



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: June 19, 2014

Date of Hearing: August 25, 2014

Attended By:

1. Mr. Irfan Ilyas, FCA
Partner
Ilyas Saeed & Co.
2. Mr. A. Rashid Mirza
Chief Executive Officer
The Asian Mutual Insurance Co. (Gte) Limited
3. Mr. Zafar Iqbal
Chief Financial Officer
The Asian Mutual Insurance Co. (Gte) Limited
4. Mr. Mubashir Raza
Ilyas Saeed & Co.

Date of Order: December 19, 2014

ORDER

(Under Section 158 of the Insurance Ordinance, 2000)

.....

This Order shall dispose of the proceedings initiated against M/s The Asian Mutual Insurance Company (Guarantee) Limited ("the Company") and its Directors under Section 158 of the Insurance Ordinance, 2000 (the "Ordinance") for making material misstatements in the Annual Audited Accounts of the Company for the year ended December 31, 2011 (the "Accounts").

SECURITIES & EXCHANGE
COMMISSION OF PAKISTAN

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Background Facts

2. An Onsite Inspection of the Company was conducted on the order of the Commissioner - Insurance dated February 1, 2013, under Section 59A of the Ordinance.

3. Note 6.2 to the Accounts states that:

"The company operates an un-funded retirement gratuity scheme. Gratuity is accounted for as and when paid. The requirement of IAS19, employee's benefits (revised 1998) has been partially complied with."

Inspection team inquired the Company about the gratuity scheme but the team was informed that the Company is not operating any employment benefit scheme so there is no data available in this regard.

4. It was also observed during the course of the Onsite Inspection that the Company pays 16% Federal Excise Duty (FED) and 1% Federal Insurance Fee (FIF) on the amount recorded as premium written and the balance after these deductions is considered as the Net Premium. After that the Company deducts 15% as commission to the agents and the remaining amount is recorded in the financial statements as 'Branch Balances'. The Company does not give commissions to its agents through cross cheque rather the Company adjusts the amount of commission from the balance receivables from its agents.

The Company issues the blank policy documents i.e. passenger guarantee & third party risk to its Agents on the agreed price (price is verbally negotiated between agents and the Company for which there is no written and proper record available in the Company). There is no uniformity in amount charged by the Company to its agents; it varies from agent to agent and city to city as appears in the incomplete premium register of the Company. Agents sell these policies at whatever price they want, and the Company is totally unaware of the actual price these Agents charge from the policyholders.

After issuing the policies, agents send the carbon copies of the issued policies (passenger guarantee only) back to the Company. It is pertinent to mention here that amount of premium received from the customer is not written on policy documents. The Company after receiving these documents from agents counts the policies, and charged a verbal pre- decided amount as premium against each document without knowing the exact amount charged by the agents against each policy. The total of those amounts is considered as the premium written by the Company. Then the Company pays 16% FED and 1% FIF on that amount and the balance is considered as the Net Premium.



Thereafter, the Company deducts / adjust 15% as commission to the agents and the remaining amount is recorded in the financial statements as 'Branch Balances'. Therefore, the Company does not give commissions to its agents through cross cheques rather the Company adjusts the amount of commission from the receivables from its agents.

It is also worth mentioning here that the Company pays 10% withholding tax on the amount paid as commissions from its own sources and do not receive that amount of tax from its agents.

5. In view of the above, it appeared to the Commission that the premium written on the face of the financial statements of the Company is misstated. Since, the actual amount of premium underwritten is not reported, and since the levies are paid out on the basis of the estimated premium, therefore, the overall authenticity of the financial statements is at stake, which is material and appeared to be willful, all at the same time.

6. Furthermore, while reviewing the ownership of the assets of the Company, copy of the registration documents of the Company's Motor cycle (Registered No. LZA-4851) revealed that the motor cycle was registered in the name of an employee of the Company. Therefore the Company's asset was not registered in the name of the Company. The Company has boldly misstated its assets by giving an impression that the said Motor cycle was registered in the name of the Company.

7. Hence, it appeared to the Commission that the Company has made material misstatements in the Accounts for which the Commission could take action as provided under Section 158 of the Ordinance.

Show Cause Notice

8. Accordingly, the Show Cause Notice was issued on June 19, 2014 under Section 158 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 158 of the Ordinance, should not be imposed upon the Company and/or its Directors and the Chief Executive Officer for making material misstatements in the Accounts as aforesaid.

Company's Response to the Show Cause Notice

9. In response to the said Show Cause Notice, the Company, vide their letter no. AM-05/14/147 dated July 26, 2014, stated that:



"...

1. Employee Benefit

The Company had all along the policy of recognizing employee retirement benefit (Gratuity) on payment basis, as and when it is actually been made. The Company had been applying its accounting policy consistently over past many years.

The staff inadvertently communicated to the inspection team that no data for employee benefit scheme maintained. In fact no employee was eligible for gratuity as on December 31, 2011. All the permanent employees of the Company had left before December 31, 2011 and there were no permanent employees of the Company as on December 31, 2011. The Company only have 4 support staff and all are on yearly contract basis. Therefore, no data for gratuity was separately available.

Without prejudice to the foregoing, it is stated that even if gratuity is being charged as expense on accrual basis, it will not make any effect on Balance Sheet footing, neither it will hamper any rights of any member of the Company, not it will make any difference to the state (Exchequer).

We assure you of our compliance of Regulation 13(1) of the Regulations in our financial statements for the accounting period December 31, 2014.

2. Payment / Adjustment of Commission

The policy price is always variable depending on the competition with the competitors and volume of business generated by the agents. However, it is assured that the premium issued against insurance policy is totally recorded in the books of accounts of the Company. In no case, the company is unaware of its policy and premium price, since the policy is only registered when it is recorded in the books of accounts of the Company.

For commercial expediency and under the norms of business, the agents deduct their due share of commission, after tax, from the balance to be remitted to the Company, instead of transferring all the balance first to the Company and then Company issuing cheques of commission to the agents.

Payment of commission is paid / adjusted to agents by way of adjustment. Withholding tax applicable on commission is duly received from agents in their adjusting balances and is paid to the Exchequer.

You have been kind to observe the fact that the Company pays withholding tax on commission from its own sources. Being withholding agent, it is the obligation of the Company to discharge its responsibility to deduct and deposit withholding tax.

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However, the same is duly adjusted / credited to the accounts of agents as and when commission adjustment is made.

It is categorically stated that there is no lapse in compliance with tax law under withholding tax on commission.

3. Premium Written

It is humbly submitted that the amount of premium written on the face of the financial statement show a true and fair picture of the revenue earned. The same can be verified from difference sources, as follows;

- a. FED returns,
- b. FIF returns,
- c. Commission to the agents
- d. Re-insurance Premium Ceded Statements.

It is reiterated that the insurance policy is only got registered with the Company when its particulars are full in all respect, including premium. No policy can be registered with the Company with open or on estimated amount of premium.

All government dues are dependent on the premium amount as above and Company discharges its legal obligations in true letter and spirit. On mere preemptions, it may not be imposed on the Company that the financial statements are at stake willfully. The Company complies with all the requirements of Insurance Ordinance, Companies Ordinance and other regulatory laws in doing business and reports each and every transaction truthfully in the financial statements are true in all material respects.

4. Fixed Assets

It is humbly submitted that the ownership of the motor bike (LZA-4851) was registered in the name of the employee, rather than in the name of the Company for commercial expediency. Under taking from the employee was duly obtained in this regard.

The asset has been disposed off during the financial year 2013 and the disposal proceeds have been recorded in the accounts of the Company. The asset belonged to the Company and its disposal proceeds were returned in the Company.

However, we assure you of full compliance of provision of law in future.

We sincerely hope that you will please find the above said explanations to your entire satisfaction. There is no no misstatement in the reports made by the Company. Penalty proceedings are criminal proceedings in nature for which mens

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*rea and actus rea are the condition precedent. In this case, mens rea (intentions) were never involved to gain any benefit. As a general rule, criminal liability does not attached to a person who merely acted with the absence of mental fault.
..."*

10. The response of the Company reveals the following:

a. Employee Benefit

The staff of the Company, liaising with the Onsite Inspection Team, miscommunicated that there was no data for employee benefit scheme. And, no employee of the Company is entitled to the Company's gratuity scheme, as all employees are contractual ones.

b. Payment / Adjustment of Commission

The Company has admitted that the policy price is variable depending on the competition with the competitors and the volume of business generated by the agents. It was further stated that the premium is fully recorded in the books of accounts of the Company, and that the Company is fully aware of whatever price is being charged on each individual policy.

Moreover, the Company has also admitted that the agents deduct their commissions after tax and the remaining amount is passed onto the Company. Resultantly, the provisions of Section 99(4) of the Ordinance get violated. Over and above the violation of the said provisions of the law, the Company has no control over the agents that the amount of premium disclosed by those agents and the commissions deducted thereon are true as those have been so disclosed. The agents can, at any time, charge more premiums from the policyholders than actually disclosed by them. Under this arrangement, the Company is, by all means, bound to rely on the premiums reported / disclosed by its agents.

c. Premium Written

The Company has offered the Commission to verify the amount of premium from such sources / documents which have been reported / produced by the Company itself. The Commission, at this stage, has not raised any objection on whether the levies or other liabilities have been paid off on the basis of the reported premium, or not. In fact, the Commission has raised its concerns over the recording and reporting of the premium in its books of accounts.

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The Company states that an insurance policy is registered when and only when all its requirements are complete. However, the procedure and reliability of the reported premiums has been deliberated in the preceding part of this Order.

d. Fixed Assets

The Company has admitted that the motor bike (LZA-4851) was registered in the name of the employee of the Company thereby the violation of Section 39 of the Ordinance is quite evident. However, the said bike has been sold out in the year 2013, and the sale proceed has been recognized by the Company.

In the light of the above, it is quite evident that the Company, by virtue of the title of the said bike, could not have recognized it on the face of the balance sheet of the Company.

Hearing of the Case & Subsequent Developments

11. Although, the Company had not requested for hearing in the matter vide his letter dated July 26, 2014, the Commission, on its own motion, had scheduled the hearing in the matter for August 25, 2014 at 12:30 p.m., which was communicated to the Company via the Commission's hearing notices no. ID/ENF/AMICL/2014/20407 dated August 8, 2014.

12. The hearing of August 25, 2014 was attended by the following persons:

1. Mr. Irfan Ilyas of M/s Ilyas Saeed & Co., Chartered Accountants;
2. Mr. A. Rashid Mirza, Chief Executive of the Company;
3. Mr. Zafar Iqbal, Chief Financial Officer; and
4. Mr. Mubashir Raza of M/s Ilyas Saeed & Co., Chartered Accountants

13. However, right at the start of the said hearing, Power of Attorney in favor of M/s Ilyas Saeed & Co., Chartered Accountants was handed in, and hence, the representatives from M/s Ilyas Saeed & Co. will be referred to as the "Company's Representatives" hereinafter.

14. Brief proceedings of the hearing of August 25, 2014 are as follows:

- a. The Company's representatives stated that the gratuity is offered to the permanent employees of the Company, and that the Company does not have any permanent employee since after 2011. In this regard, copies of the service documents of the Company's contractual employees were provided;



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Insurance Division

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- b. The Company's representatives stated that the policy price has been variable depending on the competition with the competitors and the volume of business generated by each agent. It was further stated that the premium is fully recorded in the books of accounts of the Company, and that the Company is fully aware of whatever price is being charged on each individual policy;
- c. Moreover, the Company's representatives also admitted that the agents deduct their share of the commissions after tax and the remaining amount is passed onto the Company. Thereupon, the attention of the Company's representatives was drawn towards the provisions of Section 99(4) of the Ordinance, the violation of which was admitted by the Company's representatives;
- d. It was further clarified to the Company's representatives that by this arrangement of disclosure of premium by the agents, the Company loses the control over reliability and authenticity of the amount of premium disclosed by those agents. The agents can, at any time, charge more premiums from the policyholders than actually disclosed by them to the Company. Under this arrangement, the Company is, by all means, bound to rely on the premiums reported / disclosed by its agents;
- e. The Company's representatives further mentioned that the Company, being the withholding tax agent, adjusts withholding tax on the commissions from the balance payable to each agent. Later on, the amount of that tax is deposited in the Federal Exchequer. In this regard, the Company's withholding tax payments / returns were provided;
- f. On account of the recording of the motor bike (LZA-4851), the Company's representative submitted that in order to commercially tackle the provisions of the law that relates to the traffic rules, the Company had registered the bike in the name of one of its employees, named Mr. Zafar Iqbal Shaheen, from which an undertaking was obtained wherein Mr. Zafar had undertaken that he had no claim over the said bike and that this bike belonged to the Company. Copies of the title of the said bike were provided;
- g. Lastly, the Company's Representatives, while submitting that the mala fide on part of the Company cannot be attached in the instant case, requested the Commission to take a lenient view in the instant matter.

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Consideration of Company's Submissions

15. I have carefully examined and given due consideration to the written and verbal submissions of the Company (through the Company's Representatives, M/s Ilyas Saeed & Co., Chartered Accountants), and have also referred to the provisions of the Ordinance and the findings of the Onsite Inspection as laid down in the Onsite Inspection Report. I am of the view that there have been various misstatements in the books of accounts of the Company, which were made knowingly and deliberately.

16. 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 true and fair reporting of the material facts in the Company's accounts, therefore, it could be legitimately inferred that the default was committed knowingly and willfully.

Conclusion

17. After carefully examining the arguments and studying the facts and findings of the case as mentioned in the above paras of this Order, various material misstatements have been established. Therefore, the penalty as provided under Section 158 of the Ordinance can be imposed onto the Company and/or its Directors.

18. Section 158 of the Ordinance states that:

"Penalty for false statement in document.- Except as otherwise provided in this Ordinance, 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, wilfully 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."

Order

19. In exercise of the power conferred on me under Section 158 of the Ordinance, a fine of Rs. 100,000/- (Rupees One Hundred Thousand only) is imposed onto the Company based on the grounds as stipulated in the above paras hereof.

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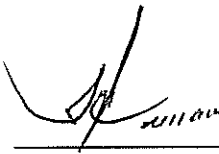


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20. M/s. The Asian Mutual Insurance Company (Guarantee) Limited is hereby directed to deposit the aforesaid fine of Rs. 100,000/- (Rupees One Hundred Thousand only) in the designated bank account maintained in the name of Securities and Exchange Commission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

21. 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.


19/12/14
Tariq Hussain
Director