Securities and Exchange Commission of Pakistan

BEFORE APPELLATE BENCH NO. IV

In the matter of

Appeal No. 03 of 2016

1. Mr. Ashfaq Ahmed, Chief Executive
2. Mr. Saqib Ashfaq, Director
3. Mr. Amir Ashfaq, Director
4. Mr.Niaz Muhammad, Director
5. Mr. M. Farooq, Director
6. Mr. Iklaq Hussain, Director
7. Mr. Saleem Abbas, Director
8. Mr. Sarfraz, Company Secretary
9. M/s Taha Spinning Mills Limited through its chief Executive

Appellants

Versus

The Executive Director, Corporate Supervision Department
Company Law Division

Respondent

Date of hearing: 01/02/16

Present:

For Appellants:

1. Mr. Muhammad Afzal Awan, Advocate High Court
2. Mr. M. Sarfraz, Company Secretary

For Respondent:

1. Mr. Abid Hussain, Executive Director CSD
2. Mrs. Amina Aziz, Director CSD

ORDER

1. This order shall dispose of Appeal No.03 of 2016 filed under section 33 of the Securities and Exchange Commission of Pakistan Act, 1997 against the order dated 18/11/15 (the Impugned Order) passed by the Respondent.

2. The brief facts of the case are that examination of annual audited accounts for the year ended 30/06/13 and quarterly accounts for the period ended 31/03/14 of Taha Spinning Mills Limited (the Appellant No.9) revealed that an amount of Rs.4 million was receivable from an associated company HMI Energy (Private) Limited (the HMI). The Respondent sought information and documents in this regard from the Appellant No.9, which were provided accordingly. The perusal of documents revealed that the Appellant No.9 sold generator having market value of Rs.15 million for a sale consideration of Rs.13 million to the HMI and Rs.4 million were still due to the HMI whereas in another case Rs.124 million as sale proceeds of property were received immediately by the Appellant No.9. Therefore, apparently Appellant No.9 provided benefit to the HMI by selling generator on credit basis without the authority of a special resolution which, prima facie, contravened the provision of section 208 of the Companies Ordinance 1984 (the Ordinance). Therefore, a Show Cause Notice (the SCN) dated 20/06/14 was issued to Appellants 1 to 7 under section 208 read with section 476 of the Ordinance.

3. The Appellants 1 to 7 replied the SCN vide letter dated 25/06/14 and stated that written down value of generator as per books was Rs12.93 million and forced sale value was Rs.10.5 million. The generator was sold to the HMI for Rs.13 million as there was no other higher offer and profit of Rs.0.68 million was made on sale. The Appellants No. 1 to 7 also denied the relation of associated company HMI and Appellant No.9. The hearing in the matter of SCN was held on 17/09/14.

4. During the hearing proceedings of SCN dated 20/06/14 it was revealed that the Board of Directors (the BOD) of Appellant No.9 approved sale of assets on the basis of old quotations invited on 12/09/12. The BOD approval was contrary to the information provided to the Respondent vide letter dated 02/02/13 wherein it was submitted that the assets will be disposed of through tender offers in newspapers and same fact was communicated to shareholders at the time of Extra Ordinary General Meeting (the EOGM) dated 20/02/13. The aforesaid approval of assets sale by the BOD on the basis of old quotations was prima facie, a misstatement as it was contrary to the information provided to the Respondent and shareholders. In view of the above stated new fact the

Respondent issued an interim order dated 07/11/14, and recommended to review the entire matter and if needed fresh/additional SCN proceedings be initiated under relevant provisions of the Ordinance. Thereafter, the matter was reviewed in its entirety and a SCN dated 10/11/14 was issued to the Appellants 1 to 8, whereby they were called upon to show cause in writing as to why penalties may not be imposed on them in terms of section 492 of the Ordinance for the alleged misstatements and omissions.

5. The Appellants 1 to 8 replied to the SCN vide letter dated 28/11/14 and stated that the Appellant No.9 has no investment in the HMI and balance amount of Rs.4 million receivable from the HMI is a trade debt. They stated that tender in newspaper was not the only mode approved by the shareholders for disposal of assets; they referred to the statement of material fact which stated that disposal of fixed assets can be made through negotiation/advertisement/tender or calling quotation. They further stated that shareholders in their EOGM empowered the BOD to sell the fixed assets of the Appellant No.9; thereafter the sale agreement was executed on 01/04/13. The management was under litigation with the banks and others, therefore, no fresh offers were invited in view of the intervention of a person already in litigation with the company. The offers received earlier were conditional and subject to clearance of all liabilities/cases, therefore, clearance took time and the BOD ultimately accepted the highest offers in their meeting held on 28/02/13.

6. The hearing in the matter was held on 12/11/15. The Respondent being dissatisfied with the response of the Appellants held that violations have been committed by the Appellants under section 208 and 492 of the Ordinance. Therefore, in exercise of the powers conferred by section 492 of the Ordinance, a penalty of Rs.25,000 was imposed on Appellant No.1 to 7 individually. The eighth Appellant Mr. M. Sarfraz, the Company Secretary was warned to be careful in future regarding compliance with section 492 of the Ordinance. However, in respect of violation of section 208 of the Ordinance, all the respondents were warned to be careful in future and ensure meticulous compliance with the applicable provisions of the law by exercising due care. Further, Appellants were directed under section 473 of the Ordinance and to take immediate steps to recover the

balance amount of Rs.4 million from the HMI along with mark up to be charged for the extended period of credit.

7. The Appellants have preferred the instant appeal against the Impugned Order on following grounds:

a) The Impugned Order is without jurisdiction therefore, a nullity in the eyes of the law.
b) The SCN dated 20/06/14 was vacated vide interim order dated 07/11/14 and no fresh cause notice was issued under section 208 of the Ordinance.
c) The SCN dated 10/11/14 under section 492 of the Ordinance was issued alleging the violation of section 208(1) of the Ordinance therefore the Respondent cannot go beyond the scope and provisions mentioned in SCN.
d) The Respondent erred to understand that Appellant No.9 and the HMI are two separate entities and have separate BOD.
e) The Respondent erred to understand that due to lingering court litigation, creditors and decree holders pressure to settle their outstanding loan, there were hurdles in sale of fixed assets of Appellant No.9.
f) The Respondent erred to understand that Appellant No.9 obtained normal trade loan of Rs.9 million from HMI on 15/01/13, and loan amount was adjusted against the sale proceeds of generator. The Appellant No.9 earned Rs.4 million from the sale of generator; however it is still receivable from HMI.
g) The Agreement to sell assets with HMI for Rs.13 million was executed on 01/04/13 after taking into consideration the offers of all the bidders. Other bidder's offers were for Rs.8 million and Rs.8.5 million.
h) The Respondent erred to understand that as per books of accounts, generator Written-down value was Rs.12.93 million and Forced Sale Value was Rs.10.50 million, therefore the Appellant No.9 has made a profit of Rs.0.068 million on sale of Generator to HMI.
i) The Respondent erred to understand that there is no provision of law that stamp paper should be purchased when the deal is being executed and date on stamp paper should correspond with the date of the deal.

j) The Respondent wrongly alleged that the Appellants communicated to the shareholders at the time of EOGM that sale would be made through tender in newspaper. As per minutes of the EOGM the Appellants stated to the shareholders that "Our preference will be through tender", however in this regard no firm commitment was made with the shareholders/Respondent, hence there is no misstatement by the Appellants.

k) The Respondent has not quoted a single complaint of any member of the company who has been affected by the alleged violation of section 208 of Companies Ordinance, 1984 and SRO 1227/2005.

l) The Respondent has not cited a single violation which has been made knowingly or willingly by the Appellants and due to which shareholders have been affected directly or indirectly.

8. The Respondents have denied and rebutted the grounds of appeal in the following manner:

a) The Impugned Order has been passed strictly in compliance with applicable law.

b) The SCN dated 20/06/14 was never vacated, rather an interim order was passed with directions to analyze the case in its entirety. Since the SCN was not vacated therefore, issuance of fresh SCN under section 208 was not required.

c) The Respondent has strictly remained within the scope and the provisions of the law while initiating and concluding the proceedings under section 208 and section 492 of the Ordinance.

d) The provisions of the Ordinance are clear and explicit and as per definition of the associated company under section 2(2) of the Ordinance the Appellant No.9 and HMI are associated companies.

e) It has been stated by the Appellants that the management was under litigation with the banks and others, therefore, no fresh offers were invited. However, perusal of the notice of the EOGM reflects that material fact of litigation of a person other than the creditors, was not disclosed to the shareholders in EOGM despite the knowledge of it being material. In any case, the Appellants were

bound to provide information to the shareholders if they had plans to dispose of the assets based on previously invited quotations and amounts of quotations so received should have been disclosed to the shareholders to enable them to make a well informed decision.

f) The generator was sold to the HMI on 01/04/13 for Rs.13 million, out of which Rs.4 million are still receivable which cannot be treated as normal trade credit and it appears that the Appellant No.9 provided benefit to HMI, by selling generator on credit basis and balance payment has not yet been received despite elapse of more than two and a half years. Since the amount receivable from associated company is without the authority of special resolution and without any return therefore provisions of section 208 of the Ordinance have been violated.

g) The agreement to sell the generator to HMI was made on the basis of old quotations and this material fact was also not disclosed to the shareholders in the EOGM that the assets will be disposed of on the basis of old quotations invited on 12/09/12. Moreover, despite the fact that the generator was being sold to HMI which was an associated company, no disclosure to this effect was given to the shareholders.

h) As per revaluation report dated 01/01/13 the value of generator was assessed to be Rs.15 million with forced sale value of Rs.10.5 million. Therefore, the Appellants plea that the Appellant No.9 had earned profit is not correct.

i) The Appellants have not been penalized on the basis of difference of dates of the stamp and actual date of sale.

j) The statement of material facts of the notice of EOGM discloses to the members that proposed mode of disposal would be through negotiation/ advertisement/tender or calling quotations and the preference will be through tender in the newspaper. However, the Appellants have not disclosed to the members that they will dispose of the aforesaid assets on the basis of old quotations. This omission of material facts was violation of section 492 of the Ordinance.

k) The violations of section 208 and 492 of the Ordinance have been established against the Appellants. The directors of Appellant No.9 were required to have

knowledge of applicable legal provisions and they are responsible to ensure due compliance. The Appellants cannot be absolved from their duties by claiming that the violations were not willful and the shareholders were not affected directly or indirectly.

l) The proceedings against the Appellants were initiated under sections 208 and 492 of the Ordinance and to invoke these provisions there is no pre-requisite or a condition of complaint from any member or shareholders. The proceedings were initiated and have since been concluded by the Respondent in discharge of the regulatory duties.

9. We have heard the parties i.e. Appellants and Respondent and perused the record of the appeal. The proceedings against the Appellants were initiated through two SCNs dated 20/06/14 issued under section 208 of the Ordinance and dated 10/11/14 under section 492 of the Ordinance. The proceedings of SCN dated 20/06/14 were not finally concluded and an interim order dated 07/11/14 was issued to review the matter in its entirety. Thereafter the matter was reviewed and a SCN dated 10/11/14 was issued to the Appellants, whereof they were called upon to show cause in writing as to why penalty may not be imposed under section 492 of the Ordinance. The Respondent has concluded the proceedings initiated through the above stated two SCNs and passed the Impugned Order. Therefore the contention of the Appellants Counsel (the Counsel) with respect to vacation of the SCN dated 20/06/14 is contrary to the record hence cannot be acceded.

10. The Counsel have also raised a basic objection in pleadings and arguments that Appellant No.9 and HMI are not associated companies hence section 208 of the Ordinance is not applicable on transactions entered into between them. However, the record speaks contrary to the stance of the Appellants, as there are two directors of HMI who hold 50% shareholding each and HMI has 49.914% shareholding in Appellant No.9, therefore each director of the HMI has 24.96% indirect shareholding in Appellant No.9. Therefore, in view of section 2(2) of the Ordinance, relationship of associated company is established between HMI and Appellant No.9.

11. The Respondent vide its letter dated 30/01/13 to the Appellant No.9 highlighted the deficiencies in notice of EOGM and advised the Appellant No.9 to issue correct and revised statement of material facts under section 160 of the Ordinance to the shareholders and the Respondent before the date of meeting. The Respondent has advised the Appellant No.9 that "the mode of disposal in this case shall be through tender in newspapers." The Respondent specifically mentioned in said letter to dispose of the undertaking including generator through tender in newspapers as required by the SRO 1227/2005 dated 12/12/05. In reply, the Appellant No.9 vide letter dated 02/02/13 communicated to the Respondent that the assets shall be disposed of through tender offers in newspapers. However, on 28/02/13 the BOD of Appellant No.9, instead of inviting fresh tenders through newspapers, approved sale of land & building and generator on the basis of old quotations invited on 12/09/12. The Appellants have also not disclosed to the shareholders in EOGM dated 20/02/13 that they intend to sell assets of Appellant No.9 on the basis of old quotations. The conduct of the Appellants is evident that they have misstated with the Respondent and failed to disclose this material fact before the shareholders that the assets shall be disposed of on the basis of old quotations, therefore, the Respondent has rightly penalized the Appellants under section 492 of the Ordinance. Moreover, despite the fact that the generator was being sold to an associated company, HMI, no disclosure to this effect was given to the shareholders.

12. The Counsel, to make out the case, argued that the assets of the Appellant No.9 were sold on the basis of old quotations because management was under litigation with the banks and others, therefore new advertisement was not possible. However, perusal of the notice of the EOGM reflects that even this material fact that a person other than the creditors was in litigation with the Appellant No.9 was not disclosed to the shareholders in EOGM despite this being material. The Appellants were bound to disclose to the shareholders, in case they intended to dispose of the assets on the basis of previously invited quotations and amounts of quotations so received to enable them to make a well informed decision. However, the Appellants failed to do the aforesaid. The Counsel further argued that the old quotations were valid as no time limitation was mentioned therein and those were subject to clearance of all the liabilities and court cases. The argument of the Counsel

could not be appreciated in absence of disclosure of material information to the shareholders.

13. Furthermore, the amount of Rs.4 million is still receivable from HMI, an associated company, whereas in respect of sale of property to Hassan Limited, sale consideration was immediately received by the Appellant No.9. The receivable from HMI is not a normal trade credit and it appears that the Appellant No.9 provided benefit to HMI, by selling generator on credit basis and balance payment has not yet been received despite lapse of more than two and a half years. The amount receivable from associated company is without the authority of special resolution and without any return therefore violation of section 208 of the Ordinance has been established.

14. In addition to the arguments during the hearing the Counsel also submitted written submissions dated 04/02/16 which were received by the Appellate Bench on 09/02/16 wherein the Counsel submitted that the case of Appellants falls under the category of "hardship cases", so they should not be penalized and the Impugned Order should be set aside. The Appellants cannot take plea of hardship as they were free to disclose to the shareholders and the Respondent the mode of sale of the assets and the Appellant has no bar or restriction to get approval in this regard. However the Appellants have failed to discharge their duties to enable the shareholders to take informed decision with respect to investment in an associated company and sale of assets.

15. The Respondent has taken a lenient view while adjudicating the issue in hand and imposed fine under section 492 of the Ordinance, whereas warring was issued for the violation of section 208 of the Ordinance although the violation of section 208 was also established. In our view the Appellants have breached the fiduciary duty by not complying the requirements of relevant laws; therefore the Respondent was also required to penalize the Appellants for violation of section 208 of the Ordinance. The Appellants have intentionally avoided compliance of the Ordinance. As per case law cited as 1987 MLD 3039, the legal duty or liability is always needed to be discharged by the person required by law and if not complied, the presumption will be that he has done so

willfully. Therefore, when a requirement of a statute has been violated then there is no need to establish malafide or mens rea to prove the non-compliance of the provisions.

16. A law is not an object to get the desired results without observing due process and requirements, rather it is a set of rules and every rule should be followed to get the desired results. To administer the justice, law should be followed in its totality. The Appellants have violated the express provisions of law, which cannot be tolerated to ensure justice and rule of law. As matter of fact the misstatements referred in the Impugned Order are material. The jurisprudence has envisaged a principle for administration of justice which requires that "If law requires that an act must be done in a particular way, it should be done in that manner as prescribed by law."

17. In the above circumstances, in addition to fine imposed under section 492 of the Ordinance through the Impugned Order, we find it appropriate to convert the warning for violation of section 208 of the Ordinance into fine. Therefore, in exercise of the powers conferred by rule 17(5) of the Securities and Exchange Commission of Pakistan (Appellate Bench Procedure) Rules, 2003, we hereby impose an aggregate fine of Rs.200,000/-(Rupees two hundred thousand only) on Appellants 1 to 8. The Appellants are directed to deposit the fines in the following manner:

S. No	Name of Appellants	Amount of Fine (Rs.)
1.	Mr. Ashfaq Ahmed, Chief Executive	25,000
2.	Mr. Saqib Ashfaq, Director	25,000
3.	Mr. Amir Ashfaq, Director	25,000
4.	Mr. Niaz Muhammad, Director	25,000
5.	Mr. M. Farooq, Director	25,000
6.	Mr. Iklaq Hussain, Director	25,000
7.	Mr. Saleem Abbas, Director	25,000
8.	Mr. Sarfraz, Company Secretary	25,000
	Total	200,000

18. The aforesaid fine for violation of section 208 of the Ordinance and fine imposed through the Impugned Order under section 492 of the Ordinance must be deposited in the designated bank account maintained with MCB Bank Limited in the name of the "Securities and Exchange Commission of Pakistan" within sixty days from the receipt of this order and furnish the challan to the Respondent, as evidence of deposit of fine. In case of non-deposit of fine, the Respondent is directed to initiate proceedings for recovery of the fines as arrears of land revenue. The aforesaid fine has been imposed on the directors and secretary of Appellant No.9 in their personal capacity.

19. In view of the above the Impugned Order dated 18/11/15 has been upheld with the conversion of warning under section 208, into fine, therefore appeal is dismissed and Respondent is directed to comply with the direction contained in para above, if needed.

20. Parties to bear their own cost.

(Fida Hussain Samoo)
Commissioner (Insurance)

(Zafar Abdullah)
Commissioner (SCD)

Announced on: 05 APR 2016