LAPSATION OF POLICY: A THREAT OR CURSE FOR LIFE INSURANCE INDUSTRY

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ABSTRACT

Life Insurance is a key driver for the economic growth of any nation. It is one of the important ingredients of the economic development of the country. Life Insurance selling often termed as dream selling or concept selling. Under the contract of life insurance the policy holder does not receive any physical product. All the benefits of life insurance will be derived at the latter stages of life such as long term return, retirement benefits etc. Hence the prospective policy holder takes some time while investing.

In today’s context, the orientation of every business is transformed from product concept to the customer concept. All the strategies are lying around the customer only. Thus each and every organization is aiming to capture the larger market share. It had been shown by the annual reports of IRDA that the Life insurance companies in the process of acquiring the new customer had losing major portion of the first year premium they collected every year towards the Lapsation of the policies. This is going to be the warning bell in the country like India where the insurance penetration is quite low. Thus in this paper an attempt has been made to find out the cause and effects relationship of the Lapsation of policy.

KEYWORDS: Life Insurance, Dream Selling, Policy Holder, Physical Product, Lapsation.

Introduction:

Life insurance has today become a primary component of any market economy as it provides a wide scope for collecting larger revenue for a longer period. Life insurance is a long term contract between the policy holder and the insurer, where the insurer agrees to reimburse on the occurrence of incident such as individual's death or other event such as terminal illness or critical illness of the insured. The insured agrees to pay the cost in terms of insurance premium for the service.

The awareness level of the customers had been increased rapidly which had forced companies to provide better services at lower cost. It is often said that customer is the king of the market. He is the person towards whom all the marketing activities and strategies are directed.

Life insurance companies can boost it sales by two ways –

- Attracting the prospective policy holders.
- Retaining the existing policy holder and propelling them for the frequent purchase which is termed as cross sales.
Today the competition in life insurance industry is threatening due to the entry of private players. So service quality becomes a basic component for the survival of any service company. In December 1999 the insurance sector was opened for the private players by passing insurance regulatory development authority in the parliament. Initially private sector companies were allowed to work in India with maximum 26% share foreign partners. In October 2012 the government had approved direct foreign investment in insurance sector up to 49%. The increased foreign direct investments will results in the greater exposure and penetration in the life insurance industry.

Objectives of the Study:
1. To know the meaning of Lapsation of policy.
2. To identify the causes of policy Lapsation.
3. To find out the impact of policy Lapsation with respect to Policy Holder, Insurance Company etc.

Research Methodology: -
The research article is based upon descriptive as well as exploratory research. Secondary sources of data collection have been adopted for the study. The relevant and required data are collected from the national and international articles on life insurance, as well as annual reports of LIC etc.

Meaning of Lapsation: -
Lapsation refers to the situation when the customer fails to pay the premium on his policy within the timeframe plus the grace period allowed by the company. It is often termed as persistency.

Causes of Policy Lapsation: -
Policy Lapsation means the termination of the life insurance contract by the default on the ground of non payment of life insurance premium by the policyholder within the stipulated time frame. There are various reasons for the policy Lapsation which are elaborated as below:-

Wrong Commitment and Malpractices:- As per the annul report of Insurance Regulatory Development Authority of India it had been found the majority of the policies had been lapsed due to the wrong commitment and malpractices on the part of the various channels of the distribution of life insurance policy. The attractive commission and incentive schemes offered by the life insurance companies had propelled the advisors to use such an unfair means which had ultimately affected on the Lapsation of policy. As per the IRDA report around 34 % complaints had been registered for using malpractices for Lapsation of life insurance policies.

Financial Burden: - Inadequate money on the due date of the premium payment is the basic root cause of the policy Lapsation. The policyholder at the initial stage pays premium but latter on the mindset changes and the financial situation if hampered he fails to pay the premium which leads in policy Lapsation.

Service Quality: - Service quality is a key ingredient in the success of the every organization. Life insurance is a long term contract which totally depends on the trust and faith. The
policyholder while taking the life insurance policy does not have complete knowledge of the products and the life insurance company. He totally relies on the knowledge and expertise of the advisor. Thus it is expected from the advisors to provide better services which will help surely reduce the Lapsation rate. But it does not happen. It had been found that the life insurance advisors for the sake of their own benefit do not provide the better service. Life insurance companies are giving lucrative commission in the first year up to 25%. The renewal commission from second year onwards is somewhat low i.e. 5 to 7%. Thus the advisors concentrate on the fresh customer rather than servicing older one.

Adverse effect of the Unit Linked Insurance Plans: - Unit linked plans are the combinations of investment and insurance cover plan. It provides the dual benefit of providing the long term return on investment and life cover. The government of India had issued guidelines on Ulips in the year 2005. The private players had launched various Ulips plan to collect large revenue. The basic reason for the adverse effect is lying in the lock in period. Initially it had been portrayed that ulip is an investment tool which provide quick returns on the investments. The initial charges in ulips are ranging from around 60% of the first year premium which automatically reduces the fund value of the policyholders. Thus it takes around 4 years to have break even point. But after considering the lower fund value in initial stage the policyholder lapse the policy.

Processing of the Insurance Proposal: - Product differentiation, mode differentiations are the main sub causes for the Lapsation of policy. It had been found that there are various alterations in the proposal form at the time of processing such as changing the product which provides more commission, changing terms. Thus ultimately it hampers the customers and results in Lapsation of policy.

Grievances and Claim Settlement: - Providing the death claim should be the core object of any traditional plans. It is why the policyholder takes a life insurance plan. Thus it is expected from the life insurance companies to settle the claims and grievance as early as possible.

Impact of Policy Lapsation: -

Policies Lapsation does have adverse effects on the life insurance company and the policyholder.

Effects on the Insurance Company:

Decrease of Public Image: - The insurance is a concept selling. Thus the companies takes due care to increase the reputation and goodwill of the company. Reputation is what through which the company can acquire the prospective policyholders. Lapsation of policy reduces the image of the company and spread negative feedback in the market which hampers the future market share.

Adverse effect on the liquidity position: - life insurance is a long term agreement hence it is expected that the policyholder should with the company for at least 15 to 20 years depending upon the tenure of the policy. But if any policyholder lapses his policy the life insurance company is benefited in the short run as it has to pay only the surrender value which is lower than the premium paid but still the life insurance companies have to make provision of funds for
the repayment of survival benefit. It is the loss of the insurance companies as it can’t invest the total fund in the long term investment tools.

**High level of initial cost:** - The insurance plans having high level of initial cost. Hence the insurance companies try to recoup this cost as early as possible. If the policy had been lapsed at initial level the companies have to incur heavy expenditure, which in turns affects the overall profitability of the company.

**Effects on the Policy Holder:** -
Policy holder is the person who is the main victim of the Policy Lapsation. It terminates the basic life cover of the policy holder.

**Ceases Life Cover:** - Due to the non-payment of the premium on the due date, the life cover of the policy holder ceases. The insurance company terminates the life cover of the sum assured till the policy has been reinstated. This is going to be the biggest loss for the policyholder. In case of the unfortunate demise of the policyholder the life insurance company will refuse to pay the claim and the ultimate aim of the policy will be in vain.

**Financial Loss:** - The insurance company does not pay a single rupee unless the policy had acquired the surrender value. The surrender value is paid only when the policy had completed at least three years or depending upon the policy terms agreed upon. Thus it is going to be loss of the hard earned money of the policyholder.

**Conclusion**
On the basis of the above we can say that the Lapsation though is beneficial to the insurance company in the short run it do have an adverse effect on the long term objective of stable growth and increased market share. Persistency decreases the public image of the company. Further we can conclude that the basic reason for the default is lying in the malpractices and using unfair trade practices by the advisors. IRDA had issued various guidelines to overcome the Lapsation such as the agent will have to maintain at least 50 % of the policy sold in the first year should be renewed otherwise the license of the advisor will be terminated.

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