



SECP
INSURANCE DIVISION
Islamabad

Before Hasnat Ahmad, Director (Insurance)

In the matter of

State Life Insurance Company Limited / State Life Insurance Corporation of
Pakistan

Number and date of Show Cause Notice: ID/Enf/StateLife/2016/7198 dated October 26, 2016

Date of Hearing: November 30, 2016

Attended By: **For the Respondent(s):**

1. Mr. Izqar Khan
Executive Director SLIC;
2. Muhammad Rashid
Divisional Head, Finance & Accounts SLIC
3. Mr. Fazal-Ur-Rehman
Divisional Head, Legal Affairs Division, SLIC;
and
4. Mr. Waqas Asad Sheikh
Advocate for the Respondents.

Date of Order: December 28, 2016

ORDER

Show Cause Notice under Section 11(1)(h) and Section 45 read with Section 156 of
the Insurance Ordinance, 2000.

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This Order shall dispose of the proceedings initiated against M/s. State Life Insurance Company Limited or State Life Insurance Corporation of Pakistan ("SLIC") and its Directors, for alleged contravention of Section 11(1)(h) and Section 45 of the Insurance Ordinance, 2000. (the "Ordinance") by the Insurance Division of SECP ("the department"). SLIC, its Directors and/or any of its authorized representatives in the instant matter shall be referred to as (the "Respondents") hereinafter.

Hasnat Ahmad



A. Background

2. SLIC is registered under the Ordinance to carry on the business of life insurance.

3. Examination of the financial statements of SLIC and further information called for by the department in this regard revealed that the statutory Auditors of SLIC in their letter dated May 15, 2016 to the Board of directors of SLIC have highlighted some observations. Moreover the department vide letter dated September 9, 2016 advised SLIC to submit ledger accounts of 500 policy holders of the Pakistan Life Fund. The SLIC in response, provided a list containing names, policy numbers, premium due dates, collection dates and premium amounts in respect of 500 policy holders instead of providing the aforesaid ledger accounts.

4. SLIC's response to the observations was not found satisfactory therefore, Show Cause Notice bearing number ID/Enf/StateLife/2016/7198 dated October 26, 2016 was issued to the Respondents by the undersigned, thereby calling upon them to show cause as to why punitive action may not be taken against them in terms of Section 156 of the Ordinance for the alleged contravention of Section 11(1)(h) and Section 45 of the Ordinance.

5. Section 11(1)(h) of the Ordinance provides that:

"Conditions imposed on registered insurers.- (1) An insurer registered under this Ordinance shall at all times ensure that:

...

(h) the insurer is, and is likely to continue to be, able to comply with such other of the provisions of this Ordinance as are applicable to it."

6. The provisions of Section 45 of the Ordinance state that:

"Books and records. - (1) Every insurer, in respect of all insurance business transacted by him, and in the case of an insurer incorporated in a jurisdiction outside Pakistan in respect of the insurance business transacted by the insurer in Pakistan, shall maintain proper books and records.

(2) Books, accounts and records in respect of insurance business transacted in Pakistan shall be maintained in Pakistan and in either the English or the Urdu language.

(3) For the purposes of this Ordinance, proper books and records shall include without limitation:

(a) a register or record of policies, in which shall be entered, in respect of every policy issued by the insurer, the name and address of the policy holder, the



date when the policy was effected and a record of any transfer, assignment or nomination of which the insurer has notice;

(b) a register or record of claims, in which shall be entered every claim made together with the date of the claim, the name and address of the claimant and the date on which the claim was discharged, or, in the case of a claim which is rejected, the date of rejection and the grounds therefor; and

(c) such other books and records as may from time to time be prescribed.

(4) For the purposes of this Ordinance, the expression "books" includes -

(a) a register;

(b) accounts or accounting records, however compiled, recorded or stored;

(c) a document; and

(d) any other record of information.

(5) A book that is required by this Ordinance or the Companies Ordinance, 1984 to be kept or prepared by an insurer may be kept or prepared:

(a) by making entries in a bound or loose leaf book;

(b) by recording or storing the matters concerned by means of a mechanical, electronic or other device; or

(c) in any other manner approved by the Commission.

Provided that the matters recorded or stored are capable, at any time, of being reproduced in a written form or a reproduction of those matters is kept in a written form approved by the Commission.

(6) An insurer shall take all reasonable precautions, including such precautions, if any, as may be prescribed, for guarding against damage to, destruction of or falsification of or in, and for discovery of falsification of or in, any book or part of a book required to be kept or prepared by an insurer."

7. 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, or any direction made by the Commission, the Commission shall have the power to impose fine on the insurer, 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."

8. Thereafter, Mr. Fazal-Ur-Rehman, Divisional Head, Legal Affairs Division of the SLIC, vide his letter dated November 2, 2016 requested to extend the period to submit reply to the aforesaid Show Cause Notice by ten days. The extension was



allowed till November 15, 2016 as requested by SLIC. Subsequently, in response to the said Show Cause Notice, Mr. Waqas Asad Sheikh, Advocate High Court, M/s. W&A Law Associates, while acting on behalf of the Respondents, provided response to the said Show Cause Notice vide letter dated November 15, 2016, whereby a power of attorney executed by the Respondents in his favor was also enclosed.

9. The reply to the SCN was not found satisfactory however, before proceeding further in the matter it was considered necessary to provide an opportunity of hearing to the Respondents. Hearing in the matter was fixed for November 24, 2016 however, on the request of the Respondents, the hearing was rescheduled on November 30, 2016 at 10:00 a.m.

10. The said hearing was attended by Mr. Izqar Khan, Executive Director of the SLIC, Mr. Fazal-Ur-Rehman, Divisional Head, Legal Affairs Division of the SLIC, Mr. Muhammad Rashid, Divisional Head, Finance & Accounts of the SLIC, and Mr. Waqas Asad Sheikh, Advocate High Court of M/s. W & A Law Associates.

11. Submission of the Respondents both through their reply to SCN and at the time of hearing are summarized as under:

- i. The Respondents denied that any violation of Section 45 of the Ordinance has been committed; The Respondents stated that Policy Status and Collection Slips of the 500 policy holders have already been provided. Therefore, it is not true that legitimate ledger accounts were not being maintained;
- ii. The Respondents submitted that there is no deficiency in the systems and protocol of SLIC and the fraud was engineered with the collusion of the employees and bank staff whereby duplicate files were created with different names and false documents were prepared. The Respondents further submitted that the employees were acting in collusion and they were running a parallel system to perpetrate the fraud. There was no loophole in the system and protocols which were exploited; rather the employees were acting in contravention to the SOPs with criminal intent, hence, they were able to defraud the SLIC. The Respondents stated that some of the amount was recovered. They further reiterated that the matter was referred to National Accountability Bureau (NAB) and accordingly the issue is under their investigation;
- iii. The Respondents stated that SLIC is consistently looking to strengthen procedures and protocols, hence, it is in process of fully implementing ERP based software in order to further upgrade its system and procedures for the purposes of achieving higher levels of efficiency;
- iv. The Respondents stated that the gross difference in General Ledger and Schedules was identified and reduced from Rs. 835.09 million to Rs.



170.94 million having net impact of Rs. 25.257 million, i.e. 79.53% of difference has been reconciled. Working on the remaining un-reconciled balance is under progress and accordingly it would be reflected in SLIC's subsequent financial statements; and

- v. That in regards to the issue pertaining to Pakistan Investment Bond (PIB) portfolio, the Respondents stated that the difference was arisen due to different method used by the auditor and the method used by SLIC. That accounting entry for the same was made and booked due to the reason that it was not clarified which of the calculation methodology was more accurate. The Respondents stated that calculations performed by them were fair and there was no mala-fide intention on part of the Respondents. Therefore, SLIC provided both hard and soft copies of the PIB data to State Bank of Pakistan (SBP) for third party verification and to check in accordance with standard formulas. The findings of SBP will be shared with the Commission as well.

B. Summary of arguments and conclusions in respect of each issue

12. **Provision of Ledger Accounts of the Policyholders:** The Respondents have provided the Policy Status and Collection Slips of 500 policy holders. The Respondents have further submitted that they are strengthening their internal controls and are moving towards implementation of ERP based software system for the purpose of minimizing the risks in future.

13. **Unreconciled Subsidiary Records:** The Respondents are in the process of eliminating unreconciled difference of Rs. 25 million in General Ledger and Schedules. The Respondents argued that the difference is between the General ledger and memorandum record and will have either little or no impact on the financial statements

14. **Fixed Assets Register:** The difference in fixed assets register caused by depreciation has been rectified by the Respondents.

15. **Subsidiary records of held to maturity investments and discrepancies in Pakistan Investment Bonds (PIB) schedule:** The difference between the method used by the SLIC and the auditor is immaterial to the financial statements. The Respondents have sent PIB working to State Bank of Pakistan to verify the calculations and would subsequently adjust the profit accordingly.

C. Overall conclusion

16. 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 the Respondents have provided the Policy Status and Collection Slips of 500 policy holders. Further, the fraud at its Lahore Central Zone, highlighted by the statutory auditors is being

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investigated by NAB, therefore no conclusion can be drawn till investigation is completed in this regard. For rest of the issues, I am of the view that the management of SLIC have not acted in a vigilant and professional manner and have even not given due consideration to the issues highlighted by the statutory auditors of SLIC. However, keeping in view the submission and arguments presented at the hearing I hereby advise SLIC and the Respondents to improve SLIC's governance system by putting in appropriate internal control systems in order to avoid any such lapses in future.

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

Hasnat Ahmad
Director (Insurance)

