



INSURANCE DIVISION  
Islamabad

Before Fida Hussain Samoo, Commissioner (Insurance)

*In the matter of*

Pak Qatar General Takaful Limited

Show Cause Notice & Issue ID/Enf/PQGT/2017/9059 Dated March 31, 2017  
Date:

Date of Hearing: May 17, 2017

Attended By:

1. Mr. Altaf Ahmed Siddiqui  
Head of Operations  
M/s. Pak Qatar General Takaful Limited
2. Mr. Kamran Saleem  
CFO and Company Secretary  
M/s. Pak Qatar General Takaful Limited
3. Mr. Muhammad Rizwan Alam  
VP Finance & Accounts  
M/s. Pak Qatar General Takaful Limited
4. Mr. Jehanzaib Ahmed  
Manager Legal & Compliance  
M/s. Pak Qatar General Takaful Limited

Date of Order: June 1, 2017

**ORDER**

Under Rule 13 of the Securities and Exchange Commission (Insurance) Rules, 2002 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. Pak Qatar General Takaful Limited (the "Company") and the Chief Executive and Directors for alleged contravention of Rule 13 of the Securities and Exchange Commission (Insurance) Rules, 2002 (the "Rules") read with Section 11(1)(c), Section 36 of the Insurance Ordinance, 2000 (the "Ordinance"). The Company, its Chief Executive and Directors shall be collectively referred to as the "Respondents" hereinafter.



2. The Company is registered under the Ordinance to carry on the business of general takaful in Pakistan.
3. The Company submitted its annual audited accounts and regulatory returns (the "financial statements") for the year ended December 31, 2015 in pursuance of the provisions of Section 46(1) and Section 51(1) of the Ordinance.
4. Review of financial statements of the Company for the year ended December 31, 2015 revealed that 'provision for Outstanding Claims' as at December 31, 2015 was understated by an amount of Rs. 316.76 million and the Company *prima facie* did not meet the minimum solvency requirements in case of adequate provisioning.
5. The provision for Outstanding Claims' as at December 31, 2015 was provided at Rs. 374.49 million for the year 2015, which was substantially lower than the previous year's estimates. The final provisions for the years 2012, 2013 and 2014 were provided at Rs. 236.26 million, Rs. 552.68 million and Rs. 691.25 million respectively. As per claim development table given below, reserving pattern of the Company in prior years showed an increasing trend in the years 2012, 2013 and 2014. However, 'provision for Outstanding Claims' in the audited accounts for the year ended December 31, 2015 was decreased.

Accident Year	2010 and Prior	2011	2012	2013	2014	2015	Total
Estimate of Ultimate Claim Costs							
-At end of accident year	64,522	207,768	257,140	569,998	659,571	374,487	
-One year later	57,010	188,306	242,573	550,139	691,246		
-Two years later	55,489	183,395	235,869	552,681			
-Three years later	55,353	184,519	236,260				
-Four years later	59,426	184,135					
Estimate of Cumulative Claims	59,426	184,135	236,260	552,681	691,246	374,487	2,098,235
Cumulative Payments	(58,246)	(180,880)	(231,149)	(542,906)	(666,956)	(306,442)	(1,986,578)
Liability recognized in the balance	1,180	3,255	5,111	9,775	24,291	68,046	111,657

6. As per the Liability Adequacy Test, the Provision for Outstanding Claims was not adequately provided as elaborated in the following table:

	Rs. in 000's
1. Outstanding Claims as at Jan 01, 2015	228,483
2. Total Paid Claims in 2015 but reported in the past years	223,167
3. Outstanding Claims as at Dec 31, 2015 for claims reported in the past years	52,991
Run-off result (1-2-3)	(47,676)
Run-off result in %	-21%

7. The excess solvency margin over minimum requirement of the Company for the year ended December 31, 2015 was Rs. 80.12 million, however, considering the impact of understatement of provision for Outstanding Claims amounting to Rs.



316.75 million, the net solvency margin of the Company became negative by Rs. 236.64 million.

	Rs. in 000'
Admissible Assets	730,155
Less: Liabilities	(500,039)
Excess Assets Over Liabilities	230,116
Solvency	(150,000)
Excess Solvency Margin Over Minimum Requirement	80,116
Less: Understatement of Provision of Claims	(316,759)
Net Solvency Margin after Adjustments	(236,643)

8. In respect of this, the Company was advised vide letter dated November 3, 2016 to provide further information/clarification. In response, the Company submitted its reply vide letter dated November 14, 2016. However, it was noted that the Company provided the methodology and factors of uncertainty rather than giving clarification about understatement of provision of Outstanding Claims.

9. As per the afore-mentioned provisions, an insurer incorporated in Pakistan, registered under the Ordinance is required to have at all times admissible assets in excess of its liabilities in Pakistan of an amount greater than or equal to the minimum solvency requirement.

10. The minimum solvency requirement (i.e. excess of admissible assets over liabilities) for the Company is Rs. 150.00 million. However, the Company's solvency margin vis-à-vis the minimum solvency requirements fell short by an amount of Rs. 201.58 million.

11. The Company therefore, *prima facie* failed to meet the mandatory requirements relating to the minimum solvency as given under Rule 13 of the Rules read with Section 11(1)(c) and Section 36 of the Ordinance.

12. 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;*

*....."*

13. 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."

14. The relevant provisions of Rule 13 of 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) until 31 December 2011, fifty million rupees; and
- (b) thereafter as per the following table:

<b>On or After</b>	<b>Rupees</b>
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 following shall be the prescribed percentage, namely: -

- (a) In the case of an insurance company registered after the commencement date, twenty per cent; and
- (b) in the case of an insurance company registered at the commencement date-
  - (i). ten per cent until the 31st December, 2002;
  - (ii) fifteen per cent until the 31st December, 2004; and



(iii) thereafter the percentage as set out in clause (a) of this sub-rule.

(3) For the purposes of clause (c) of sub-section (3) of section 36 of the Ordinance, the following shall be the prescribed percentage, namely: -

(a) In the case of an insurance company registered after the commencement date, twenty per cent; and

(b) in the case of an insurance company registered at the commencement date-

(i) ten per cent until the 31st December, 2002;

(ii) fifteen per cent until the 31st December, 2004; and

(iii) thereafter the percentage as set out in clause (a) of this sub-rule."

15. Therefore, a Show Cause Notice (SCN) ID/Enf/PQGTL/2017/9059 dated March 31, 2017 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.

16. Subsequently, the Respondents vide their letter dated April 11, 2017, submitted their comments, which are summarized as under:

- i. While comparing estimates of liability calculated at the year-end with their actual future results/outcome in the next year, we find variances in actual results in general due to certain factors including methodology for estimation of Outstanding Claims & IBNR and sources of uncertainty effecting best estimation. These factors effect estimation of outstanding claims/respective retakaful & salvage recovery to reduce claim cost/partially reported claims/claims reported but not enough reported to enable estimates/one-off cases/co-takaful adjustments inclusive of reconciliation lag/customer tendency to litigation for demerit claims, and above all management's commercial decision having dominance over merit of claims on account of market competition & objective of long term relation with existing clientage.
- ii. For Liability Adequacy Test (LAT) of outstanding claims liability of the year-end 2014, we compared it with aggregate of their actual payments made during year 2015 and their respective remaining outstanding liability at the next-year end 2015. (For this, Claims incurred in year 2015, their payments during year 2015 & their respective outstanding liability at year end 2015 are excluded in working as the above working is to assess adequacy of claim liability booked at year end 2014 only, i.e opening liability for year 2015. Similarly, IBNR claims at year end 2015 reflects provision for those claims that have incurred in year 2015 but not reported in 2015, therefore it is also excluded in working as not having relation with closing liability of year ended 2014).





- iii. LAT is performed on the basis of data from financial statement for year 2015 to assess adequacy of Closing Claims Liability for year ended 2014, i.e. opening liability for year 2015; therefore its variance effect (run-off result) is ultimately incorporated in financials & regulatory return for year ended 2015. The reasons of the phenomenon of the gross run-off negative result analyzed and being one-off isolated event of Rs 23.90 million is excluded as referred in (i) to reach net run-off variance of Rs 14.00 million. This payment of Rs 23.90 million was executed in year 2015 but relates to the claims of prior year which were closed as no loss owing to deficiencies in their merit, hence these claims were not included in closing liability of year end 2014. However, client negotiations, market stiffened competition and litigation avoidance approach, compelled the management to settle those claims on commercial terms on ex-gratia basis.
- iv. The expected liability for year ended 2014 (i.e. opening liability for 2015) was estimated with prudence and professional judgment, while finalizing accounts for the year ended 2014. It is valuable to submit in respect of total run-off result for year end 2014 closing gross claims liability that its effect has been incorporated in profit & loss and solvency margin for the year ended 2015, after deducting its respective Retakaful recovery which resultantly further decreased its adverse effect.
- v. Given the elements of uncertainty & sensitivity in estimation process, 10% adverse variance of Rs 21.40 million in closing claim liability (excluding IBNR) for year ended 2014 was also disclosed in financial statements for year ended 2014. Guidance of 10% factor has been sought from the SECP Guidelines, Clause 3.9 & 4.4 (for non-life insurer).
- vi. We assure you that way forward, we will take additional prudence and professional diligence in estimation of claim liability to minimize uncertainty and adverse claim development variance.
- vii. Data of Claim Development Table (CDT) has been used for determination of Adequacy of Provision for Outstanding Claims Liability for year ended 2015 and accordingly respective Claim Expense for the year ended 2015
- viii. It appears that claims cost of Rs 691.25 million for the year 2014 is compared with claims cost of Rs 374.48 million for the year 2015. Their difference is worked out as  $\text{Rs. } 691.246 - \text{Rs } 374.478 = \text{Rs } 316.759$  million and this decrease in claim cost was presumed as an understatement of claim expense & provision for outstanding claim liability, which simultaneously used in solvency recalculation.
- ix. CDT working provides comparison of future development in estimation of claims expense of particular year with its previous estimates in prior years, i.e. it goes back till its accident year. However, analysts of the year 2015 may



not be compiled without data pertaining to its future development in next year 2016 i.e. one year later.

- x. Decrease in claims expense in absolute amount in year 2015 as compared to prior year claims expense is not necessarily an indication of understatement. Similarly, in isolation to other factors, the high claims expense in prior years do not necessarily project similar trend for future claims expense. In our honest understanding, CDT in isolation may not indicate inadequacy of provision for outstanding claims & claims expense for the year 2015.
- xi. We submit extracts from financials and explanation for decrease in gross provision for outstanding claim & gross claim expense for the year 2015. In general, the accounting cycle of outstanding claims is influenced by claim expense and claim payments, while factors affecting 'claim expense' are usually, change in business volume, business mix, portfolio of clients with high claim ratio, claim occurrence pattern, occurrence of one-off claims, claim handling procedure, non occurrence of large claims and reversal of large claims.
- xii. The Company's business growth was dominated by health segment in the year 2013 & 2014, and likewise growth trend in gross claims is also witnessed. Decrease in business volume by 30% in year 2015 is mainly due to decrease in health segment, which also supplemented the decrease in overall gross claim expense. In health segment, due to non-availability of re takaful treaty, effect of gross health claims expense was completely passed on to profit & loss.
- xiii. Further, due to high claims ratio in year 2013 & 2014 in health segment, management strategically curtailed business in this segment in year 2015, which resultantly helped in decreasing overall claim expense and outstanding claim in absolute amount for the year 2015. Based on review of its business strategy and segment performance, the Company sheds off some loss making clients to maintain balanced and profitable portfolio mix and resultantly helped in decreasing claim expense. Further, in year 2015, a one-off large claim in fire class of Rs 48.50 million was decided as no loss owing to deficiency in merit, accordingly it also supplemented the decrease in overall gross claim expense for the year 2015.
- xiv. In year 2015, change was observed in our executive management, as a result, certain functions and processes were revisited to realign them with a focus on proactive claim handling procedure including active management and pursuing of claims. On account of significant settlement of Rs. 529 million in year 2015 coupled with concerted efforts to review claim cost, has resulted in noticeable decrease of gross outstanding claims to Rs 102.00 million at the year-end 2015 in comparison to comparative outstanding claims of 214.00 million at the year-end 2014.



- xv. It is relevant to discuss that Claim Development Table (i.e. actual claims comparison with its previous estimate in prior years up to its accident year) which is covered in IFRS-4, under the 'Disclosure' paras. We humbly submit that plain reading of the IFRS-4 Para 39(c)(iii) with para IFRS-4 Para 38 provides that subject CDT serves disclosure purpose that enables users of its financial statements to evaluate the nature and extent of risks arising from insurance contracts. In our honest understanding, CDT in isolation may not indicate inadequacy of provision for outstanding claims & claims expense for the current year 2015, whose future development is awaited.
- xvi. Analysis of 'Estimates of Claims Cost of Accident Year' with 'Estimate of claim cost in Future years i.e claim Development' has witnessed the adequacy of claims estimation in initial year i.e accident year; with only exception for the year 2014. As analysis of the year 2015 may not be compiled without data pertaining to its future development in next year 2016 i.e one year later. Therefore, in isolation and without considering other factors, understatement of one year can not be evaluated based on comparison of one year absolute amount with prior year absolute amount.
- xvii. We hereby seek your kind consideration to our explanations, analysis of business growth, claim growth, linked factors effecting claims expense, management business strategy, curtailment of loss making health segment and analysis of CDT. In consideration to aforesaid explanations/working, we assume reasonable ground to conclude that adequacy is observed in claims expense and provision for outstanding claims for the year 2015 and resultantly solvency provisions have been complied with.
17. Thereafter, the Commission vide letter no. ID/ENF/PQGTL/2017/9337 dated April 26, 2017, scheduled a hearing for May 10, 2017 to provide an opportunity of being heard to the Respondents. However, the Respondents vide letter dated April 28, 2017 requested to reschedule the hearing. Hence, the hearing was rescheduled on May 17, 2017 at 11:30 am.
18. The hearing of May 17, 2017 was held at the Head Office of the Commission in Islamabad which was attended by officers of the Company; namely Mr. Altaf Ahmed Siddiqui, Head of Operations, Mr. Kamran Saleem, CFO & Company Secretary, Mr. Muhammad Rizwan Alam, VP Finance & Accounts and Mr. Jehanzaib Ahmed, Manager Legal & Compliance., who furnished a authority letter in their favor to represent the Respondents before the Commission in the instant matter.
19. During the hearing, the Respondents stated that due to commercial consideration, the claims that were closed/no loss were subsequently reopened and subsequently settled. These ex-gratia claims were higher in year 2015 as the Company settled cases due to tough market conditions. They however, maintained that there is no increasing trend in ex-gratia payments. The Respondents explained that ex-gratia payments were made with the special approval of the





senior management and these cases can be considered as a waiver of breach of warranty. They claimed that outstanding claims lag has been reduced as claim payments have been expedited. The Respondents stated that the Company is doing claims monitoring through due diligence and continuous training of the staff. The Respondents stated that ex-gratia claims amounting to Rs. 23.90 million were already included in the payments of paid claims of 2015. They also claimed that no ex-gratia payments were made in the year 2016. The Respondents requested the Commission to take lenient view in the instant matter.

20. The Respondents were required to ensure compliance with the mandatory provisions of Rule 13 of the Rules read with Section 11(1)(c) and Section 36 of the Ordinance. While factors highlighted by the Company such as decrease in business volume by 30% in year 2015, decreasing the overall gross claim expense appears reasonable. I am of the opinion, that Company is meeting minimum solvency requirement. However, Company's response on Liability Adequacy Test (LAT) of year ended 2014 is not satisfactory.

21. The Company in its LAT of year ended 2014 has excluded Ex-gratia claim payments which were previously closed but were reopened in 2015. These claims payments amounting to Rs. 23.90 million were included in total paid claims in year 2015. If the Company had intention of reopening the claims on ex-gratia basis then it should have reflected/reported in claims liability for the year end 2014. The response of the Company that due to commercial decision, the claims were reopened is not tenable. The whole purpose of recognizing adequate provisioning that books and accounts of Company reflect true picture of the financial position of the Company. If Company had used prudence and professional judgment then this factor should have been taken into account.

22. The Company in its reply has provided working of LAT calculation. If the Commission dis-allow ex-gratia payment of Rs. 23.90 million then the run off result is negative Rs 38.30 million (-16.7%). Even if the explanation as provided above is considered regarding ex-gratia payment then Run off result is still negative by an amount of Rs. 14.40 million (-6.3%). It is apparent that the Company did not adequately provide the Provision for Outstanding Claims.

23. 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 Company has made inadequate provisioning of Rs. 23.90 million in the name of ex-gratia payments for which fine as provided under Section 156 of the Ordinance can be imposed onto the Respondents i.e. the Company, its Chief Executive and Directors.

24. Section 156 of the Ordinance states 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]16 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."*

25. In exercise of the power conferred on me under Section 156 of the Ordinance, I impose a fine of Rs. 100,000/- (Rupees Hundred Thousand Only) on the Company, due to inadequate provisioning, as mentioned in the above paras hereof. The Respondents are further directed to ensure full compliance with the Ordinance, rules, regulations and directives of the Commission in future.

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

Fida Hussain Samoo  
Commissioner (Insurance)

