

IC-39 Fraud Risk Management in Insurance

Original Text in book

Chapter 4 Page no.65 & 67

1. Indian Penal Code (IPC) and Criminal Procedure Code (CRPC)

There are no specific Acts or Laws to take action against the people and/or organizations involved in insurance frauds. Insurance fraud is not defined in the Indian Penal Code (IPC) and none of the sections of IPC or Criminal Procedure Code (CRPC) deals specifically with the punishment for insurance frauds. With no Indian act or law directly dealing with insurance frauds, if frauds are detected, fraudsters are not subjected to any specific penalty or penal action, and there is a good chance that they are let free. That is, if they are caught, they would not gain the money which they were intending to get through fraudulent means, but may go unpunished for trying to defraud.

In the absence of specific provisions, this chapter examines the indirect laws which are guiding the transaction of insurance business in India, which can be helpful to initiate criminal action against the fraudster and can be used by insurers in the Indian context.

Another notable point is that no reference is made regarding punishments to insurers in case there is any fraudulent intention of the insurer or the representatives of the insurer. No provision for redress for the policy holder (the other party to the contract) is mentioned.

Punishment under IPC 23, 24 and 25:

Sections 23, 24 & 25 of IPC generally explain about Dishonesty and Fraud. With some amount of interpretation, Sections 24 & 25 of IPC are being used by insurers so that the fraudsters are subjected to necessary punishment.

Definition

“Dishonesty” is doing anything with the intention of causing wrongful gain to one person or wrongful loss to another person. Fraud is stated as an act of deliberate deception with the design of securing something by taking unfair advantage of another. It is a deception in order to gain by another’s loss.

Comment: Section 23 and 24 mention the term “wrongful gain” which is relevant to some extent.

Definition

The word “Fraudulently” is defined and explained in Section 25. A person is said to do a thing fraudulently if he does that thing with the intent to defraud but not otherwise.

Comment: In many cases, the court may ask the insurer to prove fraudulent intent, which is often very difficult. The defendants may maintain that it was an oversight, or that they did not know it was significant, or that someone else completed the form on their behalf.

Reference to some fraudulent activities/ actions related to removal or concealment of property is made in Sections 406, 415, 421, 422, 423 and 424 of IPC which might be relevant/ useful in certain contexts.

Section 406 of IPC provides for punishment for criminal breach of trust. Whoever commits criminal breach of trust shall be punished with imprisonment of either description for a term which may extend to three years, or with fine, or with both.

Case Study:

A Delhi-based gang of 45 impersonating employees of Life Insurance Corporation (LIC), Reserve Bank of India (RBI), Insurance Regulatory and Development Authority of India (IRDAI) and other government institutions duped a 74-year-old man from Vadodara of Rs 1.51 crore. According to

police, the victim was lured into investing in as many as 64 policies for higher returns since September 2014 by the gang. He was first contacted by a woman, claiming to be an official from 'central government insurance and verification department' under IRDAI. The woman told him that a file containing his details of Rs 3.5 lakh investment in LIC had come to her department for verification. She asked if he wished to invest in other policies for higher returns. Then he was contacted by various persons claiming themselves to be from IRDAI, RBI, SBI and lured him to invest in 64 policies in total of Rs 67.15 lakh and then he was asked to pay Rs 16.27 lakh as fees and Rs 67 lakh as other surcharges from 2014 to 2020. Then accused group duped him to the tune of Rs 1.51 crore in seven years. Taking cognizance, the police booked a case against 45 persons under IPC 406 for criminal breach of trust, 420 for fraud and sections of the IT Act.

[Source: The Indian Express dated June 12, 2021 - <https://indianexpress.com/article/cities/ahmedabad/vadodara-man-duped-of-rs-1-51-crore-in-insurance-fraud-7355108/>]

Section 415 of IPC states that whoever, by deceiving any person, fraudulently or dishonestly induces the person so deceived to deliver any property to any person, or to consent that any person shall retain any property, or intentionally induces the person so deceived to do or omit to do anything which he would not do or omit if he were not so deceived and which act or omission causes or is likely to cause damage or harm to that person in body, mind, reputation or property is said to be cheat.

Section 421 of IPC speaks about dishonest or fraudulent removal or concealment of property to prevent distribution among creditors.

Section 422 of IPC is on dishonestly or fraudulently preventing debt being available for creditors.

Section 423 of IPC says about dishonest or fraudulent execution of deed of transfer containing false statement of consideration.

Section 424 of IPC is about dishonest or fraudulent removal or concealment of property. It states that whoever dishonestly or fraudulently conceals or removes any property of himself or any other person, or dishonestly or fraudulently assists in the concealment or removal thereof, or dishonestly releases any demand or claim to which he is entitled, shall be punished with imprisonment of either description for a term which may extend to two years, or with fine, or with both.

These sections can be interpreted by insurers in their defense while dealing with insurance frauds.

Test Yourself 1

The IPC makes reference to several fraudulent activities/actions in which of the following sections?

- A. Sections 25, 415, 421, 423 and 426
- B. Sections 25, 415, 426, 423 and 412
- C. Sections 25, 413, 421, 425 and 426
- D. Sections 125, 415, 421, 423 and 426

Similarly, references to different types of mischief and the punishments that those mischiefs attract are made under Sections 425 to Sections 440 of IPC.

Section 425 of IPC states that whoever, with intent to cause, or knowing that he is likely to cause, wrongful loss or damage to the public or to any person, causes the destruction of any property, or any such change in any property or in the situation thereof as destroys or diminishes its value or utility, or affects it injuriously, commits "mischief".

The Section explains that it is not essential to the offence of mischief that the offender should intend to cause loss or damage to the owner of the property injured or destroyed. It is sufficient

if he intends to cause, or knows that he is likely to cause, wrongful loss or damage to any person by injuring any property, whether it belongs to that person or not.

The Section explains also that mischief may be committed by an act affecting property belonging to the person who commits the act, or to that person and others jointly.

The following illustrations mentioned in IPC would help in understanding the concept better and relate mischief in an insurance context.

(a) If A voluntarily burns a valuable security belonging to Z intending to cause wrongful loss to Z, A has committed mischief.

(b) If A introduces water in to an ice-house belonging to Z and thus causes the ice to melt, intending wrongful loss to Z, A has committed mischief.

(c) If A voluntarily throws into a river a ring belonging to Z, with the intention of thereby causing wrongful loss to Z, A has committed mischief.

(d) If A, knowing that his effects (belongings) are about to be taken in execution in order to satisfy a debt due from him to Z, destroys those effects, with the intention of thereby preventing Z from obtaining satisfaction of the debt, and of thus causing damage to Z; A has committed mischief.

(e) If A having insured a ship, voluntarily causes the same to be cast away, with the intention of causing damage to the underwriters (claiming insurance money), A has committed mischief.

(f) If A causes a ship to be cast away, intending thereby to cause damage to Z who has lent money on bottomry on the ship, A has committed mischief.

(g) If A, having joint property with Z in a horse, shoots the horse, intending thereby to cause wrongful loss to Z, A has committed mischief.

(h) If A causes cattle to enter upon a field belonging to Z, intending to cause and knowing that he is likely to cause damage to Z's crop, A has committed mischief.

Based on the context of the fraudulent claim, these mischiefs can be interpreted to defend the insurers' position while dealing with insurance frauds.

Revised text as below

Chapter 4 Page no.65 & 67

1. Indian Penal Code (IPC) Revised with Bharatiya Nyaya Sanhita (BNS) 2023 References

Insurance fraud is not defined as a distinct offence under the Bharatiya Nyaya Sanhita (BNS), 2023. However, several provisions of BNS apply to fraudulent activities relevant in the context of insurance. This document presents the sections of BNS applicable to fraud and dishonesty in insurance, replacing the earlier references under IPC.

Definitions under BNS

Section 21 - Wrongful gain: Gain by unlawful means of property to which the person gaining is not legally entitled.

Section 22 - Wrongful loss: Loss by unlawful means of property to which the person losing it is legally entitled.

Section 23 - Fraudulently: A person is said to do a thing fraudulently if he does that thing with the intent to defraud but not otherwise.

Dishonestly: Doing anything with the intention of causing wrongful gain to one person or wrongful loss to another.

Section 316 - Criminal Breach of Trust

Whoever, being entrusted with property, or with any dominion over property, dishonestly misappropriates or converts to his own use that property, or dishonestly uses or disposes of that property in violation of law or contract, commits criminal breach of trust.

Punishment: Up to 5 years imprisonment or fine or both. Enhanced punishment up to 7 years or 10 years/life in fiduciary positions.

Section 318 - Cheating

Whoever, by deceiving any person, fraudulently or dishonestly induces the person so deceived to deliver any property to any person, or to consent that any person shall retain any property, or intentionally induces the person so deceived to do or omit to do anything which he would not do or omit if he were not so deceived, and which act or omission causes or is likely to cause damage or harm to that person in body, mind, reputation or property, is said to cheat.

Explanation: A dishonest concealment of facts is a deception within the meaning of this section.

Punishment: Basic cheating up to 3 years. If involves breach of trust/loss of person bound to protect interest - up to 5 years. If it involves delivery of property/valuable security - up to 7 years and fine.

Other Relevant BNS Sections

Section 322 - Dishonest or fraudulent removal/concealment of property to prevent distribution among creditors.

Section 323 - Dishonestly or fraudulently preventing debt being available for creditors.

Section 324 - Fraudulent execution of deed of transfer containing false statement of consideration.

Section 325 - Dishonest or fraudulent removal or concealment of property (punishable up to 2 years or fine or both).

Sections 327-336 - Mischief offences: causing wrongful loss or damage to property. Punishments vary depending on severity.

Case Study - Vadodara LIC Fraud

A Delhi-based gang of 45 impersonating employees of LIC, RBI, IRDAI and others duped a 74-year-old man of Rs.1.51 crore. Originally booked under IPC 406 (Criminal breach of trust) and 420 (Cheating). Under BNS 2023, these correspond to Section 316 (Criminal breach of trust) and Section 318 (Cheating).

Test Yourself 1

The BNS makes reference to several fraudulent activities/actions in which of the following sections?

- A. Sections 23, 318, 322, 324 and 327
- B. Sections 21, 318, 325, 324 and 336
- C. Sections 23, 318, 322, 325 and 327
- D. Sections 21, 318, 324, 325 and 336

Annexure - Extracts from BNS 2023

Section 316: Criminal Breach of Trust

Whoever, being in any manner entrusted with property, or with any dominion over property, dishonestly misappropriates or converts to his own use that property, or dishonestly uses or disposes of that property in violation of any direction of law, or of any legal contract, commits criminal breach of trust.

Punishment: Imprisonment up to 5 years, or with fine, or both. In aggravated circumstances (agents, fiduciaries, bankers), punishment can extend to 10 years or even life imprisonment along with fine.

Section 318: Cheating

Cheating is defined as deceiving any person, fraudulently or dishonestly inducing them to deliver property, retain property, or to do/omit any act that they would not do but for the deception, thereby causing damage or harm.

Explanation: Concealment of facts is also cheating.

Punishment: Basic cheating - imprisonment up to 3 years, or fine, or both. Where cheating causes loss to a person bound to be protected - up to 5 years and fine. Where cheating involves delivery of property, alteration or destruction of valuable security - up to 7 years and fine.

Sections 322-325: Property Offences

These sections deal with fraudulent removal or concealment of property, prevention of debts, false execution of deeds, and fraudulent concealment/removal of property. Punishments vary up to 2 years or fine or both.

Sections 327-336: Mischief Offences

These sections describe offences of mischief, including causing wrongful loss or damage to property and describe varying punishments depending on the extent of damage or public harm caused.

Quick Reference Table - IPC vs BNS (Fraud Related Offences)

IPC Section (Old)	BNS Section (2023)	Offence Description
IPC 23, 24, 25	BNS 21, 22, 23	Definitions: Wrongful gain/loss, Dishonestly, Fraudulently
IPC 406	BNS 316	Criminal Breach of Trust
IPC 415	BNS 318	Cheating
IPC 420	BNS 318(4)	Cheating - delivery of property/valuable security
IPC 421	BNS 322	Fraudulent removal/concealment of property to prevent distribution among creditors
IPC 422	BNS 323	Fraudulently preventing debt being available for creditors
IPC 423	BNS 324	Fraudulent execution of deed of transfer containing false statement
IPC 424	BNS 325	Fraudulent removal/concealment of property
IPC 425-440	BNS 327-336	Mischief offences - wrongful loss/damage to property

4. Insurance Act, 1938 & Insurance Laws Amendment Act, 2015

The Insurance Act, 1938 also does not have any provisions to specifically deal with the fraudsters in insurance. It has certain provisions related to prohibition of rebate in the insurance premium. However, the Insurance laws (Amendment) Act, 2015 has some provisions for penalties for insurance fraud committed by agents/ insurance companies for wrongly selling the products or misrepresentation of facts. These amendment laws are about the role of insurance agents and other insurance intermediaries and the duty of insurers about monitoring them. Sec.49, 50, Sec.51 and Sec.55 of the Insurance Act 2015 may be referred to determine the scope and cases of violation. Let us learn about some of the sections.

4.1. Section 49 of the Insurance Act

Sec.49 (4) of Insurance Laws (Amendment) Act, 2015 states that any person who acts as an insurance agent in contravention of the provision of this Act, shall be liable to a penalty which may extend to ten thousand rupees. Similarly, if an insurer or any person acting on behalf of the insurer appoints any person as an insurance agent who is not permitted to act as such, or transacts any insurance business in India through any such person shall be liable to penalty which may extend to one crore (10 million) rupees.

Sec.49(5) states that the insurer shall be responsible for all the acts and omissions of its agents including violation of code of conduct specified under clause (h) of sub-section (3) and liable to a penalty which may extend to one crore (10 million) rupees.

4.2. Section 50 of the Insurance Act

The Section provides that:

- 1) No insurer shall, on or after the commencement of the Insurance Laws (Amendment) Act, 2015 appoint any principal agent, chief agent and special agent and transact any insurance business in India through them.
- 2) No person shall allow or offer to allow, either directly or indirectly, as an inducement to any person to take out or renew or continue an insurance policy through a multilevel marketing scheme.
- 3) The Authority may, through an officer authorized in its behalf, make a complaint to the appropriate police authorities against the entity or persons involved in a multilevel marketing scheme.

Sec 50 further explains that for the purpose of this section, "multilevel marketing scheme" means any scheme or program or arrangement or plan (by whatever name called) for the purpose of soliciting and procuring insurance business through persons not authorised for the said purpose with or without consideration of whole or part of commission or remuneration earned through such solicitation and procurement and includes enrolment of persons into a multilevel chain for the said purpose either directly or indirectly.

4.3. Section 51 of the Insurance Act

Sec 51 (8) of the Insurance Laws (Amendment) Act, 2015 states that any person who acts as an intermediary or an insurance intermediary without being registered under this section to act as such, shall be liable to a penalty which may extend to ten lakh (one million) rupees and any person who appoints as an intermediary or an insurance intermediary or any person not registered to act as such or transacts any insurance business in India through any such person, shall be liable to a penalty which may extend to one crore (10 million) rupees.

Sec 51 (9) of the Act, 2015 states that where the person contravening sub-section (8) is a company or a firm, then without prejudice to any other proceedings which may be taken against the company or firm, every director, manager, secretary or other officer of the company and every partner of the firm who is knowingly a party to such contravention shall be liable to a penalty which may extend to ten lakh (one million) rupees.

4.4. Section 55 of the Insurance Act

Sec. 55 (2) of the Act, 2015 provides that a policy of life insurance may be called in question at any time within three years from the date of issuance of the policy or the date of commencement of risk or the date of revival of the policy or the date of the rider to the policy, whichever is later, on the ground of fraud, provided that the insurer shall have to communicate in writing to the insured or the legal representatives or nominees or assignees of the insured the grounds and materials on which such decision is based.

Explanation to Sec.55 (2) provides that for the purposes of this sub-section, the expression "fraud" means any of the following acts committed by the insured or by his agent, with intent to deceive the insurer or to induce the insurer to issue a life insurance policy:

- a) the suggestion, as a fact of that which is not true and which the insured does not believe to be true;
- b) the active concealment of a fact by the insured having knowledge or belief of the fact;
- c) any other act fitted to deceive; and any such act or omission as the law specially declares to be fraudulent.

Explanation II to Sec.55 (2) provides that mere silence as to facts likely to affect the assessment of the risk by the insurer is not fraud, unless the circumstances of the case are such that regard being had to them, it is the duty of the insured or his agent keeping silence, to speak, or unless his silence is, in itself, equivalent to speak.

Sec.55 (3) provides that notwithstanding anything contained in sub-section (2), no insurer shall repudiate a life insurance policy on the ground of fraud if the insured can prove that the misstatement of or suppression of a material fact was true to the best of his knowledge and belief or that there was no deliberate intention to suppress the fact or that such misstatement of or suppression of a material fact are within the knowledge of the insurer:

Provided that in case of fraud, the onus of disproving lies upon the beneficiaries, in case the policyholder is not alive.

Sec, 55 (4) provided further that in case of repudiation of the policy on the ground of misstatement or suppression of a material fact and not on the ground of fraud, the premiums collected on the policy till the date of repudiation shall be paid to the insured or the legal representatives or nominees or assignees of the insured within a period of ninety days from the date of such repudiation.

Sec.50, Sec.51 and Sec.55 of the Insurance Act, 2015 as mentioned above define and determine the scope and consequences of frauds perpetrated by any person in the insurance business. Insurance professionals need to have proper understanding of the above-noted provisions of the Insurance Amendment Act, 2015 to legally handle insurance frauds.

Revised Text

Chapter.4, Page no. 70, 71, 72&73

4. Insurance Act, 1938 & Insurance Laws Amendment Act, 2015

The Insurance Act, 1938 also does not have any provisions to specifically deal with the fraudsters in insurance. It has certain provisions related to prohibition of rebate in the insurance premium. However, the Insurance laws (Amendment) Act, 2015 has some provisions for penalties for insurance fraud committed by agents/ insurance companies for wrongly selling the products or misrepresentation of facts. These amendment laws are about the role of insurance agents and other insurance intermediaries and the duty of insurers about monitoring them. Sec.40, Sec.41, Sec.42 and Sec.45 of the Insurance Act 2015 may be referred to determine the scope and cases of violation. Let us learn about some of the sections.

4.1. Section 40 of the Insurance Act

The Section provides that:

- 1) No insurer shall, on or after the commencement of the Insurance Laws (Amendment) Act, 2015 appoint any principal agent, chief agent and special agent and transact any insurance business in India through them.
- 2) No person shall allow or offer to allow, either directly or indirectly, as an inducement to any person to take out or renew or continue an insurance policy through a multilevel marketing scheme.
- 3) The Authority may, through an officer authorized in its behalf, make a complaint to the appropriate police authorities against the entity or persons involved in a multilevel marketing scheme.

4.2. Section 41 of the Insurance Act

Sec 41 (8) of the Insurance Laws (Amendment) Act, 2015 states that any person who acts as an intermediary or an insurance intermediary without being registered under this section to act as such, shall be liable to a penalty which may extend to ten lakh (one million) rupees and any person who appoints as an intermediary or an insurance intermediary or any person not registered to act as such or transacts any insurance business in India through any such person, shall be liable to a penalty which may extend to one crore (10 million) rupees.

Sec 41 (9) of the Act, 2015 states that where the person contravening sub-section (8) is a company or a firm, then without prejudice to any other proceedings which may be taken against the company or firm, every director, manager, secretary or other officer of the company and every partner of the firm who is knowingly a party to such contravention shall be liable to a penalty which may extend to ten lakh (one million) rupees.

4.3. Section 42 of the Insurance Act

Sec.42 (4) of Insurance Laws (Amendment) Act, 2015 states that any person who acts as an insurance agent in contravention of the provision of this Act, shall be liable to a penalty which may extend to ten thousand rupees. Similarly, if an insurer or any person acting on behalf of the insurer appoints any person as an insurance agent who is not permitted to act as such, or transacts any insurance business in India through any such person shall be liable to penalty which may extend to one crore (10 million) rupees.

Sec.42(5) states that the insurer shall be responsible for all the acts and omissions of its agents including violation of code of conduct specified under clause (h) of sub-section (3) and liable to a penalty which may extend to one crore (10 million) rupees.

Sec 42A further explains that for the purpose of this section, "multilevel marketing scheme" means any scheme or program or arrangement or plan (by whatever name called) for the purpose of soliciting and procuring insurance business through persons not authorised for the said purpose with or without consideration of whole or part of commission or remuneration earned through such solicitation and procurement and includes enrolment of persons into a multilevel chain for the said purpose either directly or indirectly.

4.4. Section 45 of the Insurance Act

Sec. 45 (2) of the Act, 2015 provides that a policy of life insurance may be called in question at any time within three years from the date of issuance of the policy or the date of commencement of risk or the date of revival of the policy or the date of the rider to the policy, whichever is later, on the ground of fraud, provided that the insurer shall have to communicate in writing to the insured or the legal representatives or nominees or assignees of the insured the grounds and materials on which such decision is based.

Explanation to Sec.45 (2) provides that for the purposes of this sub-section, the expression "fraud" means any of the following acts committed by the insured or by his agent, with intent to deceive the insurer or to induce the insurer to issue a life insurance policy:

- a) the suggestion, as a fact of that which is not true and which the insured does not believe to be true;
- b) the active concealment of a fact by the insured having knowledge or belief of the fact;
- c) any other act fitted to deceive; and any such act or omission as the law specially declares to be fraudulent.

Explanation II to Sec.45 (2) provides that mere silence as to facts likely to affect the assessment of the risk by the insurer is not fraud, unless the circumstances of the case are such that regard being had to them, it is the duty of the insured or his agent keeping silence, to speak, or unless his silence is, in itself, equivalent to speak.

Sec.45 (3) provides that notwithstanding anything contained in sub-section (2), no insurer shall repudiate a life insurance policy on the ground of fraud if the insured can prove that the misstatement of or suppression of a material fact was true to the best of his knowledge and belief or that there was no deliberate intention to suppress the fact or that such misstatement of or suppression of a material fact are within the knowledge of the insurer:

Provided that in case of fraud, the onus of disproving lies upon the beneficiaries, in case the policyholder is not alive.

Sec, 45 (4) provided further that in case of repudiation of the policy on the ground of misstatement or suppression of a material fact and not on the ground of fraud, the premiums collected on the policy till the date of repudiation shall be paid to the insured or the legal representatives or nominees or assignees of the insured within a period of ninety days from the date of such repudiation.

Sec.40, Sec.41, Sec.42 and Sec.45 of the Insurance Act, 2015 as mentioned above define and determine the scope and consequences of frauds perpetrated by any person in the insurance business. Insurance professionals need to have proper understanding of the above-noted provisions of the Insurance Amendment Act, 2015 to legally handle insurance frauds.