



SECP
INSURANCE DIVISION
Islamabad

Before Shaukat Hussain, Commissioner (Insurance)

In the matter of

M/s. Adamjee Life Assurance Company Limited

Show Cause Notice No. ID/Enf/AdamjeeLife/2018/13848
& Issue Date: dated February 27, 2018

Date of Hearing: February 28, 2019

Attended By: Mr. Jalaluddin Meghani
CFO and Company Secretary/ Authorized Representative
M/s. Adamjee Life Assurance Company Ltd.

Mr. Iqbal Bawaney
Authorized Representative

Mr. Bilal Ashfaq Memon
Authorized Representative

Date of Order: April 4, 2019

ORDER

Under Regulation 14(2) of the Bancassurance Regulations, 2015 read with Section 156 of the Insurance Ordinance, 2000

.....
This Order shall dispose of the proceedings initiated against the Chief Executive and Directors of M/s. Adamjee Life Assurance Company Limited (the "Company") for alleged non-compliance with Regulation 14 (2) of the Bancassurance Regulations, 2015 (the "Regulations"). The Chief Executive and Directors of the Company shall be referred to as the "Respondents" hereinafter.

2. The Commission had initiated thematic review of Bancassurance business of insurers in order to check compliance of conduct of business with applicable regulatory provisions by the insurers. Accordingly, call for information notice under Section 61 of the Ordinance dated September 25, 2017 was issued to the Company. The call for information notice as aforementioned, required the Company to provide information as per the Information Seeking Memorandum (the "ISM") and formats provided therein. The response of the Company, against the call for information notice was received through letter dated October 16, 2017 and subsequent emails from time to time.

3. While reviewing the Annexures B1 and B2, it was observed that the Company did not submit the cost of insurance consultants in respect of MCB Bank referral model. The Company was advised to provide the cost of insurance consultants vide email dated January 4, 2018, to which, the company responded vide email dated January 11, 2018 and provided the cost of insurance consultants for MCB Bank referral model for 2016 and



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Continuation Sheet - 2 -

92

4. It was observed that the Company incurred aggregate costs in respect of commissions, sales and marketing incentives, and insurance consultants, in excess of the regulatory prescribed limit i.e. 55% of the first year premium. The computation of all first year costs is illustrated as follows:

MCB Referral	Grand Total			
	HY Ended June 30, 2017	Percentage	2016	Percentage
First year Premium	276,968,386		272,352,196	
First year commission	111,765,054	40%	108,940,878	40%
Incentive	13,374,570	5%	13,617,610	5%
Cost of insurance consultant	30,705,985	11%	38,867,185	14%
Sum of costs	155,845,609	56%	161,425,673	59%
Excess cost	3,512,997	1.27%	11,631,965	4.27%

5. As evident from the table above, the aggregate cost of commission, sales and marketing incentive and cost of insurance consultants exceeded the first year limits given in Regulation 12 and 13 of the Regulations i.e. 55% of first policy year premium.

6. Explanation was called from the Company regarding the excessive cost, vide email dated January 17, 2018, to which, the Company responded vide email dated January 23, 2018 as follows:

"Please note that in the above observation, the threshold for maximum cost of referral model was taken 50%, whereas in order to make it more comparable, it should be 55% (i.e. 50% commission + 5% market incentive) as market incentive was also included in above calculations.

The cost in the year 2016 (9 months) is 4% above the threshold. It needs to be appreciated that the referral model was launched from April 2016 and it is not possible to arrive at the targeted ratio in the gestation period when the business has to gradually pick up whereas the fixed cost has to be incurred in the shape of salaries for developing the model irrespective of the premium generated.

In the 6 months of the year 2017, it is evident that business is growing up and hence the cost of consultant went down from 14% to 11%. On the question that it is still 1% above the threshold, the answer is that these consultants also contributed in generating top up premium of Rs. 145 million in Jan-Jun 2017 on which we paid 2% commission to Bank, however, this premium has not been accounted for under premium figures in your table whereas full salary of consultants have been accounted for."

7. The cost of insurance consultants is essential component of the total Bancassurance cost (whether or not it is paid to the bank); therefore, it should have been reported in the Bancassurance returns under Regulation 18 and statement of itemized computation of acquisition cost under Regulation 20 of the Regulations.

8. In view of the above, it transpired that the Company contravened the provisions of Regulation 14(2) of the Regulations.

9. The terms "Direct Sales Model", "Referral Model" and "Insurance Consultant" have been defined in the Regulations as follows:



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Continuation Sheet - 3 -

23

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

(i) **"Direct Sales Model"** means a particular bancassurance distribution model where the Bank uses its own sales force to market and distribute insurance products through its network;

(s) **"Referral Model"** means a particular bancassurance business distribution model where the Insurer uses its own Insurance Consultants to market and distribute insurance products through the Banks' distribution network based on sales leads generated by the Bank;"

"(l) "Insurance Consultant" means a specified person who is an employee of the Insurer and is responsible for soliciting and procuring insurance business under the Bancassurance Agency Agreement;"

10. Regulation 12(a)(1) of the Regulations provides that:

"(i)First Policy Year Commission to Bank.- In the first policy year the commission to the bank will be subject to the maximum limit given as per Table A1 in Schedule to these Regulations;

Table A1: Commission Schedule for Direct Sales Model

Product	Year 1	Year 2	Year 3	Year 4+
Regular Premium Individual Life Plans	50%	5%	2.5%	2.5%
Single Premium Investment Plans	4%	NA	NA	NA
Regular Premium Annuities	10%	2.5%	2.5%	2.5%
Regular Premium Personal Accident	50%	40%	40%	40%
Group Credit Life and Similar Plans	50%	NA	NA	NA

11. Regulation 13 (1) of the Regulations requires that:

"Sales and Marketing Incentives to Banks.- (1) To promote Bancassurance business, an Insurer shall be allowed to share with the Bank in the costs of sales and marketing incentives including sales conventions and awards called by whatever name in respect of bancassurance business. The share of the Insurer in such activities shall not exceed 5% of the first policy year collected premium."

12. Regulation 14(2) of the Regulations provides that:

"(2) The total direct expenses incurred by the Insurer in respect of new business as commission to the Bank, salaries and commission to its Insurance Consultants, sales and marketing incentives to the Bank or its Insurance Consultants and production bonuses shall be within the aggregate of all first year limits prescribed in Regulation 12 and 13 above for each type of product."

13. In view of the violations highlighted in the preceding paras, the Commission initiated penal action by issuance of a Show Cause Notice (SCN) on February 27, 2018



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Continuation Sheet - 4 -

bearing No. ID/Enf/Adamjeelife/2018/13848 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 for non-compliance with Regulation 14(2) of the Regulations.

14. The Company, vide letter dated March 8, 2018, sought an extension to submit reply to the aforesaid SCN. The request of the Company was acceded to and the Company was granted extension until March 22, 2018, intimated through letter dated March 12, 2018.

15. Thereafter, the Respondents submitted their reply vide letter dated March 22, 2018, which is reproduced hereunder:

".....

*At the outset, the Hon'ble Commission may please rest assured that it has always been the policy of Adamjee Life Assurance Company Limited ("**Company**") to conduct its affairs in accordance with the highest legal and ethical standards and to comply with all applicable laws, rules and regulations and the directions of the Hon'ble Commission. Therefore, the Management of the Company cannot even think of violating the statutory provisions.*

We wish to invite Hon'ble Commission's kind attention towards the fact that the Referral Model was introduced by the Company from April, 2016 which required gestation period during which the employees had to work hard to achieve the target. During this period, fixed costs in shape of salaries and development of the Model had to be incurred, irrespective of the premium generated. Therefore, the costs during the gestation period would appear to be on a higher side, which is common phenomenon in all new businesses of any kind whatsoever. With the passage of time, the business grows-up and the percentage of the costs gradually declines with the increase in revenue. Moreover, the premium had not been accounted for till actual realization, whereas full salaries of consultants, being employees of the Company had to be fully accounted for such period, which resulted in the difference.

The Company's Model was hybrid model comprising Direct Sales Model, as well as Referral Model and the employees had to be geared and motivated to achieve the targets, entailing high costs in comparison to the premium generated.

It may be appreciated that a new business or product takes time and the initial costs are also quite high as compared to the costs for the subsequent period after the business gains momentum.

However, from the year 2017 onwards, there has been no such disparity. In the first six months of the year 2017, the cost of consultants, being employees of the Company reduced from 14% to 11% and were fully accounted for, whereas consultants have also generated adhoc/top-up premium of Rs. 145 Million during the period of January-June, 2017 (Year 2016 Rs. 110 Million) and the commission to MCB Bank was also reduced to 2%. However, this adhoc/top-up premium has not been accounted for under premium figures in the Table contained in Para 10 of the SCN, whereas full salaries of consultants have been accounted for.



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Continuation Sheet - 5 -

It may kindly be appreciated that the Company has not concealed any material fact, nor any undue advantage has been gained by the Company, whereas the Company and its Management have all along acted in good faith and there has been no willful contravention of the Regulations. Hence, it would not be fair to penalize the Company, if there is any procedural or accounting deviation.

We fully respect the Commission's approach in implementing the law in its true letter and spirit and pledge our full co-operation with the Commission in all statutory compliances. Therefore, without prejudice, if the Hon'ble Commission does not concur with our submissions, then we would respectfully request the Commission to take a lenient view, since we have acted in a good faith without any malafide intent."

16. Subsequently, the Commission vide letter dated June 25, 2018 scheduled the hearing on July 4, 2018 at 11th Floor, NIC Building, Jinnah Avenue, Blue Area, Islamabad. However, the Authorized Representatives, vide letter dated June 30, 2018 requested to defer the hearing for any date in August, 2018. The hearing was rescheduled on February 28, 2019 at the Commission's Karachi Office. The said hearing was attended by the Authorized Representatives namely, Mr. Iqbal Bawaney, Mr. Bilal Ashfaq Memon, and Mr. Jalaluddin Meghani for and on behalf of the Respondents.

17. During the hearing, the Authorized Representatives reiterated their written comments and stated that 'Referral Model' was introduced by the Company from April, 2016 and accordingly the costs during the gestation period appeared to be on a higher side. However, they maintained that in the first six months of the year 2017, the cost of consultants, being employees of the Company reduced from 14% to 11% and were fully accounted for whereas the adhoc/top-up premium generated by them during the said period was not accounted for. The Authorized Representatives requested the Commission to take a lenient view in the instant case.

18. Regulation 14(2) of the Regulations requires that the total direct expenses incurred by the insurer in respect of new business as commission to the Bank, salaries and commission to its Insurance Consultants, sales and marketing incentives to the Bank or its Insurance Consultants and production bonuses shall be within the aggregate of all first year limits prescribed in Regulation 12 and 13 for each type of product.

19. While Regulation 12 and 13 require that total direct expenses incurred by the insurer in respect of new business as commission to the bank, salaries and commission to its insurance consultants, sales and marketing incentives to the bank or its insurance consultants and production bonuses shall be within first year limits prescribed vide Table A1 i.e. 50% of first policy year premium. Furthermore, share of the insurer in costs of sales and marketing incentives including sales conventions and awards in respect of bancassurance business shall not exceed 5% of the first policy year collected premium as prescribed in Regulation 13(1), making total of 55% of the first policy year premium.

20. However, in the instant case, the Company incurred aggregate costs in respect of commissions, sales and marketing incentives, and insurance consultants, in excess of the regulatory prescribed limit i.e. 55% of first policy year premium. It is clarified that cost



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Continuation Sheet - 6 -

ab

of insurance consultants cannot be excluded as it is essential component of the total Bancassurance cost (whether or not it is paid to the bank), therefore, it should have been reported in the Bancassurance returns under Regulation 18 and statement of itemized computation of acquisition cost under Regulation 20 of the Regulations. The Company has cited reasons of fixed cost and gestation period for exceeding the prescribed regulatory limit. The explanation provided by the Company regarding excess of aggregate cost of commission, sales and marketing incentive and cost of insurance consultant is not tenable.

21. 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 violation of Regulation 14(2) of the Regulations is clearly established, for which the Respondents may be penalized in terms of Section 156 of the Ordinance.

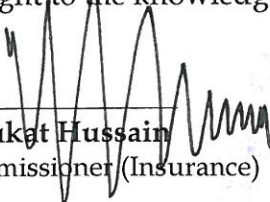
22. Section 156 of the Ordinance provides that:

“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.”

23. In exercise of the power conferred on me under Section 156 of the Ordinance, I impose a fine of Rs. 100,000/- (Rupees One Hundred Thousand only) on the Company under the said provision of the Ordinance, due to the non-compliances, as mentioned hereinabove. Moreover, the Respondents are hereby warned and directed to ensure full compliance with the Ordinance, rules, regulations and directives of the Commission in future.

24. Hence, the Company is hereby directed to deposit the applicable fine in the designated bank account maintained in the name of Securities and Exchange Commission of Pakistan with MCB Bank Limited within thirty (30) days from the date of this Order and furnish receipted vouchers issued in the name of the Commission for information and record.

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.


Shaukat Hussain
Commissioner (Insurance)

