



SECP
Insurance Division
Karachi

[Karachi]

Before Tariq Hussain, Director (Insurance)

In the matter of

The Asian Mutual Insurance Company (Guarantee) Limited

Show Cause Notice Issue Date: March 22, 2013

Date of Hearing: April 25, 2013

Attended By:

1. Mr. Irfan Ilyas, FCA
Partner
Ilyas Saeed & Co.
2. Mr. Tahir Mahmood
Manager
The Asian Mutual Insurance Co. (Gte) Limited

Date of Order: June 21, 2013

ORDER

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

.....

This Order shall dispose of the proceedings initiated against M/s The Asian Mutual Insurance Company (Guarantee) Limited ("the Company") for not complying with the provisions of Regulation 16(1)(b) of Part B of Annexure II of the Securities and Exchange Commission (Insurance) Rules, 2002 (the "Rules").

Background Facts

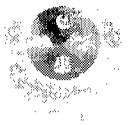
2. The relevant provision of Sub-section (1) of Section 46 of the Insurance Ordinance, 2000 (the "Ordinance") requires every non-life insurer to file annual

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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:

...

(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. The Company, in pursuance of Section 46(1)(b) and Section 51(1) of the Ordinance, had filed its Annual Audited Financial Statements for the year ended December 31, 2011 (which shall be referred to as “the Accounts” hereinafter).

4. The Company’s Statement of Assets for Solvency Purposes (Form GJ) as at December 31, 2011 showed that the Company had taken all its Available for Sale investments at market value.

5. Regulation 16(1)(b) of Part B of Annexure II of the Rules (the “Regulations”) lays down the requirement for recording and reporting the investment properties 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.

...

(b) Investment Properties shall be stated on the basis of Cost Model under IAS - 40. In case there is any impairment in the value then this shall be recognized. The market value of properties shall be determined at least once in every financial year and disclosed, as shall the effect of non-compliance with IAS 40;”

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6. The Accounts revealed that the Company has an investment property (Land & Building) amounting to Rs. 9,180,000/- which was previously revalued in the year 2004, and the Company had booked Surplus on Revaluation of Fixed Assets amounting to Rs. 8,395,000/-. It was further observed that the Company has not carried out any revaluation of the said property since the year 2004. Accordingly, the Company has not recorded any impairment in the value of the said property, if any, which is required under Regulation 16(1)(b) of the Regulations. Further that the Note 13.1 to the Accounts revealed that the revalued assets are held for capital appreciation and are not being used for any purpose by the Company.

7. Since the Company had not stated the carrying amount of the property at cost, and hence, it appeared that the Company had chosen to follow the fair value model under IAS 40, which is against the provisions of Regulation 16(1)(b) of the Regulations. Moreover, the Company was required to revalue its investment property at least once in every financial year.

8. In view of the foregoing paras of this Notice, it appeared that the Company has contravened the requirements of the Regulations relating to the recording and reporting of the investment properties as laid down under Regulation 16(1)(b) of these Regulations, which calls for the penal provision as provided under Section 156 of the Ordinance.

Show Cause Notice

9. Accordingly, the Show Cause Notice was issued on March 22, 2013 under Regulation 16(1)(b) of Part B of Annexure II of the Rules and Section 46(1)(b) read with Section 156 of Ordinance to the Chief Executive and Directors of the Company, 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)(b) of Part B of Annexure II of the Rules.

Company's Response to the Show Cause Notice

10. In response to the said Show Cause Notice, the Company, vide their letter of April 8, 2013, stated that:

"...we were extremely engaged in the finalization of closing of F-Y 2012. The Company has just concluded its Annual General Meeting held on 7th April, 2013 and could not respond to the matter earlier.

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We shall submit a detailed reply to the above by April 30, 2013 it is earnestly requested to kindly adjourn the case till then for our submissions.

It is submitted that there was no willful default of any kind.

It is humbly requested that the case may kindly be adjourned as solicited accordingly..."

11. Thereafter, the Company, vide their letter no. Audit/A-56/13 dated April 13, 2013, stated that:

"...The company in financial statement has not carried out any revaluation of the investment property (land and building) since long (since 2004) (relevant extracts from financial statements for financial year 2004 is enclosed as Annex "A"). The company and the directors have adopted a prudent policy, as given under Regulation 16(1)(b) of Part B of Annexure II of the SEC (Insurance) Rules 2002.

It may be pointed out that the directors in the past have internally carried out review of the valuation, and have determined that there was no impairment in the value of asset. Whenever, there will be any impairment, this would be accordingly reported.

It is submitted that by practice and inference over last many years, the SECP has graciously accepted the company's position since long.

It is pointed that the company did not carry out revaluation of land / building in Financial Year 2011 (relevant extracts from the financial statements for financial year 2011 is enclosed as Annex "B") and has stated value of Land and Building as per carrying amount since 2004. Since then, the company is taking its carrying value of Land and Building held as Investment Property.

The company has taken the exercise of valuation of investment property every year and market value of the investment property has duly been disclosed in statement of "Classified Summary of Assets in Pakistan" in the financial statements. There had been no impairment in the value of property. Copy of valuation report for the year 2011 is enclosed as Annex "C" for your ready reference.

It may be added that the company was issued letter by the Assistant Director (Insurance; Division) Securities & Exchange Commission of Pakistan, Karachi, on the same issue which was explained vide submissions dated May 21, 2012. No adverse inference was drawn on the same and the issue since accepted by the Securities & Exchange Commission of Pakistan.

It is also pointed out that on similar observation, the same was explained to the auditors along with the reply of Securities & Exchange Commission of Pakistan and valuer's report, hence, no adverse audit observation was noted by them.

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It is submitted that an inspection team was deputed by SECP vide letter No. 1539 dated 01-02-2013, who was mandated for audit / verification / inspection of FY 2011 and 2012, 7-lists of their requirements were issued spread over several pages, these were duly complied, along with photo copies of documents, certificates and other as demanded, to their satisfaction, and no adverse observation was noted by them. It is submitted that this issue was also explained to them.

It is not out of place to mention that by practice of over many years now, the issue of valuation of investment property has been a closed transaction. The company has not made any gains out of this valuation (carried out in 2004) and the Company has not violated any requirements for the year 2011.

The mistake, which is carried forward since 2004, if any, is harmless and it is reiterated that neither the company has made any gain out of this nor the State or general public has suffered any lose.

The mistake, if any, has been perpetuated since 2004, which stands vindicated by inference of practice of last so many years.

It is humbly requested to kindly accept our submissions and in view of the facts and history of the case, please do not draw any adverse inference. The company has authorized Mr. Irfan Ilyas FCA son of Sheikh Muhammad Ilyas FCA to make submission to you personally on our behalf. (Power of Attorney is attached as Annex "D")..." (Underlined to put emphasis)

12. The reply of the Company reveals that the Company has itself assumed that if any non-compliance / contravention of any provision of the law was not pointed out by the Commission, the same stands vindicated / justified and that it may be continued forever. However, law is open to everyone, and ignorance / misunderstanding of the applicable law cannot be treated as valid excuse based on which the Commission may not take any action against the Company.

13. Moreover, the Company was well-informed about the aforementioned contravention of Regulation 16(1)(b) of the Regulations, and the Commission, vide its letter dated March 26, 2012, had pointed out the same issue to the Company. The said letter of the Commission stated that:

"...2. The Company has reported an amount of Rs.9,180,000/- as the book value of the Land, which was last revalued in the year 2004, since then no revaluation of the said piece of Land was conducted.

3. The Accounting Regulation No.16(1)(b) of Part B of Annexure II of the Securities and Exchange Commission (Insurance) Rules, 2002 states:

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"For the purpose of all statements prepared under these regulations, and for the purpose of S34(1) of the Insurance Ordinance 2000:

(b) Investment Properties shall be stated on the basis of Cost Model under IAS - 40. In case there is any impairment in the value then this shall be recognized. The market value of properties shall be determined at least once in every financial year and disclosed, as shall be effect of non-compliance with IAS 40."

4. Neither the impairment/appreciation in the value of the aforesaid piece of Land has been recorded nor has there been any revaluation carried after the year 2004. It appears that the Company has contravened the aforesaid provision of the Law. However, as per the Statement of Classified Summary of Assets the market value of the Land has been Rs.15,375,800/-, which is over and above the book value.

5. The Company in response to the abovementioned observation stated that:

"The note attached to the FS is reproduced below for reference;

The revalued assets are held for capital appreciation and are not being used for any purpose by the company.

There is no impairment in the value of Land & Building, however there estimated market value is stated at Rs.15,375,800/-. As and when these are revalued or impairment occurs these will be reported.

The revaluation was carried out by independent valuers vide report dated 5th APRIL, 2004"

6. The viewpoint of the Company appears to be incorrect because the Company has not revalued its Land & Building after April 5, 2004, therefore, the Company could not ascertain that there was no impairment in the value of their investment properties.

7. Therefore, the Company has contravened the provisions of the Accounting Regulation No.16(1)(b) of Part B of Annexure II of the Securities and Exchange Commission (Insurance) Rules, 2002.

16. Therefore, you are hereby called upon to clarify your position as to why the Company has apparently not followed the provisions of both the IAS 40 as well as the Regulation No. 16(1)(b) of Part B of Annexure II of the Securities and Exchange Commission (Insurance) Rules, 2002."

14. The Company, vide their letter dated April 23, 2013, also gives a mixed statement regarding conducting valuations of the property each year, as at one place the Company admits that it has not carried out any revaluation during the year 2011, whereas on the other hand, the Company claims to have got the property revalued in

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each year. However, the annexure to the aforesaid reply of the Company contains a valuation report no. KHZ/VAL-013/2012 dated January 4, 2012, which was issued by M/s K.H.Z Associates (Private) Limited, wherein the Land and Building of the Company was valued at Rs. 15,000,000/- and Rs. 375,800/-, respectively.

15. Furthermore, the minutes of the meeting of the Board of Directors of the Company of February 22, 2012 also endorse the fact that the Company's land was last revalued in 2004.

Hearing of the Case & Subsequent Developments

16. Although, the Company had not requested for hearing in the matter vide their letter of April 8, 2013, the Commission, on its own motion, had scheduled the hearing in the matter for April 25, 2013 at 3:00 p.m., which was communicated to the Company via the Commission's hearing notices no. ID/ENF/Asian Mutual/2013/16333 dated April 12, 2013.

17. The Company, vide its letter dated April 23, 2013, had nominated Mr. Irfan Ilyas - FCA of M/s Ilyas Saeed & Co., Chartered Accountants, to represent the Company, and had provided the Power of Attorney in his favor.

18. Accordingly, the said hearing was attended by Mr. Irfan Ilyas of M/s Ilyas Saeed & Co., Chartered Accountants (who will be referred to as the "Company's representative" hereinafter), however, the Company's representative was accompanied by Mr. Tahir Mahmood, Manager of the Company.

19. Brief proceedings of the hearing of April 25, 2013 are as follows:

- a. The Company's representative was asked to present the stance of the Company, to which the Company's representative stated that the Company has, in one way or the other, disclosed the market value of the land in the financial statements for the year ended December 31, 2011, which was based on the valuation report that has already been submitted vide the Company's letter dated April 23, 2013;
- b. The Company's representative also mentioned that the Company has been getting its properties valued each year, on which the Company was asked to provide the documentary evidences of the Company's argument that the Company has been carrying out valuations each year;
- c. The Company's representative further stated that the Company has not drawn any benefit out of this treatment of the Company's investment properties, and that the default was not willful;



- d. The Company's representative then requested the Commission to take a lenient view and stated that the Company shall be careful in future while disclosing the market value of the property.

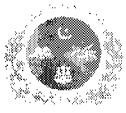
20. Subsequent to the hearing of April 25, 2013, the Company, vide its letter no. Audit/A-56/13 dated May 2, 2013, had provided the valuation reports no. KHZ/VAL-010/2010 dated January 10, 2010 and KHZ/VAL-008/2011 dated January 6, 2011, which were issued by M/s K.H.Z Associates (Private) Limited.

21. Surprisingly, the valuation reports of all the three years show up the same value i.e. Land of Rs. 15,000,000/- and Building of Rs. 375,800/-, totaling to an amount of Rs. 15,375,800/-.

Consideration of Company's Submissions

22. I have carefully examined and given due consideration to the written and verbal submissions of the Company (through the Company's representative, Mr. Irfan Ilyas - FCA of M/s Ilyas Saeed & Co., Chartered Accountants, 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)(b) of the Regulations, as the Company was required to state their Investment Properties at Cost Model under IAS 40 in terms of the provisions of Regulation 16(1)(b) of the Regulations, which has essentially been violated by the Company, as these Investment Properties have been stated at the prevailing market value as on the date of the last revaluation i.e. in 2004. The Company has neither complied with the provisions of Regulation 16(1)(b) of the Regulations nor has it followed the allowed provisions of IAS 40. Moreover, the Company was previously informed vide the Commission's letter dated March 26, 2012 that they have contravened the provisions of the law, which appears to have been casually / unconcernedly taken by the Company.

23. 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 Regulation 16(1)(b) of the Regulations, as aforesaid, therefore, it could be legitimately inferred that the default was committed knowingly and willfully.



Conclusion

24. 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 Regulation 16(1)(b) of the 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.

25. 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

26. In exercise of the power conferred on me under Section 156 of the Ordinance, a fine of Rs. 100,000/- (Rupees One Hundred Thousand Only) is imposed onto the Company based on the following grounds:

- a. that the Company had failed to ensure compliance with the provisions of Regulation 16(1)(b) of the Regulations, by not stating their Investment Properties at cost thereby not following the Cost Model under IAS 40, as required under Regulation 16(1)(b) of the Regulations;
- b. that the Company had taken the Commission's earlier reservations on the same issue casually and unconcernedly, which were communicated to the Company vide the Commission's letter dated March 26, 2012; and
- c. that the impact of the Company treatment regarding its Investment Properties had resulted in the overstatement of the Company's balance sheet footings by an amount of Rs. 8,395,000/-.

27. M/s. The Asian Mutual Insurance Company (Guarantee) Limited is hereby directed to deposit the aforesaid fine of Rs. 100,000/- (Rupees One Hundred Thousand Only) in the designated bank account maintained in the name of Securities and



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Exchange Commission of Pakistan with MCB Bank Limited within thirty (30) days from the receipt of this Order and furnish receipted vouchers issued in the name of Commission for information and record.

28. Moreover, the Company is hereby directed to reverse the treatment and book their Investment Properties using Cost Model under IAS 40, in order to ensure compliance of Regulation 16(1)(b) of the Regulations, failing which a stronger action against the Company and its Directors & Chief Executive Officer shall be taken.

29. This Order is issued without prejudice to any 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