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Legislation

The insurance industry in Malaysia is governed by the Insurance Act 1996 (Act) which came into force on 1 January 1997. The Act is supplemented by the Insurance Regulations 1996 (Regulations) which prescribe the details of mandatory requirements contained in certain provisions of the Act. In addition, the Act also empowers Bank Negara Malaysia (the Bank) to specify matters pursuant to the provisions of the Act.

Specifications

In 2002, insurers were given greater flexibility in terms of assets which could be taken into account for the purpose of computation of the margin of solvency (admitted assets) of an insurer. Pursuant to section 46(2) of the Act, the changes in the admitted assets specified by the Bank were:-

- (i) the minimum requirement on investment in low risk assets was reduced to 10% from 20% of an insurer's margin of solvency; and
- (ii) the proportion of aggregate investments in unsecured credit facilities was increased to 30% from 20% of an insurer's margin of solvency.

Exemptions

Section 198 of the Act empowers the Minister of Finance to exempt a person or class of persons from all or any of the provisions of the Act if he considers it consistent with the purposes of the Act or in the interest of the public. In 2002, the Minister approved the exemption of licensed local insurers from the restriction on dividend payments under section 93(a) of the Act. This exemption, which represents an extension of a similar exemption in 2001 which expired on 31 December 2001, allows an insurer to pay dividends on its shares during the period in which goodwill arising from the acquisition of another licensed insurer is being written off. The exemption would apply to acquisitions completed between 1 January 2002 and 30 June 2002, as an incentive to facilitate the consolidation of the insurance industry through mergers and acquisitions.

Licensing and Market Structure

Licensing of Insurers, Insurance Brokers and Adjusters

As at 31 December 2002, a total of 54 insurers were licensed under the Act compared with 63 at the end of 2001. The reduction in the number of licensed insurers was the result of the revocation of nine licences, of which eight were revoked following the completion of several mergers and acquisitions. One licence for the conduct of professional general reinsurance business was revoked following the closure of the Malaysian branch of Arig Reinsurance Company B.S.C. (c) of Bahrain due to the consolidation of the global operations of its parent company. As part of General Cologne Re Group's rationalisation exercise, the reinsurance business of General Reinsurance Corporation in Malaysia was transferred to Cologne Reinsurance Company, Plc (Cologne Re). As a result, a reinsurance licence was issued to Cologne Re, while the reinsurance licence of General Reinsurance Corporation was revoked. The life insurance licence of Prudential Assurance Malaysia Berhad was replaced by a licence to conduct both direct general and life insurance businesses with the reinstatement of its general insurance licence effective 12 March 2002. A breakdown of the 54 insurers licensed under the Act as at end December 2002 is as follows:-

- 28 insurers carrying on direct general insurance business;
- seven insurers carrying on direct life insurance business;
- nine insurers carrying on direct life and general insurance business;
- eight professional reinsurers carrying on general reinsurance business;
- one professional reinsurer carrying on life reinsurance business; and
- one professional reinsurer carrying on life and general reinsurance business.

During the year, the licences of one broker and one adjuster were revoked following the completion of their mergers with other licensees. As a result, the total number of

Table 1.1
Number of Licensees

As at end of December	2001	2002
Direct insurers		
<i>Malaysian-incorporated</i>	50	42
<i>Foreign-incorporated</i>	2	2
Sub-total	52	44
Professional reinsurers		
<i>Malaysian-incorporated</i>	2	2
<i>Foreign-incorporated</i>	9	8
Sub-total	11	10
Total insurers	63	54
Insurance brokers	36	35
Adjusters	41	40

licensees in the insurance industry as at the end of 2002 stood at 129, comprising 54 insurers, 35 brokers and 40 adjusters as shown in Table 1.1. The lists of licensed insurers and reinsurers, insurance brokers and adjusters are given in Appendices II, III and IV to this Report.

Agents

Although not directly supervised by the Bank, the Act requires agents to be registered with the mandatory insurance associations under the Act, namely, the Life Insurance Association of Malaysia (LIAM) for life insurance agents and Persatuan Insuran Am Malaysia (PIAM) for general insurance agents. To ensure a minimum level of professionalism among the agency force, all agents are required to pass a compulsory Pre-Contract Examination for Insurance Agents (PCEIA) conducted by the Malaysian Insurance Institute as a prerequisite to registration.

There were 138,522 (2001: 133,750) registered insurance agents at the end of 2002. The number of life insurance agents registered with LIAM decreased from 88,504 at the end of 2001 to 87,205 at the end of 2002, while the number of general insurance agents registered with PIAM increased from 45,246 to 51,317 over the same period. Part-time agents continued to account for the majority (61.1%) of the life insurance agents.

Change of Company Status

Section 14 of the Act requires all licensed insurers (other than professional reinsurers which are allowed to operate as branches in

Table 1.2
Number of Branches Approved

	Insurers	Insurance Brokers	Adjusters
Approved in 2002	18	2	21
As at 31 December 2002	738	31	122

Malaysia) to be incorporated as public companies under the Companies Act 1965. As at the end of 2002, all licensed direct insurers had been incorporated locally, with the exception of two foreign insurers which had been given an extension of time to comply with the requirement. The list of foreign insurers which had restructured into Malaysian-incorporated insurers since 1975 is given in Appendix V.

Offices of Licensees

Section 36 of the Act requires a licensee to obtain the prior written approval of the Bank to establish an office in or outside Malaysia. In 2002, approval was given for the establishment of 41 branch offices bringing the total number of branches to 891 at the end of 2002. The number of approved branch offices of licensees as at the end of 2002 is shown in Table 1.2.

Changes in Equity

Section 18 of the Act requires a Malaysian-incorporated licensee to maintain a minimum paid-up capital as prescribed by the Bank. Licensed foreign insurers are required to maintain a corresponding surplus of assets over liabilities in Malaysia. Pursuant to this requirement, with effect from 30 September

Table 1.3
Distribution of Paid-up Capital of Malaysian-incorporated Insurers

As at end of December	2001		2002	
	RMm	%	RMm	%
Held by Malaysians	3,088.3	61.3	2,897.5	59.3
<i>Bumiputera</i>	1,575.6	31.3	1,420.3	29.1
<i>Non-Bumiputera</i>	1,512.7	30.0	1,477.2	30.2
Held by non-Malaysians	1,948.5	38.7	1,989.4	40.7
Total	5,036.8	100.0	4,886.9	100.0

Table 1.4
Distribution of Paid-up Capital
of Insurance Brokers

As at end of December	2001		2002	
	RMm	%	RMm	%
Held by Malaysians	39.3	93.1	41.6	95.0
<i>Bumiputera</i>	32.9	78.0	34.2	78.1
<i>Non-Bumiputera</i>	6.4	15.1	7.4	16.9
Held by non-Malaysians	2.9	6.9	2.2	5.0
Total	42.2	100.0	43.8	100.0

2001, the minimum paid-up capital/surplus of assets over liabilities prescribed for direct insurers was increased from RM50 million to RM100 million. Insurance brokers and adjusters meanwhile are required to maintain a paid-up capital unimpaired by losses of RM500,000 and RM150,000 respectively.

As at 31 December 2002, the capitalisation of Malaysian-incorporated insurers stood at RM4,886.9 million, compared with RM5,036.8 million in 2001. The reduction in the total capitalisation of insurers was due to mergers and acquisitions, which saw the revocation of eight direct insurance licences during the year. The mergers and acquisitions have however, resulted in an increase in the average capitalisation of Malaysian-incorporated insurers by 14.7% from RM96.9 million in 2001 to RM111.1 million in 2002. The capital distribution of Malaysian-incorporated insurers is given in Table 1.3.

As at the end of 2002, the total paid-up capital of licensed insurance brokers increased by 3.8% to reach RM43.8 million, while licensed adjusters registered a total capitalisation of

Table 1.5
Distribution of Paid-up Capital of Adjusters

As at end of December	2001		2002	
	RMm	%	RMm	%
Held by Malaysians	11.1	90.2	12.4	87.9
<i>Bumiputera</i>	5.7	46.3	6.7	47.5
<i>Non-Bumiputera</i>	5.4	43.9	5.7	40.4
Held by non-Malaysians	1.2	9.8	1.7	12.1
Total	12.3	100.0	14.1	100.0

RM14.1 million, an increase of 14.6% from 2001. The capital distribution of insurance brokers and adjusters are shown in Table 1.4 and Table 1.5 respectively.

Margin of Solvency

Part IX of the Regulations prescribes the margin of solvency required to be maintained by licensed insurers for each class of insurance business as follows:-

- for life insurance business, the aggregate of a specified percentage of the actuarial valuation liabilities, sums at risk and net premiums on all life policy extensions, plus total liabilities of the life insurance fund determined at the end of the financial year; and
- for general insurance business, the aggregate of a specified percentage of claims or net premiums, plus total liabilities of the general insurance fund determined at the end of the financial year.

The computed amount derived in the manner described above for each class of business is subject to a minimum amount of RM50 million in the case of licensed direct insurers and locally-incorporated professional reinsurers, and RM10 million in the case of branches of foreign professional reinsurers. Assets supporting the margin of solvency must be in the form of admitted assets specified by the Bank.

The combined aggregate solvency surplus (assets in excess of the required margin of solvency) of the industry decreased by 14.5% to RM3,365.1 million for the financial year ended 2001/2002 (Table 1.6). Seven insurers reported technical solvency deficiencies in their general insurance funds at the close of the 2001/2002 financial year. During the year, one insurer rectified its solvency deficiency, while another three insurers were acquired by other insurers. Of the remaining three insurers, one insurer was in the process of being acquired by another insurer, one insurer was running off its general business while another insurer was in the process of rectifying its solvency deficiency. However, all three insurers had sufficient assets to meet the liabilities of their general insurance funds.

Table 1.6
Solvency Surplus

As at Financial Year End	General Insurance Fund		Life Insurance Fund		Shareholders'/ Working Fund ¹		Total	
	2000	2001	2000	2001	2000	2001	2000	2001
	RM million							
Margin of solvency	12,409.3	13,229.3	35,618.1	42,073.8	n.a.	n.a.	48,027.4	55,303.1
Admitted assets	13,629.3	14,419.1	37,555.0	43,461.6	780.7	787.5	51,965.0	58,668.2
Solvency surplus							3,937.6	3,365.1

¹ Assets can be assigned from the shareholders'/working fund with the prior approval of the Bank to meet the solvency margin requirement
n.a. Not applicable

As at the end of financial year 2001/2002, retained profits registered by the industry recorded a significant increase of 38.5% to RM2,390.8 million, compared with a decrease of 15.5% to RM1,726.4 million during the preceding financial year. In total, the shareholders' funds of Malaysian-incorporated insurers increased by 14% (2000/2001: 3.2%) to RM8,018 million in 2001/2002 (Table 1.7).

Supervision

In 2002, the Insurance Supervision Department of the Bank conducted commercial examinations on 20 head offices and 16 branch offices of insurers, as well as three insurance brokers and three adjusters. During the year, officers from the Department had extended assistance to the Insurance Board of Sri Lanka to train the Board's officers as well as to develop a rating system for insurance entities in Sri Lanka similar to the EMAS (Earnings, Management, Asset Quality and Solvency) rating framework of the Bank.

Table 1.7
Shareholders' Funds of
Malaysian-incorporated Insurers

Shareholders' Fund	Financial Year End	
	2000	2001
	RM million	
Paid-up capital	4,320.4	5,058.9
Retained profit/loss	1,726.4	2,390.8
Other reserves	983.5	568.3
Total	7,030.3	8,018.0

Apart from the commercial examinations, the Information Systems Supervision Unit of the Bank conducted 11 information system examinations on insurers during 2002. The focus of these examinations was on internal controls, risk management systems and insurance operations.

In line with the objective of effective supervision of the financial institutions, on 1 March 2002, the Bank achieved the ISO 9002:1994 certification for the on-site examination processes of its three Supervision Departments. The ISO 9002 project was undertaken by the Bank with the aim of enhancing its current examination work processes, promoting greater efficiency and providing quality services to its stakeholders.

As part of the Bank's efforts to ensure effective enforcement of the regulations in line with Recommendation 4.22 of the Financial Sector Masterplan, the Bank issued the Informal Enforcement Actions Framework (IEAF) for the insurance and takaful industries on 20 December 2002. The objective of the framework is to establish a structured approach towards the enforcement of pre-emptive and corrective measures. The IEAF is applicable to all insurers and takaful operators and was implemented with effect from 2 January 2003.

To improve the efficiency in the submission of data on frauds, suspected frauds and defalcations by insurance brokers and adjusters, the reporting of such information to the Bank was computerised in 2002. Insurance brokers

Table 1.8
Compounding of Offences

Nature of Offence	Number of Licensees Fined
Contravention of:-	
Section 67(2)	1
Section 70(1)	1
Section 87	1

and adjusters are required to transmit the information to the Bank through the Electronic Fraud Information Database System (eFIDS).

Compounding of Offences

Section 211(1) of the Act empowers the Governor of the Bank to compound an offence under the Act or Regulations. In 2002, fines were imposed on three adjusters (Table 1.8) for the following offences:-

- transfer of shares without the prior approval of the Bank;
- appointment of a director without the prior approval of the Bank; and
- late submission of annual audited accounts to the Bank.

Public Complaints

The Customer Service Bureau (CSB) which was established in 1998 in the Insurance Regulation Department of the Bank serves to provide the public with an avenue to direct their complaints and enquiries on insurance matters. The CSB analyses the emerging trends of complaints lodged for the purpose of identifying any adverse developments in insurance practices that may require remedial regulatory action.

Providing policy owners with an alternative avenue to direct complaints, the Insurance Mediation Bureau (IMB) currently serves to assist in disputes between policy owners and their own insurers (third party claims do not fall within the ambit of IMB). Set up in 1992 by the insurance industry, the scope of IMB is confined to claims for amounts not exceeding RM100,000 each. In 2002, the IMB handled 1,013 cases (2001: 704), of which 24% were related to motor insurance. As in the previous

years, the bulk of the cases involved general insurers, accounting for 64% of the cases handled. It is envisaged that the role of IMB will be expanded to encompass adjudicating in disputes between insurers and third party claimants, providing counselling and advice to policy owners and claimants and dealing with complaints against adjusters and insurance brokers.

Insurance Guarantee Scheme Fund

Section 173(1) of the Act empowers the Bank to establish and maintain a separate Insurance Guarantee Scheme Fund (IGSF) for general business and life business in respect of Malaysian policies for the purpose of partially meeting the liabilities of any insolvent insurer. The IGSF is funded mainly from levies imposed on licensed insurers. Other sources of remittances into the IGSF include income from investments of the fund, proceeds from the realisation of investments, moneys recovered from insurers being wound up, borrowings, donations or contributions and 50% of all fines collected from the compounding of offences under the Act.

Currently, levies are imposed only for general insurance business. The total collection of annual levies for the year 2002 amounted to RM15.8 million (2001: RM59.8 million). The reduction in the amount of annual levies collected in 2002 was due to the reduction in the quantum of levies payable by general insurers from 1% to 0.25% of gross direct premiums. During the year 2002, the IGSF for general insurance business also received income of RM80.1 million as a result of the assignment of interim dividends declared by Mercantile Insurance Sdn. Bhd. (MISB). The dividend was assigned to the Bank by claimants and policy owners in return for payments from the IGSF. As at 31 December 2002, the total amount in the IGSF increased to RM463.7 million (2001: RM356.9 million). Although no levies are currently imposed for life insurance business, fines collected for offences related to life insurance business are credited into the IGSF for life insurance business. As at 31 December 2002, the amount in the IGSF for life insurance business stood at RM0.4 million.

Insurance claims in respect of three liquidated insurers, namely, First General Insurance (M)

Table 1.9
IGSF: Compensation and Expenses

	FGI		SEG		MISB		Total	
	2001	2002	2001	2002	2001	2002	2001	2002
	RM'000							
Amount settled todate								
Judgement awards	4,856	4,856	11,326	11,326	64,794	66,041	80,976	82,223
Out-of-court settlements	1,295	1,295	517	517	108,971	111,358	110,783	113,170
Expenses: MIB (Administrative Unit)	269	269	-	-	-	-	269	269
Professional charges	763	763	-	-	-	-	763	763
Premium refunds	-	-	-	-	1,977	1,977	1,977	1,977
Deposit refund (bond)	-	-	-	-	409	409	409	409
Others	8	8	-	-	8,695 ¹	10,192 ¹	8,703	10,200
Total	7,191	7,191	11,843	11,843	184,846	189,977	203,880	209,011
% change	-	-	1.8	-	4.3	2.7	7.1	2.5
No. of cases settled in the year	-	-	4	-	1,059	721	1,063	721
No. of cases settled todate	883	883	1,227	1,227	44,595	45,316	45,642	47,426

¹ Solicitors' and adjusters' fees

Sdn. Bhd. (FGI), SEG Insurance Sdn. Bhd. (SEG) and MISB, are payable from the IGSF for general insurance business. While there were no claims paid in respect of FGI and SEG for the year, payments were made from the IGSF for the

settlement of 721 claims against MISB amounting to RM5,131,219. The total cumulative payments made to date from the IGSF for general insurance business is shown in Table 1.9.