



SECP
Insurance Division
Karachi

[Karachi]

Before Mr. Muhammad Asif Arif Commissioner (Insurance)

In the matter of

M/s Shaheen Insurance Company Limited

Date of Show-Cause Notice: May 6, 2013

Date of Hearing: September 19, 2013
November 11, 2013

Attended by: Mr. Farhan Janjua
Chief Financial Officer & Company Secretary
Mr. Sohail N. Kidwai
Chief Operating Officer
Mr. Aijaz Ali Khan
Head of Operation
Mr. Imran Hussain
Legal Advisor

Date of Order: March 7, 2014

ORDER

(Under Section 12 Read with Section 11(1)(f) and Section 63 (1) and Section 156 of Insurance Ordinance, 2000)

This Order shall dispose of the proceedings initiated against M/s Shaheen Insurance Company Limited (hereinafter referred to as ("the Company")) and others for making a default in complying with the requirements of Section 12 and Section 11(1)(f) of Insurance Ordinance, 2000 ("the Ordinance").

Background Facts

The relevant facts for the disposal of this case are briefly stated as under:

2. Section 11(1)(f) of the Ordinance states that:

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"Conditions imposed on registered insurers.-(1) An insurer registered under this Ordinance shall at all times ensure that:

...
(f) the insurer meets, and is likely to continue to meet, criteria for sound and prudent management including without limitation those set out in section 12;"

3. AND WHEREAS, Section 12(1)(a), (d) & (e) of the Ordinance require that:

"Criteria for sound and prudent management.- (1) For the purposes of this Ordinance, the following shall, without limitation, be recognised as criteria for sound and prudent management of an insurer or applicant for registration as a person authorized to carry on insurance business:

(a) the business of the insurer or applicant is carried on with integrity, due care and the professional skills appropriate to the nature and scale of its activities;

...
(d) the insurer or applicant maintains adequate accounting and other records of its business; and

(e) the insurer or applicant maintains adequate systems of control of its business and records."

4. AND WHEREAS, Section 12(2) to (5) of the Ordinance state that:

"(2) Accounting and other records shall not be regarded as adequate for the purposes of clause (d) of sub-section (1) unless they are such as:

(a) to enable the business of the insurer or applicant to be prudently managed; and

(b) to enable the insurer or applicant to comply with the obligations imposed on it by or under this Ordinance.

(3) In determining whether any systems of control are adequate for the purposes of clause (e) of sub-section (1), the Commission shall have regard to the functions and responsibilities for those systems which are held by the persons who are responsible for the direction and management of the insurer or applicant and to whom clause (b) of subsection (1) applies.

(4) The insurer or applicant shall not be regarded as conducting its business in a sound and prudent manner if it fails to conduct its business with due regard to the interests of policy holders and potential policy holders.

(5) The insurer or applicant shall not be regarded as conducting its business in a sound and prudent manner if it:



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- (a) *fails to satisfy an obligation to which it is subject by virtue of this Ordinance;*
or
(b) *fails to supervise the activities of a subsidiary with due care and diligence and without detriment to the insurer's or applicant's business."*

5. That on November 27th, 2012, the Commissioner (Insurance) ordered an onsite inspection of the Company, in exercise of the powers conferred under Section 59A of the Insurance Ordinance, 2000. However, the Company, vide its letter dated December 6, 2012, requested the Commission to extend the date of commencement of onsite inspection, which was acceded to by the competent authority vide letter dated December 7, 2012, and hence, onsite inspection commenced on December 17, 2012 instead of December 10, 2012 as mentioned in inspection order dated November 27, 2012.

6. During the course of the onsite inspection of the Company, the inspection team made the following observations:

- **Claims record**

The inspection team while reviewing claim files related Miscellaneous class found that 67 files were missing from the Company's record. These files pertained to settlement with Worldcall group for offsetting outstanding premium with outstanding claims. Total amount involved in respect of these missing claims files was Rs. 4.3 million. The Company in its reply to Inspection team's query stated that these files are not found in the Company's record. Unavailability of these files raises serious doubts on genuineness and authenticity of all these claim settlements. This not only creates a substantial doubt about the validity of the related claims but also indicates the inappropriate maintenance of claims records by the Company and lack of Board's commitment to run the Company in a sound and prudent manner with enhanced system of internal controls to ensure availability and authenticity of the record of the Company.

- **Company without CEO, CFO and Company Secretary**

The inspection team noted that the Company is operating without a Chief Executive Officer (CEO), a Chief Financial Officer (CFO) and a Company Secretary. It further indicates that the Board of Directors of the Company lacks interest in the smooth and sound running of the Company's day-to-day affairs.



- **Investment Committee**

The inspection team noted that there is no separate investment wing or section in the Finance Department comprising of adequate number of persons to look for available investment opportunities in the market. It was further noted that no detailed discussions were made on investment strategy in Directors' meetings especially during the last two years. Furthermore, no rationale was available for roll over of investment in repo transaction despite the investee company incurring losses.

- **Investment strategy**

The inspection team noted that neither there is any investment policy nor is there any department in the Company to make investment decisions. Furthermore, the inspection team was also not provided with any research report or rational on the basis of which investment decisions were made by the Company. The inefficiency and ineffectiveness in the investment decision making has resulted into unrealized amount related to repo transaction to the extent of Rs. 99.88 million during the year ended December 31, 2011. Heavy investments were made in / through M/s First Capital Equities Limited, a related party without any rational or justification. The existing mechanism of investment decision making seems to be *ad hoc* and lacks proper structure including guidelines and policies which has caused the Company to face serious financial / liquidity problems in the form of non-realization of funds till date. There are no risk management policies / functions to guide the investment in risky avenues, which creates significant doubts about the sound and prudent investment decisions of the Company.

- **Investment transactions through single broker**

The inspection team noted that the Company has executed its investment decisions primarily through a single broker, namely M/s First Capital Equities Limited ("FCEL"). Engaging a single broker for all significant investments, i.e. sale and purchases carries concentration risk for the Company. Moreover, the Company may be exposed to uncompetitive services and charges.

- **Insurance of Risks in excess of Company's treaty Capacity**

The Company has provided Fire coverage to risks for which their treaty limit is exhausted and remaining amount has to be taken on their net account. Although the Company has maintained reinsurance



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arrangements but these arrangements are grossly inadequate to cater the Company's risks that it has underwritten. This can further increase financial difficulties for the Company.

7. In view of the abovementioned observations made by the Inspection Team, it, *prima facie*, appeared that the Board of Directors have failed to take measures for the sound and prudent running of the Company, as the key officers (including the Chief Executive Officer and the Company Secretary) of the Company have not been appointed, the Company lacks proper investment policies and procedures, the Company grossly lacks adequate internal controls, and has also failed to maintain the claims record that is essentially required to be maintained in terms of Section 45 of the Ordinance, and hence, the internal controls system of the Company are very weak particularly due to the absence of major policies, procedures and manuals that are vital for carrying out the operations of the Company.

This indicated that the business of the Company is not being carried out with due care and professional skills, as required by the abovementioned relevant provisions of Section 11 and Section 12.

Show-Cause Notice

8. On May 6, 2013, a Show-Cause Notice under Section 12 read with Section 11(1)(f), Section 63 (1) and Section 156 of the Ordinance was served to the Company, its Directors and Chief Executive, whereby they were asked to clarify their position as to why the penalty under Section 63(1) and Section 156 of the Ordinance may not be imposed on them for various negligence on part of the management of the Company in respect of inadequate internal control system of the Company and carrying out the business without due care and diligence, thereby contravening the provisions of Section 12 and Section 11(1)(f) of the Ordinance.

Company's Reply

9. In response to the said Show Cause Notice, the Company, vide their letter of May 15, 2013 requested to allow two week time for submission of the written reply of the said notice, which was allowed via letter dated May 20, 2013. The Company further sought time for submission of written reply via letter dated July 2, 2013, which was again allowed letter dated July 3, 2013 but no response was received instead the Company again requested to allow ten day time, which was accepted by the Commission via letter dated July 29, 2013 to submit the written reply till August 7, 2013 but no written reply received from the Company despite the number of extensions given in this regard.



Proceedings of the Hearing and Subsequent development

10. The hearing in the matter was initially scheduled for September 19, 2013 which was communicated to the Company via hearing notice dated September 12, 2013. However, on the day of hearing the Company vide its letter dated September 19, 2013 requested to adjourned the hearing. On written and verbal request the hearing was adjourned.

11. Thereafter, another hearing opportunity was given to the Company, its Directors and the Chief Executive Officer of the Company, and hearing notice dated October 31, 2013 was issued to them, whereby the hearing in the matter was scheduled for November 11, 2013 at 2:30 p.m., accordingly, the said hearing was attended by Mr. Farhan Janjua, Chief Financial Officer & Company Secretary, Mr. Sohail N. Kidwai, Chief Operating Officer, Mr. Aijaz Ali Khan, Head of Operation and Mr. Imran Hussain, Legal Advisor (they will be referred to as the "Company's representative" hereinafter).

12. Following arguments were made by the Company's representatives during the course of the hearing:

- a. The case was briefed by the Deputy Director on the instruction of Commissioner Insurance, Company's representative replied that they have the complete record of the claim files and its related matters and also explained that the files pertained to their Lahore Office and due to the shifting of the office, the files could not be provided to the Inspection team then, by now any time the SECP can visit and verify the claim files mentioned in this notice;
- b. Commissioner Insurance asked about the CEO of the Company, that since how long the Company is running without the CEO? Company representative responded that the Company does not have its CEO since April 2013, Mr. Asif Suleman was resigned in December 2012 but his resignation was not accepted and he was in Company till April 2013 as evident from the payroll of the Company. Commissioner Insurance asked did the Company inform the situation to the Commission and if the resignation had been accepted, who would then have been held responsible in case something wrong had happened during the vacancy of the post.
- c. Company's representative replied that in the given situation of Shaheen Foundation and Shaheen Insurance, its board tried a number of persons for the appointment of the CEO but could not succeed so Commissioner Insurance argued that if this situation continue to prevail for further 10



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- years then what would happen, who would be responsible for the situation so, and asked them to appoint CEO without further delay;
- d. Commissioner Insurance asked about Chief Financial Officer and the Company Secretary, Company's representative replied that Mr. Farhan Janjuah was appointed as the CFO and Company Secretary;
- e. Commissioner Insurance asked about the Investment Committee and investment strategy of the Company and what about the status of the investment mentioned in the accounts with wrong classification in the Accounts of the Company, Company's representative responded that yes there was no investment committee previously, now, the company have Investment committee and the investment made four years back as reported in the accounts only one property is under construction and the remaining three are now in company's name. and also replied that the reclassification has been made by the Company in their Accounts;
- f. Commissioner Insurance asked about the under writing of the risks beyond the company capacity; the Company's representative replied that the Company is by now fully compliant with its under writing capacity as per law;
- g. The Company's representative requested to the Commissioner Insurance that the Company will submit the comprehensive business plan on the future course of the Company to meet the solvency and other regulatory requirements as mentioned in the Inspection Report on the Company and for that requested to give them time till November 30, 2013 for submission of the business plan of the Company, which was allowed;
- h. The Company also submitted the written response of the notice during the hearing, which stated that;
- (1) *".....Claim Record; in this regard we wish to submit that 67 files referred in the report could not be provided to the Inspection Team due to the fact that the all these files pertain to a specific client of Lahore City and the mail Branch in Lahore was shifted to Shaheen Complex Lahore in 2012 and during that shifting over to new place the indexing of storage facility was over loaded with data which caused the delay to providing these files.*
- (2) *Company running without CEO, CFO and Company Secretary; Efforts made by the Board of Directors for appointing CEO has already been submitted to SECP vide letter dated July 19, 2013 and July 25, 2013. Also we like to add that Mr. Asif Suleman worked as CEO until March 2013. In the meantime Mr. Naveed Y. Butt was appointed as Acting Chief Operating Officer-SICL w e f December 07, 2012 vide letter dated December 07, 2012. After that Mr.*



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Faisal Hassan Jehangir was appointed and terminated on not fulfilling criteria by SECP. At present Mr. Sohel N. Kidwai is looking after the affairs of SICL as Chief Operating Officer. It is expected that Mr. Sohel N. Kidwai will take charge as CEO to be approved by BoD.

Mr. Farhan Janjua has recently joined as CFO and Company Secretary. Form-29 is enclosed for reference. Past efforts made by Board of Directors have already been submitted to SECP vide letter dated July 19, 2013.

- (3) Investment Committee; In the past we agree there was lack of Investment Committee for overseeing Investment decisions. However at present Chairman-SICL has formally nominated as in-house Finance Committee. This will ensure transparency and all the investments will also be brought before the Committee. In the past decisions based on Associated company investment had produced ill-liquid and non-generating revenues.*
- (4) Investment Strategy; Investment Policy Statement will be prepared and put up before discussion in the Board. This will be based on liquid and income generating investments. Avoidance of Investments Policy Statement will be shared with SECP after it's implementation.*
- (5) Investment transactions through single broker; No further investments had been made through the single broker i.e. First Capital Equities Limited. We are removing FCEL as brokers.*
- (6) Insurance of risks in excess of Company's treaty capacity; In this respect we have to submit that due to a lower premium rate the risk referred to could not be placed on facultative basis and therefore it remained uncovered though it was excess of Company's Treaty Capacity. However, we have renewed the policy for a further one year with increased premium rate and proper facultative reinsurance arrangement has been made with Pakistan Reinsurance Company Limited, hence now the risk is properly covered....."*

13. The Company vide its letter dated November 29, 2013 sought extension of ten days for submission of the business plan as committed in November 11, 2013 hearing, which was allowed on December 3, 2013 to submit the required information till December 10, 2013, the Company vide letter dated December 14, 2013 submitted the information/business plan which briefly stated that;

- (1) The Company will inject Rs. 150 million by way of Right issue of shares, which will complete till March 30, 2014;
- (2) To cope up with the Solvency issue, the Company will take measures to generate funds as under:
 - Value of properties Rs. 120 million
 - Receivables from FCSC Group Rs. 188 million
- (3) Plan for disposal of extra assets (Vehicles) of the Company which likely to fetch Re. 30 million;



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- (4) To reduce the overheads, manpower in the Company has been curtailed which will save Rs. 10 million;
- (5) Internal and external committees have been constituted in compliance with the Code of Corporate Governance; etc.

14. During the hearing, the Company's representative told that the Claim files mention in the notice are available, therefore, on December 31, 2013 Commission Inspector visited the Company premises for verification of the 67 claim files and relevant records and found that the 67 claim files and relevant records i.e. loss voucher signed and stamped by the Company. Survey reports, statement of happening, letter of acceptance, claim form, copies of insurance policy, preliminary loss advice, claim intimation pro-forma and pictures etc. were available with the Company and also found that these claims were adjusted against premium receivable from M/s World Call Limited.

Consideration of the Submission

15. Before proceeding further, I find it relevant to discuss the duties of the Directors. The Directors, in addition to the day to day running of the company and the management of its business, also have some 'fiduciary' duties i.e. duties held in trust and some wider duties imposed by statute and breach of these statutory duties will usually be a criminal offence, punishable by fine or imprisonment. Hence the Directors are gauged against a higher standard of accountability which requires them to be vigilant and perform their duties with due care. In the instant case, however, the Directors have failed to perform their duties with due care and prudence. As the Directors are supposed to be well aware of their legal obligations in connection with the aforesaid statutory requirement of the Section 12 read with Section 11(1)(f) of the Ordinance i.e. the Directors of the Company were required to put in-place formal policies and procedures covering all the operational aspects and decision making, especially in the case of making investments, sound and prudently running the affairs of the Company therefore, it could be legitimately inferred that the default was committed.

Conclusion

16. After carefully examining the arguments and studying the facts and findings of the case as mentioned in the above paras of this Order, the default of Section 12 read with Section 11(1)(f) of the Ordinance is established, and to a greater extent, the Company has also accepted its default. Therefore, the penalty as provided under Section 63 (1) and 156 of the Ordinance can be imposed on the Company, which states that:

The provisions of Sub-section (1) of Section 63 of the Ordinance state that:



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"Power of Commission to issue direction to cease entering into new contracts of insurance.- (1) The Commission may issue a direction to cease entering into new contracts of insurance if it believes on reasonable grounds that an insurer registered under this Ordinance has failed, or is about to fail, to comply with the conditions of registration set out in section 11."

AND WHEREAS, Section 156 provides that:

"Penalty for default in complying with, or acting in contravention of this Ordinance.- Except as otherwise provided in this Ordinance, any insurer who makes default in complying with or acts in contravention of any requirement of this Ordinance, [or any direction made by the Commission, the Commission shall have the power to impose fine on the insurer]16, and, where the insurer is a company, any director, or other officer of the company, who is knowingly a party to the default, shall be punishable with fine which may extend to one million rupees and, in the case of a continuing default, with an additional fine which may extend to ten thousand rupees for every day during which the default continues."

Order

17. In exercise of the power conferred on me under Section 63 (1) and 156 of the Ordinance, instead of imposing the maximum penalty, take a lenient view, and thus, condone the Company due to the following reasons:

- a. The Company's management including its Directors have taken cognizance of the fact that they did not have proper policies and procedures, and they have initiated, and to some extent finalized, the formulation of policies and procedures including constituting committees including investment committee, internal audit committee and others as required under Code of Corporate Governance and required under the Law;
- b. The Company has appointed its CFO and Company Secretary and evidence thereof provided to me;
- c. The Claim records were verified and found it available with the Company; and
- d. The business plan submitted by the Board of Directors reveal that the Company took measures to rectify their acts of non-compliance and also steps have been taken to meet the requirements of the Ordinance to run



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and manage and affairs of the Company to run the concern sound and prudently.

Nonetheless, the Company is hereby issued a stern warning that similar acts of non-compliance in future will warrant a strict disciplinary action against the Company.

18. This Order is issued without prejudice to any other action that the Commission may initiate against the Company in accordance with the law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.

Muhammad Asif Arif
Commissioner Insurance