



SECP

INSURANCE DIVISION
Islamabad

Before Tahir Mahmood, Commissioner (Insurance)

In the matter of

Crescent Star Insurance Limited

Show Cause Notice No. and ID/Enf/CrescentStar/2017/8002,
Date: dated January 3, 2017

Date of Hearing: April 20, 2017

Attended By: Mr. Zeeshan Abdullah,
Advocate, M/s. Rabbani & Ansari, Advocates

Barrister Ali Tahir
M/s. Rabbani & Ansari, Advocates

Date of Order: October 5, 2018

ORDER

Under Section 86 read with Section 492 of the Companies Ordinance, 1984.

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This Order shall dispose of the proceedings initiated against M/s. Crescent Star Insurance Limited (the "Company") and its Board of Directors for alleged contravention of Section 86 read with Section 492 of the Companies Ordinance, 1984. (the "Ordinance"). The Company and its Directors shall be referred to as the "Respondents" hereinafter.

2. Facts of the matter are that the Company in its circular dated December 17, 2015 under Section 86(3) of the Ordinance disclosed the following reasons for which the additional funds were sought:

"To improve the solvency and liquidity of the Company. To diversify into other businesses which would complement, provide new avenues for earning and will improve the profitability of the Company to benefit all the stakeholders."

3. The review of the financial statements / regulatory returns for the year ended September 31, 2016 transpired that the additional funds did not result in any improvement in the solvency of the Company rather the Company became insolvent.

4. It was also observed that the 7.6 million 'Right Shares' were deceptively raised by the directors against 'Share Deposit Money' amounting to Rs.76 million against the 33% right shares approved by the Board of Directors meeting held on November 10, 2015.



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5. The review of the bank statement further evidenced that share deposit money amounting to Rs. 76 million was credited and on the same day, two amounts i.e. Rs. 27 million and Rs. 49 million, totaling Rs. 76 million were debited from the account. Banker to the Right Issue included all branches of Bank Alfalah Limited, NIB Bank Limited and Soneri Bank Limited; while this particular amount was deposited in United Bank Limited, which was not a designated bank for receipt of the subscription money.

6. The last date of subscription request and payment was February 4, 2016 and Rahman Sarfaraz Rahim Iqbal Rafiq, Chartered Accountants certificate for release of funds from the Subscription Accounts was March 11, 2016. However, the amount of Rs. 76 million was routed to Dost Steel Limited dated December 22, 2015. The aforesaid amount was routed to Dost Steel Limited on December 22, 2015 even before getting NOC for release of subscription amount from Pakistan Stock Exchange.

7. It appeared that the Company failed to comply with the mandatory provisions of Section 86 of the Ordinance by misstating in the circular to the members dated December 17, 2015.

8. Section 86 of the Ordinance states that:

“(1) Where the directors decide to increase the capital of the company by the issue of further shares, such shares shall be offered to the members in proportion to the existing shares held by each member, irrespective of class, member is entitled and limiting a time, within which the offer, if not accepted, will be deemed to be declined.

Provided that the Federal Government may, on an application made by any public company on the basis of special resolution passed by it, allow such company to raise its further capital without issue of right shares.

Provided further that a public company may reserve a certain percentage of further issue of its employees under “Employees Stock Option Scheme” to be approved by the Commission in accordance with the rules made under this Ordinance.

(2) The offer of new shares shall be strictly in proportion to the number of existing shares held:

Provided that fractional shares shall not be offered and all fractions less than a share shall be consolidated and disposed of by the company and the proceeds from such disposition shall be paid to such of the entitled shareholders as may have accepted such offer.

(3) The offer of new shares shall be accompanied by a circular duly signed by the directors or an officer of the company authorised by them in this behalf in the form prescribed by the Commission containing material information about the affairs of the company, latest statement of the accounts and setting forth the necessity for issue of further capital.

(4) A copy of the circular referred to in sub-section (3) duly signed by the directors or an officer authorised as aforesaid shall be filed with the registrar before the circular is sent to the shareholders.



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(5) The circular referred to in sub-section (3) shall specify a date by which the offer, if not accepted, will be deemed to be declined.

(7) If the whole or any part of the shares offered under sub-section (1) is declined or is not subscribed, the directors may allot and issue such shares in such manner as they may deem fit].”

9. Section 492 of the Ordinance, states that:

“ Penalty for false statement. - Whoever in any return, report, certificate, balance sheet, profit and loss account, income and expenditure account, prospectus, offer of shares, books of accounts, application, information or explanation required by or for the purposes of any of the provisions of this Ordinance or pursuant to an order or direction given under this Ordinance makes a statement which is false or incorrect in any material particular, or omits any material fact knowing it to be material, shall be punishable with fine not exceeding [five] hundred thousand rupees.”

10. Hence, a Show Cause Notice bearing ID/Enf/CrescentStar/2017/8002 dated January 3, 2017 was issued to the Respondents, thereby calling upon them to show cause as to why punitive action may not be taken against them in terms of Section 492 of the Ordinance for the alleged contravention of Section 86 of the Ordinance.

11. The following extensions as requested by the Respondents were granted to submit response to the SCN dated January 4, 2017:

Sr. No.	Date of letter through which extension requested	Time allowed by the Commission to respond	Status of submission of response
1	January 16, 2017	February 1, 2017	Nil
2	February 4, 2017	February 15, 2017	Nil
3	February 17, 2017	One week	Nil
4	February 25, 2017	March 22, 2017 (hearing scheduled)	Response submitted vide letter dated March 18, 2017

12. The Respondents through Mr. Zeeshan Abdullah & Mr. Ali Tahir, from M/s. Rabbani & Ansari, Advocates, hereinafter referred to as (the “Authorized Representatives”) submitted their response vide letter dated March 18, 2017 along with the request to reschedule the hearing of March 22, 2017 to any other date. Subsequently, the hearing was scheduled on April 20, 2017 vide letter dated April 10, 2017 bearing no. ID/Enf/CrescentSrar/2017/9161.

13. The hearing was held at Head Office of the Commission and was attended by the Authorized Representatives. Response to the SCN as well as submissions made during the hearing are summarized below:



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- i. It is not within the purview of the Commission in its role as a regulator to substitute its opinions and observations in relation to the commercial decision taken by the Board of a Company;
- ii. The Company has actually made a gain of about Rs. 127 million and counting due to the rising stock prices of Dost Steel Ltd., in which the company had invested;
- iii. The Commission has already prejudged and decided in the show cause notice with regard to solvency of the Company without giving an opportunity of hearing to the Company. It is beyond understanding how the solvency of the Company has any relevance to showing cause as to why the Company has not violated Section 86 of the Ordinance;
- iv. The amount of about Rs. 421 million invested in DSL is admissible in solvency and if taken it as it is, CSIL is solvent and question of misstatement in circular i.e "to improve solvency and Liquidity does not arise;
- v. The original proposal to issue right share was approved by the Board of Directors of the Company through resolution dated November 10, 2015. In compliance of Section 86 of the Ordinance, the Company issued right allotment letter to its shareholders, proportionate to their shareholding and to the public at large. The circular was duly communicated to the Commission.
- vi. Weavers Pakistan (Pvt.) Limited ("Weavers"), which is a shareholder of the Company, was offered 8,561,398 share as per their entitlement under Section 86 of the Ordinance, vide letter dated December 16, 2015. The Company in the said letter requested Weavers to advance the amount in consideration of their right entitlement, if they wished to en-cash on their entitlement. Subsequently, Weavers vide letter dated December 21, 2015, advanced an amount of Rs. 76 million for 7.6 million shares, that they subscribed to as per their right entitlement;
- vii. There is no legal bar in receiving the amount of consideration against a right entitlement in advance, in fact the 'advance payment by sponsors is a general practice and since this amount of consideration against right entitlement was received well in advance, it was deposited in UBL;
- viii. The Commission is also urged to take into account the PSX Rule Book, which provides 'no bar in the amount not being deposited in the account of a banker' to the issues, unless and until it is in relation to the issue and subscription of the public, as opposed to a shareholder with a right entitlement.
- ix. The advance amount of consideration, which was paid by Weavers against their right entitlement, was there until utilized by investing in M/s. Dost Steel Limited. The NOC is required for release of subscription amount from PSX only for money paid by the public, indeed if amount was utilized before NOC of



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PSX even then the same may not be construed as as violation of Section 86(3) as the PSX rules do not empower the SECP with the jurisdiction to rule on the consequences of violation of such rules, if any, nonetheless, the professed issue of routed money in DSL before any NOC of PSX fails to hold any relevance the SCN under reference under Section 86(3) read with Section 492. In fact there is no legal restriction on the use of sponsors' money whether paid in advance or as due for their right entitlement, if it is invested as per the directions of the board.

x. Furthermore, the right shares can be issued against credit balance, loan, advance money and unpaid dividends etc. of sponsor shareholders when truthfully, the money was received from them even before the announcement of rights shares issued to raise further capital.

xi. By issuing rights, Company's liquidity improved which is evident from Company's account wherein from designated accounts money credited. Further, the Company invested proceeds from the right issue into other businesses, namely DSL and Crescent Star Foods (Pvt.), Ltd. This injected equity into the Company in the form of shares and resulted into better liquidity for the Company. Shares are a form of Liquidity. Better liquidity of the Company would automatically result into better solvency for the Company. It is beyond the scope of the regulatory function of the Commission to question the result of the commercial decisions undertaken by the Board of the Company.

xii. A separate show cause notice has been sent to the Company under Rule 13 of the Securities and Exchange Commission (Insurance) Rules, 2002 read with Sections 11(1)(c), 32(2)(g), 36 & 156 of the Insurance Ordinance, 2000, relating to the solvency of the Company and it is humbly submitted that the Commission may not make up its mind at this stage on that show cause notice under reference, In any event the requirement of mens rea is the gist of the offence under Section 492 of the Ordinance as has been held time and again by the courts of law in Pakistan, Therefore, what the Commission should satisfy itself on is whether the company was making a malafide false statement or not? Acquiring shares would actually result in increased solvency and liquidity (in Show Cause Notice pertaining to solvency, the plea of CSIL is that the investments are admissible for solvency, therefore, the invested amount has to be counted for solvency), and in the present case it also ought to satisfy about the purpose of the right issue as stated in its latter half in the circular and it would 'only go to show that question of any misstatement in circular, as alleged does not arise.

14. Circular dated December 17, 2015 under Section 86(3) of the Ordinance issued by the Company disclosed that the additional funds were sought to improve the solvency and liquidity of the Company and to diversify into other businesses which would complement, provide new avenues for earning and will improve the profitability of the Company to benefit all the stakeholders. However, examination of Accounts for the year ended September 31, 2016 revealed that the additional funds did not result in any improvement in the solvency of the Company rather the Company's



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solvency margin became negative. The Respondents have argued that separate show cause notice regarding solvency has been issued to the Company and requested that the Commission may not make up its mind at this stage as the aforesaid Show Cause is pending.

15. Considering the request of the Respondents, the Commission agreed that the matter of solvency in SCN dated January 4, 2017 issued to the Company under Rule 13 of the Rules read with Section 11(1)(c), Section 32(2)(g), Section 36 and Section 156 of the Insurance Ordinance, 2000 may be concluded before the subject SCN relating to misstatement in the circular is decided. The matter of solvency was referred back to the Insurance Division to re-evaluate the solvency position in light of additional facts submitted by the Company.

16. Despite the fact that the Commission allowed the Company to submit its statement of assets for solvency purposes for the year ended December 31, 2017, in order to decide the matter on the basis of recent regulatory returns. Upon receipt of the financial statements and regulatory returns for the year ended December 2017, it was observed that the Company's solvency margin was still deficient by an amount of Rs.179.949 million. Accordingly, the Commission vide Order dated May 16, 2018 imposed a fine of Rs. 1,000,000/- on the Company for its failure to meet the mandatory requirements relating to the minimum solvency for the year ended December 31, 2016.

17. It was argued by the Respondents that by issuing right shares, Company's liquidity improved. Better liquidity of the Company would automatically result into better solvency for the Company. Furthermore, circular dated December 17, 2015 under Section 86(3) of the Ordinance clearly stated that reason for additional funds is to improve the solvency of the Company. However, solvency of the Company did not improve. Thus, the misstatement in the circular issued under Section 86(3) of the Ordinance is established.

18. Section 492 of the Ordinance provides that whoever in any return, report, certificate, balance sheet, profit and loss account, income and expenditure account, prospectus, offer of shares, books of accounts, application, information or explanation required by or for the purposes of any of the provisions of this Ordinance or pursuant to an order or direction given under this Ordinance makes a statement which is false or incorrect in any material particular, or omits any material fact knowing it to be material, shall be punishable with fine. Thus, penalty under Section 492 of the Ordinance can be imposed on to the Respondents.

19. I have carefully examined and given due consideration to the written and verbal submissions of the Respondents, and have also referred to the provisions of the Ordinance and other legal references. I am of the view that default of Section 86 read with Section 492 of the Ordinance is established.

20. In exercise of the power conferred on me under Section 492 of the Ordinance read with S.R.O. 750(I)/2017 dated August 2, 2017, I, instead of imposing a fine as provided under the said provision, take a lenient view, and issue a stern warning that




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in case of similar non-compliance in future a stronger action against the Respondents will be taken.

21. This Order is issued without prejudice to any other action that the Commission may initiate against the Company and / or its management (including the chief executive officer or directors of the Company) in accordance with the law on matters including those subsequently investigated or otherwise brought to the knowledge of the Commission.


Tahir Mahmood
Commissioner (Insurance)

