



SECP

INSURANCE DIVISION
Islamabad

Before Hasnat Ahmad, Director (Enforcement)

In the matter of

M/s. Chubb Insurance Pakistan Limited

Show Cause Notice No. and Date : ID/Enf/Chubb/2019/365 Dated April 05, 2019

Date of Hearing: August 8, 2019

Attended By: Mr. Humzah Chaudhry
Country President
M/s. Chubb Insurance Pakistan Limited

Mr. Hasan Mahmood
Company Secretary
M/s. Chubb Insurance Pakistan Limited

Mr. Furkan Ali
Legal Consul
M/s. Chubb Insurance Pakistan Limited

Date of Order: September 6, 2019

ORDER

Under Regulation 24, 26 and 28 of the Insurance Accounting Regulation Rules, 2017
read with Section 46 and Section 156 of the Insurance Ordinance, 2000

.....

This Order shall dispose of the proceedings initiated against M/s. Chubb Insurance Pakistan Limited (the "Company"), its Chief Executive and Directors for alleged contravention of Regulation 24, 26 and 28 of the Insurance Accounting Regulation, 2017 (the "Regulations") read with Section 46 of the Insurance Ordinance, 2000 (the "Ordinance"). The Company and its Directors shall be referred to as the "Respondents" hereinafter.

2. The Company is registered with the Securities and Exchange Commission of Pakistan (the "Commission") under the Ordinance to carry on general/ non-life insurance business in Pakistan.

3. Upon examination of the bancassurance returns of the Company for the year ended December 31, 2017, it was observed that the Statement of Premium (for aggregate bancassurance business and for each bank) did not disclose the amounts

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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

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related to "unearned premium reserve" and "prepaid reinsurance premium ceded" as required under Regulations 24 and 26 of the Regulations, respectively. Furthermore, the Statement of Expenses also did not disclose the amounts related to "deferred commission" as required under Regulation 28 of the Regulations.

4. As per Note 2.2 of the bancassurance returns submitted by the Company, the premium, claim and expenses were disclosed and accounted for on the same basis as mentioned in the annual audited financial statements.

5. The Commission vide examination letter dated August 20, 2018, advised the Company to provide the comments regarding non-provision of the aforementioned amounts in the bancassurance returns.

6. The Company vide letter dated December 19, 2018 while furnishing the list of its 7,605 policyholders clarified that:-

"The Company offers accidental death and disability and hospitalization products on a monthly premium through Bancassurance arrangement. During 2017 the Company had Bancassurance arrangements with three banks namely UBL, HBL, and ABL. However, new policies were only sold through UBL and the Company continued to service existing customers of HBL and ABL. The bank sent monthly MIS of premium collected that is recorded as premium written for the month, therefore, at the end of the month Unearned Premium, Prepaid Reinsurance Premium ceded and Deferred Commission Expense are nil."

7. The Company submitted the following information vide email dated January 22, 2019 in response to the Commission' letter dated January 17, 2019:

a) *"The coverage to a covered person commences from the effective date, i.e. the date on which the customer accepts to enroll in the policy, irrespective of its payment to the Company by the Bank.*

b)

S.NO	Month	MIS Period	Date Received	MIS	Cheque Date
1	July 2017	1 June 2017 to 30 June 2017	27-Jul-17		5-Jul-17
2	August 2017	1 July 2017 to 31 July 2017	23-Aug-17		3-Aug-17
3	September 2017	1 August 2017 to 31 August 2017	7-Sep-17		7-Sep-17
4	October 2017	1 September 2017 to 30 September 2017	10-Oct-17		4-Oct-17
5	November 2017	1 October 2017 to 31 October 2017	16-NOV-17		6-NOV-17
6	December 2017	1 November 2017 to 30 November 2017	19-Dec-17		6-Dec-17

c) *Policy wordings of three plans with UBL are attached."*

8. The review of the aforesaid response and MIS data of the Company and its banca partner revealed that the Company did not properly follow the Regulations while preparing the bancassurance returns.

H/O



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9. The Company did not disclose the correct amount of "unearned premium reserve" and "prepaid reinsurance premium ceded" in the Statement of Premium (for aggregate bancassurance business and for each bank) as required under Regulations 24 and 26 of the Regulations. Furthermore, the Company did not disclose the correct amounts related to "deferred commission" in the Statement of Expenses as required under Regulation 28 the Regulations.

10. Therefore, it appeared that the Company contravened the provisions of Regulations 24, 26 and 28 of the Regulations read with Section 46 of the Ordinance.

11. Regulation 24, 26 and 28 of the Regulations provide that:

"24. Premiums.- (1) *Premium receivable under a policy / cover note issued shall be recognized as written from the date of attachment of risk to the policy / cover note.*

(2) *Over the period of insurance from inception to expiry, except as stated in sub-regulation (3), premium shall be recognized as revenue as follows:*

- (i) *For direct business, evenly over the period of the policy;*
- (ii) *For proportional reinsurance business, evenly over the period of the underlying policies;*
- (iii) *For non-proportional reinsurance business, in accordance with the pattern of reinsurance service.*

(3) *Where the pattern of incidence of risk varies over the period of the policy, the premium shall be recognized as revenue in accordance with the pattern of incidence of risk.*

(4) *The unearned portion of premium income shall be recognized as a liability. Such liability shall*

(i) as a proportion of the gross premium of each policy, determined as the ratio of the unexpired period of the policy and the total period, both measured to the nearest day; or

(ii) where the majority of policies are issued for one year, the unearned premium reserve may, as an alternative to the basis specified in (i) above, be determined by applying the twenty-fourths method, whereby the liability shall equal 1/24 of the premiums relating to policies commencing in the first month of the insurer's financial year, 3/24 of the premiums relating to policies commencing in the second month of the insurer's financial year, and so on;

(iii) For treaty re-insurance business accepted, premiums are usually declared through quarterly accounts submitted by the ceding companies. Such premiums should be recognized over the period covered by each underlying policy which may be approximated by recognizing premiums on the eighths basis. Therefore the unearned premium reserve set up as at 31 December of a year should equal

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1/8 of the premium per the treaty accounts submitted in the first quarter, 3/8 of that for the second quarter, 5/8 of that for the third quarter and 7/8 of that for the fourth quarter;

(iv) For facultative acceptances the basis of recognizing premiums and determining the Unearned Premium Reserve shall be the same as for direct policies;

(v) If a company develops an alternative basis for determining reserves relating to reinsurance acceptances which it feels is more appropriate to its circumstances it may use such basis provided it discloses this fully in the notes to the financial statements.

(5) Premium/ premium adjustments not yet processed but relating to the financial year shall, so far as is practicable, be recognized as a receivable and earned over the period in accordance with these regulations.

(6) Premium revenue shall not include any levy which is an amount collected on behalf of a third party.

(7) Any levy charged on premiums which is not an amount collected on behalf of a third party shall be considered to be part of premium.

(8) Premiums accepted under a coinsurance or pool arrangement shall be considered to be revenue of the participating insurers each for their own share only, unless a contract of reinsurance exists under which an insurer has primary liability for the whole of the business and reinsures it to another or others.

(9) Where premiums for a policy are payable in installments, the full premium for the duration of the policy shall be recognized as income at the inception of the policy and a related asset set up for premiums, notwithstanding the fact that some installments may not, by agreement between the insurer and the insured, be payable until later."

"26. Reinsurance expense.- (1) Premium ceded to reinsurers must be recognized as a liability as follows:

(i) for reinsurance contracts operating on a proportional basis, on attachment of the underlying policies reinsured; and

(ii) for reinsurance contracts operating on a non-proportional basis, on inception of the reinsurance contract.

(2) Over the period of reinsurance from inception to expiry, except as stated in sub-regulation (3), reinsurance premium shall be recognized as an expense as follows:

(i) For proportional reinsurance business, evenly over the period of the underlying policies;

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(ii) For non-proportional reinsurance business, evenly over the period of indemnity.

(3) Where the pattern of incidence of risk varies over the period of the policy, the premium shall be recognized as an expense in accordance with the pattern of incidence of risk.

(4) The portion of reinsurance premium not yet recognized as an expense shall be recognized as a prepayment

(5) Premium adjustments not yet processed, and premium not yet processed but relating to the financial year shall, so far as is practicable, be recognized as a liability and brought to account as an expense in accordance with these regulations."

"28. Acquisition costs.- (1) Commissions and other incremental acquisition costs incurred in obtaining and recording policies of insurance and reinsurance may be deferred and recognized as assets where they can be reliably measured and it is probable that they will give rise to premium revenue that will be recognized in subsequent reporting periods. Incremental acquisition costs of a policy are costs of selling, underwriting and initiating an insurance policy which have been incurred because that particular policy has been issued, i.e., the costs are identified at the level of an individual policy and not at the level of a portfolio of policies. Such costs may include, for example, surveyor costs where a survey has been carried out as a part of the underwriting process.

They will not, however, include costs of permanent underwriting staff of the insurer.

(2) Deferred acquisition costs must be amortised systematically over the reporting periods over which the related premium revenue is recognized.

(3) An acquisition cost which is not incremental must be recognized as an expense during the period in which it is incurred."

12. Sections 46 of the Ordinance states that:

"(1) Every insurer shall at the expiration of each year prepare and deliver to the Commission with reference to that year annual statutory accounts comprising the following statements duly audited by an approved auditor:

in the case of a life insurer,-

(i)

(b) in the case of anon-life insurer,

(i)

(2) Every insurer shall furnish, to the Commission, following the last day of December, March, June and September in each year, a statement of assets and



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liabilities in the form and prepared in accordance with the regulations prescribed under the preceding subsection made up as of that date and such statement shall be certified by a principal officer of the insurer.

Provided that an actuarial valuation of policyholder liabilities as at the date to which such statement is made up is not required by virtue of this subsection alone, and that the regulations prescribed under this sub-section shall provide for the determination of the value which is attributed to policyholder liabilities for the purposes of this subsection.

(3) In the case of an insurer registered to conduct life insurance business, such statement shall be furnished separately in respect of each statutory fund maintained by the life insurer and in respect of the shareholders' fund.

(4) The statements referred to in the foregoing sub-sections shall be prepared in respect of all insurance business transacted by an insurer except that in the case of an insurer incorporated in a jurisdiction outside Pakistan, the statement shall be prepared in respect of the insurance business transacted by the insurer in Pakistan."

13. Accordingly, a Show Cause Notice (SCN) No. ID/Enf/Chubb/2019/365 dated April 05, 2019 was issued to the Respondents, calling upon them to show cause as to 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.

14. Thereafter, the Company vide letter dated April 25, 2019 submitted its reply to the aforesaid SCN, which is reproduced below:

"

At the outset we wish to state that compliance to country regulations is of utmost importance to the Company and we exercise due care in conduct of our business with due regard to applicable laws.

In Paras 9 and 10 of the letter you have noted that review of below table revealed that the Company did not properly follow the Regulations while preparing bancassurance returns, i.e., the Company did not disclose the correct amount of "unearned premium reserve" and "prepaid reinsurance premium ceded" in the Statement of Premium as required under Regulations 24 and 26 and "deferred commission" in the Statement of Expenses as required under Regulation 28 of the Regulations.

S. No	Month	MIS Period	Date MIS	Cheque date
1	July 2017	1 June 2017 to 30 June 2017	27-Jul-17	5-Jul-17
2	August 2017	1 July 2017 to 31 Julv2017	23-Aug-17	3-Aug-17
3	September	1 August 2017 to 31 August 2017	7-Sep-17	7-Seq-17
4	October 2017	1 September 2017 to 30 September 2017	10-Oct-17	4-Oct-17
5	November	1 October2017 to 30 October 2017	16-Nov-17	6-NOV-17
6	December 2017	1 November 2017 to 30 November 2017	19-Dec-17	6-Dec-17

It should be noted that the Company offers accidental death and disability and hospitalization products on a monthly premium through bancassurance arrangements. The cases mentioned above relate to products offered to the credit card customers of United Bank Limited and are paid for through their credit cards. The cover is for a one



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month period with an automatic renewal option.

Since the Bank collects premium by charging the credit cards of customers, the collection of premium for any given month is on an on-going basis throughout the month as each customer has a different credit card billing cycle. Accordingly, premium is collected throughout the month. As a result, it is only after the month ends that the Bank is able to generate its MIS Report for the preceding month and share the same with us.

Pursuant to the above process flow, premium recorded in December 2017 pertains to the period November 1, 2017 to November 30, 2017 (per MIS report received in December 2017). Since this is a monthly cover, the premium up to November 30, 2017 had been fully earned with the corresponding acquisition expenses and reinsurance costs also expensed within the same period thus no unearned premium reserve, prepaid reinsurance premium reserve and deferred commission are warranted. For policies issued from December 1 to December 31, 2017, the MIS report from the Bank was received in January 2018, hence premium for the same was recorded in January 2018. Our bancassurance returns reflect this position.

Further, in this regard, we wish to refer to Regulation 24(5) of the Insurance Accounting Regulations 2017 which state as under:

premium/ premium adjustments not yet processed but relating to the financial year shall, so far as is practicable (emphasis ours), be recognized as a receivable and earned over the period in accordance with these regulations.

You will appreciate that as per Black's Law Dictionary, 2nd Edition, "practicable" has been defined as "...any idea or project that can be brought to fruition or reality without any unreasonable demands..."

In the case of *Federation of Pakistan and others vs. Mian Muhammad Shahbaz Sharif* [PLD 2009 Supreme Court 391], the Hon'ble five member bench while interpreting the phrase "so far as is practicable" in a statutory provision held that "...[the statute does not] lay down an inflexible rule...rather the provision acknowledges the practical aspect of the matter by providing "as far as practicable"..."

It is clear from the above that where a legal requirement introduces the phrase 'so far as is practicable' then the duty that it qualifies has to be complied with in the light of practicalities of the situation.

Given the explanation above, you would appreciate that it was "not practicable" to record the premium for the period December 1, 2017 to December 31, 2017 during the year ended December 31, 2017 and therefore, there was no violation of Regulation 24 of the Accounting Insurance Regulations, 2017.

We reiterate that due regard to applicable law is a priority for the Company and we endeavor to remain compliant at all times. Trust the above serves to clarify our position as regards your observations on the subject and we request your understanding in the matter.

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Should you require any further information please let us know."

15. The Commission vide its notice No. ID/Enf/Chubb/2019/705 dated May 16, 2019, scheduled the hearing for May 23, 2019 at the Commission's Head Office. However, at the request of the Company, the hearing was rescheduled on August 8, 2019. The said hearing was attended by Mr. Humzah Chaudhry (Country President), Mr. Hasan Mahmood (Company Secretary), and Mr. Furkan Ali (Legal Counsel) in person as Authorized Representatives on behalf of all the Respondents.

16. During the hearing, the Respondents reiterated their comments submitted vide letter dated April 25, 2019 and stated that the Company offers accidental death and disability and hospitalization products on monthly premium through bancassurance arrangements. They further maintained that the cases mentioned in the SCN relate to products offered to the credit card customers of the United Bank Limited and are paid for through their credit cards. The Authorized Representatives explained that the covers are for one-month period with an automatic renewal option, therefore in their view, no provisions for unearned premium reserve, prepaid reinsurance premium reserve and deferred commission were required.

17. In terms of Regulation 24(9) of the Regulations, where premiums for a policy are payable in installments, the full premium for the duration of the policy shall be recognized as income at the inception of the policy and a related asset set up for premiums, notwithstanding the fact that some installments may not, by agreement between the insurer and the insured, be payable until later.

18. The Respondents have stated that the MIS report from the Bank for policies issued from December 1 to December 31, 2017 was received in January 2018, hence premium for the same was recorded in January 2018. Relevant excerpt from the reply dated April 25, 2019 is reproduced hereunder:-

".....For policies issued from December 1 to December 31, 2017, the MIS report from the Bank was received in January 2018, hence premium for the same was recorded in January 2018. Our bancassurance returns reflect this position...."

19. It is evident from the above response that the Respondents failed to record the premium received against policies issued in December 2017 in the month of December 2017 and January 2018 on accrual basis and did not follow the Regulations while preparing the bancassurance returns. Furthermore, the Respondents did not disclose the correct amount of "unearned premium reserve" and "prepaid reinsurance premium ceded" in the Statement of Premium as required under Regulation 24 and 26 of the Regulations.

20. It is an understood principle of *Accrual basis of accounting*, provided in Paragraph 27 of the International Accounting Standard 1 (Presentation of Financial Statements), which states as follows:

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"Para-27 An entity shall prepare its financial statements, except for cash flow information, using the accrual basis of accounting."

21. The Insurance Accounting Regulations, 2017 lay down procedures to record premium, unearned premium, claims, reinsurance and commissions, in line with the accrual nature of transactions. The Respondents misinterpreted the concept of "so far is practicable" in Regulation 24(5) of the Regulations. Regulation 24(5) of the Regulations provides that not yet processed premium/premium adjustments be recognized as receivable and earned over the period, based on the information available with the insurer. Here the term 'so far practicable' refers to the judgement on the basis of information available about the policy issued/processed or not yet processed. Therefore, the argument given by the Respondents i.e. "so far is practicable" is not tenable in the instant case.

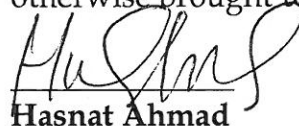
22. I have carefully examined and given due consideration to the written and verbal submissions of the Respondents, and have also referred to the provisions of the Ordinance, the Rules made thereunder and/or other legal references. I am of the view that violation of Regulations 24, 26 and 28 of the Regulations read with Section 46 of the Ordinance, are clearly established, for which the Respondents may be penalized in terms of Section 156 of the Ordinance.

23. 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."

24. In exercise of the power conferred on me under Section 156 of the Ordinance, I instead of imposing any penalty under Section 156 of the Ordinance, take a lenient view as the Respondents have assured to remain compliant at all times. However, the Respondents are hereby warned and directed to ensure compliance with Regulations 24, 26 and 28 of the Regulations in future.

25. 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.



Hasnat Ahmad

Director/ HoD (Enforcement)

