



BEFORE APPELLATE BENCH NO. I

In the matter of

Appeal No. 2 of 2009

Ms Credit Insurance Company

.....

APPELLANT

Versus

Securities and Exchange Commission of Pakistan NIC Building, Jinnah Avenue, Blue
Area, Islamabad.

.....

RESPONDENT

ORDER

Date of Hearing

17 February 2009

Present:

For the Appellant:

Munawar Salam
Advocate

For the Respondent Department:

Mr. Ali Azeem
Director

Mr. Iftikhar Hussain
Assistant Director



1. This order shall dispose of appeal No. 2 of 2009 filed under section 33 of the Securities and Exchange Commission of Pakistan Act, 1997 by Credit Insurance Company (the "Appellant") against the directive of the Chairman, Securities Exchange Commission of Pakistan ("SECP"), (the "Impugned Directive") dated 4-12-2008.
2. SECP in exercise of its powers under section 63 (1) of the Insurance Ordinance, 2000 ("Ordinance") called upon the Appellant through the Impugned Directive to comply with the requirements of section 11(1) of the Ordinance within one month of the issuance of the Impugned Directive, failing which the Appellant was directed to cease entering into new contracts of insurance. The Impugned Directive was issued on the basis that the Appellant had:
 - i) failed to maintain proper reinsurance treaty arrangements for the year, 2008 in violation of section 41(1) and clause (d) of section 11(1) of the Ordinance.
 - ii) failed to meet the criteria for sound and prudent management, as required under section 12 of the Ordinance.
 - iii) failed to maintain the prescribed level of statutory deposit i.e. *"the higher of ten million rupees and ten percent (10%) of the insurer's paid up capital"*, (which in case of this Company comes to Rs.12.130 million) with the State Bank of Pakistan for and on behalf of the Federal Government as per clause (a) of section 29 (2) of the Ordinance.



- iv) failed to meet the minimum solvency requirements for the years 2006 & 2007 as set forth under clause (c) of section 11(1) and section 36 of the Ordinance.
- v) failed to comply with the minimum paid up capital requirement as prescribed under section 28 of the Ordinance.

3. The Appellant aggrieved by the Impugned Directive has preferred the instant appeal. Mr. Munawar Salam, counsel for the Appellant, made the following preliminary submissions on the Impugned Directive before us (the "Bench") :

- i) that the direction under section 63(1) of the Ordinance was issued to the Appellant without any show cause. He contended that the SECP was required to give opportunity of hearing before it issued the Impugned Directive and drew our attention to PLD 2004 Supreme Court 441, where it has been held that the principle of *audi alteram partem* is applicable to judicial as well as non-judicial proceedings and it is read in every statute as its part if right of hearing has not been specifically provided therein. PLD 1982 Lahore 1, was cited, where it has been held that where the statute does not make any mention of giving opportunity of hearing to effected person, the right of hearing nevertheless is to be read into statute unless specifically prohibited therein. Reliance was also placed on 1965 Supreme Court 90, where it has been held that the principle of natural justice has to be observed if the proceeding might result in consequences affecting "the person or property or other right of the parties concerned".



- ii) that the basic requirement of section 63(1) of the Ordinance is that SECP must "believe on reasonable ground" that the Appellant has failed or is about to fail to comply with the conditions of registration set out in section 11 of the Ordinance, however there was no reasonable ground made out in the Impugned Directive. Moreover the requirement set out in 63 (4) of the Ordinance regarding the direction to be accompanied with statement of reasons for the direction was never complied with. In support of this contention, the counsel relied on PLD 1976 Supreme Court 6, 1996 CLC 293 and 1994 CLC 2041 wherein the term "satisfaction" has been defined and elaborated.

4. The counsel for the Appellant in addition to the foregoing assailed the merits of the Impugned Directive on the following grounds:

- i) on the point listed as para 2(i) above, it was stated that the Appellant has always complied with the reinsurance arrangements and relied on annexure 'B' to the appeal as evidence of compliance. The attention of the Bench was invited to section 41 (1) of the Ordinance, which is a special provision dealing with re-insurance, and the counsel argued that the special provision must override the general provision as such the Appellant was deprived of the right of hearing under section 41(4) of the Ordinance.
- ii) on the point listed in para 2(ii) above, it was argued that the Chief Executive and Directors of the company fully meet the criteria as they have sound knowledge of the business and have been running the insurance company for the last many years,



- iii) on the point listed in para 2 (iii) above, it was argued that the statutory deposit was suspended by the Supreme Court of Pakistan as such the Appellant is not required to comply with the requirement of the statutory deposit. It was also argued that SECP was informed about the status of the proceedings being pending before the Supreme Court of Pakistan and since there was no letter addressed by the SECP on the above issue for a considerable time, therefore it cannot ask for compliance with the statutory deposit through the Impugned Directive. In support of the contention, the Appellant counsel relied on PLD 1970 SC 453 where it has been held that if a departmental practice has gone on for a considerable period of time then it will be extremely unfair to make a departure from it after lapse of years and to disturb rights that have been settled by a long and consistent course of practice.
- iv) on the point listed in para 2 (iv) above, it was contended that the solvency level alleged to have been breached by the Appellant are for the years 2006 and 2007 and are being challenged after a lapse of over 3 years through the Impugned Directive. The Appellant counsel relied on the solvency statements attached with the appeal documents as annexure 'E' and stated that the Appellant has always complied with the solvency levels.
- v) on the point listed in para 2(v) above, the counsel argued that the Appellant increased its paid up capital from Rs. 85,600,000/- to Rs. 121,300,000/- in the year 2007 in order to meet the requirement set out by SECP from time to time, therefore the increase in the paid up capital shows that the Appellant is fully compliant.



5. In response to preliminary submissions of the Appellant's counsel, the departmental representative Mr. Ali Azeem and Mr. Iftikhar Hussain stated that:

- i) the objections of the Appellant are not valid as section 63(1) of the Ordinance, does not provide for an opportunity of hearing. It was argued that the Impugned Directive called upon the Appellant to comply with certain requirements for registration set out in section 11 (1) of the Ordinance within a period of one month. The period of one month was given to the Appellant to comply with requirement of registration. The Appellant however, has failed to comply with the requirements of registration.
- ii) that the Impugned Directive was in compliance with section 63 (4) of the Ordinance as it contained not only the directive to cease entering into new contract of insurance, it also specified the reasons for the issuance of Impugned Directive.

6. In response to the arguments itemized in para 4 above by the Appellant's counsel on merits of the case, the departmental representatives submitted:

- i) that the Appellant's reinsurance arrangement with East Africa Reinsurance Co Ltd ("EARC") for the year 2008 was not confirmed by EARC who informed SECP that it had no re-insurance arrangement with the Appellant for the year 2008. In support of the contention our attention was invited to letter dated 14 October 2008 written by EARC, the contents of which are reproduced below

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“.....

We wish to inform you that for the year 2008 underwriting year, we do not have reinsurance treaty arranged with the named company and no premium has been paid to date on account of the said reinsurance treaty arrangements by the company....

.....”

It was argued that maintaining re-insurance arrangement is a requirement of registration and on failure to maintain re-insurance arrangements, the Appellant was given one month notice for due compliance, but it failed to provide SECP with proof of re-insurance arrangements for the years 2008 and 2009.

- ii) on the issue of failure to meet the criteria for sound and prudent management, as required under section 12 of the Ordinance, we were informed that the Chief Executive and Directors of the company are not qualified to hold the positions as Chief executive and Directors as they do not possess the professional insurance qualifications. It was argued that on inspection of the Appellant under section 231 of the Companies Ordinance 1984, it transpired that one person namely Abdul Qayyum Khan was working as Chief Financial Officer, Manager Head office, Manager Claims and Company Secretary as such the principle enshrined in section 12 of the Ordinance is blatantly violated.
- iii) on the issue of maintaining statutory deposit of higher of 10 million or 10% of the insurers paid-up capital in accordance with clause (a) of section 29 (2) of the Ordinance. It was argued that Appellant's contention that the requirement of statutory deposit has



been suspended by the Supreme Court of Pakistan is not correct as the Supreme Court has suspended the Orders of the High Court and the issue relates to a dispute between the Appellant and one of its insured namely M/s Ravi Enterprises whose claim had not been satisfied and has no nexus with the Impugned Directive.

- iv) that the Appellant has failed to meet the minimum solvency requirements for the years 2006 & 2007, set forth under clause (c) of section 11(1) and section 36 of the Ordinance, as the admissible assets shown in the solvency statement annexure 'E' to the appeal are not admissible under section 32 of the Ordinance.
- v) with respect to the Appellant's contention that it increased its paid up capital in the year 2007 and has therefore complied with the requirement of paid up capital, we were informed that the injection of the paid up capital was artificial, as the amount was withdrawn on the same day as advances to the directors or others and as such the Appellant has not complied with the requirement of the law in letter and spirit.

7. We have heard the parties at length and our findings on the preliminary submissions of the Appellant's counsel are:

- i) The contention that the Appellant ought to have been given an opportunity of hearing, has been considered and needs to be looked at in the context of the provisions of law, particularly section 63 of the Ordinance, which is reproduced for ease of reference:

63. Power of Commission to issue direction to cease entering into new contracts of insurance.- (1) The Commission may issue a direction to cease entering into new contracts of insurance if it believes on reasonable grounds that an insurer registered under this Ordinance has failed, or is about to fail, to comply with the conditions of registration set out in section 11.

(2) The Commission shall issue a direction to cease entering into new contracts of insurance if:

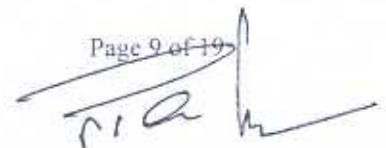
(a) a petition is presented for the winding up of the insurer and has not been withdrawn or vacated within a period of sixty days;

(b) the whole of the business of an insurer has been transferred to any person;

(c) the Tribunal has made an order that a direction be given to that insurer to cease entering into new contracts of insurance; or

(d) the insurer has failed to comply with a directive issued under this Ordinance concerning a contravention of the Ordinance or the rules made thereunder, within the time specified in the Ordinance or, if not so specified, within the time specified in the directive or three months, whichever is longer, and the directive had stated that the failure to comply would lead to a direction to cease entering into new contracts of insurance.

Provided that a direction shall not be issued under clause (d) without giving the insurer an opportunity to be heard.



(3) A direction to cease entering into new contracts of insurance shall have effect one month from the date of the direction unless a later date is specified in the direction.

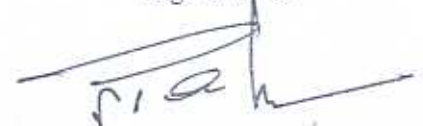
(4) A direction to cease entering into new contracts of insurance shall be accompanied by a statement of the reasons for the direction.

(5) A direction to cease entering into new contracts of insurance shall only be revoked if the reasons for the direction as given in the statement required to be given by the preceding sub-section shall have ceased to exist.

(6) An insurer shall not be in contravention of a direction to cease entering into new contracts of insurance by reason only that the insurer continues to carry out its obligations under contracts of insurance entered into before the direction came into effect.

Emphasis Added

Section 63 (1) of the Ordinance, deals with situation where the conditions for registration as stipulated in section 11 of the Ordinance are not met. In such situation SECP has been entrusted with the power to direct the insurance company to cease entering into new contract of insurance. The principle of natural justice are fully met in this case, as the Appellant was given one month to comply with the requirement of registration and only on failure to comply with this requirement that the Appellant was debarred from entering into new contracts of insurance. The Appellant, merely had to provide the SECP with relevant documents to illustrate its compliance. It is pertinent to mention here that the Appellant has not been directed to cease





the business; as such it can still continue to carry out the obligations under the contract of insurance entered into before the Impugned Directive came into effect. The Impugned Directive has not affected the Appellant's right to act as an insurance company in any manner. The Appellant shall be allowed to enter into new contract of insurance as soon as it complies with the requirements of registration stipulated in section 11 (1) of the Ordinance.

The legislature while drafting section 63 of the Ordinance appears to have been cognizant of the need to have personal hearing in cases where the contraventions are other than one relating to the requirement of registration set out in section 11 of the Ordinance; it has therefore given an opportunity of personal hearing under section 63 (2) (d) of the Ordinance. The legislature was fully conscious of the principles of natural justice has wisely crafted the section by expressly mentioning the right of hearing in proviso of section 63 (2) (d) of the Ordinance thereby excluding the right of hearing in section 63 (1) of the Ordinance. In support of our view, we rely on maxim "*Expressio Unius est Exclusio Alterius*" i.e. "the express mention of one thing implies the exclusion of another". We would however add here that the SECP may, where it views any matter needing hearing, always call upon in a given circumstance the party against whom action is proposed to explain the position prior to passing an order. In reaching the decision, we are further aided by the following judgment of Supreme Court of Pakistan reported in PLD 1991 Supreme Court 1029 where it has been held:

"Audi alteram partem. Right of opportunity of hearing is not merely a technical right, it is linked with the tangible, factual and legal aspects of the case and it would depend upon the facts and circumstances thereof as to whether observance of the technical rule of audi alteram partem by a lower forum and the ritualistic



performance in this behalf would serve the ends of justice or it would negate the ends of justice. If the forum before which such a question is raised is able to examine the merits, there would be nothing wrong in deciding the matter finally and refraining from multiplicity of proceedings which as an end-product also causes injustice and misery in so far as the delay, expenses and anxiety are concerned".

In another case of the Indian Supreme Court reported in AIR 1987 SC 593 page 605 it was held:

"These principles audi alteram partem do not apply to all cases and situation. Application of these unmodified rules are often excluded by express provision or by implication. This right can also be excluded 'where' the nature of action to be taken, its object and purpose and the scheme of relevant statutory provisions warrant its exclusion, nor can the audi alteram partem rule be invoked if importing it would have the effect of paralyzing the administrative process or where the need for promptitude or the urgency of taking action so demands."

Emphasis added

In the light of the express provision of law and the judgments cited above, we are of the view that an opportunity of hearing, where action is taken under section 63(1) of the Ordinance is not to be given as the scheme of the law excludes the opportunity of hearing in instances where the requirement of registration are not complied. It would negate the ends of justice, if the Appellant was allowed to carry on business without meeting the requirements of law. However, where the issue pertains to maintaining



proper re-insurance treaties as discussed in para 8 (1) below proper opportunity of hearing must be provided.

- ii) On the point of need for statement of reasons in accordance with section 63(4) of the Ordinance, we agree with the departmental representative submission that the directive to cease entering into new contracts of insurance had specified the reasons for the Impugned Directive as well. The judgments cited in support of the Appellant's argument on the issue of "satisfaction" have also been perused and appreciated; however, the term used in section 63(1) of the Ordinance is "believe on reasonable ground" as opposed to "satisfied" and we agree with the departmental representatives that reasonable grounds have been spelled out in the Impugned Directive.

8. Our para-wise findings on the points, raised by the Appellant's counsel on the Impugned Directive are as under:

- i) The Appellant was required to submit the re-insurance treaty for the year 2008 with SECP latest by 15 January 2008; however from the contents of the letter dated 14th October 2008 shown to us by the department representative, it appears that the reinsurance arrangement was not in place with EARC. The Appellant's counsel on the other hand contended that there was a dispute with EARC which stood resolved and under the circumstances, the letter of EARC dated 14th October 2008 must not be considered.

We however, without considering the contention raised, agree with the Appellant's counsel that in presence of section 41(1) of the Ordinance, the general provision i.e. section 11 of the Ordinance will not be attracted therefore, before passing any order under section 41(1) of the Ordinance,



the Appellant ought to have been allowed to be heard in person, in accordance with section 41(4) of the Ordinance. Under the circumstances, if the department has reason to believe that the Appellant is in contravention of section 11 (1) (d) read with section 41(1) of the Ordinance, it may initiate show cause proceedings.

- ii) On the point of failure to meet the criteria for sound and prudent management, as required under section 12 of the Ordinance, we are of the view that for the position of Chairman, or the Chief Executive or principle officer in Pakistan, the requirement of experience or qualification is of direct relevance to the conduct of insurance operations, therefore either of the two may compensate for the other; as in this case, where the Chief Executive and Directors have put in considerable time in the insurance industry. However, we take strong exception to the fact that the operations of the Appellant are conducted by one officer who is acting as Chief Financial Officer, Manager Head office, Manager Claims and Company Secretary which is against the norms of business. The principle of "fit and proper person" as enshrined in section 12 of the Ordinance has not been fully explained and we believe that there is need to prescribe the criteria of "fit and proper person"; unless it can be demonstrated by the department that the violation is so gross that despite no criteria having been prescribed, it is clear that the people working for a particular company and handling its affairs are not fit and proper to have been entrusted with such responsibility and as a result action under section 12 of the Ordinance is proper. For the foregoing, we are of the view that the Appellant meets the criteria for sound and prudent management.
- iii) The argument of the Appellant that it is exempted from maintaining statutory deposit, as the Supreme Court of Pakistan has suspended such a



requirement has been examined. The orders of the Supreme Court have been filed as annexure 'D' to the appeal. The facts of the case are that one, Ms. Ravi Enterprise filed a writ petition No 1244/1998 before the High Court against the Appellant; contending that the Appellant had failed to make the payment of its insurance claim as decided by the Controller of Insurance. The High court after hearing the parties remanded the case to the Controller of Insurance with the instruction to decide the matter afresh and in the meanwhile the statutory deposit of Rs. 3.2 million available with the Controller of Insurance was freezed. The Controller of Insurance found the claim bonafide, but showed inability to make payment out of the statutory deposit of the Appellant in absence of an order of competent court of law. The inability shown by the Controller of Insurance to make payment out of the statutory deposit was once again challenged in writ petition before the High Court, and the High Court after examining the case, directed the Controller of Insurance to satisfy the claim of M/s Ravi Enterprise. The order of the High Court was challenged by the Appellant before the Supreme Court of Pakistan, which has suspended the order of the High Court and has granted leave to appeal.

We do not see how the Appellant is protected by the order of the Supreme Court of Pakistan from maintaining and enhancing the statutory deposit as required by section 29(2) of the Ordinance. Nothing has been produced before us which would show that the Appellant has been exempted from maintaining the statutory deposit level as in existence on the date of the issue of the Impugned Directive. The Appellant in 2008 was required to maintain statutory deposit of higher of ten million rupees or 10% of the insurer paid up capital in accordance with section 29 (2) (a) of the Ordinance, i.e. Rs. 12.130 million, which it failed to do. In any case the statutory deposit in question before the Supreme Court of Pakistan is not



more than 3.2 million, as such the deposit is far short of the required level of Rs 12.130 million. Moreover, the requirement of the law to maintain the statutory deposit in no way prejudices the proceedings before the Supreme Court of Pakistan.

The argument of the Appellant that since SECP did not proceed against the Appellant on the issue of statutory deposit for considerable period of time and therefore the Appellant cannot be asked to maintain the statutory deposit is without any merit. The judgment referred to in support of the argument has also been reviewed; however, we cannot see how the judgment cited advances the case of the Appellant. The mere fact that there was inaction on SECP's part or the failure to maintain statutory deposit had not come to light does not mean that it would be considered a departmental practice not to take action, where there is violation of law.

- iv) The issue of failure to meet the minimum solvency requirements for the years 2006 & 2007 has been examined. The assets shown in the solvency statement for the year 2006 annexure 'E', includes an amount of Rs. 34,779,730/- under the head of sundry receivables. The breakdown of sundry receivable shows Rs.12,379,730/- as advance for vehicles, which is an inadmissible asset under clause (u) of section 32 (2) of the Ordinance; an amount of Rs 18,400,000/- shown as advance for purchase of land which is an inadmissible asset under clause (l) of section 32 (2) of the Ordinance as the documents presented during the hearing by the Appellant shows that entire payment against the land has not been made and therefore the land is under encumbrance; and an amount of Rs. 4,000,000/- shown as advance for construction of office building, which is inadmissible asset under clause (g) of section 32 (2) of the Ordinance as the documents presented during the hearing by the Appellant shows that



the contract for building was cancelled and therefore the amount advanced is to be refunded to the Appellant, thus it is "amount due" as defined in clause (g) of section 32 (2). We have also perused the solvency statement for the year 2007 which also includes advances amounting to Rs 56,342,589/- under the head of sundry receivables. The breakdown of sundry receivable shows Rs.13,828,289/- as advance for vehicles, which is an inadmissible asset under clause (u) of section 32 (2) of the Ordinance; an amount of Rs. 18,400,000/- shown as advance for purchase of land which is an inadmissible asset under clause (l) of section 32 (2) of the Ordinance as the documents presented during the hearing by the Appellant shows that entire payment against the land has not been made and therefore the land is under encumbrance; and an amount of Rs. 24,114,300/- shown as advance for construction of office building, which is inadmissible asset under clause (g) of section 32 (2) of the Ordinance as the documents presented during the hearing by the Appellant shows that the contract for building was cancelled and therefore the amount advanced is to be refunded to the Appellant, thus it is "amount due" as defined in clause (g) of section 32 (2). After excluding all inadmissible assets in the year 2007, the company was insolvent by a margin of 28.15 million. As regards the argument of the Appellant that the solvency level are being challenged after three years, we do not see, how the SECP is barred from taking an action after lapse of 2-3 years.

- v) Finally, we have analyzed the contention of the Appellant on the issue of increase in paid-up capital. The Appellant's paid-up capital was increased from Rs. 85,600,000/- to Rs. 121,300,000/- in the year 2007. The department representatives contend that the inspection report conducted by SECP under section 231 of the Companies Ordinance 1984 reveals that Appellant has come up with a novel strategy to show that it had complied



with the requirement of paid up capital. Cash was injected in the Appellant's bank account in order to comply with the requirement of paid up capital, and on the same day the amount was paid back as advances to directors or others. It transpires from the record that the advances were made in the name of M/s Friends construction company, which is represented by Mr. Moazzam Chughtai, who happens to be the husband of one of the Directors namely Mrs. Adeeba Moazzam. On our comparing annexure 'F/3' at page 197 of the appeal, which shows the details of the increase in the Appellant's paid up capital and the bank statement of United Bank Limited at pages 205, 206 of the appeal, we find that cash was injected and withdrawn on the same day illustrating that the transaction was merely cosmetic and was made to meet the requirements of paid-up-capital.

Be that as it may, the department ought to have proceeded under section 231 of the Companies Ordinance 1984 instead of holding that the Appellant was non-compliant with the paid up capital requirement. The proceedings under section 231 of the Companies Ordinance 1984 ought to be taken to its logical conclusion by the department. Until the proceedings are concluded the Appellant cannot be held to be non-compliant with respect to maintaining of paid up capital.

9. The Appellant requested the Bench to allow filing of comprehensive application in support of its contention on 1-4-09. The request was acceded to by the Bench, upon which the Appellant filed an application dated 11-4-09. Neither the application nor the documents submitted add any substance to the contention raised in the appeal. In any case we have addressed the points raised at this late stage in paragraph 8 of this order.



10. For the reasons stated above we are of the view that the Appellant has failed to maintain the required statutory deposit and solvency levels and is therefore in violation of section 63(1) of the Ordinance. The Appellant is directed to comply with the aforesaid requirements within thirty (30) days and shall not enter into new contracts of Insurance until it is fully compliant, failing which the concerned department must proceed against the appellant in accordance with law.

(SALMAN ALI SHAIKH)
Chairman

(S. TARIQ A. HUSAIN)
Commissioner (LD)

Announced on: 8th June 2009