintained by GIC, indicating that the information system requires to be strengthened.

(c) In OIC, during the period 2004-07, reinsurance business was placed with five companies with credit rating lower than ‘BBB’.

The companies stated that the reinsurers with whom they had placed such business were the ones with whom they either had reciprocal arrangements or were backed by sovereign guarantees or may not have been rated. However, these placements need to be viewed in the light of the specific regulatory requirement that reinsurers need to have a minimum of 'BBB' (Standard & Poor) or equivalent rating of any other international credit rating agency. If required, the companies should approach IRDA for a special dispensation.

3.16 Information flow from the regional offices

Regional Underwriting Cell (RUC) reports sent by the regional offices of companies list the details of large and medium risk undertaken to the Reinsurance department at Head Office for making cessions. Delays were noticed in furnishing such information as indicated in Table 3.7.

Table 3.7: Details of delays

Delay range	No. of instances		
	NIA	**NIC**	**UIIC**
30 to 60 days	12	52	265
61 to 90 days	2	5	177
91 to 180 days	3	3	66
181 to 365 days	1	-	2
>365 days	3	-	-
Total	**21**	**60**	**510**

Due to delay in receipt of information the companies could not arrange required reinsurance or initiate recoveries from the reinsurers. Some illustrative cases are discussed below:

(a) The divisional office III, MRO-II of NIA accepted co-insurance of an erection risk underwritten by Maharashtra State Insurance Fund (MSIF). The cover was for a period of five years from April 2000 to March 2005 and the premium was to be received in 19 instalments. The division received 11 instalments and did not intimate the fact of acceptance of risk to the reinsurance department. Consequently no reinsurance arrangement was made. The non-receipt of the balance instalments was not taken up with MSIF. MSIF extended the period of cover from April 2005 to March 2007. The remaining eight instalments were paid by MSIF in January 2006 and the premium for the extended period only in May 2007. A major claim with NIA's share Rs.36.48 crore had occurred in June 2005. As there was no reinsurance arrangement the company passed on the claim to the Inter company Group Treaty (IGT) for Rs.22.24 crore and borne the balance amount of Rs.14.24 crore. The failure of the divisional office to inform the reinsurance department of the acceptance of the risk resulted in burdening the IGT with a claim without prior concurrence of the participating insurers.

(b) In OIC, it was found that there were 28 and 85 policies during 2005-06 and 2006-07, respectively that had not been placed with reinsurers. In terms of the reinsurance programme applicable for the respective years, reinsurance protection should have been made for Rs.1262.93 crore. The company made delayed cessions in respect of 85 policies for Rs.1052.47 crore resulting in additional exposure during 2006-07. Of these, in respect of 25 polices the company had to retain these risks to its account as facultative support could not be arranged at such a late stage. This resulted in additional exposure amounted to Rs. 210.46 crore for 2005-06.

(c) In UIIC, during the year 2006-07, recoveries were not raised by Reinsurance department in respect of nine accidents, amounting to Rs.54.65 lakh as these were not reported by Operating offices to Reinsurance department. UIIC stated (July 2007) that they were taking up the recoveries for the above cases and recoveries would be effected in 2007-08.

(d) It was also noticed that the Namakkal Divisional office of NIC during 2004-05 did not intimate the RI department about large claims (two accidents) of Rs.1.08 crore for effecting prompt recovery from the reinsurers.

(e) In UIIC, during 2006-07 it was found that in respect of two policies (Miscellaneous department) cessions were made automatically by Integrated Reinsurance System (in-house software used in Reinsurance department). This resulted in retention of Rs.25 crore, against the permissible retention of Rs. Seven crore under the reinsurance programme for the year. UIIC stated (August 2007) that there had been an inadvertent error and corrections would be made during the current year.

The companies stated that the delays would be overcome once CORE Insurance Solutions/INLIAS are in place.

3.17 Recoverables from reinsurers

It was noticed that UIIC and OIC had large amounts recoverable from the reinsurers at the close of the financial years 2004-2005 to 2006-2007. The amounts outstanding were Rs.225.80 crore, Rs.1428.39 crore and Rs.140.73 crore in UIIC and Rs.245.43 crore, Rs.401.33 crore and Rs.580.31 crore in OIC for the year 2004-05, 2005-06 and 2006-07, respectively. The amounts recoverable from reinsurers were Rs.924.17 crore in GIC, Rs.1489.63 crore in NIA, and Rs.118.95 crore in NIC as on 31 March 2007.

In UIIC, it was noticed that of the amount outstanding as on 31 March 2007 an amount of Rs.22.92 crore was recoverable from 25 reinsurers who had gone into liquidation. Similarly, in respect of OIC, an amount of Rs.42.91 crore remained un-recovered for over six years. It was also noted in OIC that Rs.1.44 crore was due to be received from the reinsurers who had gone into liquidation.

In NIA, the recovery from foreign Facultative Reinsurance was pending for more than three years to the extent of Rs.4.64 crore (Engineering Department) and Rs.1.67 crore (Miscellaneous Department).

The companies (GIC, UIIC and OIC) replied that steps were being taken to recover the amounts due.

3.19 Settlement of balances and rendering of accounts

In NIC, the outstanding claims as per Marine Hull Register maintained at Reinsurance department was Rs.131.36 crore and as per balance sheet it was Rs.37.33 crore as on 31 March 2007. This amount has not been reconciled

NIC stated that the reconciliation would be carried out.

3.20 Internal audit

Internal Audit of the Reinsurance departments would normally cover key aspects of the implementation of the reinsurance strategy. These would include examining whether cessions were made as per the approved Reinsurance programme; whether all risks were covered in time and whether recoveries in respect of each treaty were effected as per the cessions made. Internal audit would also examine terms and conditions of all treaties (Inward, Outward, Facultative and Excess of Loss) and review whether these were communicated by the treaties department to the accounts department in time. Internal audit would also review the efficacy of systems and procedures in place. These areas have been outlined in the Internal Audit Manual of UIIC. Internal audit, in the other companies would also need to review these aspects.

It was noticed that during the period 2004-05 to 2006-07, internal audit of Reinsurance departments was not conducted in UIIC and OIC. In NIA and NIC, the internal audit was completed up to 2006-07. In GIC, the internal audit work has been outsourced from 2006-07 onwards. Given the nature and significance of reinsurance transactions, it is essential that regular and effective internal audit be undertaken. The need for regular internal audit had also been emphasised in IRDA's circular of November 2004 on corporate governance.

OIC stated that internal audit was programmed for the Reinsurance Department for the year 2007-08.

Recommendation No.2

The companies should:

(i) ***develop an over-arching strategic document, outlining policies and procedures under which annual Reinsurance Programmes should be framed, as required by IRDA guidelines on Corporate Governance;***

(ii) ***bring before the Boards of the companies the deviations from reinsurance programmes along with details of cumulative risk exposure for approval;***

(iii) ***institute a transparent system for empanelment and selection of brokers as required by the Ministry of Finance circular of September 2002;***

(iv) ***strengthen measures to build up appropriate data on ratings of reinsurers as well as ensure adherence to IRDA stipulations on ratings of reinsurers; and***

(v) ***strengthen internal control measures to monitor recoverables from reinsurers and timely flow of information from regional offices to the Reinsurance department.***