



**Insurance Regulatory and Development Authority of India
Survey No.115/1, Financial District, Nanakramguda,
HYDERABAD 500 032.**

IRDAI/NL/GDL/SIC/01/01/2022

3rd January, 2022

To

The Chairman-cum- Managing Directors/Chief Executive Officers of
General Insurance Companies (except ECGC Ltd and AIC Ltd)

Madam/Sir,

IRDAI (Surety Insurance Contracts) Guidelines, 2022

The Authority, considering the specific nature of Surety Insurance owing to the unique risk and features of the products, hereby issues the following guidelines to regulate and develop Surety Insurance business.

The guidelines shall come into force with effect from 1st April, 2022. The guidelines have been placed on the IRDAI website (<https://www.irdai.gov.in>).

Yours faithfully,

Chief General Manager (Non-Life)

IRDAI (Surety Insurance Contracts) Guidelines, 2022

1. Introduction

The Insurance Regulatory and Development Authority of India (“the Authority”), having considered it necessary to promote and regulate sustainable and healthy development of Surety Insurance Business, in exercise of the powers conferred under section 14 (2) (i) of IRDA Act, 1999, hereby issues the following guidelines.

2. Short title, commencement

2.1 These guidelines shall be called the “IRDAI (Surety Insurance Contracts) Guidelines, 2022.”

2.2 These guidelines shall come into force with effect from 1st April, 2022.

3. Applicability

3.1 All Insurers registered under the Insurance Act, 1938, to transact the business of general insurance may transact the business of Surety Insurance, subject to compliance with eligibility criteria as set out in these guidelines.

3.2 No person shall, after the commencement of these guidelines, transact the business of Surety Insurance in India unless the person is an Indian Insurance Company as defined in Section 2 (7A) of the Insurance Act, 1938.

4. Essential Features of Surety Insurance contract

The essential features of a Surety Insurance contract shall be as follows.

4.1 It shall be a contract of guarantee under Section 126 of the Indian Contract Act, 1872. It is a contract to perform the promise, or discharge the liability of a third person in case of his default. The person who gives the guarantee is called the “Surety”; the person in respect of whose default the guarantee is given is called the “principal debtor”, and the person to whom the guarantee is given is called the “creditor”.

4.2 A contract of Surety shall be deemed to be an insurance contract only if made by a Surety who or which, is an insurer registered under the Insurance Act, 1938 to transact the business of general insurance.

5. Types and Definitions of Surety Contracts

- (a) In these guidelines, unless the context otherwise requires, the terms herein shall bear the meanings assigned to them below.
- (i) **Advance Payment Bond:** It is a promise by the Surety provider to pay the outstanding balance of the advance payment in case the contractor fails to complete the contract as per specifications or fails to adhere to the scope of the contract.
 - (ii) **Bid Bond :** It is an obligation undertaken by a bidder promising that the bidder will, if awarded the contract, furnish the prescribed performance guarantee and enter into contract agreement within a specified period of time. It provides financial protection to an obligee if a bidder is awarded a contract pursuant to the bid documents, but fails to sign the contract and provide any required performance and payment bonds.
 - (iii) **Contract Bond:** It provides assurance to the public entity, developers, subcontractors and suppliers that the contractor will fulfil its contractual obligation when undertaking the project. Contract bonds may include: Bid Bonds, Performance Bonds, Advance Payment Bonds and Retention Money.
 - (iv) **Customs and Court Bond:** This is a type of guarantee where the obligee is a public office such as tax office, customs administration or the court, and it guarantees the payment of a public receivable incurred from opening a court case, clearing goods from customs or losses due to incorrect customs procedures.
 - (v) **Performance Bond:** It provides assurance that the obligee will be protected if the principal or contractor fails to perform the bonded contract. If the obligee declares the principal or contractor as being in default and terminates the contract, it can call on the Surety to meet the Surety's obligations under the bond.
 - (vi) **Retention Money:** It is a part of the amount payable to the contractor, which is retained and payable at the end after successful completion of the contract.
- (b) All words and expressions used herein and not defined but defined in the Insurance Act, 1938 or the IRDA Act, 1999, or in any Rules or Regulations made thereunder shall have the meanings assigned to them in those Acts, Rules, or Regulations.

6. Requirements of Underwriting of Surety Insurance Business

(a) General Provisions

6.1 A General Insurer shall commence Surety Insurance business subject to:

- (a) Meeting the requirement of maintaining a solvency margin of not below 1.25 times of the control level of solvency specified by the Authority. Provided that where the solvency margin of the insurer falls below the specified threshold limit at any point of time, the insurer shall stop underwriting new Surety Insurance business until its solvency margin is restored to above the threshold limit.
- (b) Premium charged for all Surety Insurance policies underwritten in a financial year, including all instalments due in subsequent year/s for those policies, shall not exceed 10% of the total gross written premium of that year, subject to a maximum of Rs. 500 crores.
- (c) Having a Board approved underwriting philosophy on Surety Insurance business, adequate underwriting competence and skills, risk management and required infrastructure for underwriting the Surety Insurance.
- (d) Establishing risk assessment mechanism/ internal risk management guidelines to evaluate technical/financial strength of principal before and after underwriting the Surety Insurance business.
- (e) Compliance with specific conditions imposed by the Authority for issuance of Surety Insurance contracts, based on assessment of the insurers' capabilities to handle this business.

6.2. The insurers can work together with the following.

- (a) Banks or other financial institutions such as NBFCs to share risk information, technical expertise to monitor projects, cash flow amongst other aspects.
- (b) Contracting awarding authorities in order to evaluate the risk with more information and data.

(b) Underwriting Philosophy

6.3 The Insurers shall have a Board approved underwriting philosophy for Surety Insurance business. The underwriting policy relevant to Surety Insurance contracts, at the minimum, cover the following:

- (a) Incorporate all aspects for managing this business and ensure that Surety Insurance operations are well supported by prudent underwriting practices, sound risk management and internal controls that are commensurate with these operations.
- (b) The Board of Directors of the insurer shall approve the methodology and procedures to set the maximum limit of accumulation of risks per contractor and its group companies/firms and maximum retention limit for risk accumulation and these aspects need to be built in by the insurer in their underwriting policy and philosophy.
- (c) The Board of Directors or Risk Management Committee of the insurer shall assess the ability of the insurer to retain Surety risks on their balance sheet based on the financial strength of the insurer and mandate appropriate reinsurance requirements to ensure that disproportionate Surety risks are not written by the insurer. It shall conduct review on quarterly basis.
- (d) Include due diligence relating to the contractor/principal debtor such as good references and reputation, the ability to meet current and future obligations, experience that matches the contract requirements, the necessary equipment to do the work, the financial strength to carry and support its share of the project work. The underwriting process shall include review of contractor's financials, cash flow, tax returns, liquidity and debts.
- (e) Provision of timely, accurate, independent and objective reporting to Board on the related risks of the Surety Insurance business, including the procedures and controls in place to manage the risks, and the overall effectiveness of risk management processes.

(c) Underwriting Guidelines

6.4 An Insurer underwriting Surety Insurance business shall comply with the following:

- (a) Surety Insurance Contracts may be offered to infrastructure projects of Government/Private in all modes.
- (b) The Contract Bonds may include Bid Bonds, Performance Bonds, Advance Payment Bonds and Retention Money.
- (c) Apart from Contract Bonds, the insurers may underwrite Customs or Tax Bonds and Court Bonds.
- (d) The limit of guarantee shall not exceed 30 percent of the contract value.
- (e) Surety Insurance contracts shall be issued only to specific projects and not clubbed for multiple projects.
- (f) The insurer shall not issue any Surety Insurance contracts on behalf of its promoters/their subsidiaries, groups, associates and related parties.
- (g) The insurer shall not enter into “alternate risk transfer” mechanism.
- (h) No Surety Insurance contract shall cover Financial Guarantee in any form. Financial Guarantee comprises of any bond, guarantee, indemnity or insurance, covering financial obligations in respect of any type of loan, personal loan and leasing facility, granted by a bank/credit institution, financial institution or financier, or issued or executed in favour of any person or legal entity in respect of the payment or repayment of borrowed money or any contract, transaction or arrangement, the primary purpose of which is to raise finance or secure sums due in respect of borrowed money.
- (i) The insurer shall ensure that no single risk and aggregate risk is disproportionate to the capital of the insurer.
- (j) Surety Insurance contracts shall be issued in compliance with applicable laws.
- (k) Surety Insurance contracts shall not be issued where the underlying assets / commitment are/is outside India. Further, the payment for risk covered under the Surety Insurance contracts shall also be made in Indian rupees.

6.5 These guidelines set out the minimum underwriting requirements expected of an insurer in accepting business in respect of Surety Insurance business for the purposes of ensuring its ability to manage the portfolio or fulfil the reasonable expectations of policy holders. It shall be the sole responsibility of the insurers concerned to have due regard to all relevant factors, including the quality of their business portfolio and risk exposure, in determining whether additional level of underwriting safeguards should be maintained.

7. Product Filing

7.1 Surety Insurance products shall be subject to all provisions and relevant procedures of File & Use as stipulated under the Guidelines on Product Filing Procedures for General Insurance Products. The insurers shall market the Surety Insurance products only after the same has been filed and noted by the Authority.

7.2 This insurance business shall be classified under Miscellaneous line of business.

8. Maintenance of Data Base, Information and Reports

8.1 The data of Surety Insurance contracts underwritten by all general insurers shall be submitted to Insurance Information Bureau of India (IIBI) as may be prescribed.

8.2 The insurers shall maintain the relevant records and data pertaining to Surety Insurance business and submit to the Authority as and when requisitioned.

9. Interpretation

In order to remove any difficulties in respect of the application or interpretation of any of the provisions of these guidelines and for the purpose of giving effect to the provisions of these guidelines, the Chairperson or Senior-most Whole Time Member (WTM), on the recommendations of the WTM concerned with the subject matter may issue necessary clarifications in respect of any matter covered herein from time to time.

Chief General Manager (Non-Life)