



Securities and Exchange Commission of Pakistan

BEFORE THE APPELLATE BENCH

In the matter of

Appeal No. 122 of 2021

Ilyas Saeed & Co. Chartered Accountants

..... Appellant

versus

Director/HOD, Adjudication Department-I, Adjudication Division, Securities and Exchange Commission of Pakistan

..... Respondent

Date of hearing:

November 1, 2024

Present:

For the Appellant:

1. Mr. Imran Ilyas FCA, Managing Partner
2. Mr. Usman Mansha (Associate Trainee)

For the Respondent:

1. Mr. Shafique Ur Rehman, Additional Joint Director, Adjudication-I

ORDER

1. This Order shall dispose of Appeal No. 122 of 2021 filed by M/s. Ilyas Saeed & Co. Chartered Accountants (the Appellant) against the Order dated July 26, 2021 (the Impugned Order) passed by the Head of Department, Adjudication Department-I, Adjudication Division, SECP (the Respondent) under Section 260(1) of the Companies Ordinance 1984 (the Ordinance) on account of the defaults of Section 255 of the Ordinance and Section 48(4) of the Insurance Ordinance, 2000 (the Insurance Ordinance).



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2. The brief facts of the appeal are that the Appellant was appointed as the statutory auditor of SPI Insurance Company Limited (the Company) for the audit of its annual accounts for the year ended December 31, 2016 (FY2016). An onsite inspection of the Company was conducted by the inspection team of the Securities and Exchange Commission of Pakistan (the Commission) under Section 59A of the Insurance Ordinance in pursuance of the inspection order dated July 5, 2017. During the course of inspection, various instances were noted where the Auditors, *prima facie*, had failed to discharge their duties, obligations and responsibilities as envisaged under section 255(3) of the Ordinance and Section 48(4) of the Insurance Ordinance. The inspection team observed that the Auditors failed to identify and report that the Company had overstated its premium revenue and understated its claims expense, resulting in overstatement of underwriting results and net profit.
3. In light of the aforementioned violations of the requirements of the Ordinance, a Show-Cause Notice (the SCN) dated June 22, 2020 was issued to the Appellant, requiring the Appellant to explain its stance. Subsequently, the Appellant submitted its written response to the SCN vide its letter dated April 05, 2021. Hearing in the matter was held on April 09, 2021 which was attended by the authorized representatives of the Appellant, and after hearing the Appellant, the Respondent in exercise of powers delegated, was of the considered view that non-compliance with the requirements of Section 255 of the Ordinance and Section 48(4) of the Insurance Ordinance were established and therefore a penalty of (Rs. 100,000/-) Rupees One Hundred Thousand was imposed under Section 260(1) of the Ordinance through the Impugned Order.
4. The Appellant has challenged the Impugned Order *inter alia* on the grounds that the penalty has been imposed without justifying the fundamentals for imposition of penalty as there was no willful default on part of the Appellant. The Authorized representative of the Appellant before delving into the arguments of the appeal stated that the engagement partner of the Appellant firm at the time of the audit of the Company has passed away in September, 2021 which is two months after the impugned order was passed, therefore, the Bench may condone the penalty imposed upon the Appellant.



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5. The Bench inquired from the Respondent that whether the order been passed against the Appellant or against the engagement partner of the firm to which the Respondent replied that the order has been passed against the Appellant firm. Upon confirmation, the Bench directed the Authorized representative to conclude the arguments of the Appeal on merits as the Bench will pass an order based on the merits of the Appeal.
6. The Appellant submitted that the Audit is done on a sample basis and during the course of audit, the Appellant concluded that there were ample internal controls over the selected sample of population for the purpose of obtaining audit evidence and that it is merely a coincidence that nothing came to the Appellant's attention from the selected sample which could cause the Appellant to believe that there were 962 policies not pertaining to the year under audit. The Appellant further stated that the Respondent has charged the whole amount of premium received on account of self-owned assets/self-insurance without considering the reversal, merits and allowability of the same. The Appellant further argued that the Respondent has ignored the fundamentals of audit and that the audit is conducted on a 'test/check' basis and did not consider the fact that the Code of Corporate Governance (the Code) was implemented for the first time near the close of the end of the financial year and the company was given a grace period to comply with the requirements of the code and that the Respondent did not consider the fact that there was nothing material which needed to be reported as non-compliance with the Code of Corporate Governance. The Appellant further stated that during the course of audit it was concluded that the internal controls over the selected sample were satisfactory and thus the Appellant selected a small sample of population for the purpose of obtaining audit evidence and it was merely a coincidence that from the selected sample, nothing came to the Appellant's attention which could cause the Appellant to believe that there were certain policies not pertaining to the year under audit and it was also submitted that the 962 policies not pertaining to year under audit, only comes to a fraction part i.e 1.5% of the overall number of policies undertaken by the Company. The Appellant further argued that during the course of audit, a few policies were identified which pertained to self-owned assets of the company but on pointing out the error, all such policies were subsequently cancelled by the management of the Company. The third submission by the Appellant was that it did



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not observe any material inconsistency in adoption and application of accounting policy consistently applied by the management in the financial statements for claim liabilities and that there always remains an uncertainty in making the provision for outstanding claims due to the inherent limitations and that the risks associated with the insurance contracts are complex and subject to a number of variables which complicate quantitative sensitivity analysis. The Appellant while concluding the arguments, prayed for a lenient decision by the Bench as the defaults committed by the Appellant were not willful and that nothing in the sample of the accounts came to the knowledge of the Appellant which was required to be rectified.

7. The Respondent rebutted the grounds of appeal and stated that the Appellant being the statutory auditors of the Company were under an obligation to carry out the audit vigilantly and with maximum accuracy and that despite the material mis-statements in the annual accounts of the company for FY2016, the Appellant failed to discharge their duties as envisaged under section 255(3) of the Ordinance read with section 48(4) of the Insurance Ordinance and issued an unqualified audit report on the financial statements FY2016. The Respondent referred to Section 2 (xxvii) of the Insurance Ordinance and stated that self-insurance of assets is not permitted or recognized under the definition of insurance in the Insurance Ordinance. The Respondent further argued that the Appellant has failed to bring on record the liability adequacy test carried out by the Appellant, therefore, the discrepancies as highlighted by the Commission should be accepted and admitted. The Respondent further stated that with regard to the issue of self-insurance, whereby the Company recorded gross premium by issuing policies to itself pertaining to motor and miscellaneous class, the Appellant has admitted that the company insured its own assets but stated that the amount of gross premium in respect of 131 motor vehicle policies was only Rs. 1,703,546/-. The Respondent argued that the Appellant failed to give any clarification on self-insurance policies pertaining to miscellaneous class of business as the inspection team noted 178 self-insurance policies with an aggregate premium of Rs. 17,894,433/- for FY2016, which pertain to motor and also miscellaneous business of the Company. The Respondent stated that it is an admitted fact that the company has been engaged in self-insurance business in violation of Section 2 (xxvi) of



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the Insurance Ordinance but the Auditors did not consider to issue a modified auditors' report on the accounts of the Company for FY2016 and treated the violation as merely an "error". The Respondent further argued that it is also an established fact that all 962 policies, which were not underwritten in FY2016 but their premium was accounted for in FY2016, escaped the audit sample selected by the Auditor/Appellant. Regarding one of a policy with a premium amount of Rs. 7.785 million, the Appellant in its reply dated April 29, 2021 stated that "the said policy was being shown in the list of 'total premiums received during the year' as the same was received during the FY2016. The aforementioned fact was contested by the Respondent, as the Respondent stated that as per record, a cheque dated January 10, 2017 amounting to Rs. 3.932 million in lieu of premium was received by the company from the policy holder, which was cleared on January 13, 2017, as per copy of the bank statement of the Company. The Respondent further submitted that an aggregate premium of Rs. 10.415 million pertaining to policies written in the succeeding FYs 2017, 2018, 2019 and 2020 was also accounted for in FY2016 and despite the manipulation of 'Gross Premium' in the financial statements of the Company for FY2016, the Appellant failed to point out the discrepancies and an audit report was issued.


8. The Appellate Bench (the Bench) has heard the parties and perused the record including the grounds of Appeal and Respondents' written comments. The Bench is of the view that statutory auditors have a fiduciary duty towards the stakeholders of a company and that an audit report also helps the regulator to carry out its oversight of the affairs of a company. Firstly, the Bench finds it paradoxical to know that all 962 policies not pertaining to the FY2016 escaped the sample selected by the Appellant, as the Appellant should have applied professional diligence in formulating the sampling criteria and the assessment of reliance on selected sample for obtaining audit evidence. From the arguments put forth by the parties, the Bench is of the view that the Appellant failed to highlight the non-compliances of the Company with the Code as the non-compliances, as highlighted by the inspection team, were significant in nature and should have been pointed out and conveyed by the Appellant to the Company. To the extent of self-insurance of vehicles, it has been conceded by the Appellant that the issue was pointed



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out and informed to the Company which was subsequently resolved. To the extent of the 962 policies which were not underwritten in the FY2016 but their premium was accounted for in the FY2016, the Bench has observed that Appellant has failed to discharge their duty with regard to accurately reflecting the books and records of the Company in the auditor's report, therefore not carrying out their professional duties in a diligent, transparent and professional manner.

9. Furthermore, the Bench has noted that the Appellant has not presented any evidence as to how the liability and adequacy test was carried out by the Appellant, therefore, the Bench endorses the liability adequacy test and its findings as carried out by the Respondent. The Bench expects statutory auditors to be more vigilant while carrying out the statutory audit of a company and in view of the above-mentioned facts it is established that the Appellant has failed to comply with the requirements of the duty of auditors as laid down under the Insurance Ordinance as it is clear that the Appellant did not adopt an attitude of professional skepticism, regardless of the prior experience and internal controls of the Company.
10. Hence, in view of the forgoing, the Bench finds no reason to interfere with the merits of the Impugned Order, therefore, we hereby dismiss this appeal without any order as to cost.



(Akif Saeed)

Chairman/Commissioner



(Abdul Rehman Warraich)
Commissioner

Announced on:

04 MAR 2025