



INSURANCE DIVISION  
Islamabad

Before Tahir Mahmood, Commissioner (Insurance)

*In the matter of*

Unique Insurance Broker (Pvt.) Limited

Show Cause Notice No. and Issue Date: ID/Enf/Unique/2018/13386 dated  
January 25, 2018

Date of Hearing: March 28, 2018

Attended By:

1. Mr. Irshad Ahmad  
Chief Executive Officer  
M/s. Unique Insurance Broker (Pvt.)  
Limited
2. Faisal Khan  
CFO  
M/s. Unique Insurance Broker (Pvt.)  
Limited
3. Mr. Tariq Hussain  
Consultant

Date of Order: April 30, 2018

**ORDER**

**Under Rule 7 & Rule 23 of the Insurance Rules, 2002 and Section 165 of the Insurance Ordinance, 2000 read with Section 102(6) of the Insurance Ordinance, 2000.**

.....

This Order shall dispose of the proceedings initiated against M/s. Unique Insurance Broker (Pvt.) Limited (the "Company"), its Chief Executive and Directors for alleged contravention of Rule 7 & Rule 23 of the Insurance Rules, 2002 (the "Rules") and Section 165 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 licensed by the Commission as a broker to carry on the direct insurance broking business in Pakistan in pursuance of Section 102 of the Ordinance.

3. The term 'direct' has been defined in the Ordinance as follows:

*"direct", in relation to the business of insurance, means insurance other than reinsurance.*



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4. During the year 2016, the Company reported its major part of the revenue i.e. 68% (2015: 65%) from the consultancy services i.e. reinsurance related services, although the Company was licensed as a direct insurance broker. Furthermore, the Company did not have any formal agreement with M/s. Marsh for carrying out reinsurance broking or placement facilitation.

5. The Company, in its response regarding reinsurance related transactions, stated that it was not acting as a reinsurance broker but merely as a Correspondent of Marsh for providing local services like liaising with the clients and acting as a facilitator for the transactions. As per its agreement with Marsh (the "Agreement"), the Company had been appointed as Marsh's Correspondent. However, the word 'Correspondent' was neither defined in the Agreement nor its definition was available in the local laws. Clause 3 of the Agreement, titled 'Appointment' described two main areas of business between the two entities:

- i. *Referrals by Marsh to Correspondent: whereby Marsh will refer its existing clients to the Company for direct insurance broking services.*
- ii. *Referrals by Correspondent to Marsh: whereby the Company will refer to Marsh, Prospects (which are defined as companies or individuals introduced by the Company to Marsh, excluding Marsh's existing clients) who are interested in the purchase of insurance and who may wish to establish a business relationship with Marsh to use the Services.*

6. Reinsurance was not mentioned in the Agreement, except the following:-

*"In the event that the Correspondent and Marsh agree to develop joint businesses not included under the terms of this Agreement, such as facultative reinsurance placements as well as advisory and other consulting services, the terms and conditions of such joint arrangements, including, without limitation, the amount of compensation payable to the parties, shall be determined by mutual agreement on a case-by-case basis."*

7. Facultative reinsurance placements were not covered under the terms of the Agreement, which were being conducted informally between the two entities without documented terms and conditions. In response to the query regarding the governing contract for these transactions, the Company responded as under:

*"The governing agreement between Marsh and Unique Insurance Broker is the Correspondent agreement specifying the terms and conditions for duties and obligations, remuneration etc."*

8. The Company was taking active part in the reinsurance placement broking / facilitation as it was obtaining substantial amounts in the form of fees from these transactions.

9. As per Rule 14(1)(iv) of the Rules, an application for grant/renewal of licence to act as an insurance broker shall contain "a description of business carried on by it (other than insurance broking)." However, the Company did not mention the reinsurance



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placement broking/facilitation in the application and merely stated "Insurance Broking, Insurance Risk Management, Insurance Consultancy and Insurance Advisory Service" under serial number (iv) of its application for renewal of insurance broker's licence.

10. The Company was also *prima-facie* involved in fronting transactions routed through Marsh, which were used to subvert the provisions of Rule 23 of the Rules read with Section 165 of the Ordinance and Rule 7(2) of the Rules. The Company explicitly informed the clients that it would try to keep the local retention at a minimum. The Company then proposed the name of an insurer as the fronting agent and then stated that if the proposed insurer did not agree with the level of retention desired by the client then the Company would look for another insurer who would comply with the demands of the client. In such fronting cases, the Company was communicating directly with the original insured without the involvement of the insurer. In one of the case, the original policyholder's confirmation was sought by the Company regarding the reinsurance orders and local retention of insurers involved in the transaction. This signified that the Company, to circumvent the provisions of Rule 23 of the Rules and Section 165 of the Ordinance, placed insurance business outside Pakistan in the form of reinsurance through the practice of fronting and by including *cut-through* clauses in the reinsurance policies. The Company was *prima-facie* assisting the insureds in this practice.

11. Furthermore, in cases involving fronting, it was also observed that the dates on the reinsurance placement slips were earlier than that of the policies issued by the local insurer, signifying that such risks were placed with the reinsurers before issuance of the policies by the local insurer. Moreover, in one of the cases, it was observed that the name of the insurer was listed as TBA (To Be Advised) on the reinsurance placement slip issued by Marsh, which showed that reinsurance was placed before deciding the insurer for fronting the transaction. This was further supported by the communication between the Company and the insured, where the Company stated that it would choose an insurer that would agree to minimize local retention.

12. In view of the above, it appeared that the Company was involved in fronting transactions routed through Marsh in circumvention of the provisions of Rule 23 of the Rules and Section 165 of the Ordinance and also subverted the provisions of Rule 7(2) of the Rules.

13. Section 41(5) of the Ordinance states that:

*"Requirement to effect and maintain reinsurance arrangements:-*

.....

*(5) The Federal Government may make rules, not inconsistent with sub-section (1), governing the reinsurance outside Pakistan, other than on a treaty basis, of insurance business underwritten by an insurer in Pakistan."*

14. Rule 7 of the Rules states that:



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*“Reinsurance outside Pakistan. – (1) For the purposes of sub-section (5) of section 41 of the Ordinance, no insurer shall reinsure facultatively outside Pakistan any insurance business or any part thereof underwritten by it in Pakistan without the permission of the Commission.*

*(2) The Commission may, grant permission under sub-rule (1) in any of the following circumstances, namely*

*(a) The insurance or any part thereof is in excess of the insurer’s treaty arrangements, and the Commission is provided with documentary evidence that such excess cannot be reasonably placed within Pakistan;*

*(b) the insurance business, although covered by a treaty arrangement shall be desired to be reinsured facultatively for protecting the treaty or for any other special reason:*

*Provided that such facultative reinsurance shall not run contrary to subsisting contractual obligations under the treaty; and*

*(c) the insurance business is of special nature and there are no treaty arrangements for it.*

*(3) No insurer in Pakistan shall accept reinsurance on facultative basis in excess of its net retention if the insurer seeking such reinsurance so indicates in the reinsurance slip, request note or otherwise in writing.*

15. Section 165 of the Ordinance states that:

*“ Insurance of interests in Pakistan.- (1) The Federal Government may make rules, not inconsistent with this Ordinance, imposing conditions on the ability of any person to insure outside Pakistan any risk or part thereof in respect of any property or interests which are located in Pakistan at the time the insurance is effected.*

*(2) The Federal Government may make rules, not inconsistent with this Ordinance, imposing conditions on the ability of any insurer to issue life insurance policies denominated in currencies other than the Pakistan Rupee to persons who are citizens of Pakistan and resident in Pakistan at the time the insurance is effected.”*

16. Rule 23 of the Rules requires that:

*Insurance of interests in Pakistan . – (1) For the purposes of subsection (1) of section 165 of the Ordinance, no person shall insure outside Pakistan any risk or part thereof in respect of any property or interest which is located in Pakistan at the time the insurance is effected.*

*(2) The Federal Government may grant exemption to any person from the requirements of sub-rule (1) –*

*(a) Where any risk cannot be insured suitably in Pakistan; or*



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*(b) Where there are reasons of exceptional nature for granting exemption.*

*(3) The exemption under sub -rule (2) shall be for such property or interests, and for such period as the Federal Government may deem fit.*

17. Accordingly, a Show Cause Notice (SCN) No ID/Enf/Unique/2018/13386 dated January 25, 2018, was issued to the Respondents, calling upon them to show cause as to why the action under Section 102(6) of the Ordinance should not be taken against the Company for the aforementioned alleged contraventions of the law.

18. The Respondents, vide letter dated January 29, 2018, sought extension for a period of one month to submit reply to the aforesaid Show Cause Notice. However, the Respondents were allowed extension until February 13, 2018 to submit their reply.

19. Thereafter, the Respondents submitted their reply vide letter dated February 12, 2018, which is summarized hereunder:

- (i) The Show Cause Notice is based upon alleged non-compliance of Rule 7 and Rule 23 of the Rules. It is evident from the language of the said Rules that both the provisions are not applicable to the Company (Unique Insurance Brokers (Pvt) Ltd) (an insurance broker).
- (ii) As per Rule 7 of the Rules, only the insurer (local insurance company) can directly seek approval from the Commission after circulating the facultative request note in the local market. You will appreciate that no facultative reinsurance can be placed outside Pakistan until and unless approved by the Commission and such approvals are given to 'insurers' only and not to "insurance brokers" or to the Company. The language of Rule 7 cannot be stretched to include the Company (an insurance broker) and to any alleged non-compliance thereof by the Company. In any case, the Company has never reinsured any insurance business outside Pakistan.
- (iii) The Company has not insured any risk outside Pakistan in respect of any property or interest located in Pakistan in violation of Rule 23 of the Rules. In fact, the 'insureds' i.e. local entities have insured their risks in respect of properties and interests in Pakistan with 'insurers' who issue 100% insurance policy documents in Pakistan.
- (iv) There is no role of "insurance brokers" in the whole process of facultative reinsurance placement and the Commission (as regulator) is the sole authority to grant approval through a well-defined process at their own accord. Please note that the Commission has clarified the manner of acceptance and placement of facultative reinsurance under Rule 7 of the Rules read with Section 41 (5) of the Ordinance vide its Circular No. 22/2013 dated December 05, 2013.
- (v) The aforesaid matter has been decided by the learned Commissioner Insurance vide his Order dated July 03, 2017 in response to the Show Cause Notice



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ID/Enf/Chubb/2017/9746 dated May 30, 2017 to M/s Chubb Insurance Pakistan Ltd. In the said order, the learned Commissioner Insurance stated that the compliance of Rule 7 and Rule 23 is the obligation of insurer. In the said order, in fact the insurer was held responsible for non-compliance of the said rule.

- (vi) The entire process of facultative reinsurance arrangements and compliance thereto is the responsibility of the local insurer, therefore, the insurance broker is neither in control nor responsible for compliance with Rule 7 and Rule 23 of the Rules read with Section 165 of the Ordinance. As per the said Rules, the Commission gives the approval for placement of the facultative reinsurance abroad.
- (vii) The Company is duly licensed under Section 102 of the Ordinance to act as a broker for the direct insurance business in Pakistan. Further, it is inherent fact that the Ordinance only regulates the direct insurance broking business in Pakistan and the reinsurance broker is not the subject matter of the Ordinance. A large number of both local and foreign entities are doing reinsurance broking business without registration and/or licensing under the Ordinance. Therefore, reinsurance business is out of ambit of the law.
- (viii) The Company did not carry out any reinsurance business but restricted itself to the extent of providing brokerage and consultancy services to the insured entities in accordance with the law and hence did not violate the existing regulatory framework.
- (ix) The revenue stream generated by the Company is related to the brokerage business and providing consultancy services as per the law and have a valid Agreement in place. The Company is not involved in reinsurance placements or broking of the reinsurance contracts as per the definition of "reinsurance" in the Ordinance. Kindly appreciate that "reinsurance related services" have not been defined in the Ordinance. The reinsurance broking arrangement is between the insured, cedant and the reinsurance broker. The Company's role is restricted only to the direct insurance broking part of this arrangement which involves insured, insurer and direct insurance broker. The Company being Marsh representative/ Correspondent in Pakistan acts as a contact point for Marsh and provides services and maintains business relationship between the insured and Marsh and for such services the Company is remunerated in the form of consultancy fee as defined in Para 6.1 and 6.2 of the Correspondent Agreement.
- (x) The Companies Act, 2017 also allow the Company to carry out any business activity unless it is prohibited / restricted , with necessary licensing, registration, permission or approval required under any regime.
- (xi) The Company" is working as a Correspondent of Marsh and only facilitates the clients and Marsh and charges consulting fee accordingly. The insurer, Marsh and reinsurers enter into the reinsurance transaction and accordingly, the



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insurer submits an application to the Commission for approval of facultative reinsurance placement with reinsurers. Hence, there is no role of "the Company" in reinsurance placement.

- (xii) The Company is licensed as a foreign insurance broker under the Ordinance and only acting as liaison between Marsh, insurer and insured. The facultative reinsurance is placed by Marsh through their slip, directly for insurers. Hence the Company neither conducted any business related to reinsurance broking nor placed any risk outside Pakistan.
- (xiii) The revenue stream generated by the Company is related to brokerage business and providing consultancy services as per the law and have a valid Agreement in place. The Company is not involved in reinsurance placement or broking of the reinsurance contracts as per the definition of the reinsurance in the Ordinance.
- (xiv) It is submitted that the Company did not mention the reinsurance placement broking in the application as the Company is not engaged in reinsurance placement broking. The Company is carrying out its business activities in accordance with the object clause of the Memorandum of Association.
- (xv) The Board of Directors deleted the word "reinsurance" from Memorandum and Articles of Association of the Company to comply with the condition set by the Commission for renewal of insurance broker licence for the year 2016-2017.
- (xvi) Fronting business has been taken in incorrect context by the Commission. It is usually exercised in global insurance programs of multinational companies placed through their central risk management practice with or without a reinsurance intermediary with a global insurer/reinsurer.
- (xvii) In one of the case, the client was taking time to decide the name of local insurer, therefore the term TBA was mentioned in the reinsurance slip.
- (xviii) The mere fact that the earning from consultancy services is more than the brokerage is not violation of any law. We overwhelmingly deny that the Company is involved in fronting transactions.

20. Thereafter, the Commission, vide its notice no. ID/Enf/Unique/2018/14096 dated March 20, 2018, scheduled the hearing for March 28, 2018 at the Commission's Company Registration Office Karachi.

21. The hearing was attended by Mr. Irshad Ahmad Chief Executive Officer along with Mr. Faisal Khan and Mr. Tariq Hussain as Authorized Representatives representing all the Respondents before the Commission in the instant matter.



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22. During the hearing, the Representatives reiterated their written comments submitted to the Commission. They were of the view that the Company is only facilitating the reinsurance broker and insurer.

23. With regards to the role of the Company as a Correspondent of Marsh, the Company stated that it was not acting as a reinsurance broker but merely as a Correspondent of Marsh. The Agreement provided to the inspection team does indicate that the Company has been appointed as Marsh's Correspondent. However, the word 'Correspondent' itself has not been defined in the Agreement and no definition is available in the local laws. The Company, during the hearing agreed to revise the Agreement with Marsh by incorporating issues highlighted by the Commission in order to bring more clarity in the Agreement.

24. Another issue highlighted by the Commission was fronting. Fronting occurs when a broker or foreign insurer/reinsurer uses a local insurer as a fronting agent to place risks outside Pakistan in the form of reinsurance. In such cases, a very small portion of the risk is retained in Pakistan and a major portion of the risk is placed abroad in the form of facultative reinsurance placements. In such cases, the local insurer sometimes receives instructions from the foreign reinsurer, local insured and brokers. Rule 23 ensures that no property or interest located within Pakistan is insured outside Pakistan, unless approved by the Federal Government. This implies that businesses or individuals situated in Pakistan must get their risks insured by local insurers. Insureds, foreign reinsurers and brokers often employ the practice of fronting to bypass this regulation. The practice of fronting is also an indirect violation of Rule 7 of the Rules, which stipulates that local insurance risks could only be placed outside Pakistan in the form of reinsurance after determining that such risks cannot be suitably reinsured within the country. In cases involving fronting, the broker, insured or foreign reinsurer often dictate terms to the local insurer and try to minimize the local retention.

25. In the instant case, the Company also appears to be involved in facilitating fronting transactions routed through Marsh, which are used to subvert the provisions of Rule 23 of the Rules read with Section 165 of the Ordinance and Rule 7(2) of the Rules. It has been observed that Company explicitly informed the client that it would try to keep the local retention at a minimum. If the proposed insurer did not agree with the level of retention desired by the client then the Company would look for another insurer that would comply with the demands of the client. As per the sample collected by the inspection team, fronting was observed in three cases.

26. It is notable that while fronting is apparently riskless, it poses a number of risks to local insurers and is against the spirit of Rule 7 and Rule 23 of the Rules and Section 165 of the Ordinance. In case of failure of a reinsurer, the insurer is held responsible to bear all risks incurred by the insured. Secondly, fronting often distorts the underwriting practices of a jurisdiction where insurers focus on commission instead of premium retention and the performance of the underlying risks. Finally, fronting negates the spirit of local legislation by allowing foreign companies to circumvent local licensing and retention requirements. The Commission is of the view that both the insurer as well



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as the broker, directly or through their advisory and other consultancy services, cannot indulge into the practice of fronting to negate the provisions of the Ordinance.

27. The Company has facilitated the fronting transactions routed through Marsh in circumvention of the provisions of Rule 23 of the Rules and Section 165 of the Ordinance and has also subverted the provisions of Rule 7(2) of the Rules.

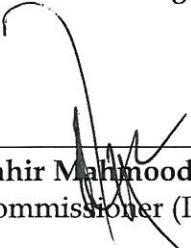
28. I have carefully examined and given due consideration to the written and verbal submissions of the Respondents, and have also referred to the provisions of the Ordinance, the Rules made thereunder and/or other legal references. I am of the view that the violations of Rule 7 & Rule 23 of the Rules and Section 165 of the Ordinance are clearly established, for which the Respondents may be penalized in terms of Section 102(2) of the Ordinance.

29. Section 102(6) of the Ordinance provides that:

*"The Commission may cancel or refuse to issue or renew a broking licence, where the Commission believes on reasonable grounds that the broker has contravened a provision of the Ordinance, including without limitation that the broker has failed to maintain prescribed minimum levels of paid-up capital, statutory deposit or professional indemnity insurance."*

30. In exercise of the power conferred on me under Section 102(6) of the Ordinance, I, instead of cancelling the licence as provided under the said provision hereby strictly warn the Company to desist from facilitating / indulging in the fronting transactions. The Company is also directed to submit its revised Agreement after incorporating the issues highlighted by the Commission.

31. 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)

