



# SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

Adjudication Department-I

Adjudication Division

Before Ali Azeem Ikram, Executive Director/HOD(Adjudication-I)

*In the matter of*

IGI General Insurance Limited

Show Cause Notice No. and Issue Date	ID/Enf/IGIGeneral/2020/453 May 28, 2020
Date of Hearing:	October 26, 2020
Attended By:	Mr. Nadeem Ahmad (Orr, Dignam & Co. Advocates)
Date of Order:	December 3, 2020

## ORDER

Under Rules 2(1)(b)(i) and 4(2) of the Credit and Suretyship (Conduct of Business) Rules, 2018 read with Section 60 and Section 156 of the Insurance Ordinance, 2000

.....

This Order shall dispose of the proceedings initiated against M/s. IGI General Insurance Limited (the "Company") on account of alleged contraventions of Rules 2(1)(b)(i) and 4(2) of the Credit and Suretyship (Conduct of Business) Rules, 2018 in relation to the policies issued by the Company under Credit and Suretyship business, as disclosed in Form GCS for the year ended December 31, 2018.

2. The Company is registered under the Ordinance to carry on non-life insurance business in Pakistan.

3. While examining the Annual Audited Accounts and Regulatory Returns of the Company for the year ended December 31, 2018, it was revealed that the Company, prima facie, did not comply with the requirements of Rule 4(2) of the Rules as the adequate collateral was not procured in respect of its guarantees/bonds policies of an amount equivalent to at least 80% of sum insured/amount of bond/guarantee less reinsurance. It was also observed that the Company kept the collateral in the form of 'undated cheques' which is, prima facie, in contravention of definition of collateral as given under Rule 2(1)(b)(i) of the Rules.

4. The Commission vide its email dated January 28, 2020 advised the Company to clarify its position in the subject matter. In response, the Company vide its letter dated February 11, 2020 submitted its reply as follows:



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"we would like to submit that the undated cheques are neither promissory notes nor post-dated cheques but a valid banking instrument that can be presented in bank for encashment at any date. Therefore, undated cheques duly qualify as collateral as per the requirements of Credit and Suretyship (Conduct of Business) Rules, 2018."

5. The applicable provisions of the law provide that:

Rule 2(1)(b)(i) of the Credit and Suretyship (Conduct of Business) Rules, 2018 ("the Rules") provides that:

".....

(b) Collateral means-

- (i) Cash, ready money which can be used as money without being converted into another form and which circulates as money including bank bills but does not include promissory notes or post-dated cheques."

Rule 4 of the Credit and Suretyship (Conduct of Business) Rules, 2018 ("the Rules") states that:

**"Net Retained Exposure Limit and Collateral Requirement:-** (1) An insurer's net retained exposure under any type of guarantee/bond issued by the insurer to a party or a group shall not exceed 2.5% of the insurer's shareholders' equity as per the latest available audited accounts of the insurer on the date of issuance of a guarantee/bond;

(2) Subject to limit prescribed under sub-rule (1), an insurer shall procure collateral in case of guarantees / bonds of an amount equivalent to at least 80% of sum insured / amount of bond/ guarantee less reinsurance in respect of a particular guarantee /bond;

(3) An insurer shall, at all times, ensure that the aggregate net retained exposure on all outstanding and in-force bonds shall not exceed the greater of 100% of shareholders' equity."

6. Since the reply of the Company was not found to be satisfactory Show Cause Notice No. ID/Enf/IGIGeneral/2020/453 dated May 28, 2020 (SCN) was issued to the Respondent Company, calling upon it to show cause as to why the fine as provided under Section 156 of the Ordinance may not be imposed on it for the aforementioned alleged contraventions of the law.

7. In response to the SCN, the Company vide its letter dated June 10, 2020 submitted its reply as follows: -

"We act on behalf of IGI General Insurance Limited ("IGI General") and refer to SECP's Show Cause Notice to IGI General dated May 28, 2020 (Ref: ID/Tn/IGI General/2020/453) ("Notice"). We also refer to SECP's earlier letter No. ID/OSM/IGI/2020/696 dated January 28, 2020 and IGI General's reply dated February 11, 2020.





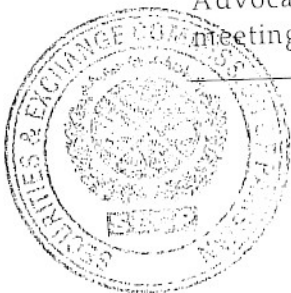
As background, IGI General obtains 'un-dated cheques' from its customers as part collateral in addition to certain cash margin for bond/guarantees issued by the company pursuant to the Credit and Suretyship (Condition of Business) Rules, 2018 (the "Rules").

SECP has taken the view that undated cheques cannot be categorized as collateral and therefore the company's practice is a violation of the requirements of the Rules. The position taken by the SECP in its earlier correspondence and the Notice is that IGI General is not in compliance with Rule 4(2) of the Rules which states that 'Subject to limit prescribed under sub-rule (1), an insurer shall procure collateral in case of guarantees/bonds of an amount equivalent to at least 80% of sum insured / amount of bond / guarantee less reinsurance in respect of a particular guarantee/bond;'. The term "collateral" is defined in Rule 2 (1)(b) (i) of the Rules to mean 'cash', ready money which can be used as money without being converted into another form and which circulates as money including bank bills but does not include promissory notes or post-dated cheques;" (Emphasis is ours).

We would respectfully submit that the spirit of the requirement under Rules 2(1)(b) and Rule 4(2) of the Rules is clearly to impose an obligation on insurers to retain cash and/or liquid assets which could be readily used for meeting an insurers obligations and exposure under any type of guarantee/bond issued by it. We would respectfully submit that the language of Rule 2(1)(b) should be reviewed carefully based on its plain natural meaning to ascertain the scope of the definition of collateral/cash. In this respect, the term collateral - in addition to cash - means ready money but expressly excludes promissory notes or post-dated cheques. The use of the words postdated cheques is clearly consistent with the rationale of ready money as a postdated cheque may not be encashed prior to the date mentioned on the cheque. The definition does not exclude all forms of cheque but postdated cheques only and therefore a cheque with a current date should be covered by the definition of collateral. As regards the practice of obtaining undated cheques as security and filing in a date and presenting it for payment when required, this is a fairly standard practice in the banking, finance and commercial sectors and is envisaged in the Negotiable Instruments Act, 1881 and the banking recovery laws. There is an argument that a cheque should not be considered cash or ready money and it is not a guarantee of payment as it may be dishonoured upon presentment if there are insufficient funds in the underlying bank account of the drawer. However, we would respectfully submit that if this was the intention then instead of using the words 'postdated cheques' only the word 'cheques' should have been used in the Rules.

In view of the above explained position, it is submitted that IGI General is in compliance with the requirements of the Rules and would therefore request the SLCF to kindly withdraw the Notice."

8. In order to provide the Respondents an opportunity of making personal representation in the matter, hearing in the matter was fixed for October 26, 2020. The said hearing was attended by Mr. Nadeem Ahmad (M/s. Orr, Dignam & Co., Advocates) as the Authorized Representative of the Respondent through zoom meeting link. During the hearing, the Authorized Representative was advised to





submit the reasons for alleged non-compliances, as narrated in the SCN. The Authorized Representative reiterated the submissions made in the written reply dated June 10, 2020.

9. During the hearing proceedings, the Authorised Representative stated that in their opinion, Rule 2(1)(b)(i) of the Rules excludes only promissory notes or post-dated cheques from admissible collaterals under the Rules. However, any duly signed cheques which are un-dated should be acceptable as collateral. The Authorised Representative stated that in accordance with the legal principle that "whatever is not prohibited is admissible", un-dated cheques should be accepted as admissible collateral in terms of the Rules. He submitted that the said principle is also recognized by the Courts. He further stated that whoever issues a cheque dishonestly towards fulfilment of an obligation and that cheque is dishonoured on presentation, he shall be punishable with an imprisonment or with fine or with both, under Section 489F of Pakistan Penal Code, 1860.

10. As per the information received from the Insurance Division subsequently, during the offsite examination of Form GCS filed by the Company for the year ended December 31, 2019, the afore said alleged non-compliance has been observed as the Company has again accepted "undated cheques" as collateral against policies issued during the year. The Insurance Division advised the Company to clarify its position in the matter vide email dated October 2, 2020. The Company vide email dated October 9, 2020 submitted its reply as under.

*"We note from your e-mail the view that undated cheques cannot be categorized as collateral and therefore the company's practice is a violation of the requirements of the Rules. The position taken by SECP is that IGI General is not in compliance with Rule 4(2) of the Rules which states that: "Subject to limit prescribed under sub-rule (1), an insurer shall procure collateral in case of guarantees/bonds of an amount equivalent to at least 80% of sum insured / amount of bond / guarantee less reinsurance in respect of a particular guarantee/bond;". The term "collateral" is defined in Rule 2 (1)(b) (i) of the Rules to mean "cash, ready money which can be used as money without being converted into another form and which circulates as money including bank bills but does not include promissory notes or post-dated cheques;".*

*Rule 2(1)(b) and Rule 4(2) require insurers to retain cash and/or liquid assets which could be readily used for meeting an insurer's obligations and exposure under any type of guarantee/bond issued by it. The plain meaning of the term collateral – in addition to cash – means ready money but expressly excludes promissory notes or post-dated cheques. The use of the words postdated cheques is consistent with the rationale of ready money as a postdated cheque may not be encashed prior to the date mentioned on the cheque. The definition does not exclude all forms of cheque but postdated cheques only and therefore a cheque with a current date should be covered by the definition of collateral. As regards the practice of obtaining undated cheques as security and filing in a date and presenting it for payment when required, this is a standard practice in the banking, finance and commercial sectors and is envisaged in the Negotiable Instruments Act, 1881 and the banking recovery laws. If the intention of the Rules was not to allow*





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*all forms of cheques, then instead of using the words 'postdated cheques' only the word 'cheques' should have been used in the Rules.*

*In view of the above explained position, it is submitted that IGI General is in compliance with the requirements of the Rules."*

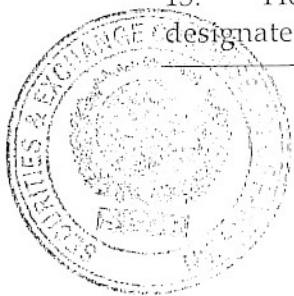
11. I have carefully examined the facts of the case in light of applicable provisions of the law and have given due consideration to the written as well as verbal submissions of the Respondent/ Authorised Representative. Rule 2(1)(b)(i) lays down the criteria for a valid and admissible forms of collateral in terms of the Rules as it requires that "Collateral means Cash, ready money which can be used as money without being converted into another form and which circulates as money". Undated cheques would neither be regarded as cash nor they could be recognized as ready money since ready money is money in the form of cash that is immediately or readily available i.e. without any delay or difficulty. Since, there could be situations where cheques may delay the procurement of cash, thus they might not fall within the desired scheme of "cash" or "ready money". Hence, undated cheques or even current dated cheques do not fulfill the criteria as they cannot be used as ready money without being converted into cash upon being presented and honoured at a bank. Furthermore, for a cheque to be a valid instrument there are certain basic ingredients and date is one of them. Hence, undated cheque cannot be termed as a valid financial instrument, thus, procuring the same as collateral does not fulfill the regulatory requirements. In view of the foregoing, the defaults of Rule 2(1)(b)(i) and Rule 4(2) of the Rules have been established. The defaults of Rule 2(1)(b)(i) and Rule 4(2) of the Rules have also been committed in respect of policies issued under Credit and Suretyship business in the year 2019. Therefore, the Respondent Company is liable to be penalized under Section 156 of the Ordinance, which provides that:

## Section 156:

*"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, for 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."*

12. In exercise of the powers conferred on me under Section 156 of the Ordinance, I, hereby, impose fine of Rs. 175,000/- (Rupees One Hundred Seventy Five Thousand only) on the Company on account of the defaults of Rule 2(1)(b)(i) and Rule 4(2) of the Rules, as mentioned in the above paras hereof. The Respondents are hereby warned to ensure full compliance with the Ordinance, rules, regulations and directives of the Commission, in future.

13. Hence, the Company is hereby directed to deposit the aforesaid fine in the designated bank account maintained in the name of Securities and Exchange



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Commission of Pakistan with MCB Bank Limited within thirty (30) days from the date of this Order and furnish receipted voucher issued in the name of the Commission for information and record.

14. This Order is issued without prejudice to any other action that the Commission may initiate against the Company and / or its management (including the CEO of the Company) in accordance with the law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.

*Ali Azeem Ikram*

**Ali Azeem Ikram**

Executive Director/HOD (Adjudication-I)

