



SECP

Insurance Division  
Karachi

[Karachi]

Before Tariq Hussain, Director (Insurance)

*In the matter of*

Takaful Pakistan Limited

Show Cause Notice Issue Date: February 13, 2013

Date of Hearing: April 4, 2013

Attended By: Mr. Taimur Mirza  
Advocate / Legal Counsel  
M/s Mohsin Tayebaly & Co.

Date of Order: May 8, 2013

**ORDER**

(Under Regulation 3(1) and Regulation 16(1)(a) of Part B of Annexure II of the Securities and Exchange Commission (Insurance) Rules, 2002 and Section 46(1)(b) Read with Section 34 and Section 156 of Insurance Ordinance, 2000)

.....

This Order shall dispose of the proceedings initiated against M/s Takaful Pakistan Limited ("the Company") for not complying with the requirements of Regulation 16(1)(a) of Part B of Annexure II of the Securities and Exchange Commission (Insurance) Rules, 2002 (the "Rules") and Section 34 of the Insurance Ordinance, 2000 (the "Ordinance").

**Background Facts**

2. The relevant provision of Sub-section (1) of Section 46 of Ordinance requires every non-life insurer to file annual audited financial statements. For the purpose of ready reference, Section 46(1) of the Ordinance is reproduced as follows:

*"Accounting and reporting.- (1) Every insurer shall at the expiration of each year prepare and deliver to the Commission with reference to that year annual statutory accounts comprising the following statements duly audited by an approved auditor:*

*llh*

SECURITIES & EXCHANGE  
COMMISSION OF PAKISTAN

Insurance Division, State Life Building-2  
4th Floor, Wallace Road, Karachi, Pakistan

Tel: +92-21-32461053, +92-21-32465469 Fax: +92-21-32423248 Web: www.secp.gov.pk



...  
(b) in the case of a non-life insurer,

- (i) a statement of assets and liabilities;
- (ii) a statement of profits and losses;
- (iii) a statement of cash flows;
- (iv) a statement of premiums;
- (v) a statement of claims;
- (vi) a statement of expenses;
- (vii) a statement of investment income;
- (viii) a statement of claims analysis;
- (ix) a statement of exposures; and
- (x) such other statements as may be prescribed by the Federal Government;

each in such form as may be prescribed by the Commission and prepared in accordance with such regulations as are issued by the Commission from time to time in this behalf."

3. Further that Regulation No. 3(1) of Part - B of Annexure II of the Rules prescribes the additional financial statements, which amongst others, includes the Statement of Assets for Solvency Purpose (Form GJ). The said Regulation states that:

*"The form of Regulatory Returns shall consist of the following which shall be submitted according to the published Forms annexed to these Regulations:*

- ...  
- Statement of Assets for Solvency Purposes (Form GJ) which is hereby prescribed under S46(1)(b)(x) of the Ordinance.  
..."

4. The Company had filed its Statement of Assets for Solvency Purposes (Form GJ) for the year ended December 31, 2011 in pursuance of Section 51(1) of the Ordinance, which showed that the Company had taken all its Available for Sale investments at market value.

5. Section 34 of the Ordinance lays down the condition for the valuation of assets and liabilities for the purpose of solvency. This Section requires that:

*"Valuation of assets and liabilities.- (1) For the purposes of this Part, assets and liabilities shall, subject to sub-section (2), be valued in accordance with such accounting rules as may be prescribed by the Commission.*

*(2) For the purposes of this Part, as at any date (the "balance date") to which a statement of assets and liabilities (however called or described) is made up:*



(a) *no asset of an insurer shall be valued at more than the amount, net of transaction costs incurred by the transferor, at which it could be transferred in an orderly market in a transaction between two willing but not anxious parties;  
..."*

6. Regulation 16(1)(a) of Part B of Annexure II of the Rules lays down the requirement for valuation of Available for Sale investments as:

*"Investment and Investment Properties.- For the purpose of all statements prepared under these regulations, and for the purpose of S34(1) of the Insurance Ordinance 2000.*

(a) *available for sale investments shall be stated at the lower of cost or market value (market value being taken as lower if the fall is other than temporary). In the case of fixed income investments redeemable at a given date and where the cost is different from the redemption value, such difference shall be amortized uniformly between the date of acquisition and the date of maturity in determining "cost". The market value of investments at the balance sheet date shall be disclosed, as shall the effect of non-compliance with IAS 39;  
..."*

7. In this view, it appeared that the Company has contravened the provisions of Section 34 of the Ordinance read with Regulation 16(1)(a) of Part B of Annexure II of the Rules.

8. Thereupon, the Company was asked to comment on the matter, on which the Company, while admitting the contravention, has stated that:

*"...your observation in respect of available for sale investments is correct. However, in our opinion, the more realistic approach is to account for the investment in equity shares of listed companies at market value for solvency purpose. This view is also endorsed by our auditors and in accordance with industry practice"*

9. In view of the foregoing paras, it appeared that the Company has failed to comply with Regulation 16(1)(a) of Part B of Annexure II of the Rules and Section 34 of the Ordinance, which attracts penal provision as provided under Section 156 of the Ordinance.

#### Show Cause Notice

10. Accordingly, the Show Cause Notice was issued on February 13, 2013 under Regulation 3(1) and Regulation 16(1)(a) of Part B of Annexure II of the Rules and Section 46(1)(b) Read with Section 34 and Section 156 of Ordinance to the Company



and its Directors, calling upon them to show cause as to why the penalty, as provided under Section 156 of the Ordinance, should not be imposed upon the Company and/or its Directors for not complying with provisions of Regulation 16(1)(a) of Part B of Annexure II of the Rules and Section 34 of the Ordinance.

Company's Response to the Show Cause Notice

11. M/s Mohsin Tayebaly & Co., vide their letter no IM894/TKPL/04/414/2013 dated February 27, 2013, while acting on behalf of the Company, submitted response to the aforesaid Show Cause Notice, whereby they had stated that:

*"...We have been instructed to reply to the Notice as follows:*

- 1. That the contents of paragraphs 1 and 2 of the Notice warrant no comments, being reproduction of the applicable laws.*
- 2. That in respect of the contents of paragraph 3 of the Notice it is submitted that our Client has complied with all applicable laws pertaining to the necessary filings and valuations.*
- 3. That the contents of paragraphs 4 and 5 of the Notice warrant no comments, being reproductions of the applicable laws.*
- 4. That the contents of paragraphs 6 and 7 of the Notice are vehemently denied as the same are misconceived and incorrect. It is submitted that solvency, as universally recognized, is a measure of determining the quantum of excess liquidity of the admissible assets over the total liabilities of a non-life risk concern on a given Balance Sheet date. Accordingly, as per the requirements of the Insurance Ordinance, 2000, the solvency of our Client as on 31 December, 2011 stands as follows:*

<i>Admissible Assets:</i>	<i>Rs.372.4m</i>
<i>LESS: Total Liabilities:</i>	<i>Rs.280.0m</i>
<i>Solvency Margin:</i>	<i>Rs.92.4m</i>

*As the Commission was informed earlier, investment in shares of our Client was Rs.4,960,000/- (market value) which comprised 1.33% of the Total Admissible Assets, as against a cost value of Rs. 3,700,000/-. However, our Client had sold its investment in the shares in 2012, at a gain of Rs. 1,900,000/- . Without prejudice to the above stand which we maintain, if we momentarily accept the contention to take the investment in such shares at its cost value, it is submitted that the impact such a stance would have been negligible, and the stance would in no manner have infringed the minimum compliance of our Client's solvency requirement level of Rs. 50,000,000/-.* It is emphasized that

*M/s:*



the purpose of such laws is to substantively prevent companies from over valuing investments that are available for sale which would have a misleading impact on the balance sheet. Since such shares have already been sold at a higher value than stated, the valuation provided was not misleading or over-valued.

5. In view of the above, there has been no contravention of the applicable laws and contents of paragraph 8 of the Notice are therefore denied as the same are incorrect and misconceived. It is reiterated that our Client has abided by the applicable laws and that there has been no violation or evasion of the substantive procedures prescribed in the said laws.
6. That as regards the contents of paragraph 9 of the Notice and in view of the aforesaid it is submitted that no action contemplated under Section 156 of the Insurance Ordinance, 2000 or any other adverse action can be taken against our Client as our Client has not committed the contraventions alleged in the Notice.
7. It is further submitted that the Notice may kindly be withdrawn by the Commission and the Commission give the finding that our Client has not committed the contraventions alleged in the Notice.
8. It is also submitted that our Client would like to appear before the Commission through us in order to put forth its defense to the allegations raised in the Notice against it and also produce further documents in support of its defense as such hearing, if the same is deemed necessary." (Underlined to put emphasis)

12. The reply of the Company, through M/s Mohsin Tayebaly & Co., reveals that the Company has misinterpreted the provisions of Section 34 of the Ordinance and the applicability of the Accounting Regulations (i.e. Part B of Annexure II of the Rules). The provisions of Section 34 of the Ordinance and the Accounting Regulations go hand-in-hand with the provisions of the Ordinance relating to the minimum solvency requirements. Accordingly, the Company was required to state its assets as per the provisions of Section 34 of the Ordinance and the Accounting Regulations in order to evaluate solvency as on any given date.

13. The reply further endorses in its Para 4 that the purpose of solvency regime is to prevent insurers from overvaluing their investments that are classified as available for sale investments, which would otherwise have a misleading impact on the balance sheet footings of that insurer as on any given date. However, selling of these available for sale investments at high prices on any future date i.e. after the balance sheet date has nothing to do with the valuation of these investments as at the balance sheet date, in terms of the applicable laws.

14. The provisions of sub-Section (2) of Section 34 of the Ordinance determines the maximum reachable value of an asset or liability, but it does not bind the Commission



to prescribe a value that is lower than the maximum reachable value, and in the instant case, the insurers shall be bound to comply with the provisions of the Accounting Regulations in terms of sub-Section (1) of Section 34 of the Ordinance.

### Hearings of the Case & Subsequent Developments

15. As the Company had requested for hearing in the matter, vide their reply to the aforesaid Show Cause Notice, as quoted hereinabove, the Commission had initially scheduled the hearing in the matter for March 15, 2013 at 10:30 a.m., which was communicated to the Company via the Commission's hearing notice no. ID/Enf/TPL/2013/15850 dated March 8, 2013. However, the Company, through M/s Mohsin Tayebaly & Co. vide their letter no. IM894/TKPL/01/485/2013 dated March 14, 2013 requested the Commission to adjourn the hearing with at least 10 to 15 days' notice.

16. Accordingly, the Commission had rescheduled the hearing in the matter for April 4, 2013 at 12:00 p.m., which was communicated to the Company via the Commission's hearing notice no. ID/Enf/TPL/2013/16108 dated March 22, 2013.

17. Accordingly, the said hearing, which was held on April 4, 2013 at 12:00 p.m., was attended by Mr. Taimur Mirza, Advocate, M/s Mohsin Tayebaly & Co., on behalf of the Company (who will be referred to as the "Company's representative" hereinafter).

18. Brief proceedings of the hearing of April 4, 2013 are as follows:

- a. Prior to the start of the hearing proceedings, the Company's representative handed over the undated Power of Attorney / Vakalatnama to the Commission.
- b. The said Power of Attorney / Vakalatnama was signed by Dr. Mumtaz Ahmed Hashmi, the Director of the Company, who was empowered by the Chairman of Board of Directors of the Company to appear himself, or to engage or appoint any legal practitioner to act on behalf of the Company and its Board of Directors in any legal cases, vide Circular Resolution of the Board of Directors dated January 9, 2013;
- c. The Company's representative was asked to present the stance of the Company, to which the Company's representative stated that the Company's contentions have already been communicated to the Commission vide the letter of M/s Mohsin Tayebaly & Co. dated February 27, 2013, and that there are no additional submissions to be made;



### Consideration of Company's Submissions

19. I have carefully examined and given due consideration to the written and verbal submissions of the Company (through Mr. Taimur Mirza of M/s Mohsin Tayebaly & Co., and have also referred to the provisions of the Ordinance and the Accounting Regulations. I am of the view that there has been an established default of Regulation 16(1)(a) of the Accounting Regulations and Section 34 of the Ordinance, as the Company was required to state their Available for Sales investments at lower of cost or market value in terms of the provisions of Regulation 16(1)(a) of the Accounting Regulations and Section 34 of the Ordinance, which have been violated as the Company has stated its Available for Sale investments at the prevailing market value on the date to which the Statement of Assets for Solvency Purpose was made up.

20. However, 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 34 of the Ordinance read with Regulation 16(1)(a) of the Accounting Regulations, as aforesaid, therefore, it could be legitimately inferred that the default was committed.

### Conclusion

21. 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 34 of the Ordinance read with Regulation 16(1)(a) of the Accounting Regulations (i.e. Part B of Annexure II of Rules) is established. Therefore, the penalty as provided under Section 156 of the Ordinance can be imposed onto the Company and/or its Directors.

22. Section 156 of the Ordinance states 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, 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**

23. In exercise of the power conferred on me under Section 156 of the Ordinance, I, instead of imposing penalty, take a lenient view, and thus, condone the Company due to the fact that the effect of such contravention has not grossly plunged the Company into insolvency.

However, the Company is hereby issued a stern warning that in case of similar non-compliance in future a stronger action against the Company will be taken.

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

**Tariq Hussain**  
Director