



SECP
Insurance Division
Karachi

[Karachi]

Before Tariq Hussain, Director (Insurance)

In the matter of

East West Insurance Company Limited

Show Cause Notice Issue Date: March 28, 2014

Date of Hearing: May 13, 2014

Attended By:

1. Mr. Mirza Kazim Raza
Director (Operations)
M/s East West Insurance Company Limited
2. Mr. Johry Lal
Internal Auditor
M/s East West Insurance Company Limited

Date of Order: November 28, 2014

ORDER

(Under Section 236 Read with Section 492 of the Companies Ordinance, 1984)

.....

This Order shall dispose of the proceedings initiated against M/s East West Insurance Company Limited ("the Company") for making material misstatement in the statements in the Directors' Report, required under Section 236 of the Companies Ordinance, 1984 (the "Ordinance") annexed to the Company's balance sheet as on December 31, 2012.

Background Facts

2. The relevant provisions of Section 236 of the Companies Ordinance, 1984 (the "Ordinance") state that:

Handwritten signature

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



"Director's report. - (1) The directors shall make out and attach to every balance-sheet a report with respect to the state of the company's affairs, the amount, if any, which they recommend should be paid by way of dividend and the amount, if any, which they propose to carry to the Reserve Fund, General Reserve or Reserve Account shown specifically in the balance-sheet or to a Reserve Fund, General Reserve or Reserve Account to be shown specifically in a subsequent balance-sheet.

(2) In the case of a public company or a private company which is a subsidiary of a public company, the directors report shall, in addition to the matters specified in sub-section (1),-

- (a) disclose any material changes and commitments affecting the financial position of the company which have occurred between the end of the financial year of the company to which the balance-sheet relates and the date of the report;*
- (b) so far as is material for the appreciation of the state of the company's affairs by its members, deal with any changes that have occurred during the financial year concerning the nature of the business of the company or of its subsidiaries, or in the classes of business in which the company has interest, whether as a member of another company or otherwise, unless the Commission exempts any company from making such disclosure on the ground that such disclosures would be prejudicial to the business of the company;*
- (c) contain the fullest information and explanation in regard to any reservation, observation, qualification or adverse remarks contained in the auditor's report;*
- (d) circulate with it information about the pattern of holding of the shares in the form prescribed;*
- (e) state the name and country of incorporation of its holding company, if any, where such holding company is established outside Pakistan ; and*
- (f) state the earning per share;*
- (g) give reasons for incurring loss and a reasonable indication of future prospects of profit, if any; and*
- (h) contain information about defaults in payment of debts, if any, and reasons thereof.*

(3) The report referred to in sub-section (1) shall be signed by the chairman of the directors or the chief executive of the company on behalf of the directors if authorised in that behalf by the directors and, when not so authorised, shall be signed by the chief executive and such number of directors as are required to sign the balance-sheet and profit and loss account under section 241.

..."

llc



3. The Directors' Report annexed to the balance sheet of December 31, 2012 misstated the following facts and figures:

- a. General Insurance industry in Pakistan has 29 companies registered by SECP under Insurance Ordinance 2000 whereas more than 29 companies have been registered.
- b. Investment Income for the year under review was shown Rs.37.78 million whereas it is 36.78 million as per income statement

4. Comments on the said observation were sought from the Company, vide the Commission's letter dated September 30, 2013, to which the Company replied, vide its letter of October 11, 2013, as under:

- a. *"Kindly note that we specified in the director's report that the general insurance industry in Pakistan has 29 companies registered with SECP. This was based on the list we obtained from the IAP.*
- b. *Your findings are correct but this was not an intentional act, considering the fact that all digits are correct as per the Statement of Investment Income except one digit that Rs.36.78 million is mistakenly publish as 37.78 which is a typographical error."*

5. It would be pertinent to mention that the Insurance Association of Pakistan (IAP) is not the competent authority to disclose as to how many companies are registered with the Commission as "insurers" under the Insurance Ordinance, 2000. The Commission is the most appropriate source of such information which can be relied upon in this context, and that the relevant information could have easily been obtained from the Commission's official website.

6. It appeared that the Company has aimlessly misstated the real facts relating to the number of registered non-life / general insurers in Pakistan. Likewise, the amount of investment income in the Directors' Report was not accurate compared to that in the financial statements for the year ended December 31, 2012. Accordingly, the Commission may take action in terms of Section 492 of the Ordinance, as the Directors of the Company have made out false and deceptive information to the members of the Company in their report to the members.

Show Cause Notice

7. Accordingly, the Show Cause Notice was issued on March 28, 2014 under Section 236 read with Section 492 of the Ordinance to the Company's Chief Executive Officer and the Directors, calling upon them to show cause as to why the penalty, as

Ali



provided under Section 492 of the Ordinance, should not be imposed onto them, for the misstatement as aforesaid.

Company's Response to the Show Cause Notice & the Hearing

8. The Managing Director & Chief Executive Officer of the Company submitted the response to the Show Cause Notice vide his letter bearing no. EWI/KHQ/CEO/2014-859 dated April 11, 2014, in which he stated as follows:

"...we wish to apprise that it is surprising for us to receive the under reply Show Cause Notice on such minor observations. Whereas, the company in its comments has already very honestly replied that:

- a. The general insurance industry in Pakistan has 29 registered companies was stated on the basis of the list obtained from IAP and the same was also provided with the comments.*
- b. The error was correctly observed by the Commission but that was not an intentional act, rather it was a typographical mistake where in the Statement of Investment Income only one digit was mistakenly printed as 37.78 against the actual figure of 36.78.*

For the paras 4 and 5 of the show cause we wish to reply that:

- 1. We agree that the IAP is not the competent authority to disclose as to how many companies are registered with the Commission as 'insurers', but you will also agree that being Association of all the member insurance companies it is a reliable source to obtain such information. However, our honest reply reflects that the information stated in the Director's Report has the basis which is backed by the evidence in shape of IAP's list already provided to the Commission.*
- 2. The Show Cause Notice itself speaks in its para 5 that the company has 'aimlessly' stated regarding number of registered insurance companies is true, as the company has not made any aimed or deliberate misstatement to achieve any benefit or gain. Simultaneously, it is agreed that the amount of Investment Income in the Director's report is not accurate but as commented earlier there is a reason to believe that mistake of only one digit is a typographical error and not an intentional misstatement for any gain or benefit and did not cause harm to any concern.*

In the light thereof, the observations made in the subject show cause do not in any way attract the penal action under section 492 of the company's ordinance 1984...

Observations made in the show cause in fact do not fall in this section. In both the observations of this Show Cause there is no "False Statement". The False Statement is

Alu



elaborated in the above section as a deliberate incorrect statement in any material particular and knowing it to be material.

- *As all the facts stated above, there was a basis of the statement regarding number of registered insurance companies, hence it could not be treated as false statement.*
- *Difference of only one digit in the figure of Investment income has a reason to believe being a typographical error and could not be termed as a 'false statement' in any material particular.*

In the light of the above submission, the Management is quite certain that, the observations made in the Show Cause Notice does not attract any penal action under section 492 of the Company's Ordinance, 1984, especially in view of the fact that in accordance with the said section the company has in both the observations do not made any false statement. Hence, it is requested that the Show Cause Notice under reply may kindly be withdrawn and any action in consequence may be dropped.

In case you still require further explanation / clarification or our above explanation is not acceptable to the commission, we would like to request for a personal hearing before the commission alongwith legal counsel..."

9. The Managing Director & Chief Executive Officer of the Company, through his response letter dated April 11, 2014, while acting on behalf of the Company, had requested for a personal hearing before the Commission. Accordingly, the Commission had scheduled the hearing for May 13, 2014, which was communicated to the addressees of the Show Cause Notice vide the Commission's hearing notice no. ID/Enf/EWICL/2014/19490 dated April 23, 2014.

10. The hearing in the matter of the aforesaid Show Cause Notice was attended by Mr. Mirza Kazim Raza, Director (Operations) of the Company, who was authorized to represent the Company's Directors and the Chief Executive Officer in the instant matter, through a General Power of Attorney dated May 5, 2014. Accordingly, Mr. Kazim Raza shall be referred to as the "Company's representative" hereinafter.

12. In the hearing of May 13, 2014, the Company's representative was duly assisted and accompanied by Mr. Johry Lal, the Internal Auditor of the Company.

13. During the course of the said hearing, the Company's representative reiterated the contents of the letter of the Company's Managing Director & Chief Executive Officer dated April 11, 2014.

Mirza



Consideration of Company's Submissions

14. I have carefully examined and given due consideration to the written and verbal submissions of the Company's Directors and the Chief Executive Officer of the Company, through the letter of the Company's Managing Director & Chief Executive Officer dated April 11, 2014 and the personal appearance of Mr. Kazim Raza, Director (Operations) of the Company, and have also referred to the provisions of the Ordinance. I am of the view that there has been an established misstatement in the Directors' Report annexed to the balance sheet of December 31, 2012, which was prepared under Section 236 of the Ordinance.

15. However, before proceeding further, I find it relevant to comment on 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 performing their duties with due care. In the instant case, however, the Company and its 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 towards mitigation of the misstatements in the reports, returns, certificates, balance sheets, profit & loss account and other documents / information that are required to be prepared or submitted under the law, therefore, it could be legitimately inferred that the misstatement was committed, as aforesaid.

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 misstatement in the Directors' Report attached to the balance sheet of December 31, 2012, required under Section 236 of the Ordinance is established and admitted by the Company's management, therefore, the penalty as provided under Section 492 of the Ordinance can be imposed onto the Company's Directors and the Chief Executive Officer. However, the misstatement appertaining to the number of registered non-life insurance companies was not of direct relevance to the purpose for which the Directors' Report is made out and attached to the balance sheet of the Company, and that the misstatement appertaining to the investment income of the Company appeared to be a typographical error.

17. 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

Alex:



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."

Order

18. In exercise of the power conferred on me under Section 492 of the Ordinance, I, instead of imposing the maximum penalty as provided therein, take a lenient view, and thus, condone the Company's Directors and the Chief Executive Officer due to the fact that the misstatement appertaining to the number of registered non-life insurance companies was not of direct relevance to the purpose for which the Directors' Report is made out and attached to the balance sheet of the Company, and that the misstatement appertaining to the investment income of the Company appeared to be a typographical error.

However, the Company's Directors and the Chief Executive Officer are hereby issued a stern warning that in case of similar non-compliance in future a stronger action shall be taken.

19. 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 of the Company) in accordance with the law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.

Tariq Hussain
Director - Insurance