SECP
INSURANCE DIVISION
Islamabad

<u>*Before Tahir Mahmood, Commissioner (Insurance)*</u>

In the matter of

Atlas Insurance Company Limited

Show Cause Notice No. and Issue Date:	ID/Enf/Atlas/2018/13202 dated January 11, 2018
Date of Hearing:	October 11, 2018
Attended By:	Mr. Rashid Amin Chief Financial Officer M/s. Atlas Insurance Company Limited
Date of Order:	October 24, 2018

ORDER

Under Rule 15 of the Insurance Rules, 2017 read with Section 11(1)(c), Section 36 and Section 156 of the Insurance Ordinance, 2000

....

This Order shall dispose of the proceedings initiated against M/s. Atlas Insurance Company Limited (the "Company"), its Chief Executive and Directors for alleged contravention of Rule 15 of the Insurance Rules, 2017 (the "Rules") read with Section 11(1)(c) and Section 36 of the Insurance Ordinance, 2000 (the "Ordinance"). The Company and its Directors shall be collectively referred to as the "Respondents" hereinafter.

2. The Company is registered under the Ordinance to carry on the business of non-life insurance and General Takaful/Window Takaful in Pakistan.

3. While examining the annual audited accounts and regulatory returns of the Company for the year ended December 31, 2016, it was revealed that admissible assets of the Company were in excess of its liabilities by an amount of Rs. 195.092 million.

4. The solvency margin as of greatest of three methods, as prescribed under Section 36 of the Ordinance read with Rule 15 of the Rules, was Rs. 213.241 million as on December 31, 2016. Hence, the Company did not meet the minimum solvency requirement by an amount of Rs. 18.149 million as calculated below:-

SECURITIES AND EXCHANGE
COMMISSION OF PAKISTAN
Insurance Division, NIC Building,
63 Jinnah Avenue, Islamabad, Pakistan

PABX: +92-51-9207091-4, Fax : +92-51-9100496, Web: www.secp.gov.pk

METHOD	HEAD/ACCOUNT	2016
Method A	Section 36 (3a)	
	As Prescribed By The Commission	150,000,000
Method B	Section 36 (3b)	
	Gross Earned Premium	2,132,414,000
	Less - Reinsurance Expense (Upto 50%)	1,066,207,000
	Earned Premium	1,066,207,000
	20% of Earned Premium	213,241,400
Method C	Section 36 (3c)	
	Provision For Unearned Premium (UC)	963,485,000
	Provision For Outstanding Claims (OC)	414,528,000
	Sub-total Provisions	1,378,013,000
	Less Prepaid Reinsurance Premium (Upto 50%)	481,742,500
	Less Reinsurance Recoveries Against OC (Upto 50%)	207,264,000
	Less-Sub-total	689,006,500
	Total Unearned Premium & Outstanding Claims (T UC&OC)	689,006,500
	20% of Total UC&OC	137,801,300
Solvency Calculations		
	Admissible Assets As Per Auditor's Regulatory Return	2,426,157,000
	Liabilities As Per Annual Accounts	2,231,065,000
	Excess Assets Over Liabilities	195,092,000
		213,241,400
Solvency Requirement		
	Solvency Requirement (Greatest of Method A,B &C)	213,241,400
	Excess Solvency Margin Over Minimum Requirement	(18,149,400)
	Solvency Ratio	0.91
	Solvent (Yes/No)	No

5. The Commission vide letter dated September 5, 2017 advised the Company to clarify its stance over the deficit in the solvency margin. In response, the Company, vide letter dated September 21, 2017, replied as under:-

> *"the minimum solvency margin requirement was Rs. 213.241 million. The admissible assets as determined in Form – GJ of Rs. 2,426 million does not include Rs. 19.4 million being amount of deposit against performance bonds. However, admissible liabilities of Rs. 2,231 million mentioned in your letter includes liability in respect of deposit against performance bond of Rs. 19.4 million which needs to be excluded from the admissible liabilities for comparison purposes. After excluding the above amount the admissible liabilities are Rs. 2,190 million and the solvency margin is Rs. 235.5 million (Rs. 2,426 million – Rs. 2,190 million) which is above the minimum solvency requirement of Rs. 213.241 million".*

6. The Company's stance was not justified because the deposit against performance bonds amounting to Rs. 19.4 million was not admissible as per Section 32(2)(k) of the Ordinance. However, the corresponding liability could not be excluded from the total liabilities of the Company as per Section 36(1) of the Ordinance.

7. Hence, it appeared to the Commission that the Company failed to meet the mandatory requirements relating to the minimum solvency as given under Rule 15 of the Rules read with Section 11(1)(c), and Section 36 of the Ordinance .

8. Section 11(1)(c) of the Ordinance states that:

> *"**Conditions imposed on registered insurers**. - (1) An insurer registered under this Ordinance shall at all times ensure that:*
>
> .....
>
> *(c) the provisions of this Ordinance relating to minimum solvency requirements are complied with;*
>
> ..... "

9. The relevant provisions of Section 36 of the Ordinance state that:

> *"**Insurers of non-life insurance business to have assets in excess of minimum solvency requirement. -** (1) An insurer registered under this Ordinance to carry on non-life insurance business shall at all times have admissible assets in Pakistan in excess of its liabilities in Pakistan of an amount greater than or equal to the minimum solvency requirement.*
>
> *(2) An insurer incorporated in Pakistan and registered under this Ordinance to carry on non-life insurance shall at all times have admissible assets in excess of its liabilities of an amount greater than or equal to the minimum solvency requirement.*
>
> *(3) For the purposes of this section, the minimum solvency requirement is the greatest of:*
>
> *(a) such required minimum amount as may be prescribed by the Commission;*

(b) such percentage as may be prescribed by the Commission of its earned premium revenue in the preceding twelve months, net of reinsurance expense subject to a maximum deduction for reinsurance of fifty per cent of the gross figure; and

(c) such percentage as may be prescribed by the Commission of the sum of its liability for unexpired risk and its liability for outstanding claims, net of reinsurance subject to a maximum deduction for reinsurance in each case of fifty per cent of the gross figure:

Provided that in the case of an insurer incorporated in a jurisdiction outside Pakistan the amounts set out in clauses (b) and (c) of this sub-section shall be calculated with reference to the earned premium revenue, unexpired risk liability and outstanding claims liability and related reinsurance balances of that insurer in respect of its insurance business in Pakistan only.

(4) The Commission may direct an insurer not to deal with any specified asset for any specified period of time in order to ensure compliance by the insurer with the provisions of this Part."

10. The relevant provisions of Rule 15 of the Insurance Rules, 2017[1] (the "Rules") state that:

"Solvency of non-life insurer. - *(1) For the purposes of clause (a) of subsection (3) of section 36 of the Ordinance, the following shall be the prescribed amount, namely:-*

(a) till 31 December 2011, fifty million rupees; and
(b) thereafter as per the following table:

On or After	***Rupees***
31 December 2012	*One hundred million*
31 December 2013	*One hundred and twenty five million*
31 December 2014	*One hundred and fifty million*

(2) For the purposes of clause (b) of sub-section (3) of section 36 of the Ordinance, the prescribed percentage shall be twenty per cent.

(3) For the purposes of clause (c) of sub-section (3) of section 36 of the Ordinance, the prescribed percentage shall be twenty per cent. "

11. Accordingly, a Show Cause Notice (SCN) No ID/Enf/Atlas/2018/13202 dated January 11, 2018 was issued to the Respondents, calling upon them to show cause as to

[1] Rule 13 of the Securities and Exchange Commission (Insurance) Rules, 2002

why the fine as provided under Section 156 of the Ordinance should not be imposed on them for the aforementioned alleged contraventions of the law.

12. Thereafter, the Respondents submitted their reply vide letter dated January 22, 2018, as under:-

"......
In this regard we would like to submit that full compliance with the law is of utmost importance for Atlas Insurance Limited and we always endeavor to make sure that as a responsible company we comply with all the legal requirements unless it is due to unintentional oversight or divergent interpretation of law.

We would like to make following submissions in support of our plea that Atlas Insurance Limited has met the solvency requirements as per the Insurance Ordinance, 2000.

(a) The calculation given in para 6 of your show cause notice whereby the solvency margin of the Company is calculated as Rs. 195.092 million as difference of admissible assets of Rs. 2,426.157 million and admissible liabilities of Rs. 2,231.065 million. The minimum required solvency margin is Rs. 213.241 million and hence the shortfall as per your calculation is Rs. 18.149 million.

(b) It may please be noticed that although the admissible assets do not include the balance of the bank account containing the deposit against performance bonds of Rs. 19.421 million, the liabilities do include this amount. This bank account is specifically opened to keep the funds which will be used to settle the corresponding liability appearing as deposit against the performance bonds only. We have a number of historical transactions to prove that money from this specific bank account is used to settle liability appearing as deposit against the performance bond. The question is that if deposit against performance bond was not specifically addressed as inadmissible liability in the Insurance Ordinance from where this liability will be discharged, will it be discharged from the general funds of the Company present in other bank accounts or through this specifically maintained separate bank account. It is always deemed to be understood that the deposit against performance bond will be returned through a cheque from this specific separate Bank account opened under Section 226 of the Companies Ordinance, 1984. It is under this premise that since liability appearing as deposit against performance bonds will be settled through this separate bank account in order to determine the solvency this separate bank account will be excluded from the admissible assets along with its corresponding liability. Moreover, when the Company receive this deposit from its customer this receipt necessitates the creation of liability along with the corresponding assets through a journal entry by debiting asset (Bank Account) and crediting liability(Deposit against performance bond) in the books of accounts of the company.

(c)Therefore, if we exclude this liability from the liabilities appearing in annual accounts of Rs. 2,231.065 the liabilities that will be met through admissible assets which amount to Rs. 2,211.644 million, the solvency margin becomes Rs. 214.513 million which is above the minimum required solvency margin of Rs. 213.241 million.

2. *We may add here that additionally the investments of Rs. 927.697 million in the mutual funds of Atlas Asset Management have not been considered as admissible assets under section 32(2)(g) of the Insurance Ordinance. As you know that these are funds that are separately managed and are under the custody of trustees and they are readily available to the Company through redemption at NAV which have not been accounted for the purpose of this calculation. Your goodself is aware of the fact that such funds though placed with associated company but are not considered as 'investment' but can be taken as admissible assets for the purpose of calculating solvency margin. In our humble opinion due credit should also be given against these investments to the company by considering as assets that are available for meeting the liabilities.*

3. *We have taken adequate steps in the year ended December 31, 2017 to ensure that we have sufficient admissible assets available in good amount not only to meet but substantially exceed our solvency margins to avoid such tight neck situation which we can share with you.*

Despite all these, we sincerely apologies for the misunderstanding purely unintentional/or interpreting the statute differently and assure you that in future we will be more vigilant in maintaining the solvency margin and generally complying with all the requirements of the law.

We therefore request you that a lenient view may please be taken and this inadvertent misunderstanding be ignored and condoned being unintentional."

13. The Commission, vide its notice no. ID/Enf/Atlas/2018/15298 dated June 11, 2018, scheduled the hearing for June 22, 2018 at the Head Office of the Commission in Islamabad. However, the said hearing was cancelled and rescheduled on October 11, 2018, intimated vide letter dated October 4, 2018.

14. The hearing was attended by the Authorized Representative of the Respondents namely Mr. Rashid Amin, Chief Financial Officer of the Company, representing all the Respondents before the Commission in the instant matter.

15. During the hearing, the Authorized Representative stated that the Company has complied with the minimum solvency requirement in the financial year ended December 31, 2017 as per Rule 15 of the Rules read with Section 11(1)(c), and Section 36 of the Ordinance. He regretted that the omission was caused by the Company due to different interpretation of the relevant provisions of the Ordinance. The Authorized Representative assured the Commission that in future, the Company would be more vigilant in maintaining the solvency margin and general compliance with all the requirements of the Ordinance. The Authorized Representative requested the Commission to condone the omission and take a lenient view in the instant matter.

16. In terms of Section 11(1)(c) of the Ordinance an insurer registered under the Ordinance shall at all times ensure that the provisions of this Ordinance relating to minimum solvency requirements are complied with. Furthermore, Section 36(1) of the Ordinance requires that an insurer registered under this Ordinance to carry on non-life

insurance business shall at all times have admissible assets in Pakistan in excess of its liabilities in Pakistan of an amount greater than or equal to the minimum solvency requirement. Whereas the solvency requirement for the Company for the year ended December 31, 2016 prescribed under Section 36 of the Ordinance read with Rule 15 of the Rules, was Rs. 213.241 million. However, admissible assets of the Company were in excess of its liabilities by an amount of Rs. 195.092 million only. Accordingly, a shortfall of an amount of Rs. 18.149 million was observed. Therefore, the Company did not meet the minimum solvency requirement as envisaged under the law.

17. The Company's earlier argument to exclude the liabilities against performance bonds is not tenable. It is clarified that the deposit against performance bonds amounting to Rs. 19.4 million was excluded from the admissible assets as per Section 32(2)(k) of the Ordinance, which explicitly states that, the amounts available to the insurer under guarantees are not admissible assets. Nonetheless, the corresponding liability cannot be excluded from the total liabilities of the Company as per Section 36(1) of the Ordinance. However, it has been apprised by the Company that the Company is meeting the minimum solvency requirement for the financial year ended December 31, 2017.

18. Needless to say that the Company failed to meet the required minimum solvency for the year ended December 31, 2016. The arguments, documents and evidences which have been submitted by the Respondents so far have been found to be evidencing the fact that the Company has failed to comply with Rule 15 of the Rules read with Section 11(1)(c) and Section 36 of the Ordinance.

19. I have carefully examined and given due consideration to the written and verbal submissions of the Respondents, and have also referred to the provisions of the Ordinance, the Rules made thereunder and/or other legal references. I am of the view that the violations of Rule 15 of the Rules read with Section 11(1)(c) and Section 36 of the Ordinance is clearly established, for which the Respondents may be penalized in terms of Section 156 of the Ordinance.

20. Section 156 of the Ordinance provides that:

> *"**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."*

21. In exercise of the power conferred on me under Section 156 of the Ordinance, I, instead of imposing the fine as provided under the said provision, take a lenient view,

and issue a stern warning that in case of similar non-compliance in future a strict action against the Respondents will be taken.

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

Tahir Mahmood
Commissioner (Insurance)

SECURITIES & EXCHANGE COMMISSION OF PAKISTAN