



Perbadanan Insurans Deposit Malaysia
Protecting Your Insurance And Deposits In Malaysia

**PUBLIC CONSULTATION PAPER ON
PROPOSED INSURANCE COMPENSATION SCHEME**

ISSUE DATE : 24 JUNE 2010
CLOSING DATE : 23 JULY 2010



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1.0 BACKGROUND

- 1.1 Further to the announcement of the Government to implement an enhanced financial consumer protection package, Perbadanan Insurans Deposit Malaysia (“PIDM”) has developed the key design features of the proposed insurance compensation scheme (“ICS”).
- 1.2 This Consultation Paper sets out the proposed design features of the ICS and PIDM seeks comments from the public on the proposed key design features particularly those set out in paragraphs 7, 8 and 9 of this document. All comments will be treated in strictest confidence. All comments will be considered and, where appropriate, incorporated into the proposed ICS. The final design features will then be incorporated into the Malaysia Deposit Insurance Corporation Act 2005 to give effect to the ICS.

2.0 DEADLINE FOR COMMENTS

- 2.1 The deadline for submission of comments to PIDM is 23 July 2010.
- 2.2 Members of the public may call at 1800 88 1266 or provide written comments, directed to:

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Perbadanan Insurans Deposit Malaysia
Level 19, 1 Sentral
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3.0 INSURANCE GUARANTEE SCHEME FUND

- 3.1 There is currently an Insurance Guarantee Scheme Fund (“IGSF”) which has been established by Bank Negara Malaysia (“BNM”) under the Insurance Act 1996 with the aim of building up a readily available pool of funds to meet the claims of policy owners of failed insurance companies.
- 3.2 The IGSF is funded by the insurance industry to minimise the need to utilise public funding for resolving claims of failed insurance companies. There are separate funds for insurance companies that conduct life insurance and general insurance business.
- 3.3 Pursuant to Section 173 of the Insurance Act 1996, the IGSF for general insurance business is funded by way of levies assessed on general insurance companies. Presently, levies are collected annually from the general insurance companies at a rate of 0.25% of gross direct premiums. The Fund has been used to settle the claims of policy owners and other claimants of failed general insurance companies.
- 3.4 Levies have yet to be imposed on life insurance companies as no life insurance company has failed.
- 3.5 In respect of takaful companies, BNM is empowered to establish an IGSF for takaful companies pursuant to Section 21 of the Takaful Act 1984. However, an IGSF for takaful companies has yet to be established.

4.0 RATIONALE FOR ICS

- 4.1 There are strong public policy objectives for establishing the proposed insurance compensation scheme (“ICS”). The insurance and takaful industry (collectively referred to as “insurance industry”) is an integral part of the Malaysian financial system (total industry assets account for 5.4% of the financial system as at end-2009). Many Malaysians increasingly consider life insurance policies and takaful plans as a form of savings. As at end-2009, there are currently 14.4 million life policies and takaful plans (collectively referred to as “policies”) in force compared with 13.7 million as at end-2008. The general insurance premiums have increased from RM11.2 billion as at end-2008 to RM12.6 billion in 2009. It is important from policy owners and takaful participants’ (collectively referred to as “policy owners”) perspective that their savings be protected in the unlikely event of a failure of an insurance or takaful company. Such protection and assurance of payment in the

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event of a failure will enhance public confidence as well as promote consumer demand for insurance products.

- 4.2 The proposed ICS is also expected to benefit the insurance industry as it will level the playing field between the banking and insurance industries. This will further promote confidence.
- 4.3 The IGSF provides compensation to policy owners and other claimants only upon the failure of an insurance or takaful company. As compared with the IGSF, the proposed ICS would have a broader function, including, complementing BNM's efforts to promote sound risk management of insurance and takaful companies. More importantly, PIDM would have a risk minimiser function that would enable it, subject to legislative checks and balances and consultation with BNM, to resolve and intervene in a troubled insurance and takaful company before it becomes insolvent. In this regard, the ICS enables PIDM to act as a proxy for policy owners in monitoring the health and soundness of insurance and takaful companies.

5.0 HOW ICS WORKS

- 5.1 A number of countries around the world have established ICS systems to protect their citizens against the loss of their claims when failures of insurance companies occur. PIDM will provide that protection in Malaysia, subject to the specified limits and scope of coverage proposed in paragraphs 8 and 9 of this document.

6.0 GUIDING PRINCIPLES FOR DESIGN OF ICS

- 6.1 The design of the proposed ICS is guided by considerations that it:
- will protect at least 95% of all insurance and takaful policy owners;
 - is equitable for both the conventional insurance companies and takaful companies, such that competitive distortion is minimised;
 - is Shariah compliant in respect of all takaful dealings; and
 - will meet the unique needs of our local environment.

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7.0 PROPOSED DESIGN FEATURES APPLICABLE TO CONVENTIONAL INSURANCE AND TAKAFUL

7.1 The following are the proposed key design features of the ICS that are applicable to both general conventional insurance and life insurance as well as general takaful and family takaful companies:

	Proposals	Rationale
(i)	<p>Membership will be compulsory for:</p> <ul style="list-style-type: none"> • Insurance companies licensed under the Insurance Act 1996 to conduct life and/or general insurance business in Malaysia; and • Takaful companies licensed under the Takaful Act 1984 to conduct family and general takaful business in Malaysia. <p>Excluded are:</p> <ul style="list-style-type: none"> (i) Reinsurance and retakaful companies; (ii) Captive insurers; (iii) Offshore insurance companies; (iv) International takaful operators licensed under the Takaful Act 1984; and (v) Other players in the insurance industry, such as insurance brokers, insurance adjusters and insurance agents. 	<ul style="list-style-type: none"> • Life insurance policies and family takaful plans are important long-term savings and income protection vehicles for households while general insurance policies and general takaful plans provide indemnity and protection to the public against losses arising from unforeseen events or other contingencies. Given the social implications to policy owners arising from losses of insured benefits if ever an insurance or takaful company should fail, it is important for the ICS to provide financial protection to policy owners. • We propose to exclude other players in the insurance industry for the following reasons: <ul style="list-style-type: none"> (i) reinsurers/retakaful and captive specialists companies do not conduct business for members of the Malaysian public; (ii) offshore insurers and international takaful operators conduct business in foreign currencies; and (iii) other players are intermediaries with no financial commitment to pay claims to policy owners. The intention of the proposed ICS is to protect policy owners strictly against financial loss from an insurance policy. Also, intermediaries are agents of insurance companies and takaful companies which are accountable and liable for the actions of their intermediaries.

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(ii)	<p>Separation of Deposit Insurance and ICS Funds</p> <ul style="list-style-type: none"> • PIDM will maintain separate Deposit Insurance and ICS Funds. • PIDM will maintain four separate ICS Funds for the different business classes. There will be no mingling of income or costs between the ICS Funds or the Deposit Insurance Funds. The Funds are: <ul style="list-style-type: none"> ➢ Conventional Life ICS Fund; ➢ Conventional General ICS Fund; ➢ Family Takaful ICS Fund; and ➢ General Takaful ICS Fund. 	<ul style="list-style-type: none"> • Currently, PIDM maintains 2 separate Deposit Insurance Funds, namely the Conventional Deposit Insurance Fund and the Islamic Deposit Insurance Fund. There is no mingling of funds. • For purposes of equity, transparency and accountability, four separate funds under the proposed ICS, will be maintained since each fund will be built from levies from different categories of insurance and takaful companies for the benefit of their respective policy owners. • The above approach is also consistent with the deposit insurance system and compliant with the Shariah principle that there be clear segregation between Islamic and Conventional Funds.
(iii)	<p>Funding</p> <ul style="list-style-type: none"> • The ICS will be funded from annual levies assessed against insurance and takaful companies. 	<ul style="list-style-type: none"> • This approach is consistent with the deposit insurance system. Policy owner protection benefits insurance and takaful companies. Hence, they should fund the cost of providing it.
(iv)	<p>Subrogation and priority ranking</p> <ul style="list-style-type: none"> • Should PIDM be called upon to exercise its mandate to policy owners, PIDM, having paid claims due to policy owners, will automatically be subrogated to the rights of the claimants to the extent of claims paid by PIDM. • PIDM's claims against the liquidator of the failed insurance company will rank pari passu with other unpaid claims of policy owners. 	<ul style="list-style-type: none"> • This is consistent with the current legal position under the deposit insurance system and is equitable since PIDM would have paid claims to the policy owners. • If a policy owner has an unpaid claim over and above the ICS limit, his unpaid claim will rank equal with PIDM's claims against the liquidator, thus ensuring equity and fairness.

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(v)	<p>Aggregation rule</p> <ul style="list-style-type: none"> • Claims for death, critical illness and permanent disability, medical expenses and disability benefits will be aggregated based on a “per life insured per policy owner per insurance company” rule. • Riders on a basic life policy will be included in the aggregation of sums assured for the respective insured benefits. • Claims for damage to property will be aggregated on a “per property per policy owner per insurance company” rule. <p>Please refer to Illustration 1 on how the aggregation rules will be applied.</p>	<ul style="list-style-type: none"> • The aggregation rule requires the insured person’s claims be aggregated for the purpose of meeting the compensation limit. In general, the aggregation rule that is commonly used for payment of claims to policy owners is based on a “per life per insurance company”. • The proposed ICS aggregation rule is more flexible and advantageous for policy owners. The effect is that separate policy owners, including employers who purchase employee group policies, will get separate coverage although the policies are purchased on the same life assured. This is more equitable since the insured has no influence over a policy owner’s choice of insurance company. Please see Illustration 1 on how the rule will be applied. • In respect of properties insured, the intention of the rule is to ensure that policy owners get coverage up to the maximum limit for each property insured for each occurrence of an insured event.
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8.0 PROPOSED LIMITS AND SCOPE OF COVERAGE FOR LIFE AND FAMILY TAKAFUL

8.1 The following are the limits and scope of coverage that are proposed under the ICS for conventional life insurance and family takaful companies:

	Proposal	Rationale
(i)	<p>Insured events and benefits to be protected</p> <ul style="list-style-type: none"> • Protection is provided only to individuals holding Malaysian policies which insure the following events or insured benefits: <ul style="list-style-type: none"> ➤ Death; ➤ Permanent disability; ➤ Critical illness; ➤ Maturity value¹; ➤ Accumulated value²; ➤ Surrender value³; ➤ Medical expenses; ➤ Disability income; and ➤ Income benefits. • Investment-linked products are not proposed to be covered under the ICS. 	<ul style="list-style-type: none"> • These insured risks and benefits are the common benefits required by an individual to maintain their well-being and should therefore be protected from financial loss arising from the failure of an insurance company or takaful company. • The majority of individuals and retail policy owners are not in the position to adequately assess the health of their insurance and takaful companies and therefore should be provided protection as an avenue to mitigate their losses in the event of a failure. • The insurance portion of investment-linked products which insure events and benefits protected under the ICS will be covered subject to the ICS limits.
(ii)	<p>Policy owners to be protected</p> <ul style="list-style-type: none"> • All policy owners who purchase a policy or takaful plan on the life of an individual. 	<ul style="list-style-type: none"> • Protecting individual policy owners is in line with the universally adopted rationale that the compensation scheme covers those consumers who are not in a position to adequately assess the health of their insurance or takaful companies.

¹ Maturity value represents the insured amount received by a policy owner at the end of an endowment period (usually the face value of the endowment policy).

² Accumulated values represent the value of accumulated dividends and bonuses that are vested for the benefit of the policy owner. The accumulated values are separate from the maturity values. Prepaid premiums are not part of accumulated values.

³ Surrender values represent the amount available in cash upon voluntary termination of a policy before it becomes payable on death or maturity.

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(iii)	<p>Proposed limits and scope of coverage</p> <ul style="list-style-type: none"> • Cap of RM500,000 for death, critical illness, permanent disability and maturity value. • Cap of RM100,000 for accumulated value. • Cap of RM500,000 for surrender value. • Cap of RM10,000 per month for disability income and annuity income. • 100% on medical expenses incurred. 	<ul style="list-style-type: none"> • Based on a recent survey, the proposed coverage limit of RM500,000 provides adequate coverage for 97% of life policy owners (94% of total value of policies insured).
(iv)	<p>Prepaid premiums</p> <ul style="list-style-type: none"> • Full refund on prepaid premiums. 	<ul style="list-style-type: none"> • These are monies belonging to policy owners and should rightfully be refunded.

Basis for RM500,000 and other limits

- 8.2 As mentioned above, a survey was conducted on the value of life policies held by life insurance companies and takaful companies in November 2009. At this proposed maximum limit of RM500,000, up to 97% of all life policy owners will be covered in full and this accounts for 94% of total value of policies insured. The effect is that almost all policy owners would be covered in full. In addition, those policy owners who wish to have full ICS coverage, may purchase insurance policies from several insurance and takaful companies, thereby distributing their coverage risks.
- 8.3 In respect of accumulated values, a cap is being proposed at RM100,000 as policy owners usually have the option to take out cash that is accumulated in their policies.
- 8.4 It is being proposed that the surrender value would be covered up to RM500,000 to provide confidence to life policy owners to retain their policies. PIDM's preferred approach in the resolution of a troubled insurance company is to transfer policies with surrender values to another insurer. Therefore, a high surrender value is proposed so as not to penalise policy owners who surrender their policies due to economic or other circumstances. In respect of medical expenses, our proposal is to not put a cap on this benefit.

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8.5 In respect of disability income and income benefits, we are proposing a cap of RM10,000 per month. Based on a study conducted in 2007 by the Statistics Department, 95% of households earn RM10,000 and less⁴. As such, if all Malaysian households purchase a disability insurance policy, the proposed cap of RM10,000 will cover 95% of all Malaysian households in full.

We seek comments and suggestions on whether:

- (i) the proposed limits and scope of coverage as set out in paragraph 8.1 (iii) are appropriate to meet the insurance needs of Malaysians; and
- (ii) there are other events or benefits that should be protected under the proposed ICS.

8.6 Table 1 below summarises the above proposals for conventional life insurance and family takaful.

Table 1: Summary of Proposals on Limits and Scope of Coverage for Conventional Life Insurance and Family Takaful

Insured Events and Benefits	Malaysian Policies Covered	
	Individual Policies	Employee Group Policies
	Maximum limit	Maximum limit
Death	RM500,000	RM500,000
Permanent disability	RM500,000	RM500,000
Critical illness	RM500,000	RM500,000
Maturity values	RM500,000	RM500,000
Accumulated values	RM100,000	RM100,000
Surrender value	RM500,000	RM500,000
Medical expenses	100% on expenses incurred	100% on expenses incurred
Disability income	RM10,000 per month	RM10,000 per month
Income benefits (annuity)	RM10,000 per month	RM10,000 per month
Prepaid premiums	To be refunded	

⁴ Extract from Parliament Hansaard, Dewan Rakyat for July 2008 Session dated 9 July 2008.

9.0 PROPOSED LIMITS AND SCOPE OF COVERAGE FOR GENERAL INSURANCE AND GENERAL TAKAFUL

9.1 The following are the proposed key design features of the ICS that are applicable to conventional general insurance and takaful general companies:

	Proposal	Rationale
(i)	<p>Insured benefits and events to be protected</p> <ul style="list-style-type: none"> Protection is provided for Malaysian policies that insure risks relating to death, critical illness, permanent disablement, medical and property damage. 	<ul style="list-style-type: none"> Individuals and retail policy owners are generally not in a position to assess the health of their insurance and takaful companies and should therefore be protected from financial losses arising from the failure of an insurance or takaful company.
(ii)	<p>Policy owners to be protected</p> <p>The following policy owners will be protected:</p> <ul style="list-style-type: none"> Individuals; Sole proprietors; Partnership of individuals; Trade unions; Registered societies; Cooperatives; Registered charities; and Small medium enterprises (SMEs)⁵. <p>The following policy owners are proposed not to be protected:</p> <ul style="list-style-type: none"> Corporations which are not listed above are not covered under the ICS. However, the group employee policies that corporations purchase for their employees will be protected. 	<ul style="list-style-type: none"> Protecting individual policy owners is in line with the universally adopted rationale that an ICS should cover consumers who are not in a position to adequately assess the health of their insurance or takaful companies. In respect of SMEs, providing coverage for SMEs is in line with the national policy of supporting the SMEs given their important role as one of the engines of economic growth.

⁵ As defined by the National SME Development Council on 9 June 2005:

- (i) For primary agriculture sector, it refers to an enterprise with full-time employees not exceeding 50 or annual sales turnover not exceeding RM5 million.
- (ii) For manufacturing sector (including manufacturing related sector), it refers to an enterprise with full-time employees not exceeding 150 or with annual sales turnover not exceeding RM25 million.
- (iii) For services sector (including information and communications technology), it refers to an enterprise with full-time employees not exceeding 50 or annual sales turnover not exceeding RM5 million.

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(iii)	<p>Proposed limits and scope of coverage</p> <p><u>Property damage</u></p> <ul style="list-style-type: none"> • Cap of RM500,000 for damage to property of a protected person. • Cap of RM500,000 for 3rd party claims for damage to property of 3rd party claimant. <p><u>Personal Accident, Medical and Health</u></p> <ul style="list-style-type: none"> • Cap of RM500,000 for death, critical illness and permanent disability. • 100% on medical expenses incurred. • RM10,000 per month for disability income. • The above caps are applicable to claims by for 3rd party claimants. However, a 3rd party motor claim is excluded. 	<ul style="list-style-type: none"> • Based on a recent survey conducted by BNM, the proposed coverage limit of RM500,000 provides adequate coverage for the protected risks insured by individuals. The survey indicated more than 98% of policy owners holding motor, fire and personal accident policies would be fully covered. • A 3rd party motor claim is excluded as these claims will be insured by the new corporation that is to be jointly owned by the Government and the insurance industry.
(iv)	<p>Unearned Premiums</p> <ul style="list-style-type: none"> • To be refunded based on the unexpired period of insurance to those categories of protected owners. 	<ul style="list-style-type: none"> • A refund will enable policy owners to purchase alternative insurance coverage.

Basis for RM500,000 and other limits

9.2 It is suggested that the ICS compensation limit be subject to a cap of RM500,000 for death, critical illness and permanent disablement. As mentioned earlier, the survey conducted showed that this cap is sufficient to protect 95% of policy owners. Disability income is subject to a cap of RM10,000 per month. This limit should be sufficient to protect policy owners as 95% of households earn RM10,000 per month and less. Medical expenses incurred will be fully met under the ICS. This means that in the unlikely event of an insurance company or takaful company failure, policy owners who incurred medical expenses that are covered under their policies would be able to claim for all such medical expenses subject to the terms of their respective insurance contracts.



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We welcome comments and suggestions on whether:

- (i) the proposed limits and scope of coverage as set out in paragraph 9.1 (iii) are appropriate to meet the general insurance needs of Malaysians; and
- (ii) certain classes of property, especially luxurious properties, such as yachts or private airplanes, should be excluded from the ICS, since the ICS is intended to cover retail policy owners;
- (iii) any of the proposed categories of policy owners should be excluded; and
- (iv) large policy owners within the proposed categories should be protected. For example, should only small or medium size cooperatives be protected under the ICS?

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9.3 The above proposals for general insurance limits and scope of coverage are summarised in Table 2 below.

Table 2: Summary of Proposals on Limits and Scope of Coverage for General Insurance and General Takaful

Policy owners	Malaysian Policies covered	
	Policies insuring against damage to property ⁶	Policies insuring against death, critical illness, permanent disability ⁷ and medical
	Maximum limit	Maximum limit
Individuals, sole proprietor	RM500,000 on each property damaged under a single event.	(i) RM500,000 for insured persons who suffer death, critical illness or permanent disablement (ii) RM10,000 per month for persons insured for disability income (iii) 100% on medical expenses incurred for insured persons.
Partnership of individuals		
Trade unions		
Registered societies &		
Cooperatives		
Small medium enterprises		
Corporations not listed above.	Excluded	(i) RM500,000 for employees insured under a group scheme, who suffer death, critical illness or permanent disablement (ii) RM10,000 per month for employees insured under a group scheme for disability income (iii) 100% on medical expenses incurred for employees insured under a group scheme.
Third party claimant ⁸	RM500,000 on damage to a 3 rd party claimant's property.	RM500,000 on death, critical illness, permanent disablement and medical expenses suffered by a 3 rd party claimant other than under a 3 rd party motor policy. ⁹
Unearned premiums	To be refunded to above protected policy owners.	

⁶ Claims may arise from any damage caused by accidents, theft, fire, floods, earthquakes, etc to the insured or 3rd party. As an example, a claim for damage to luggage under a travel insurance policy will fall within this category of property damage. If a yacht owned by an individual suffers damage, the individual can file a claim for up to RM500,000.

⁷ Claims may arise due to accidents, illness or from any related cause and such claims will be honoured so long as the insured person suffers death, critical illness or permanent disablement. Claims may be made under a Personal Accident, medical or travel policy. For example, a workman may claim under this category if he injures himself while working.

⁸ Refers to a claimant who is a person or an entity who falls within one of the protected categories of policy owners listed above i.e. an individual, a sole proprietor, etc. For example, an owner (who is an individual) suffered damage to his yacht caused by a ship (owned by a corporate) may claim for 3rd party damage to his yacht notwithstanding that the ship is owned by a corporate.

⁹ 3rd party motor policy will be covered under BNM's recent proposed initiative.

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Illustration 1: Application of Aggregation Rule

General Insurance Company B fails		
Policy owners of Company B	Amount insured	Life insured
Kong Sin Kee , a sole proprietor has 4 employees (Kong, Abu, Bala and Chin)	The sole proprietor purchased an Employee Group Personal Accident (PA) of RM100,000 for each employee. This policy also covers medical expenses of RM50,000 per employee.	Mr Kong and his three employees
Abu has a separate PA under his own name	RM250,000	Abu
Chin has 2 separate PA policies in his own name, namely Policy 1 and 2	PA Policy 1: RM300,000 PA Policy 2: RM300,000	Chin
Three employees of Mr Kong were involved in a road accident and the following events occurred: <ul style="list-style-type: none"> (i) permanent disablement of Abu; (ii) hospitalisation of Bala due to minor injuries. Incurred bill of RM50,000; and (iii) death of Chin. 		
Injury of Abu – claims under the ICS		
Amount to be claimed under the sole proprietor’s Employee Group PA for Abu’s injuries		RM100,000
Amount to be claimed by Abu under his PA policy.		RM250,000
Injury of Bala – claims under the ICS		
Amount to be claimed under the sole proprietor’s Employee Group policy - Hospitalisation charges of RM50,000 are fully covered under the ICS.		RM50,000
Death of Chin – claims under the ICS		
Amount to be claimed under the sole proprietor’s Employee Group PA policy for Chin’s death.		RM100,000
Amount to be claimed by Chin’s next of kin under Chin’s PA policies (RM600,000 = RM300,000 + RM300,000) but Chin’s family can only claim RM500,000 from the ICS. They can claim the remaining RM100,000 from the liquidator.		RM500,000