

Securities and Exchange Commission of Pakistan

BEFORE THE APPELLATE BENCH

In the matter of

Appeal No. 76 of 2020

PICIC Insurance Ltd

...Appellant

Versus

Securities and Exchange Commission of Pakistan

...Respondent

Date of Hearing: 17/12/20

Present:

For the Appellant (via Zoom video conferencing):

Mr. Adam Malik, AHM & Co. (Counsel)

For the Respondent (via Zoom video conferencing):

Mr. Shafiq-ur-Rehman, Additional Joint Director (Adjudication-1)

ORDER

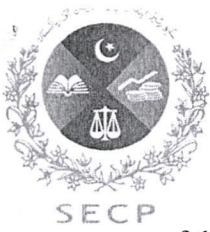
1. This Order is passed in the matter of Appeal No.76 of 2020 filed under section 33 of the Securities and Exchange Commission of Pakistan Commission Act, 1997 against the order dated 08/07/20 (the Impugned Order) passed by Director (Adjudication-1) of the Securities and Exchange Commission of Pakistan (the Respondent).
2. The brief facts of the case are that on examination of the Annual Audited Accounts of PICIC Insurance Ltd., (the Appellant) for the year ended 31/12/17, it was observed that the Appellant transferred all its insurance related assets and liabilities to Crescent Star Insurance Limited (the CSIL) without obtaining prior approval of the Securities and Exchange Commission of Pakistan (the Commission) in terms of section 67 of the Insurance Ordinance, 2000 (the Ordinance). Section 67 of the Insurance Ordinance requires that any proposed transaction in the case of a non-life insurer, if the whole or any part exceeding ten percent of the business located in Pakistan of an insurer shall not proceed unless, upon an application by the transferor, approval is accorded by the Commission. In this regard, the Appellant was advised vide letter dated 30/07/18 to provide the balances of assets



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and liabilities transferred to CSIL duly certified by the statutory auditor along with the reason for not obtaining approval from the Commission under section 67 of the Ordinance and date of the proposed transaction. In response the Company vide letter dated 26/11/18 submitted the calculations of assets and liabilities transferred to CSIL, certified by the auditor and stated that, “... *Section 67 relates to transfer of shares by seller in this case there is no sale purchase or transfer of shares and as such section 67 is not applicable. Transaction Date June 30, 2017....*”. As per the reply of the Appellant regarding transfer of assets and liabilities to CSIL, the value of transferred assets stood at Rs 196.452 million (73% of total assets) and value of transferred liabilities stood at Rs 266.192 million (approx. 100% of total liabilities) as on 30/06/17. In view of the above, it was observed that the Appellant, *prima facie*, did not meet the mandatory requirements of section 67 of the Ordinance.

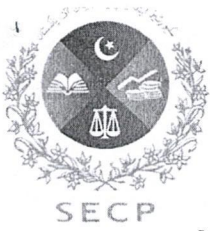
3. The Show Cause Notice dated 20/12/18 (the SCN) was issued to the Appellant and its board of directors calling upon them to show cause as to why the fine as provided under section 156 of the Ordinance may not be imposed on them for the alleged contravention of the law. In response to the SCN, the Counsel for the Appellant (M/s. AHM & Co.) and its Board of Directors submitted their reply vide letter dated 14/02/20 and hearing in the matter was held on 26/02/20 which was attended by Mr. Adam Hassan Malik as their Authorised Representative (the Authorised Representative). During the hearing the Authorised Representative reiterated the written submissions made by the Appellant. The Authorised Representative was of the view that section 67 of the Ordinance does not apply in the instant matter as transfer of assets and liabilities was done without a consideration in monetary terms. It was further submitted by the Authorised Representative that the Appellant transferred its assets and liabilities to CSIL as per the requirements of section 9(3) of the Ordinance in order to seek the revocation of its insurance license and that prior approval of the Commission was not required in respect of the proposed transaction.
4. The Respondent, after carefully examining and giving due consideration to the written/verbal submissions of the Appellants, took the view that the response of the Insurance Division confirms the fact that the insurance related assets and liabilities transferred to CSIL are not reflected in the annual audited accounts CSIL for the year ended 31/12/18. The Insurance Division had also apprised that subsequent to the decision of the Insurance Division on the previous application filed under section 9 of the Ordinance, no fresh application seeking revocation of license of the Appellant was filed. In view of the aforesaid, the violation of section 67 of the Ordinance was clearly established for which the Appellant and its Board of Directors are liable to be penalized in terms of section 156



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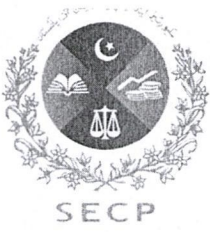
of the Ordinance. In exercise of the powers conferred under section 156 of the Ordinance, a penalty of Rs. 300,000 was imposed on the Appellant for transfer of its insurance assets and liabilities without requisite mandatory approval. It may be noted that the imposition of penalty should not be construed as regularization of the transaction or a *de facto* approval of the transfer of insurance and its liabilities. Furthermore, the Board of Directors of the Appellant was warned to ensure meticulous compliance with the provisions of section 67 of the Ordinance. Furthermore, the Respondent observed that the circumstances of the transfer were rather peculiar, the fate of the policyholders is unclear and they appear to be at risk of loss. Under these circumstances, the matter needed to be investigated closely in order to protect the interest of policyholders, claimant and shareholders. Therefore, the matter was referred to the Supervision Department of Insurance Division by the Respondent for complete investigation of the transaction of transfer of insurance assets and liabilities encompassing its entirety i.e. from the aspect of the transferor and the transferee.

5. The Appellant preferred the instant appeal *inter alia* on the following grounds:
- a) The Impugned Order is based on a faulty interpretation of section 67(1) of the Ordinance. The Respondent ignored the fact that transfer of liabilities by the Appellant to CSIL cannot be classified as an acquisition. In corporate and legal context, for something to be classified as an acquisition requires one entity/individual to buy majority interest in another entity. In absence of any consideration from CSIL, the basic ingredient of acquisition, transfer of liabilities and assets to CSIL by the Appellant cannot be classified as an acquisition, therefore, provisions of section 67(1) of the Ordinance are not attracted.
 - b) Section 67(1) of the Ordinance is applicable in cases where there is acquisition of the business as a non-life insurer and business is measured by either the premium income or the sum of the liabilities for unearned premium and outstanding claims. The Appellant stopped underwriting any new business well before the application for revocation of license and at the time of transfer of liabilities and assets to CSIL, the Appellant had no business which could be measured in accordance with the terms of section 67(1) of the Ordinance and at that instance, the Appellant just had insurance liabilities.
 - c) The Respondent ignored the fact that transfer of liabilities and assets to CSIL is in accordance with the requirements of section 9(3) of the Ordinance, which require an insurer to make adequate arrangements to irrevocably transfer the liabilities to another registered insurer prior to the revocation of the license. In the instant case, CSIL was transferred the Appellant's liabilities and assets followed those liabilities, enabling CSIL to meet with the Appellant's liabilities in future.



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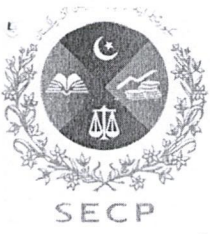
- Moreover, it is obvious from the Ordinance that the legislative intent was not to make provision of section 9(3) of the Ordinance subject to the provisions of section 67 of the Ordinance.
- d) Transfer of liabilities and assets to CSIL is made in accordance with the terms of Scheme of Arrangement agreed with Crescent Star Foods (Pvt.) Ltd (the CSF), a subsidiary of CSIL. Accordingly, in case of merger, the provisions which are related to acquisition are not applicable. Furthermore, even the Commission in its reply in Suit No. 716 of 2018 before the Honourable Sindh High Court (the Honourable High Court) acknowledged that the proposed transaction between the Appellant and CSF is a merger/amalgamation. Moreover, for there to be an acquisition for the purposes of section 67(1) of the Ordinance, CSIL must provide consideration as it is the entity to whom liabilities and assets are transferred. However, in the present case, assets were transferred merely to enable CSIL to meet with the insurance liabilities of the Appellant.
- e) The Respondent's stance that section 67(1) of the Ordinance is applicable on the transaction pertaining to Appellant's transfer of liabilities and assets to CSIL so that the interests of policy holders and shareholders could be protected is not sustainable. The liabilities in the instant case were being transferred to CSIL in accordance with section 9(3) of the Ordinance and the Appellant as an insurance company was under an obligation to satisfy the Commission that liabilities are transferred irrevocably to a registered insurer, therefore, the interests of policy holders is protected under the provisions of section 9(3) of the Ordinance.
- f) The Respondent ignored the auditors' report furnished to the Commission certifying transfer of liabilities and assets to CSIL. Therefore, the Respondent has ignored the credible piece of information issued by an approved auditor presented before it.
- g) The Respondent ignored the pendency of Suit No. 716 of 2018, whereas, the Commission's decision not to revoke the Appellant's license has been challenged before the Honourable High Court. Therefore, while proceedings are pending before a higher forum, the Appellant was not required to make a fresh application for revocation of license.
6. The Respondent rebutted the arguments of the Appellant on the following grounds:
- a) Section 67 of the Ordinance requires that any proposed transaction in the case of a non-life insurer, of the whole or any part exceeding 10% of the business of an insurer shall not proceed unless, upon an application by the transferor, the approval is accorded by the Commission. As per the calculations of assets and liabilities transferred to CSIL on 30/06/17, submitted by the Appellant, the value of transferred assets stood at Rs 196.452 million which is 73% of total assets



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and value of transferred liabilities stood at Rs 266.192 million which is almost 100% of total liabilities. Therefore, almost entire business of the Appellant was actually transferred to CSIL but the Appellant did not seek approval of the Commission on the pretext that it was not acquisition which is against the facts of the case. Therefore, the Appellant has attempted to circumvent the applicable provisions of section 67 of the Ordinance by denying the fact that the transfer of its almost 73% assets and 100% liabilities constitutes transfer of more than 10% business for which the Appellant was under statutory obligation to seek the prior approval of the Commission.

- b) Section 9(3) of the Ordinance requires that, *“Registration under this Ordinance to carry on insurance business shall not be revoked unless the Commission is satisfied that adequate provision has been made for the irrevocable transfer to a registered insurer of all insurance liabilities incurred by the insurer seeking revocation of registration under the preceding subsection.”* An insurance company acts as a fiduciary and holds the premium of policyholders in trust. The aforesaid mandatory requirement of the law aims to ensure and safeguard the policyholder’s interest, therefore, while approving the transfer, the Commission evaluates the capacity of the transferee to handle the business to be transferred. However, after considering the facts and circumstances of the case, the Commission being not satisfied, did not accord the approval for revocation of registration of the Company. Therefore, the Company was advised to comply with section 9(3) of the Ordinance.
- c) The Appellant’s argument that Section 67 of the Ordinance does not apply due to absence of consideration in monetary terms is not plausible because it is not merely transfer of liabilities of the Appellant but the Appellant’s assets amounting to Rs 196.452 million were also transferred to CSIL, which as a matter of fact does serve as a consideration in the transaction.
- d) The intention and spirit of section 67 of the Ordinance is to protect the interests of policyholders and shareholders of the Appellant, when a transaction involving more than 10% transfer of insurance business from one party to another is under contemplation. Moreover, section 67 of the Ordinance in respect of prior approval of the Commission addresses the concerns of policyholders and shareholders so that any undue advantage may not be secured by any party to the transaction which would be detrimental to the interests of shareholders or policyholders or claimants.
- e) The auditors’ report was examined in light of the applicable provisions of the law but the Commission, being not satisfied with the facts and circumstances of the case, did not accord the approval in the larger interest of policyholders and shareholders. Without prejudice to the merger

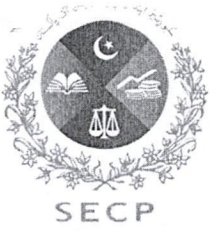


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application pending before the Honourable High Court, the Appellant was required to comply with the provisions of section 67 of the Ordinance.

- f) The Impugned Order is based on established facts and applicable provisions of the law. Furthermore, the response of the Insurance Division confirms the fact that the insurance related assets and liabilities allegedly transferred to CSIL were not reflected in the annual audited accounts of CSIL for the year ended 31/12/18. Under these circumstances, in addition to imposition of penalty, the matter needed investigation closely in order to protect the interest of policyholders, claimant and shareholders. Therefore, the matter was also referred vide the Impugned Order to the Supervision Department of Insurance Division for complete investigation of the transaction of transfer of insurance assets and liabilities. As per the latest update received from the Insurance Division, it had issued an investigation order dated 14/09/20 in the matter of the Appellant in pursuance of the Impugned Order but the proceedings could not be commenced as appeal against the Impugned Order was pending adjudication before the Appellate Bench.

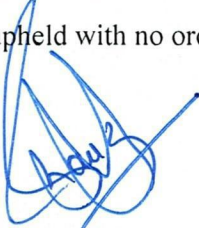
7. We have heard the parties i.e. the Appellant and the Respondent. The Appellant should have applied for approval from the Commission in terms of section 67 of the Ordinance which states that any proposed transaction in the case of a non-life insurer, of the whole or any part exceeding ten percent of the business located in Pakistan of an insurer shall not proceed unless, upon an application by the transferor, approval is accorded by the Commission. In the instant case, transfer of almost 73% of the assets and 100% liabilities constitutes transfer of more than 10% business for which the Appellant was under an obligation to seek prior approval of the Commission. The Appellant's argument that the transfer was not an acquisition in the absence of consideration by CSIL is without any merit as the Respondent is referring to that part of section 67 of the Ordinance which states that any proposed transaction in case of a non-life insurer, whereby, more than 10% of the business was being transferred meant that prior approval was necessary from the Commission. Furthermore, the Appellant's argument that in terms of section 67 of the Ordinance business is measured by either the premium income or the sum of the liabilities for unearned premium and outstanding claims is also without any merit as once all the liabilities were being transferred to CSIL by the Appellant, it would constitute more than 10% of the business and, therefore, prior approval from the Commission was necessary. Furthermore, it was important to protect the interests of policyholders and shareholders of the Appellant and direction by the Respondent for investigation was necessary as assets and liabilities allegedly transferred to CSIL were not reflected in the Annual Audited Accounts of CSIL for the year ended 31/12/18. Furthermore, even if the Appellant contends that the transfer of assets and liabilities to CSIL was made to comply with the



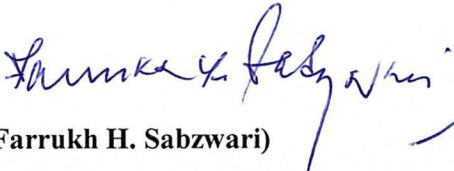
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terms of section 9(3) of the Ordinance, the said application for revocation of license had never been approved by the Commission, therefore, transfer could not take place without first seeking the Commission's approval. Moreover, the pending merger application between the Appellant and CSF also has no correlation to the matter at hand as provisions of section 67 of the Ordinance still had to be fully complied with by the Appellant.

8. In view of the foregoing, we see no reason to interfere with the Impugned Order. The Impugned Order is upheld with no order as to costs.



(Shauzab Ali)
Commissioner (SMD)



(Farrukh H. Sabzwari)
Commissioner (SCD-PRDD)

Announced on: **13 JAN 2021**