

IRDAI on Arbitration Clauses in Insurance Policies

October 2023

Overview

On 27 October 2023, the Insurance Regulatory & Development Authority of India (**IRDAI**) issued a circular on arbitration clauses in insurance policies (**Arbitration Circular**). The Arbitration Circular provides an "arbitration clause" for commercial lines of business replacing the existing arbitration clauses in those policies with a new clause: *"The parties to the contract may mutually agree and enter into a separate Arbitration Agreement to settle any and all disputes in relation to this policy. Arbitration shall be conducted under and in accordance with the provisions of the Arbitration and Conciliation Act, 1996."*

In essence, this new clause states the default position in law, which is that parties *may* mutually agree and enter into a separate arbitration agreement to settle disputes arising from a policy. The Arbitration Circular has been issued with reference to certain proceedings before the Supreme Court of India.

Supreme Court Proceedings

A brief background will put things in context. On 9 January 2023, in a case (*National Insurance v Nippon Paper SLP (C) 224-226/2023*; pending as of date) the Supreme Court of India expressed concerns over the limited scope of the arbitration clauses in many insurance policies and asked the IRDAI to indicate *"the reason why only the quantum of dispute has been made arbitrable, whereas repudiation of the Policy or denial of the claim per-se is made non-arbitrable."* It appears that the IRDAI had submitted some response to the Supreme Court because, as a follow up, on 5 April 2023, the Supreme Court sought an *additional* response from the IRDAI since the bifurcation of subject matters between quantum and liability for arbitration purposes *"... invariably leads to confusion, multiple litigation, piecemeal decision and chances of conflicting orders."* No further orders of note have been passed in the Supreme Court proceedings since then.

Arbitration Circular

While the case is yet to see a final decision, the Supreme Court's concerns seem to have prompted the IRDAI to carry out consultations with stakeholders and issue the Arbitration Circular to all general insurers. The IRDAI has recognised in the Arbitration Circular that the existing arbitration clauses are *"limited in scope and need to be amended"* (the obvious reference being to those arbitration clauses which limited the arbitration between an insurer and insured to issues of *quantum*, liability being otherwise admitted – popularly called quantum-only arbitration clauses). We had written on these types of clauses in an article published by Chambers last year, a link to which can be accessed [here](#).

The IRDAI has issued the Arbitration Circular in exercise of its powers under Section 14(2)(i) of the IRDAI Act 1999, which gives the IRDAI the power to control and regulate "*the rates, advantages, terms and conditions that may be offered by insurers in respect of general insurance business*" to the extent that it is not controlled/regulated by the Tariff Advisory Committee (which effectively is all of the general insurance as on date, as the TAC has been dismantled). Arbitration clauses in policies have been considered by the IRDAI to be "terms and conditions", justifying the invocation of the IRDAI's powers.

The effect of the Arbitration Circular is thus:

- Arbitration clauses in retail policies are deemed to be deleted.
- For commercial lines of business, the arbitration clauses in them stands replaced with the new clause (extracted in the opening paragraph of this note).
- As a transitory means, the new clause is deemed to be incorporated in all commercial insurance policies issued on or after 27 October 2023, i.e., the date of the Arbitration Circular. For existing policies issued until 26 October 2023, the existing arbitration provisions will remain valid until the expiry of the policies and, from the date of renewal on or after the date of the Arbitration Circular, the new clause would be deemed to have replaced them.
- Insurers need to (i) notify policyholders; and (ii) amend the arbitration provisions of the policies accordingly.

Our view on the impact of the Arbitration Circular

The new clause may not be a significant issue for retail policies as retail customers would likely approach consumer forums for resolution of their disputes. That said, a wholesale deletion of arbitration clauses from retail policies is questionable and, perhaps, the IRDAI could have considered whether the sum insured in question should have had some bearing on this decision. Furthermore, with the enactment of the Mediation Act 2023, the IRDAI could also have considered whether a mediation provision (even if exercisable at the behest of the insured) would have been preferable as an alternative.

Turning now to the commercial lines policies, the new clause is *not* an "arbitration clause", despite the IRDAI giving it that title. It is a clause which stipulates that parties may mutually agree and enter into a separate arbitration agreement. Courts have considered an "arbitration clause" and an "arbitration agreement" (as defined under Section 7 of the Arbitration and Conciliation Act 1996) as one and the same. Therefore, inherently, there is some scope for confusion as to whether the new clause being inserted now is an "arbitration agreement". This may, in the future, become a subject of some debate before courts in applications made under Section 11 of the Arbitration and Conciliation Act 1996 for appointment of an arbitrator. Further, a practical issue that the IRDAI should have considered is that even in commercial lines insurance policies, it is mostly the case that the insurers issue policies to millions of insureds (each of which is a separate contract of insurance), and it may be impractical for insurers to mutually agree a separate arbitration agreement in each of those with the insureds.

The elimination of existing clauses means that, on or after the date of the Arbitration Circular, the restricted quantum-only arbitration clauses also cease to exist in commercial lines policies. In the void left by this deletion, the clause prescribed by the IRDAI is inserted, which states that parties may "*mutually agree to enter into a separate agreement to settle any and all disputes in relation to this policy*". Therefore, despite the confusion with the usage of the words "arbitration clause" and "separate arbitration agreement" as discussed above, the IRDAI's overall intent appears to be to clear the decks by directing a wholesale deletion of the old quantum-only arbitration clauses, and at the same time, preserving party autonomy by leaving parties to agree the wording of an arbitration agreement with respect to "*any and all disputes*" (as opposed to quantum-only, which was the clause prevalent earlier). This may have been to address the

overhang of the old clauses, which almost created an impression that issues of liability/admissibility under insurance policies cannot be arbitrated as a matter of some rule or law. With the Arbitration Circular, that notion is dispelled, as IRDAI has specifically inserted the words to the effect that an insured and insurer can "*enter into a separate agreement to settle any and all disputes*", i.e., including disputes as to liability.

Guidance for Insurers

Since the Supreme Court matter is pending, it is possible that the Court issues further directions to the IRDAI as and when the Arbitration Circular is brought to its notice.

For now, however, in light of the Arbitration Circular, Insurers must inform the Policyholders of it while issuing a fresh policy or during renewals. The information would be on the lines that existing arbitration provisions are replaced with the arbitration provision in the Arbitration Circular. For retail lines, the information would be that any arbitration clause in the policy should be deemed to have been deleted.

Next, each insurer must consider whether it intends to incorporate an arbitration provision in its commercial lines policies. As discussed above, this decision may be a difficult one if it had to be seen in the context of agreeing with each particular insured for each particular policy, but perhaps may be an easier one if each insurer considers this for a particular line of business. If an insurer intends to agree upon an arbitration provision, it would be ideal for it to have a model clause that it can propose for agreement with the insured. This should also factor in whether the insurer would like to have an ad hoc or institutional arbitration provision.

A typical model clause for an ad hoc arbitration is set out below to provide a flavour of what such a provision would look like:

"This arbitration agreement is being entered into between parties pursuant to the Insurance Regulatory and Development Authority of India's circular dated 27 October 2023 (IRDAI/NL/CIR/MISC/188/10/2023) whereby parties agree as follows.

Any dispute, controversy, difference or claim arising out of, relating to, or concerned with, this policy, including its existence, validity, interpretation, performance, breach, termination or avoidance thereof shall be referred to and finally resolved by arbitration under the Arbitration & Conciliation Act 1996 (as amended from time to time). The parties agree to the decision of a sole arbitrator to be appointed in writing by the parties hereto or if they cannot agree upon a single arbitrator within 30 days of any party invoking arbitration, the same shall be referred to a panel of three arbitrators, comprising of two arbitrators, one to be appointed by each of the parties to the dispute and the third arbitrator to be appointed by such two arbitrators. The arbitration shall be conducted under and in accordance with the provisions of the Indian Arbitration and Conciliation Act 1996. The parties further agree that:

- 1. The seat of arbitration shall be the place of the policy-issuing office of the Insurer;*
- 2. The award rendered shall be final and binding on both the parties;*
- 3. The arbitration proceedings shall be conducted in English;*
- 4. The parties shall bear costs of the arbitration in equal proportion until any arbitral award states otherwise."*

Please note, however, that the above clause is only a sample for convenience and that any tweaks required to it by any insurer for any particular line of business, those can be considered by the insurer as well.