



Fida Hussain Samoo  
Commissioner

Before Fida Hussain Samoo, Commissioner (Insurance)

In the matter of

Pak Kuwait Takaful Company Ltd

Number and date of show cause notice	No. ID/Enf/PKTCL/2016/4827 dated April 27, 2016
Date of hearing	June 22, 2016 and July 20, 2016
Present	<p>Mr. Ijaz Ahmed, Advocate Supreme Court and Mr. Sarfaraz Ahmed, Advocate appeared on behalf of (Syed Amir Ali, Executive Director of the Pak Kuwait Takaful Company Ltd also accompanied him)</p> <ol style="list-style-type: none"><li>i. Mr. Mohd Tarmidzi Bin Ahmad Nordin,</li><li>ii. Mr. Rana Ahmed Humayun,</li><li>iii. Mr. Zaharudin Daud,</li><li>iv. Mr. Osman Kassim,</li><li>v. Mr. Mansur Khan,</li><li>vi. Syed Amir Ali, Director</li><li>vii. Mr. Nazawawe Bahari, Director and</li><li>viii. Pak Kuwait Takaful Company Ltd</li></ol> <p>Sheikh Aftab Ahmad, Executive Vice President, Saudi Pak, appeared on behalf of Mr. Kamal Uddin Khan, Director.</p>

**Order under Section 11(1)(f) and Section 12(1) read with Section 158 of the Insurance Ordinance, 2000**

This Order shall dispose of the proceedings pertaining to the matter of Show Cause Notice bearing No. ID/Enf/PKTCL/2016/4827 dated April 27, 2016 (hereinafter referred to as the "Notice") under

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COMMISSION OF PAKISTAN  
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Sections 11(1)(f) and Section 12(1) read with Section 158 of the Insurance Ordinance, 2000 (hereinafter referred to as the "Ordinance") served on the Chairman, Chief Executive, Directors of Pak Kuwait Takaful Company Limited (hereinafter referred to as the "Company") and the Company.

2. The facts leading to this case briefly stated are that, the Board of Directors of the Company, in their meeting held on Dec 1, 2014 decided to appoint M/s. Ernst & Young (hereinafter referred to as the "EY") to carry out assessment of reserves against claims, examination of paid claims, identification of potential phantom agents and assessment of adequacy of bad debts and M/S. EY submitted their report on March 6, 2015 with following significant findings:

- a. The Reserve against Claims was understated and understatement as at Nov 30, 2014 amounted to Rs.40.817 million.
- b. Out of selected sample of 122 claims, supporting documents including the final surveyors reports and invoices of 32 claims amount to Rs.1,914,694 were not made available to them and review of the remaining 90 claims disclosed that:
  - Alteration and/ or removal of dates and amounts, by hand, on the surveyor reports and its underlying document;
  - Claim number and date generated before the accident, i.e. claim lodged in Feb 2014 and date of accident is Jun 2014;
  - Supporting bills of workshop are dated before the date of accident;
  - Incorrect details of policies in the surveyor report;
  - Claim approved on a Sunday (6 July 2014).
- c. The comparison of the aging report and revised aging report identified that an additional provision of Rs. 51.740 million was required as at Nov 30, 2014.
- d. It was observed that "Sales Development Executive (SDE) Scheme Policies and Procedure Manual were not complied with in relation to recruitment of SDE. Further there was no policy at PKTCL for recruitment of cash & carry agents.
- e. Agencies may be created in the name of family member(s) of existing PKTCL agents and/or employees. We recommend that relationships, if any, should be disclosed in writing at the time of creation of an agency and should be approved. Further, the disclosure and approval documents should be made part of agents' files.

3. The management of the Company subsequently carried out an analysis of the report of M/S. EY to identify full impact of irregularities and identified the following:

- a. Contribution due but unpaid as at December 31, 2014 before adjustments amounted to Rs. 363.6 million and subsequent receipts there against amounted to Rs. 83.042 million.
- b. There were no recoveries of contributions aggregating to Rs. 31.1 million (2012: Rs. 1.05 million, 2013: Rs. 1.89 million and 2014: Rs. 28.16 million) nor they were supported by adequately documented policies.

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- c. There were no recoveries of contributions aggregating to Rs. 249.5 million (2012: Rs 20.17 million, 2013: Rs.52.2 million and 2014: Rs.177.1 million), however according to management they are supported by adequately documented polices. The specific reasons for non-recovery have not been identified. According to the Company's policy, a provision of Rs. 8.06 million has been made against the policies issued during 2014.
- d. Claims at December 31, 2012 were understand by Rs.30.8 million and at December 31, 2013 they were understand by Rs. 23.099 million.
- e. The reversal of endorsements which were made without any adequate supports effected the provision for doubtful debts in the respective year.

4. The statutory external auditors of the Company, KPMG Taseer Hadi & Co., Chartered Accountants (hereinafter referred to as the "KPMG") in their Board letter dated April 24, 2015 stated that the practice of incorrect reporting has been going on since 2012 to present positive results and to maintain solvency requirements, transpiring that business of the Company had not been managed in a sound and prudent manner and with integrity, due care and professional skills appropriate to the nature and scale of its activities. The aforesaid issues have had impact on the Regulatory Return of the preceding years and accordingly, the supervisory concerns were raised on the true and fairness of the information submitted to the Commission during the early years. The aforementioned contraventions and material misstatement necessitated action under Section 11(1)(f) and Section 12(1) read with Section 158 of the Ordinance on adopting the deceptive accounting and not managing the business in a sound and prudent manner, failure to ensure that the business is carried out with integrity, due care and professional skills appropriate to the nature and scale of its activities and material misstatement in the returns submitted to SECP since the year 2012. Thus the Notice was issued to the following Chairman, Chief executive and Directors of the Company and the Company (hereinafter referred to as the "Respondents") who *prima facie* authorized the contraventions of the provisions of the Ordinance. The following persons were called upon to show-cause, in writing, within 10 days of the date of Notice as to why necessary penal action may not be taken against them, as provided under Section 158 of the Ordinance.

S No.	Chairman, Chief Executive and Directors and Company
1	Mohd Tarmidzi Bin Ahmad Nordin, Chairman
2	Mr. Imtiaz Ahmed Bhatti, Chief Executive Officer
3	Mr. Rana Ahmed Humayun, Director
4	Mr. Zaharudin Daud, Director
5	Mr. Osman Kassim, Director
6	Mr. Mansur Khan, Director
7	Mr. Kamal Uddin Khan, Director
8	Syed Amir Ali, Director
9	Mr. Nazawawe Bahari, Director
10	Mr. Talal B A KH Al-Mesallam, Director
11	M/s. Pak Kuwait Takaful Company Limited

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5. In response to the Notice, Mr. Mansur Khan, Chairman of the Board of Directors of the Company, vide letter dated May 4, 2016 requested to grant extension of 30 days-time for submission of reply to the Notice, however, an extension upto May 17, 2016 was granted. Mr. Ijaz Ahmed, Advocate Supreme (the Authorized Representative of Respondent No. 1, 3, 4, 5, 6, 8, 9 and 11) vide letter dated May 25, 2016 submitted the reply to the Notice. It was stated that the answering Respondents have neither committed nor over intended to commit any breach of section 158 or 156 of the Ordinance. The answering respondents were appointed as the nominee directors of the reputable local and foreign institutional investors, therefore, all the answering respondents were non-executive directors and did not involve in the daily management of the business. The management headed by Chief Executive Officer is therefore responsible to ensure that all functions are performed in accordance with law, complete and accurate information is recorded in books and is placed before the Board. Non-executive directors are only involved in decision making process, in respect of the matters brought before the Board. The answering Respondents accepted the management's version of the transactions in good faith and in ordinary course of business and they were neither authorized nor were apprised of any such irregularities by the management of the Company.

6. Narrated the background, basis of the M/S. EY's report dated March 6, 2015 highlighting certain irregularities committed at the behest of the Managing Director/ Chief Executive Officer of the Company and misleading information submitted to the Board, the Board accounted for the previous years' effect of the corrections in accordance with the requirements of applicable accounting standards in order to become compliant with the regulatory requirements. Disclosed in the audited accounts and regulatory returns for the year ended December 31, 2014, while revising the annual audited accounts for the years ended December 31, 2012 and 2013. The revised regulatory returns and financial statements of the Company has been prepared and filed with the Commission. Moreover, appropriate action was also taken against the responsible persons for misconducting the business affairs of the Company. The Chief Executive Officer has been removed with effect from May 21, 2015 and Chief Operating Officer terminated on May 29, 2015.

7. Further stated that the Board was never informed of such irregularities until the same was disclosed in Board meeting held on Dec 1, 2014 when the issue was pointed out by Etiqa Overseas Investment Pte. Ltd. Hence the answering Respondents have neither committed nor ever intended to commit any breach of any provision of the Ordinance and vehemently denied that the answering Respondents have willfully submitted any false statement in respect of any material particularly, whatsoever, knowing it to be false. Therefore, it is only the Company's previous management which are responsible for the issues raised in the Notice.

8. It may be realized that investors, stakeholders and other end users of the financial statements look for true and fair information in all reports of the Company, whether balance sheet, notes to the accounts or regulatory returns attached thereto. The financial statements are one of the underlying basis for the decision making and may lead to wrong conclusion, if the financial statements does not provide true and fair information, especially when the results are materially altered. The directors of the Company are responsible for the preparation and circulation of the accounts. Accordingly, section 241 of the Companies Ordinance provides that the balance sheet and profit and loss accounts shall be

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approved by the directors. The directors of a company are supposed to be well verse with their legal obligation including the fiduciary duty of the running the day to day affairs of the company and authentication of financial statements prior to dissemination.

9. No reply to the Notice was provided by the Respondents No. 2, 7 and 10, in order to proceed further and to provide the opportunity of hearing to the Authorized Representative of the answering Respondents, the hearing of the case was fixed on June 22, 2016 to be held through Videocon facility between Head Office of the Commission, Islamabad and Company Registration Office, Karachi. On the date of hearing Mr. Sarfaraz Ahmed, Advocate and Syed Amir Ali, Executive Director of the Company alongwith the Authorized Representative of the answering Respondents appeared in person before the undersigned to plead the case. The Authorized Representative of the answering Respondents reiterated the same arguments as submitted in the written reply to the Notice and stressed that the answering Respondents are non-executive nominee directors and are not participating in day to day operations of the Company, the information provided to the Board by the management was satisfactory until the Etiqa' findings, thereafter, appropriate actions were initiated including the termination/removal of the Chief Executive Officer and Chief Operating Officer of the Company.

10. It was highlighted to the Authorized Representative of the answering Respondents that the Respondents were part of the audit committee that approved the annual audited accounts of the respective periods and the Board which authenticated the accounts prior to issue and submission/filing to the Commission, therefore, the Respondents are equally responsible for material misstatement in the Regulatory Returns of the Company, the Audited Financial Statements for the year ended Dec 31, 2013 along with Statements of Assets and Liabilities as at Mar 2014, Jun 2014 and Sep 2014 of the Company filed with the Commission under section 51 of the Ordinance. It was argued by the Authorized Representative of the answering Respondents that the matter of identified irregularities was also discussed in a meeting with the statutory auditors of the Company and questions raised by the Auditors were answered satisfactorily. Moreover, quoting to the provisions of Section 158 of the Ordinance, argued that the misstatement is subject to knowingly and willful action by the Respondents which is not found in the instant case. The decisions taken by the Board on the basis of the information provided to it which were on merit. At the end the Authorized Representative of the answering Respondents quoted the case laws on knowingly and willfully and provided the same case laws in writing to support the arguments.

11. In the matter of not answering Respondents No. 2, 7 and 10, the hearing notices dated June 24, 2016 were issued at their available residential as well as official addresses, however, no one appeared on the given date and time. In order to provide the final opportunity of hearing notice dated July 13, 2016 were issued and the case was fixed for July 20, 2016. In response, the Respondent No. 7, namely; Mr. Kamal Uddin Khan, Director of the Company vide letter dated July 13, 2016 submitted its response that the Respondent No. 7 was co-opted as nominee director in the 50<sup>th</sup>, 51<sup>st</sup> and 52<sup>nd</sup> Board meetings of the Company held on December 1, 2014, March 31, 2015 and April 30, 2015 respectively which were not attended by him due to preoccupations and leaves of absence were granted by the Board of the Company. Finally, he resigned from the directorship of the Company on May 15, 2015 therefore he has no nexus with the affairs of the Company. Moreover, it was stated that he never signed or filed any wrong/ incorrect returns, reports, balance sheets, certificates of the

Company as alleged. He authorized Sheikh Aftab Ahmad, EVP, Saudi Pak Industrial & Agricultural Investment Company Ltd ("Saudi Pak") to represent him as and when required. Subsequently, on the date of hearing, Sheikh Aftab Ahmad, EVP, Saudi Pak (the Authorized Representative of Respondent No.7) appeared in person before the undersigned and reiterated the same arguments as were submitted through written reply to the Notice. It was added by the Authorized Representative of Respondent No.7 that he remained on Board of the Company for the period Dec 1, 2014 to May 15, 2015, whereas, the issues under consideration pertains to the year 2014.

12. Before proceeding further, it is appropriate to reproduce the relevant provisions of the Ordinance.

***"Section 11(1)(f)- 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;"*

***"Section 12(1)- 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 authorised 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;*

*(e) the insurer or applicant maintains adequate system of control of its business and records;*

13. The key responsibility of board is to design, implement and review system of internal control. The internal controls protect businesses from abuse and fraud. Further it ensures the integrity of the firm's accounting and financial reporting systems, including the independent audit and compliance with the law and relevant standards. To make internal control function effective the board should set appropriate policies on internal control and seek regular assurance that will enable it to satisfy itself that the system is functioning effectively. The board must further ensure that the system of internal control is effective in managing risks in the manner which it has approved.

In order to ensure effective system of Internal Control the board should regularly receive and review reports on internal control from audit Committee and provide assessment of the significant risks and the effectiveness of the system of internal control in managing those risks. Any significant control failings or weaknesses identified should also be discussed in the reports including the impact that they have had. When reviewing reports the board should consider whether necessary actions are being taken promptly to remedy any significant failings or weaknesses or whether the findings indicate a need for more extensive monitoring of the system of internal control.

14. International Financial Reporting Standard 4 - Insurance Contracts, specifies the financial reporting for insurance contracts and disclosures. It identifies and explains the amounts in an insurer's financial statements arising from insurance contracts and helps users of those financial statements understand the amount, timing and uncertainty of future cash flows from insurance contracts. The



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Liability Adequacy Test and Claim Development information are especially of significant importance in the present case and relevant paragraphs are quoted below:

- Paragraphs 14-20 address specific requirements (liability adequacy test, when to remove a liability and impairment of reinsurance assets) and prohibitions (liability for possible future claims on contracts that do not yet exist, offset of reinsurance assets and income items against the related insurance liabilities and income items). The liability adequacy test is intended to help ensure that the liabilities calculated using existing accounting policies are not understated and that related amounts recognized as assets are not overstated. The test is based on comparing the assets and liabilities determined under existing accounting policies with the value of current estimates of future cash flows.
- Paragraph 38 provides that an insurer shall disclose information that enables users of its financial statements to evaluate the nature and extent of risks arising from insurance contracts. Whereas, Paragraph 39(c)(iii) provides that actual claims to be compared with previous estimates (i.e. claims development). The disclosure about claims development shall go back to the period when the earliest material claims arose for which there is still uncertainty about the amount and timing of the claims payments, but need go back more than ten years. An insurer need not disclose this information for claims for which uncertainty about the amount and timing of claims payment is typically resolved within one year.

15. The word "willful default" which has been defined in Oxford Dictionary of Law as "The failure of the person to do what he should do, either intentionally or through recklessness." The argument of the Authorized Representative of the Answering Respondents that the default was not "willful" holds little merit as even there may not be knowledge or intent, the Respondents did not exercise the due skill and care required of them as directors of the Company at the time of submission of the accounts. The default, therefore, would be considered as willful. It was held in the Appellate Tribunal Inland Revenue (ATIR) in 2012 PTD (Trib.) 122 held that, "...The word "default" wherever appears in the Income Tax Law should mean an act done in breach of legal obligation, a duty or in disregard of an order or direction with mala fide intention and ulterior motive.". Moreover, According to Black Law's Dictionary, these two expressions entail the 'deliberate, intentional, predetermined and fully considered' and 'Willful; voluntary and intentional, but not necessarily malicious'. It is in fact despondent that the directors have demonstrated such a level of careless approach by submitting false information purporting it to be authentic.

16. In the present case, the directors have failed to maintain adequate systems of control of its business and accounting records of its business, as required under section 12 of the Ordinance. They were unable to present true and fair financial statements for the year ended Dec 31, 2012 and Dec 31, 2013. The policyholders, shareholders, creditors and other stakeholders including regulators were misled by the materially misstated Audited Financial Statements filed with the Commission under section 46 and 51 of the Ordinance.

The representation made by the directors in the "Statement of Compliance" that the financial statements have been prepared in accordance with approved accounting standards in Pakistan, disclosed in the Audited Financial Statements, belied the underlying facts and veracity of the "Statement of Compliance" cannot be validated.



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17. The directors have not performed their duties diligently and meticulously. The adequate internal controls coupled with Liability Adequacy Test and Claim Development information could have detected fraud and helped in the removal of material misstatements. They have breached trust of the policyholders and have not even fairly communicated issues encompassing "Restatement of Comparatives" in the financial statements for the year ended Dec 31, 2104.

The importance of clear communications to investors regarding a restatement cannot be underestimated. Policyholders could have been more comfortable with news surrounding a restatement by thoroughly explaining the issue or issues that gave rise to the fraud/ misstatements and actions of the Company in this regard. Failing to do so may increase concerns about whether there is an ongoing weakness in the company or its management, which could lead to additional problems down the road. Ambiguity regarding how a company is responding to financial reporting errors can be the most damaging, because it may prompt the investment community to assume that the problem is more significant than it is in reality. The Directors Reports should have summarized the events leading to fraud/ misstatement and the Company plans to respond to the circumstances.

18. I have carefully examined and given due consideration to the written as well as verbal submissions of the Respondents through the Authorized Representatives and have also referred to the provisions of the Ordinance. It is obligatory upon the Commission to regulate the business of the insurance industry to ensure the protection of the interests of the policyholders. I am of the view that the Respondents including the non-answering Respondents have contravened the provisions of Section 11(1)(f) and Section 12(1) of the Ordinance and have not managed the business in a sound and prudent manner. They failed to ensure that the business is carried out with integrity, due care and professional skills appropriate to the nature and scale of its activities. Moreover, the accounts and returns submitted to SECP, since 2012 were materially misstated. This attracts penal provisions provided in the Section 158 of the Ordinance, which provides that whoever, in any return, report, certificate, balance-sheet or other document, required by or for the purposes of any of the provisions of this Ordinance, willfully makes a statement false in any material particular, knowing it to be false, shall be punishable by the Commission with fine which may extend to one million rupees. Therefore, I, in exercise of powers conferred upon me under Section 158 of the Ordinance, impose a penalty of Rs. 1,000,000 (Rupees One Million only) on the Chief Executive and the Company with strict warning to the remaining directors to be careful and diligent in carrying out the business of the Company. The penalty is imposed on the Chief Executive Officer and the Company, in the following manner:

S No.	Chief Executive and Company	Penalty (Rupees)
1	Mr. Imtiaz Ahmed Bhatti, Chief Executive Officer	500,000
2	M/s. Pak Kuwait Takaful Company Limited	500,000
	<b>Total</b>	<b>1,000,000</b>



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19. The Respondents are, hereby, directed to deposit the afore-mentioned amount of penalty in the designated bank account maintained in the name of the Commission with MCB Bank within thirty days from the receipt of this Order and furnish the receipted bank challans to the Commission. In case of failure to deposit the penalty, proceedings under the Land Revenue Act, 1967 will be initiated for recovery of the fines as arrears of land revenue. It may also be noted that the said penalty is imposed on the Respondents in their personal capacity; therefore, they are required to pay the said amount from personal resources.



**Fida Hussain Samoo**  
Commissioner (Insurance)



*Announced:*  
August 24, 2016  
Islamabad