## Contractual Savings

### Public Provident Funds (PPF) and Small savings

4.39 Interest rate liberalisation involving dismantling of administered rates of interest has increased the sensitivity of the link between inflation and interest rates. This implies that this link is now closely tracked by both savers and borrowers/investors. Recent trends in real interest rates (nominal interest rates minus inflation rate) on contractual savings like Public Provident Funds, small savings, etc. *vis-à-vis* interest rates on deposits of more than one year maturity with major public sector banks assume relevance in relation to the need for moving to a low interest rate regime (Table 4.8). In fact, the recent reduction by one percentage point in the administered interest rates on Public Provident Funds and Small Savings may be seen in the context of the recent trends in real interest rate.

**TABLE 4.8**

**Trends in Real Interest Rates**

*(% per annum)*

| Real Interest Rate as on | PPF& NSC (VIII) | NSS 1992 & PODs (5years) | Bank Deposits (more than one year) |
|---|---|---|---|
| 3-4-99 | 5.1 | 4.6 | 2.4 |
| 3-7-99 | 6.0 | 5.5 | 3.2 |
| 2-10-99 | 7.5 | 7.0 | 4.8 |
| 18-12-99 | 8.5 | 8.0 | 5.8 |

**Note : Real interest rates shown in this Table have been worked out by subtracting the 52-week average (WPI) inflation rate from the respective nominal interest rates, viz. 12 % for PPF and NSC(VIII), 11.50 % for NSS 1992 and Post Office Deposits (PODs) for 5 years ,and 9.25 %(average of the range of 8.00-10.50%) for Deposits with major public sector banks.**

### Insurance Reforms

4.40 The most notable development pertaining to contractual savings in the current financial year has been the passing by Parliament of the Insurance Regulatory and Development Authority (IRDA) Bill. The IRDA Act (Box 4.4) marks the end of monopoly of the Government in the insurance sector because it seeks to promote the private sector (including limited foreign equity) in the insurance sector. It, however, gives priority in the utilisation of policy holders' funds for the development of social and infrastructure sectors.

**BOX 4.4**

**Salient Features of the Insurance Regulatory and Development Authority Act (IRDAA), 1999**

- The insurance sector in India has been thrown open to the private sector. The second and third schedules of the Act provide for removal of exclusive privilege of existing corporations/companies to do life and general insurance business.
- An Indian insurance company is a company registered under the Companies Act, 1956 in which foreign equity does not exceed 26 percent of the total equity shareholding, including the equity shareholding of Non-Resident Indians (NRIs), Foreign Institutional Investors (FIIs) and Overseas Corporate Bodies (OCBs).
- After the commencement of an insurance company, the Indian promoters can hold more than 26 percent of the total equity holding for a period of ten years, the balance shares being held by non-promoter Indian share holders which will not include equity of the foreign promoters, and share holding of FIIs, NRIs and OCBs.
- After the permissible period of ten years, excess equity above the prescribed level of 26 percent will be disinvested as per a phased programme to be indicated by IRDA. The Central Government is empowered to extend the period of ten years in individual cases and also to provide for higher ceiling on share holding of Indian promoters in excess of which disinvestment will be required.
- On foreign promoters, the maximum of 26 percent will always be operational. They will, thus, be unable to hold any equity beyond this ceiling at any stage.
- The Act gives statutory status for the Interim Insurance Regulatory Authority (IRA) set up by the Central Government through Resolution in January 1996.
- All the powers presently being exercised under the Insurance Act, 1938 by the Controller of Insurance (COI) will be transferred to the Insurance Regulatory and Development Authority (IRDA).
- The IRDA Act also provides for the appointment of COI by the Central Government when the Regulatory Authority is superseded.
- The minimum amount of paid-up equity capital is Rs. 100 crore in case of life insurance as well as general insurance and Rs. 200 crore in case of re-insurance.
- Solvency margin (excess of assets over liabilities) is fixed at not less than Rs. 50 crore for life as well as general insurers; for reinsurance solvency margin stipulated at not less than Rs. 100 crore in each case.
- Insurance companies will deposit Rs. 10 crore as security deposit before starting their business.
- In the non-life sector, IRDA would give preference to companies providing health insurance.
- Safeguards for policy holders' funds include specific provision prohibiting investment of policy holders funds' outside India and provision for investment of funds in accordance with policy directions of the IRDA, including social and infrastructure investments.
- Every insurer shall provide life insurance or general insurance policies (including insurance for crops) to the persons residing in the rural sector, workers in the unorganised or informal sector or for economically vulnerable or backward classes of the society and other categories of persons as may be specified by regulations made by IRDA.
- Failure to fulfill the social obligations would attract a fine of Rs. 25 lakh; in case the obligations are still not fulfilled, license would be cancelled.