



Before Ms. Amina Aziz – Director (CSD)

In the matter of

Engro Eximp (Pvt) Limited

Number and date of SCN: No. CSD/ARN/405/2016 dated January 03, 2017
Date of hearing: February 15, 2017
Authorized Representative: Mr. Faiz Chapra -Head of Legal & Company Secretary, Engro Corporation Limited
Mr. Rahmat Kamal- Legal representative
Mr. Amir Qasim – Engro Eximp (Pvt) Limited

ORDER

UNDER SECTION 194 READ WITH SECTION 498 OF THE COMPANIES ORDINANCE, 1984

This order shall dispose of the proceedings initiated against the Mr. Khalid Mir, Chairman and Mr. Ruhail Muhammad Director (together referred to as “respondents”) of Engro Eximp (Pvt) Limited (the “Company”). The proceedings against the respondents were initiated through show cause notice dated January 03, 2017 under the provisions of section 194 read with section 476 of the Companies Ordinance, 1984 (the “Ordinance”).

2. The brief facts of the case enumerate from the examination of the annual audited accounts for year ended June 30, 2010 to June 30, 2012 that revealed that the Company had taken a Director and Officers Insurance policy that provides indemnity for claims made against the insured persons, i.e. the respondents being the directors, arising from the wrongful acts or omission, error, mismanagement, neglect or breach of duty on their part. Perusal of relevant records from the Company reflected that the statutory auditors of the Company for year ended June 30, 2010 in their letter to the Board of Directors had also drawn attention to the said insurance policy. Moreover, the abstract of terms of said insurance policy for year 2010 to 2011 (2010 policy) was provided by the Company which stated that the said policy provides indemnity for claims made against the insured arising from wrongful acts committed by the insured in capacity as an insured. The definition of wrongful acts, among others, included breach of duty.

3. Keeping in view the aforesaid, a show cause notice was issued to the respondents whereof the respondents were called upon to show cause in writing within fourteen days as to why the Company, for the year ended June 30, 2012, had obtained an insurance policy in contravention of the provision of the Ordinance.



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3. Keeping in view the aforesaid, a show cause notice was issued to the respondents whereof the respondents were called upon to show cause in writing within fourteen days as to why the Company, for the year ended June 30, 2012, had obtained an insurance policy in contravention of the provision of the Ordinance.

4. In response to the aforesaid show cause notice, Mr. Faiz Chapra, authorized representative, through his letter dated January 10, 2017 accompanied by Directors & Officers Liability Insurance Policy (2016), stated the following:

- a) Directors and officers shall continue to be liable if found by competent court or authority and insurance is simply taken to cover the cost of paying out on a claim subject to exclusions.
- b) Purchasing liability insurance is very different from company itself indemnifying its directors and officers. In that view, Section 194 of the Ordinance does not bar getting liability insurance for Directors and Officers.
- c) The insurance policy does not include taxes and fines payable as being under the category of insured loss and matter which are uninsurable under Pakistani laws, are also carved out of the definition of loss under the policy.
- d) The insurance policy does not insure for loss arising out of dishonesty/personal profit or due to fraud.
- e) Directors and officers liability insurance is a worldwide phenomenon and a key aspect of ensuring that companies who wish to have a robust system of corporate governance have qualified and experienced directors who would not join in the absence of such Policy being in place. Code of Corporate Governance also states that obtaining professional indemnity insurance for independent directors is encouraged.

5. Hearing in the matter was fixed on February 15, 2017. Mr. Faiz Chapra, Mr. Rahmat Kamal and Mr. Amir Qasim, the authorized representatives of the Company (collectively called authorized representative) appeared on behalf of the respondents on the date of hearing. The authorized representative had relied on policy covering period 2012 and requested time for submissions in writing regarding the insurance policy for year 2010 and auditors' qualification in financial statements for year ended 2012. The request was acceded to. With respect to 2016 policy, it was clarified that the definition of loss excluded all



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matters uninsurable under the laws of Pakistan, henceforth the acts specified in Section 194 of the Ordinance (i.e. negligence, default, breach of trust) were not covered in the aforementioned policy. It was also stated that the intent whilst forming the policy was to align it with the relevant laws but the structure/wordings might require rewording and assured that there was nothing unlawful. Subsequently, the Company through their letter dated March 02, 2017 reiterated their earlier stance regarding definition of loss. As for qualification of auditors, it was stated that the auditors in their covering letter to the aforesaid report had requested the Company's management to confirm the understanding that the said policy is not in contravention of Section 194 of the Ordinance. The auditors after receiving confirmation had given clean report for year 2012. As for policy for year 2010, the coverage of loss remains unchanged as that for year 2016. The SECP exclusion clause in 2010 policy was accepted to be present but was omitted for year 2012-2016. However, it was contested that the deletion of the said exclusion does not result in any contravention of Section 194 of the Ordinance owing to definition of loss already elaborated upon.

6. In terms of the Commission's notification SRO 1003 (I)/2015 dated October 15, 2015, the powers to adjudicate cases under section 194 have been delegated to the Director (Corporate Supervision Department).

7. I have gone through the requirements of law, explanation provided by the Company and facts placed before me by the Department. I have observed the following:

- i. The Directors and officers Insurance policy of year 2010 states that it is a claim made policy. It provides indemnity for claims first made against the insured during the policy period arising from **wrongful acts** committed by the insured in its capacity as an insured
- ii. Wrongful act is defined as any actual, alleged or proposed; act or omission, error, misstatement, neglect or **breach of duty** that is committed after the Retroactive date by an Insured in the capacity in which he is an Insured, or any matters claimed against an insured solely because of his capacity as an Insured.
- iii. Loss is defined as amount an insured is legally liable to pay in his capacity as an insured resulting from a claim including, among others, sums awarded by a competent court or tribunal for breach of statute and cost. However, it is stated that taxes, fine, penalties and matters uninsurable under laws of Pakistan are excluded from the definition of loss.



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- iv. The said policy also stated that the insurer shall pay on behalf of the insured any loss **to the extent that it is non-indemnifiable loss.**
 - v. Non-indemnifiable loss is defined as the loss in respect of which the Company or outside entity cannot provide an indemnity to the insured as a result of the either:
 - a) The applicable law or such company's written constitution, memorandum or articles of association; or
 - b) Such company's actual insolvency
 - vi. The aforesaid definitions of wrongful act, coverage of individuals and non-indemnifiable loss in policy for year 2016 remain the same.
 - vii. The definition of loss was amended in policy for 2016 to the extent that the loss will not include taxes, fines, penalties however in case the same is imposed by regulator, contested and upheld in court of law then the defense cost legally payable shall be payable by the insurer to the insured upto the limit of liability stated in agreement.
8. Before proceeding further, it is necessary to advert to the provisions of Section 194 of the Ordinance
- “ Save as provided in this section, any provision, whether contained in the articles of a company or in any contract with a company or otherwise, for exempting any director, chief executive or officer of the company or any person, whether an officer of the company or not, employed by the company as auditor, from, or indemnifying him against, any liability which by virtue of any law would otherwise attach to him in respect of any negligence, default, breach of duty or breach of trust of which he may be guilty in relation to the company, shall be void:*
- Provided that, notwithstanding anything contained in this section, a company may, in pursuance of any such provision as aforesaid, indemnify any such director, chief executive, officer, or auditor against any liability incurred by him in defending any proceedings, whether civil or criminal, in which Judgment is given in his favour or in which he is acquitted, or in connection with any application under section 488 in which relief is granted to him. ”*

It is evident from the above that the proviso of sub-section (1) of Section 194 of the Ordinance clearly states that it can only indemnify in cases where such officer/auditor had succeeded and thereby shown to a competent court that his act or conduct was bonafide or justified in the circumstances of the case. Thus, plain reading of Section 194 of the Ordinance suggests that indemnifying directors or officers among others



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mentioned in this section through any contract for their liabilities affixed by law, shall be considered void. It may further be inferred from the language of section 194 that if any director or officer is found guilty in relation to the company in respect of him being negligent or committing default, breach of duty or breach of trust, then such directors or officers may not be able to claim indemnity under any contract, be it in the form of an insurance policy or otherwise.

9. Furthermore, such provision of law barring indemnity for directors is not unique to corporate laws in Pakistan. Similar provisions can be found in the English as well as in Indian laws. In the Indian Law, Section 201 of the Companies Act, 1956 is predominately similar to Section 194 of the Ordinance. In the English Law, Section 232 of Companies Act, 2006 has similar provision as in Section 194 of the Ordinance.

10. In the subject insurance policies of the Company, fines/ taxes and matters uninsurable under law of Pakistan are excluded in terms of defining loss against which claims can be made. However, the definition of wrongful act includes breach of duty. Further, as per the subject policies, insurer is providing cover to the Insured against any loss which is non-indemnifiable under the law, which shall include liabilities prohibited to be indemnified under section 194 of the Ordinance. Hence strict interpretation of section 194 suggests that the Insurance Policy, which is a form of a contract with the company and which purports to provide indemnity to the directors or officers as the Insured under this Insurance Policy, is void. Courts have held in case of City Equitable Fire Insurance Co. Limited, 1925 Ch 407, that no protection or indemnity can be claimed against ultra-virus acts.

11. The essence of Directors' and officers' insurance is that competent professionals can serve as supervisors of organizations without fear of personal financial loss. It is also a norm that most policies have exclusions that, among others, denying cover for certain types of misconduct. However, it is important that the wordings on these exclusions in the policy is critically reviewed as even a subtle wording differences can significantly impact the accessibility of the cover. Further, it was contested that Code of Corporate Governance 2012 encourages professional indemnity insurance for independent directors. It is however pertinent to mention here that in the Code of Corporate Governance, 2012, professional indemnity insurance cover, a more liberal interpretation of Section 194 of the Ordinance, is encouraged in respect of independent directors only. Without prejudice to the aforesaid, the competent authority may still adhere to strict interpretation of the provision of Section 194 of the Ordinance and consider such insurance policy as void.

7th Floor, NIC Building, 63-Jinnah Avenue
Islamabad, Pakistan

PABX: + 92-51-9207091-4, Fax: +92-51-9100454, 9100471, Email: webmaster@secp.gov.pk, Website: www.secp.gov.pk



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12. Keeping in view the above, it can safely be concluded that the core purpose of a Directors and Officers Liability Insurance should be to provide financial protection for officers/auditors against the consequences of actual or alleged wrongful acts when acting in the scope of their managerial duties. Intentional illegal acts, however, are not covered under D&O policies. Therefore, such policies need to be very carefully drafted. It has been argued that company's worldwide practice acquiring directors' liability insurance. For intents and purposes the companies in Pakistan can also acquire such insurance for their directors, however, the covenants of the policy should preclude the matters indicated in Section 194 of the Ordinance. The prevalence of the practice of acquiring liability insurance in presence of similar provision in corporate laws of other international jurisdiction indicates that operational sphere of the insurance policy does not contradict the law.

13. Before deciding upon on matter, it is imperative to reassert that directors, in addition to their responsibility of overseeing and managing affairs of the Company, also have fiduciary duties towards the shareholders. They are, therefore, liable to a higher level of accountability, which requires them to be vigilant and perform their duties with care and prudence. I have analyzed the facts of the case, relevant provisions of the Ordinance, and submissions made by the respondents. I hereby conclude the proceedings and direct the respondents to be careful in future and ensure meticulous compliance with applicable laws in true letter and spirit.

Amina Aziz
Director (CSD)

Announced:
May 11, 2017
Islamabad