SECP

# SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

**Adjudication Department- I**

**Adjudication Division**

*Through Courier*

*Before*

**Shahzad Afzal Khan, Director / Head of Department (Adjudication-I)**

*In the matter of*

**IGI General Insurance Limited**

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|---|---|
| Show Cause Notice No. and Issue Date: | ID/Enf/IGIGeneral/2017/946<br>May 19, 2023 |
| Date of Hearing: | June 14, 2023 |
| Attended By: | Mr. Nadeem Ahmed, Legal Counsel<br>(Authorized Representative) |

## ORDER

**Under rule 10(1)(k) read with rule 20(1) of the Takaful Rules, 2012 and Section 156 of the Insurance Ordinance, 2000**

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This Order shall dispose of the proceedings initiated in the matter of **IGI General Insurance Limited** on account of alleged contraventions of rule 10(1)(k) read with rule 20(1) of the Takaful Rules, 2012 **(the Takaful Rules)** and Section 156 of the Insurance Ordinance, 2000 **(the Ordinance)** vide Show-Cause Notice No. ID/Enf/IGIGeneral/2017/946 dated May 19, 2023 **(the SCN)**.

2. The Company is registered under the Ordinance to undertake the non-life insurance business in Pakistan.

3. During the examination of the annual audited accounts and regulatory returns of the Company for the year ended December 31, 2021 **(FY 2021)**, it has been observed that in Form GJT-WTO while computing the solvency of Participants Takaful Fund **(PTF)**, the Company has taken receivable balance from the Operator Fund amounting to Rs. 105.339 million as admissible, which, prima facie, is in contravention of rule 10(1)(k) of the Takaful Rules. Had this balance been taken as inadmissible, total admissible assets of PTF net of liabilities, would have fallen deficient by the same amount.

4. It has been further observed that the Company failed to meet the deficit in PTF by way of actual transfer of funds as *Qard-e-Hasna*, as required by rule 20 (1) of the Takaful Rules. Instead, the Company has recorded *Qard-e-Hasna* against a receivable balance from the Operator's Fund, which does not satisfy the requirements of the law.

5. The aforesaid observation was taken up with the Company vide email dated April 18, 2023 and in response thereof, the Company vide email dated May 4, 2023 has responded as under:

> *"...we would like to inform the Commission that Participant Takaful Fund (PTF) experienced deficit of Rs. 95 million during the year ended December 31, 2021 which was significantly attributable to actuarial based provisions / reserve related to accumulated Incurred but Not Reported (IBNR) claims*

*and Contribution Deficiency calculated in accordance with SECP guidelines aggregating Rs. 52.916 million which could not be calculated prior to yearend. Therefore, management based on actuarial advice, recorded these provisions/reserves in financial statements for the year ended December 31, 2021 which contributed in solvency shortfall of Rs. 105.339 million as at December 31, 2021 together with other inadmissible assets calculated in accordance with provisions of Insurance Ordinance, 2000 related to solvency. Accordingly, management funded the deficit in PTF by way of an interest free loan (Qard-e-hasan) from Operator Fund (OPF) amounting to Rs. 105.339 million recording a receivable against Qard-e-hasan from OPF. Since, the calculation of amount of deficit in PTF was subject to finalization of actuarial report and annual statutory audit, the determination of shortfall in solvency and actual transfer of funds was not practically possible before year end. However, the management duly complied with the requirement of actual transfer of funds as soon as audited accounts for the year ended December 31, 2021 were approved by the Board of Directors and procedural formalities related to corporate approvals for transfer of funds were duly completed by March 31, 2022... "*

6. The aforesaid stance of the Company is not considered as cogent keeping in view the requirements of rule 10(1)(k) of the Rules, which provides that in case of General Takaful, each participant takaful fund shall, *at all times*, have admissible assets in excess of its liabilities and if *at any point in time* admissible assets are not sufficient to cover the liabilities, *Qard-e-Hasnā* (interest-free loan) needs to be provided in terms of rule 20(1) of the Rules. In this regard, no exemption of any sort is available under the applicable provisions of the law. Hence, it is evident from the response of the Company that as at December 31, 2021, the Company's PTF was in deficit but no *Qard-e-Hasna* (interest-free loan) was actually transferred from the Operator's Fund to PTF in order to meet the deficit. Therefore, the Company, prima facie, did not meet the mandatory requirements of rules 10(1)(k) and 20(1) of the Rules, which are reproduced as under:

**Rule 10(1)(k) of the Rules;**
***"Conditions applicable to Operator. - (1)** An Operator, -*
...
*(k) shall ensure that in case of General Takaful each Participant Takaful Fund, at all times, has admissible assets in excess of its liabilities:*
*Explanation: For this purpose any amount receivable from the Operator shall be deemed to be inadmissible."*

**Rule 20(1) of the Rules:**
*"**Qard-e-hasna:** - (1) In the case of a General Takaful if, at any point in time admissible assets in a Participant Takaful Fund are not sufficient to cover liabilities, the deficit shall be funded by way of actual transfer of funds as qard-e-hasna (interest free loan) from the Operator's Fund to that Participant Takaful Fund."*

**Section 156 of Insurance Ordinance, 2000;**
*"**Penalty for default in complying with, or acting in contravention of this Ordinance.** Except as otherwise provided in this Ordinance, any insurer who makes default in complying with or acts in contravention of any requirement of this Ordinance, or any direction made by the Commission, the Commission shall have the power to impose fine on the insurer and, where the insurer is a company, any director, or other officer of the company, who is knowingly a party to the default, shall be punishable with fine which may extend to one million rupees and, in the case of a continuing default, with an additional fine which may extend to ten thousand rupees for every day during which the default continues."*

7. Accordingly, SCN was served on the Respondent Company, calling upon it to show cause in writing within 14 days of the date of the SCN as to why penalty may not be imposed on it for contravening the aforesaid provisions of the law.

8. In response to SCN, the Company submitted its reply vide letter dated June 1, 2023, which is summarized as under:

(i) The PTF experienced deficit of Rs. 95 million during the year ended December 31, 2021 which resulted in shortfall in admissible assets against liabilities as at December 31, 2021.

(ii) The Operator recorded additional reserving / claims intimated near year-end amounting to Rs. 48.359 million on net basis during the year-end closing process which concluded subsequent to the year-end.

(iii) The Company, based on actuarial advice, recorded provision against IBNR and CDR aggregating to Rs. 52.916 million as at the year ended December 31, 2021, which could not be calculated prior to or on December 31.

(iv) The additional provisioning led to increase in liabilities of PTF which eventually resulted in deficit in PTF by Rs. 95 million and a shortfall of admissible assets over liabilities as at the year ended December 31, 2021 by Rs. 105.339 million.

(v) The determination of shortfall in solvency and actual transfer of funds was not practically possible before year-end. However, in order to express its commitment to maintain solvency of PTF, the management recorded a Qard-e-Hasan receivable from OPF of Rs. 105.339 million in PTF in the audited financial statements for the year ended December 31, 2021.

(vi) Subsequently, the management duly transferred the funds as soon as audited financial statements for the year ended December 31, 2021 were approved by the Board of Directors and procedural formalities related to corporate approvals for transfer of funds were duly completed by March 31, 2022.

(vii) In order to improve the profitability and solvency of PTF in future, the Operator re-assessed the Wakalah Fee rates charged by OPF to PTF against the expected acquisition cost and administrative cost for the financial year 2022 and reduced the wakalah Fee rates which, eventually, resulted in surplus of Rs 26.614 million in the audited financial statements for the year ended December 31 2022.

(viii) Moreover, the Operator also enhanced monitoring of solvency position of PTF during the year and took steps to reduce inadmissible assets as at the year ended December 31, 2022. Accordingly, the Operator posted admissible assets of Rs. 32.155 million in excess of its liabilities in PTF as reported in the audited regulatory return for the year ended December 31, 2022.

(ix) The Company has now taken further steps to improve the profitability of PTF as well as strengthen the process of recovery or its receivables to improve solvency margins of PTF in order to avoid the recurrence of such situation in future.

(x) We trust that the above-mentioned explanation / submissions would be considered and would request you to take into consideration the practical difficulties faced by the PTF and the additional steps undertaken to address these issues. In this background, we request you to take a lenient view on the matter and request you to condone the delay.

(xi) We trust that keeping in view the above-mentioned facts and particularly the circumstances which clearly show that the Company did not intentionally or willfully perpetrate any violation, you would show your kind indulgence in appreciating the position obtaining in the matter.

9. In order to provide the Respondent Company an opportunity of personal representation, hearing in the matter was fixed for June 14, 2023. The hearing was attended by Mr. Nadeem Ahmed, Legal Counsel as the Authorized Representative of the Respondent (**The Representative**). The Representative was advised to explain the reasons for the non-compliance, as narrated in the SCN. The Representatives reiterated the submissions already made in the written reply dated June 1, 2023.

10. I have reviewed the facts of the case and considered the written as well as verbal submissions of the Respondent Company, in light of the applicable provisions of the law and observed as under:

(a) The Company has stated that based on actuarial advice, an aggregate provision of Rs. 52.916 million for Incurred But Not Reported Claims (IBNR) and Contribution Deficiency Reserve (CDR) was made as at the year ended December 31, 2021 which could not be calculated prior to or on year-end. It has been further stated that the said additional provisioning led to an increase in liabilities of PTF which eventually resulted in deficit in PTF by Rs. 95 million and a shortfall of admissible assets over liabilities as at the year ended December 31, 2021 by Rs. 105.339 million. In view of the foregoing position, determination of shortfall in solvency and actual transfer of funds was not practically possible before year-end. However, in this regard, it needs to be emphasized that rule 10(1)(k) of the Takaful Rules requires that "*each Participant Takaful Fund, at all times, has admissible assets in excess of its liabilities.*" Therefore, in order to comply with the foregoing provisions of the law, the Company should have carried out appropriate assessment of shortfall in PTF at all times in light of its claim experience for the respective previous quarters rather than deferring it for accumulation of deficit at year-end. This assessment would have allowed the Company to make adequate provisioning in PTF on quarterly basis. Thus, the Company could have made a careful estimate of the amount of deficit in PTF through appropriate monitoring and could have ensured solvency of PTF by making actual transfer of *Qard-e-Hasna* from the Operator's Fund to PTF to meet the deficit. However, the Company neither ensured solvency of PTF at all times throughout the year nor made actual transfer of *Qard-e-Hasna* from the Operator Fund to PTF to meet the deficit. Therefore, the Company has violated the requirements of rule 10(1)(k) read with rule 20(1) of the Takaful Rules.

(b) The Company has taken stance that determination of shortfall in solvency of PTF and actual transfer of funds was not practically possible before year-end. In this regard, it may be noted that the Company could have carried out appropriate monitoring of solvency of PTF under which admissible assets and liabilities of PTF could have been worked out to determine the shortfall. For this purpose, in addition to other relevant statements, quarterly statements of assets and liabilities could have been used.

(c) The Company has stated that it has taken rectification measures to improve solvency of PTF in subsequent year i.e. FY 2022, which includes reduction in wakalah fee, strengthening recovery of receivables, reduction in inadmissible assets and monitoring of solvency. Had the Company implemented these measures on quarterly basis in FY 2021 and carried out effective monitoring, the Company could have ensured solvency of PTF at all times in FY 2021.

(d) It has been further stated in reply of the Company that in order to express its commitment to maintain solvency of PTF, the management recorded "Qard-e-Hasna Receivable" of Rs. 105.339 million from the Operator Fund in PTF. In this regard, it needs to be noted that Explanation to rule 10(1)(k) of the Takaful Rules has categorically clarified that "*For this purpose any amount receivable from the Operator shall be deemed to be inadmissible.*" Therefore, "Qard-e-Hasna Receivable" cannot be considered as an admissible asset for solvency of PTF.

11. In exercise of the powers conferred on me under Section 156 of the Ordinance, I hereby, impose a penalty of **Rs. 200,000/- (Rupees Two Hundred Thousand Only)** on the Company on account of established violations of rule 10(1)(k) read with rule 20(1) of the Takaful Rules, as mentioned in the above paras. The Respondent Company is also warned to ensure compliance with all the applicable regulatory requirements including those of the Takaful Rules, in true letter and spirit, in future.

12. The Company is hereby directed to deposit the afore-mentioned penalty in the designated Bank Account maintained in the name of the Securities and Exchange Commission of Pakistan with MCB Bank Limited or United Bank Limited within thirty (30) days of the date of this Order and furnish receipted voucher evidencing payment of the same.

13. This Order is being issued without prejudice to any other action that the Commission may initiate against the Company and / or its management (including CEO of the Company) in accordance with the law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.

**Shahzad Afzal Khan**
Director/Head of Department
(Adjudication Department-I)

**Announced:**
October 19, 2023
Islamabad