GOVERNMENT OF PAKISTAN
Securities and Exchange Commission of Pakistan

NOTIFICATION

Islamabad, the 2nd June, 2016

S.R.O.511(I)/2016–. The following draft of Credit and Suretyship (Conduct of Business) Rules, 2016 proposed to be made by the Securities and Exchange Commission of Pakistan in exercise of its powers conferred by section 83 read with sub-section (2) of section 167 of the Insurance Ordinance (XXXIX) of 2000 is hereby published in the official Gazette for information of all persons likely to be affected thereby and notice is hereby given that objections and suggestions, if any, received by the Securities and Exchange Commission of Pakistan within thirty days of the publication of this notification, will be taken into consideration.

THE CREDIT AND SURETYSHIP (CONDUCT OF BUSINESS) RULES, 2016

1. Short Title and Commencement.– (1) These Rules shall be called the "Credit and Suretyship (Conduct of Business) Rules, 2016.

(2) These Rules shall come into force at once.

2. Definitions.- (1) In these Rules, unless there is anything repugnant in the subject or context,-.

(a) "Act" means the Securities and Exchange Commission of Pakistan Act, 1997 (XLII of 1997);

(b) "collateral" means —

i. the eligible collateral; and
ii. any tangible fixed asset pledged with the insurer, the value of which shall be determined by a professional valuator / surveyor on the panel of Pakistan Banks Association and duly approved by the Commission;

(c) "Commission" means the Securities and Exchange Commission of Pakistan established under section 3 of the Act;

(d) "eligible collateral" means —

i. cash (Any form of promissory notes or post-dated cheques shall not be construed as 'cash');
ii. bearer bonds;
iii. back-to-back / counter-guarantees of banks/DFIs rated at least 'A' or equivalent by a credit rating agency, in favor of the insurer;
iv. an approved security as defined in section 2(iii) of the Ordinance; and
v. Other marketable securities duly pledged with the insurer;

(e) "financial guarantee insurance policy" means a policy that guarantees to the beneficiary of the policy the performance of a financial obligation in accordance with the terms of the obligation, including the right to receive scheduled payments on a security but excludes letters of credit issued by licensed banks, performance bonds, fidelity bonds and such other similar contracts of guarantee issued by an insurer, as may be specified by the Commission from time to time;

(f) "government unit" means the Federal Government, a Provincial Government or a local authority or any agency thereof, including a statutory corporation as defined under sub-section 2(c) of section 166 of the Ordinance;

(g) "insurer" means a non-life insurer who is registered under the Ordinance;

(h) "insurer's qualified sum" means an amount equal to the sum of the shareholders' equity of an insurer and the contingency reserves maintained by that insurer under these rules;

(i) "net exposure" under a financial guarantee insurance policy means the sum insured, net of any eligible collateral, and under a non-financial guarantee insurance policy means the guaranteed aggregate amount to be paid upon happening of respective event triggering such payment, net of value of the collateral kept by the insurer, as specified in these rules;

(j) "net retained exposure" means the portion of net exposure retained by the insurer to its own account on a particular policy net of all respective reinsurance ceded;

(k) "non-financial guarantee insurance policy" means an insurance policy issued in respect of the kinds as defined under rule 3(2) of these rules;

(l) "Ordinance" means the Insurance Ordinance, 2000 (Ordinance No. XXXIX of 2000);

(2) In these Rules, the word 'takaful' may be used interchangeably with the word 'insurance', 'general takaful' with 'general insurance', 'contribution' with 'premium' and 'company' and 'insurer' with 'takaful Operator'.

(3) The words and expressions used but not defined shall have the same meaning

assigned to them in the Ordinance.

3. Issuance of guarantee insurance policies—(1) An insurer may issue financial guarantee insurance policies in respect of any or all of the following obligations:

(a) ***asset-backed obligations —*** obligations of an entity which owns a diversified pool of assets or to which a diversified pool of assets including residential real estate and other fixed assets have been pledged, the proceeds of which, whether through collection or sale, are available to make any payments due on the obligations;

(b) ***infrastructure obligations —*** obligations issued to finance construction, maintenance, improvement or expansion of physical infrastructure;

(c) ***government obligations —*** obligations that are payable or guaranteed by a government unit or that are payable from tax revenue, rates charges or appropriation imposed or collected by such government unit;

(d) ***real estate obligations —*** obligations that are backed by cash flows or market values associated with income-producing real property excluding residential real estate;

(e) ***corporate obligations —*** obligations related to corporate bonds or promissory notes issued by a company or a body corporate; and

(f) ***obligations approved by the Commission —*** such other financial obligations as the Commission may notify from time to time through notification.

(2) An insurer may issue non-financial guarantee insurance policies in respect of any or all of the following obligations:

(a) ***fidelity bonds—*** obligations to protect the policyholders for losses that they incur as a result of fraudulent acts by specified individuals. Typical instance of such bond is to cover an employer's monies, securities, and other property from employees who have a manifest intent to cause such loss to that employer. These bonds may also include many other forms of crime-insurance policies such as burglary, fire, general theft, computer theft, disappearance, fraud, forgery, etc., aimed at protecting employer's assets;

(b) ***Bid bonds —*** obligations to protect the inviter of the bids for execution of a particular task (or set of particular interrelated tasks) or supply of particular products or services, against inability of the successful bidder to honor the baseline requirements upon winning the bid such as to deposit the security money to the inviter of the bids;

(c) ***Mobilization Advance Guarantee —*** obligations to protect the awarder of a contract against the default of the contractor for the money paid by that awarder of the contract to execute the tasks or deliver the services as laid down in the terms of contract;

(d) ***Payment bonds —*** obligations to protect the policyholder against willful inability of the contractor to pay its own liabilities concerning labour employed by it, material required to execute / fulfill the contract terms and/or other similar overheads, which may directly or indirectly hamper the contractor's performance as per the terms specified in the contract between the policyholder and the contractor;

(e) ***performance bonds —*** obligations issued to guarantee satisfactory completion of a project by a contractor (or group of contractors) concerning supply / delivery of pre-specified products, or construction, maintenance, improvement or expansion of physical infrastructure including power production and distribution, telecommunications, roads, bridges, tunnels, airports, schools, hospitals etc., as per the terms of the underlying contract of supply / delivery of pre-specified products, or construction, maintenance, improvement or expansion of the said physical infrastructure;

(f) ***administration bonds —*** obligations to assure a person who is the administrator of a will acts legally and ethically, in order to protect those in the will against fraud;

(g) ***bail bonds —*** obligations that guarantees to pay to the court the bail amount in full if a defendant fails to appear for the scheduled court appearances, and/or any other financial obligation towards any other person, as may be decided by the court. The policyholder (defendant) must have adequate assets to satisfy the face value of the bond;

(h) ***custom bonds —*** obligations to guarantee Pakistan Customs that if it cannot collect monies due from the Principal (who is required to file the bond) it can seek remedy, up to the bond amount, from the insurer; and

(i) ***Other non-financial guarantee / bond policies approved by the Commission —*** such other non-financial guarantee / bond policies as the Commission may notify from time to time through notification.

(3) All types of obligations / bonds as mentioned under sub-rule (1) and sub-rule (2) are mutually exclusive, that is to say that in case of any difficulty in classifying an obligation under any of these types of obligations / bonds, the one which is the most relevant shall prevail.

4. Single and aggregate net exposure limits— (1) An insurer shall limit its net retained exposure under any single financial guarantee insurance policy issued by the insurer to the extent of the following:

(a) ***for asset-backed obligations —*** the net retained exposure to each of the supporting assets shall not exceed the following percentage of the insurer's qualified sum:

i. 15% during the year 2017;
ii. 10% during the year 2018; and

iii. 5% during the year 2019 and thereafter;

(b) ***for infrastructure obligations that are issued in respect of projects or facilities built, owned or operated (whether at the time of construction or afterwards) by or on behalf of a government unit and for government obligations —*** the net retained exposure on the obligation shall not exceed the following percentage of the insurer's qualified sum:

i. 20% during the year 2017;
ii. 15% during the year 2018; and
iii. 10% during the year 2019 and thereafter.

(c) ***for infrastructure obligations that are issued in respect of projects or facilities built, not owned or operated by a government unit —*** the net retained exposure on an obligation shall not exceed the following percentage of the insurer's qualified sum:

i. 15% during the year 2017;
ii. 10% during the year 2018; and
iii. 5% during the year 2019 and thereafter;

(d) ***for real estate obligations that do not otherwise constitute asset-backed obligations —*** the net retained exposure to the outstanding principal including interest on an obligation less 50% of the appraised value of the underlying real estate shall not exceed the following percentage of the insurer's qualified sum:

i. 15% during the year 2017;
ii. 10% during the year 2018; and
iii. 5% during the year 2019 and thereafter; and

(e) ***for corporate obligations —*** the net retained exposure to the outstanding principal including interest shall not exceed —

(i) the following percentage of the insurer's qualified sum for secured obligation:

i. 20% during the year 2017;
ii. 15% during the year 2018; and
iii. 10% during the year 2019 and thereafter; and

(ii) the following percentage of the insurer's qualified sum for unsecured obligation:

i. 15% during the year 2017;
ii. 10% during the year 2018; and
iii. 5% during the year 2019 and thereafter.

(f) ***for other obligations —*** the net retained exposure shall not exceed such percentage of such amount as the Commission may notify from time to time through notification.

(2) An insurer shall limit its net retained exposure under any single non-financial guarantee insurance policy issued by the insurer as follows:

(a) ***for fidelity bonds —*** the net retained exposure shall not exceed the following percentage of the insurer's qualified sum:

   i. 10% during the year 2017;
   ii. 7.5% during the year 2018; and
   iii. 5% during the year 2019 and thereafter;

(b) ***for bid bonds —*** the net retained exposure shall not exceed the following percentage of the insurer's qualified sum:

   i. 15% during the year 2017;
   ii. 10% during the year 2018; and
   iii. 5% during the year 2019 and thereafter;

(c) ***for Mobilization advance guarantees —*** the net retained exposure shall not exceed the following percentage of the insurer's sum insured:

   i. 20% during the year 2017;
   ii. 15% during the year 2018; and
   iii. 10% during the year 2019 and thereafter;

(d) ***for payment bonds —*** the net retained exposure shall not exceed the following percentage of the insurer's qualified sum:

   i. 15% during the year 2017;
   ii. 10% during the year 2018; and
   iii. 5% during the year 2019 and thereafter;

(e) ***for performance bonds —*** the net retained exposure shall not exceed the following percentage of the insurer's qualified sum:

   i. 15% during the year 2017;
   ii. 10% during the year 2018; and
   iii. 5% during the year 2019 and thereafter;

(f) ***for administration bonds —*** the net retained exposure shall not exceed the following percentage of the insurer's qualified sum:

   i. 20% during the year 2017;
   ii. 15% during the year 2018; and
   iii. 10% during the year 2019 and thereafter;

(g) ***for bail bonds —*** the net retained exposure shall:

I. not exceed the following percentage of the insurer's qualified sum, in case the underlying policy / bond covers the bail amount only:

   i. 20% during the year 2017;
   ii. 15% during the year 2018; and
   iii. 10% during the year 2019 and thereafter;

II. not exceed the following percentage of the insurer's qualified sum, in case the underlying policy / bond cover any other financial obligation towards any other person, as may be decided by the court:

   i. 20% during the year 2017;
   ii. 15% during the year 2018; and
   iii. 5% during the year 2019 and thereafter.

(h) ***for custom bonds* —** the net retained exposure shall not exceed the following percentage of the insurer's qualified sum:

   i. 20% during the year 2017;
   ii. 15% during the year 2018; and
   iii. 10% during the year 2019 and thereafter.

(i) ***for other non-financial guarantees / bond policies* —** the net retained exposure shall not exceed such percentage of the insurer's qualified sum as the Commission may notify from time to time through notification.

(3) An insurer shall procure collateral in case of non-financial guarantees / bonds, and eligible collateral in case of financial guarantees, of an amount equivalent to the 80 percent of the sum insured less reinsurance in respect of a particular guarantee / bond.

(4) An insurer shall, at all times, ensure that the aggregate net retained exposure on all policies, on which these rules apply, shall not exceed the greater of 100 percent or such other percentage as the Commission may notify from time to time through notification, of the insurer's qualified sum less minimum solvency requirement as prescribed under section 36 of the Ordinance.

5. Contingency reserves— (1) In addition to the provisions and reserves required to be maintained by an insurer under the Securities and Exchange Commission (Insurance) Rules, 2002, an insurer shall maintain a reserve to be called the contingency reserve by transferring to it as at the end of each accounting period ending on or after the thirty first day of December 2019:

(a) in respect of every financial guarantee insurance policy issued by the insurer which is in force during the accounting period to be calculated as the higher of the following:

   i. 3.33% of net premiums written in respect of that policy; or

ii. the relevant percentage of the sum insured under that policy, net of reinsurance; or

iii. an amount to be calculated as per the formula notified by the Commission.

(b) in respect of every non-financial guarantee insurance policy issued by the insurer which is in force during the accounting period to be calculated as an amount equivalent to the higher of the following —

i. 10% of net premiums written in respect of that policy; or

ii. an amount to be calculated as per the formula notified by the Commission.

(2) In respect of the financial guarantee insurance policies issued by an insurer, the insurer shall not be required to make the transfer to the contingency reserve under sub-rule (1)(a) at the end of an accounting period if the contingency reserve at the end of that accounting period, but before any transfer under that sub-rule is made, is equal to or more than 4 times the highest of the following amounts:

(a) the amount of total net premiums written in respect of all financial guarantee insurance policies in force during that accounting period;

(b) the amount of total net premiums written in respect of all financial guarantee insurance policies in force in the preceding accounting period; or

(c) the amount of total net premiums written in respect of all financial guarantee insurance policies in force in the accounting period which precedes the accounting period referred to in sub-paragraph (b).

(3) In respect of the non-financial guarantee insurance policies issued by an insurer, the insurer shall not be required to make the transfer to the contingency reserve under sub-rule (1)(b) at the end of an accounting period if the contingency reserve at the end of that accounting period, but before any transfer under that sub-rule is made, is equal to or more than 50 percent of the insurer's aggregate net retained exposure on all such policies.

(4) Where the total net claims settled by an insurer during an accounting period in respect of all policies issued by the insurer, falling within the purview of these rules, exceed 80% of the total net premiums written in respect of all such policies which are in force during that accounting period, the insurer may withdraw from the contingency reserve maintained by the insurer an amount which is no greater than the difference between the total net claims settled and 80% of the total net premiums written for that accounting period.

(4) In this rule —

(a) "net claims settled", in relation to an accounting period, means the gross claims paid, including any portfolio losses, any increase or decrease (as the case may be) in outstanding claims during the period, and any medical or legal expense incurred directly in settlement of claims paid in the period, net of recoveries from salvages, subrogation and reinsurance business ceded, where applicable;

(b) "net premiums written" means the net amount of premiums after deduction of return premiums and payments in respect of reinsurance business ceded;

(c) "outstanding claims" means the incurred claims which have been reported but not yet paid and not reported to the insurer for payment, and includes expenses associated with the settlement of such claims;

(d) "relevant percentage", in relation to the sum insured under a financial guarantee insurance policy, means —

i. 0.037% of the sum insured, where the policy is issued in respect of a government obligation which is of investment grade;

ii. 0.057% of the sum insured, where the policy is issued in respect of a government obligation which is not of investment grade;

iii. 0.067% of the sum insured, where the policy is issued in respect of an infrastructure obligation which is of investment grade;

iv. 0.167% of the sum insured, where the policy is issued in respect of an infrastructure obligation which is not of investment grade;

v. 0.1% of the sum insured, where the policy is issued in respect of any financial obligation (other than a government or infrastructure obligation) which is of investment grade; or

vi. 0.167% of the sum insured, where the policy is issued in respect of any financial obligation (other than a government or infrastructure obligation) which is not of investment grade.

(5) For the purposes of the definition of "relevant percentage" in sub-rule (4), an obligation is of investment grade if, as at the end of the accounting period in question, it is in one of the top four generic lettered rating classifications (or their equivalent) awarded by a recognized credit rating agency.

6. Treatment for Collateral Procured by an Insurer and Settlement of Claim— (1) The amount of collateral procured by an insurer shall be kept in a separate bank account of the insurer in compliance with section 226 of the Companies Ordinance, 1984 (in case the collateral, partially or wholly, is procured in cash). The collateral shall be held in trust and shall be recorded as liability of that insurer until guarantee / bond is either called (i.e. claim is lodged) or the underlying guarantee / bond policy expires.

(2) In case of expiry of the guarantee / bond, the insurer shall return the collateral in full to the policyholder, after giving a notice of at least thirty (30) days to the named beneficiary of the underlying guarantee / bond, thereby clearly stating:

(a) the underlying guarantee / bond has expired on <date>;

(b) the beneficiary of the underlying guarantee / bond has not filed any claim (if applicable) and that in case the beneficiary has any claim to file, the same may be intimated to the insurer within thirty (30) days from the date of receipt of the notice. Failure to file / intimate any claim by the beneficiary shall absolve the insurer from its liability under the guarantee / bond:

Provided that the insurer shall not be absolved from its liability under the guarantee / bond in terms of sub-rule (2), in case of any litigation or legal proceeding relating to the said guarantee / bond is pending before any Court or Tribunal.

Provided further that the notice shall be sent via registered post or through a renowned courier service to the named beneficiary of an expired guarantee / bond on his last known address, the record of which shall be kept by the insurer at its registered office.

(3) In case no claim is filed / intimated on a particular guarantee / bond after the notice period, the insurer shall return the collateral to the policyholder, in full, within seven (07) days from the expiry of the notice period.

(4) In case a claim is filed / intimated on a particular guarantee / bond, the insurer shall settle the claim in accordance with the terms of that guarantee / bond.

Provided that during the course of settlement of claim, the insurer shall not require the policyholder or the named beneficiary of a particular guarantee / bond to provide any document, which has no material effect on the decision of the insurer to honor the claim on a particular guarantee/bond.

7. Pricing and Underwriting Policies— (1) Every insurer desirous to offer any insurance policy on which these rules apply shall, within a period of four months from the date of notification of these rules, be required to formulate detail pricing and underwriting policies in respect of all types of insurance policies as provided in rule 4, which shall be duly approved by the board of directors of that insurer.

Explanation: The underwriting policy shall enable the insurer to ensure that:

a. before the issuance of a guarantee insurance policy, all factors (including but not limited to, any contractual arrangements between the policyholder and the named beneficiary of a guarantee/bond) affecting the underlying policy have been properly considered and evaluated;

b. the collaterals received are properly evaluated and the guarantees/bonds are issued with due care.

(2) The policies formulated in pursuance of sub-rule (1) shall be filed with the Commission on or before the expiry of the period provided above.

8. Disclosure to Policyholder— (1) An insurer offering any insurance policy on which these rules apply shall, at all times, ensure that prior to the sale of an insurance policy, the relevant policy document shall contain a legible disclosure, in writing in both English and Urdu languages, of all policy terms including but not limited to the premium rate to be charged from the policyholder, risk(s) to be covered, exclusions (or risks not covered under the policy), coverage limits, duration of the policy, claims procedure and any other information which is required to be disclosed to the policyholder in order for him to make an informed decision about whether to purchase that policy or not.

(2) In addition to the disclosure in written form, the insurer shall also ensure that the policyholder has been explained verbally about such details and the insurer shall be required to obtain a handwritten, signed and/or stamped declaration by the policyholder stating his understanding of the policy being purchased, which shall, at all times, be kept at the registered office of the insurer.

9. Additional returns— (1) Every insurer offering a financial guarantee insurance policy in a particular accounting period, shall be required to submit the statements, for each such accounting period, along with the regulatory returns to be filed in pursuance of section 46 of the Ordinance, in the appropriate form set out in the Form GCS-1 in the Annexure hereto in addition to the returns to be lodged under section 46 of the Ordinance and / or any other section of the Ordinance or rule made thereunder.

(2) Every insurer offering a non-financial guarantee insurance policy in a particular accounting period, shall be required to submit the statements, for each such accounting period, along with the regulatory returns to be filed in pursuance of section 46 of the Ordinance, in the appropriate form set out in the Form GCS-2 in the Annexure hereto in addition to the returns to be lodged under section 46 of the Ordinance and / or any other section of the Ordinance or rule made thereunder.

(3) Any document to be submitted by an insurer under this rule shall be submitted in the manner as is applicable on the regulatory returns required to be submitted under section 46 and section 51 of the Ordinance.

ANNEXURE

FORM GCS-1
(Rule 9(1) of the Credit and Suretyship (Conduct of Business) Rules, 2016)

Statement of Credit and Suretyship Business Underwritten (Financial Guarantees)

S. No.	Policy Number	Policy Type (As specified under Rule 3(1) of the Credit & Suretyship Business Rules, 2015)	Policy Issuance Date	Premium Charged from the Policyholder (Excluding levies)	Opening Unearned Premium	Closing Unearned Premium	Sum Insured / Covered	Eligible Collateral	Net Exposure	Net Retained Exposure	Contingency Reserve

Statement of Claims Relating to Credit and Suretyship Business Underwritten (Financial Guarantees)

S. No.	Policy Number	Policy Type (As specified under Rule 3(1) of the Credit & Suretyship Business Rules, 2015)	Policy Issuance Date	Sum Insured / Covered	Claimed Amount	Claim Lodging Date	Date of Completion of All Documentation w.r.t Claim Lodged	Eligible Collateral Withheld	Claim Paid	Claim Payment Date

FORM GCS-2
(Rule 9(2) of the Credit and Suretyship (Conduct of Business) Rules, 2016)

Statement of Credit and Suretyship Business Underwritten (Non-Financial Guarantees / Bonds)

S. No.	Policy Number	Policy Type (As specified under Rule 3(2) of the Credit & Suretyship Business Rules, 2015)	Policy Issuance Date	Premium Charged from the Policyholder (Excluding levies)	Opening Unearned Premium	Closing Unearned Premium	Sum Insured	Collateral Kept by the Insurer		Net Exposure	Net Retained Exposure	Contingency Reserve
								Eligible Collateral	Form and Value of Other Collateral(s)			

Statement of Claims Relating to Credit and Suretyship Business Underwritten (Non-Financial Guarantees / Bonds)

S. No.	Policy Number	Policy Type (As specified under Rule 3(2) of the Credit & Suretyship	Policy Issuance Date	Sum Insured	Claimed Amount	Claim Lodging Date	Date of Completion of All Documentation w.r.t Claim Lodged	Eligible Collateral Withheld	Claim Paid	Claim Payment Date

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2/6/16

(Bushra Aslam)
Secretary to the Commission