

Administration of the Act

- 1-1 Legislation
- 1-3 Licensing and Market Structure
- 3-4 Margin of Solvency
- 4-5 Supervision of Licensees
- 5-5 Compounding of Offences
- 5-6 Public Complaints
- 6-7 Insurance Guarantee Scheme Fund

Administration of the Act

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 empowers Bank Negara Malaysia (the Bank) to specify matters pursuant to the provisions of the Act.

Specifications

As part of efforts to further develop and promote the efficient functioning of the domestic bond market, the following revisions were made in 2004 to the specifications on investments which are admissible (admitted assets) for the purpose of supporting the margin of solvency of insurers pursuant to section 46(2) of the Act:

- classification of investments by insurers in new Cagamas debt securities issued after 4 September 2004 as credit facilities to be consistent with other private debt issues; and
- inclusion of investments by insurers in approved ringgit-denominated bonds issued by multilateral development banks and multilateral financial institutions in the category of low risk assets.

Licensing and Market Structure

Licensing of Insurers, Insurance Brokers and Adjusters

As at 31 December 2004, a total of 49 insurers were licensed under the Act compared with 53 at the end of 2003. The reduction in the number of licensed insurers was the result of the revocation of four licences, including one general insurance licence following the completion of a merger. The licences of two foreign professional reinsurers namely, Gerling-Konzern Globale Rückversicherungs-Aktiengesellschaft and HSB Engineering Insurance Limited were revoked following the rationalisation or relocation of their operations in 2003. In addition, the licence of another

reinsurer, Cologne Reinsurance Company Plc., was revoked during the year following the transfer of its business to the Labuan International Offshore Financial Centre (IOFC). The 49 insurers licensed under the Act as at end December 2004 include:

- 26 insurers in direct general insurance business;
- seven insurers in direct life insurance business;
- nine insurers in direct life and general insurance business;
- five professional reinsurers in general reinsurance business;
- one professional reinsurer in life reinsurance business; and
- one professional reinsurer in life and general reinsurance business.

The total number of licensees in the insurance industry as at the end of 2004 stood at 120, comprising 49 insurers, 34 insurance brokers and 37 adjusters as shown in Table 1.1. The lists of licensed insurers and reinsurers, insurance brokers and adjusters are given respectively in Appendices II, III and IV of this Report.

Table 1.1
Number of Licensees

As at end of December	2003	2004
Direct insurers		
<i>Malaysian-incorporated</i>	41	40
<i>Foreign-incorporated</i>	2	2
Sub-total	43	42
Professional reinsurers		
<i>Malaysian-incorporated</i>	2	2
<i>Foreign-incorporated</i>	8	5
Sub-total	10	7
Total insurers	53	49
Insurance brokers	35	34
Adjusters	39	37

Agents

Insurance agents are not directly supervised by the Bank under the Act. However, they are required to be registered with the mandatory insurance associations approved by the Bank,

namely, the Life Insurance Association of Malaysia for life insurance agents and Persatuan Insuran Am Malaysia for general insurance agents. To enhance the level of professionalism among the agency force, the minimum entry requirement for a new agent is Sijil Pelajaran Malaysia or Malaysia Certificate of Education qualification or its equivalent qualification. In addition, all agents are required to pass the compulsory Pre-Contract Examination for Insurance Agents conducted by the Malaysian Insurance Institute.

There were 131,229 (2003: 129,631) registered insurance agents as at the end of 2004. The number of life insurance agents decreased to 82,551 (2003: 86,230) while the number of general insurance agents increased to 48,678 (2003: 43,401).

Change of Company Status

Section 14 of the Act requires all licensed insurers (other than foreign professional reinsurers which are allowed to operate as branches in Malaysia) to be incorporated as public companies under the Companies Act 1965. During the year, there were no changes effected in the status of licensed direct insurers pursuant to this section. The list of foreign insurers which have 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. The criteria for opening of a branch office include compliance with the minimum paid-up capital and solvency requirements as well as the guidelines on operating costs. In 2004, a total of 30 branch offices were approved, bringing the total number of branch offices operating to 891 as at the end of 2004, as shown in Table 1.2.

Table 1.2
Number of Branches

	Insurers	Insurance Brokers	Adjusters
Approved in 2004	23	0	7
Operating as at 31 December 2004	722	26	143

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

As at end of December	2003		2004	
	RMm	%	RMm	%
Held by Malaysians	2,892.2	59.2	2,811.5	57.6
<i>Bumiputera</i>	1,461.5	29.9	1,383.2	28.3
<i>Non-Bumiputera</i>	1,430.7	29.3	1,428.3	29.3
Held by non-Malaysians	1,992.9	40.8	2,068.4	42.4
Total	4,885.1	100.0	4,879.9	100.0

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. The current minimum paid-up capital/surplus of assets over liabilities prescribed for insurers are as follows:

- RM100 million for local/foreign direct insurers and local professional general reinsurers;
- RM50 million for local professional life reinsurers; and
- RM20 million for foreign professional life and general reinsurers.

Insurance brokers and adjusters are required to maintain a paid-up capital unimpaired by losses of RM500,000 and RM150,000 respectively.

As at the end of 2004, the total capitalisation of Malaysian-incorporated insurers reduced

Table 1.4
Distribution of Paid-up Capital of Insurance Brokers

As at end of December	2003		2004	
	RMm	%	RMm	%
Held by Malaysians	41.8	95.0	42.2	94.6
<i>Bumiputera</i>	34.4	78.2	33.5	75.1
<i>Non-Bumiputera</i>	7.4	16.8	8.7	19.5
Held by non-Malaysians	2.2	5.0	2.4	5.4
Total	44.0	100.0	44.6	100.0

Table 1.5
Distribution of Paid-up Capital of Adjusters

As at end of December	2003		2004	
	RMm	%	RMm	%
Held by Malaysians	12.2	85.9	13.3	92.4
<i>Bumiputera</i>	6.5	45.8	6.5	45.2
<i>Non-Bumiputera</i>	5.7	40.1	6.8	47.2
Held by non-Malaysians	2.0	14.1	1.1	7.6
Total	14.2	100.0	14.4	100.0

marginally to RM4,879.9 million (2003: RM4,885.1 million) (Table 1.3). Although four insurers had increased their paid-up capital during the year, the marginal reduction in capitalisation was due to the revocation of the licence of an insurer following a merger. The average capitalisation of 42 Malaysian-incorporated insurers however, has increased by 2.3% to RM116.2 million (2003: RM113.6 million).

The total paid-up capital of insurance brokers and adjusters increased marginally to RM44.6 million and RM14.4 million respectively as at the end of 2004. The distribution of paid-up capital for insurance brokers and adjusters are shown in Table 1.4 and Table 1.5 respectively.

As at the end of 2004, the retained profits of the industry increased by 34.5% to RM3,991.1 million. In total, the shareholders' equity of Malaysian-incorporated insurers increased by 13.4% to RM9,436.3 million in 2004 (Table

Table 1.6
Shareholders' Equity of Malaysian-incorporated Insurers

As at end of December	2003	2004
	RM million	
Paid-up capital	4,885.1	4,879.9
Retained profit	2,968.4	3,991.1
Other reserves	465.3	565.3
Total	8,318.8	9,436.3

1.6) while the average shareholders' equity correspondingly increased to RM224.7 million (2003: RM193.5 million).

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.

Table 1.7
Solvency Surplus

As at Financial Year End	General Insurance Fund		Life Insurance Fund		Shareholders'/ Working Fund ¹		Total	
	2002	2003	2002	2003	2002	2003	2002	2003
	RM million							
Margin of solvency	13,424.3	14,099.4	47,071.4	54,728.2	n.a.	n.a.	60,495.7	68,827.6
Admitted assets	14,771.6	15,617.7	49,515.8	58,509.0	873.6	810.7	65,161.0	74,937.4
Solvency surplus							4,665.3	6,109.8

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

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 (admitted assets in excess of the required margin of solvency) of the industry increased by 31% to RM6,109.8 million for the financial year ended 2003/2004 (Table 1.7). During the year, a total of 10 insurers transferred or assigned assets from their shareholders' funds to meet the admitted assets requirement.

in the industry. To minimise duplication of effort, the Bank leveraged on the work done by external and internal auditors, appointed actuaries and other professionals in respect of the fairness of financial statements, control environment, operational compliance with policies and procedures, and adequacy of reserves for policy liabilities. With this forward-looking approach, the Bank is able to allocate resources more optimally and give greater supervisory attention to entities that are systemically important and/or have higher risk profiles.

In order to promote a fair marketplace for consumers and insurers, market conduct supervision was carried out to continuously assess the conduct of the supervised entities

A new Risk Based Supervisory Framework was implemented in August 2004 to reinforce sound business practices and risk management culture in the industry.

Supervision of Licensees

The supervisory activities in 2004 were focused on efforts to further promote a sound and robust insurance industry through continuous and dynamic monitoring of insurers, prescribing pre-emptive measures and enforcement of prudential regulatory standards. Since 2003, the Bank embarked on a strategic shift in its supervisory philosophy and approach, which has resulted in a transformation from a bottom-up, audit-based supervision approach to one that is more holistic and forward-looking, in line with the latest global developments in the supervision of insurance entities.

In August 2004, the new Risk Based Supervisory Framework (RBSF) was launched, with the continued aim of ensuring that all supervised entities adopt sound business practices. The new supervisory process uses a structured approach to assess an insurer's risk profile, its financial condition, and the adequacy of its operational management and risk management systems, in order to form an overall assessment of the insurer's health and the probability of key risks materialising in the future. Different emphasis was accorded to supervised entities with different risk profiles, which in turn promoted a stronger risk management culture

especially in the area of claims settlement practices. These checks were conducted to ensure that insurers treat customers fairly, handle complaints adequately and avoid conflicts of interest in their business activities. The Bank will continue to enhance its market conduct supervision framework by benchmarking against best practices adopted by other regulators worldwide.

A fraud surveillance system had also been put in place through which incidences of fraud could be monitored. As a result, the Bank was able to identify new modus operandi of frauds and alert the insurance industry so as to prevent further occurrences and losses to insurers and their policy owners. In a collaborative effort between the Bank and the insurance associations to combat insurance fraud, anti-fraud committees were set up in 2004 to identify and develop recommendations for better co-ordination and co-operation between the Bank, law enforcement agencies and insurance associations.

With the rapid development of technology in the insurance industry, insurers need to be more effective in managing the related information systems (IS) risks. The Bank had

undertaken several measures to enhance the overall IS governance as well as to promote IS best practices in the industry. These include on-site examination, off-site monitoring, issuance of guidelines on the management of the IS environment and improving IS supervision by benchmarking against other proven IS auditing standards. For better assessment of the IS environment and the soundness of the IS operations of insurers, the Bank had enhanced the quality of its IS supervision function by implementing a new methodology for on-site examination, PRiSM (Information Systems Risk Assessment). This methodology provides a more balanced appraisal of the IS environment by linking the IS practices and risks to the business requirements and processes. The Bank is also developing a system which contains information on the development and usage of technology by the insurers, to enhance the off-site monitoring function. The system would be able to provide an early warning mechanism on potential systemic risks as well as to provide benchmarking of core processes across the insurers and promote best practices in IS risk management.

The Bank continued to place important emphasis on embedding strong corporate governance culture in all aspects of insurance. The roles and functions played by the board members towards enhancing their organisation's capacities, capabilities and competitiveness were continuously assessed and evaluated as part of the supervisory activities. In addition, the Bank held frequent dialogues with members of the board and senior management of insurers to keep abreast with the latest issues, business strategies, risk profile and risk management capabilities, whilst at the same time, communicating supervisory concerns to the senior management of insurers. More active involvement by the board and senior management of insurers in risk management issues had led to the creation of a strong risk management culture across the supervised entities. Directors and senior management of insurers, particularly the independent directors, are also more aware of their responsibilities and played an active role in guiding the institutions.

To combat money laundering activities, the Bank also reviewed the adequacy of anti-money laundering and anti-terrorist financing measures

Table 1.8
Compounding of Offences

Nature of Offence	Number of Licensees Fined
Contravention of:	
Section 36(1)	1
Section 70(1)	1
Section 74	2

established by the supervised entities. The Bank and the supervised entities have instituted the necessary measures to deter and detect undesirable money laundering activities, which can undermine the integrity of the insurers.

In addition to the on-site supervision, each supervised entity is also subjected to continuous monitoring of its resilience to economic shocks under stressed conditions. In this connection, insurers are required to submit the results of their stress tests to the Bank on a half-yearly basis. The stress test incorporates a set of minimum parameters as prescribed by the Bank with flexibility given to the supervised entities to adopt their own assumptions for certain parameters.

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 2004, fines were imposed on four licensees (Table 1.8) for offences relating to the opening of branch offices, reappointment of a director and appointment of auditors without the prior approval of the Bank.

Public Complaints

The Customer Service Bureau (CSB) in the Bank provides the public with an avenue to direct their complaints and enquiries on insurance matters. The CSB liaises with the industry and its relevant associations to resolve complaints against licensees. As part of the Bank's efforts to raise the standard of service provided by insurers, the CSB analyses the nature of complaints received in order to identify insurance practices that may require remedial regulatory action.

Table 1.9
IGSF: Compensation and Expenses

	FGI		SEG		MISB		Total	
	2003	2004	2003	2004	2003	2004	2003	2004
	RM'000							
Amount settled to-date								
Judgement awards	4,856	4,856	11,326	11,326	66,978	67,477	83,160	83,659
Out-of-court settlements	1,295	1,295	517	517	113,932	117,090	115,744	118,902
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 ¹	8	8	–	–	10,545	11,702	10,553	11,710
Total	7,191	7,191	11,843	11,843	193,841	198,655	212,875	217,689
% change	–	–	–	–	2.0	2.5	1.8	2.3
No. of cases settled in the year	–	–	–	–	609	605	609	605
No. of cases settled to-date	883	883	1,227	1,227	45,925	46,530	48,035	48,640

¹ Refer to solicitors' and adjusters' fees

The total number of complaints handled by the CSB in 2004 increased marginally to 2,376 cases (2003: 2,231). Complaints and disputes on motor insurance continued to dominate, accounting for 50.7% of the total complaints received against this sector. The common complaints include delay in claims settlement, dissatisfaction with the sum of settlement, repudiation of liability and delay in payment of court awards.

The Insurance Mediation Bureau (IMB), set up by the insurance industry in 1992 had served as another avenue for policy owners to resolve disputes or complaints against their own insurers. The scope of the IMB was confined to claim amounts not exceeding RM100,000 per case while third party claims did not fall within the ambit of the IMB. In 2004, the number of cases handled by the IMB increased marginally to 1,105 cases (2003: 1,070) of which 55.8% were related to general insurance. As part of efforts to strengthen the redress mechanism in the financial sector, the Financial Mediation Bureau (FMB) was established through the integration of the functions of the IMB and the Banking Mediation Bureau. The FMB now acts as a one-stop dispute resolution centre for all financial institutions under the supervision of the Bank.

The Bank has also set up a customer service centre named 'Laman Informasi Nasihat dan Khidmat' (LINK) or better known as Bank Negara Malaysia LINK at its premises in early 2005. The centre acts as a central point of contact to facilitate rapid and effective response for members of the public in matters related to the financial sector. The LINK's role includes attending to general enquiries and public complaints relating to insurance matters. The LINK operates in tandem with the CSB, with the latter being responsible for handling the more complicated disputes and complaints, and taking appropriate remedial regulatory action.

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. Under the Act, other sources of remittances into the IGSF include income from investments of the fund, proceeds from the realisation of investments, dividends assigned from claimants in return for payments received

from the IGSF 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 levies in 2004 based on 0.25% of gross direct premiums for the preceding financial year amounted to RM20.6 million (2003: RM19 million). As at 31 December 2004, the total amount in the IGSF increased to RM534.3 million (2003: RM497.8 million). The amount in the IGSF for life insurance business remained unchanged at RM0.5 million at 31 December 2004, being fines collected for offences related

to life insurance business which were credited into the IGSF.

Insurance claims in respect of three liquidated insurers, namely, First General Insurance (M) Sdn. Bhd. (FGI), SEG Insurance Sdn. Bhd. (SEG) and Mercantile Insurance Sdn. Bhd. (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 amounting to RM4.8 million were made from the IGSF for the settlement of 605 claims against MISB. The total cumulative payments made to date from the IGSF for general insurance business is shown in Table 1.9.