Securities and Exchange Commission of Pakistan

BEFORE APPELLATE BENCH NO. IV

In the matter of

Appeal No. 48 of 2017

Next Capital Limited

Appellant

Versus

The Commissioner Corporate Supervision Department (CLD), SECP.

Respondent

Date of hearing: 14/09/17

Present:

For Appellant:

i. Mr. Vaseeq Khalid, Advocate.
ii. Mr. Muhammad Najam Ali, CEO

For Respondent:

i. Ms. Amina Aziz, Director (CSD)
ii. Ms. Zohra Sarwar, AJD (CSD)

ORDER

1. This Order shall dispose of Appeal No.48 of 2017, registered on 06/07/17 (the Appeal), under section 33 of the Securities and Exchange Commission of Pakistan Act, 1997 against the Order dated 19/05/17 (the Impugned Order) passed by the Respondent under Section 86(1) of the Companies Ordinance 1984 (the Ordinance) whereby, the application dated 28/02/17 of the Next Capital Limited (the Application) for permission

to issue shares otherwise than as right shares to its Chief Executive Officer Mr. Muhammad Najam Ali (the CEO) was rejected.

2. Brief facts of the case are that Next Capital Limited (the Appellant) passed a special resolution on 13/09/11(the Resolution) whereby, the CEO was granted an option to subscribe the 2.00 million ordinary shares of the Appellant at Rs. 10 each (the Option). In view of the Resolution the Appellant entered into a stock option Agreement with the CEO on 07/10/11, which was amended on 06/03/12 (the Agreements). As per the Agreements the CEO had right to subscribe 2.00 million shares of the Appellant within a period of five and half years starting after one year from date of listing at stock exchange. The record shows that soon after passing the Resolution, the Appellant had approached the Securities and Exchange Commission of Pakistan (the Commission) vide application dated November 4, 2011 for approval of the Option however, the Appellant was advised vide letter dated 24/11/11 to approach the Commission at the time Board of Directors of the Appellant (the BOD) decides to issue shares to the CEO. The BOD in its meeting held on 02/02/17 had decided to issue the Option and in this regard the Appellant filed an Application for Commission's approval under first proviso to Section 86 (1) of the Ordinance, however, the Application was rejected by the Respondent vide Impugned Order.

3. The Appellate Bench (the Bench) has heard the parties (Appellant and Respondent) at length and perused the relevant record. On behalf of the Appellant case was argued by the CEO and a legal representative. They have *inter alia* stated that relevant disclosures regarding the Option were made in the Agreements and in the prospectus of the Appellant. They stated that the BOD had considered and shareholders had approved the Option in lieu of CEO's services towards the establishment of the Appellant and initiation of its operations. They also argued that listing does not invalidate prior agreements of the Appellant. Whereas, the Respondent's representative while reiterating the submissions made through the written comments dated 27/07/17, stated that in 2011 eleven shareholders having 100% shareholding, had passed the Resolution and now, as

on December 2016, shareholding status has been changed considerably and only six out of eleven are the shareholders of the Appellant. These six shareholders including the CEO hold 47% of the shareholding, meaning thereby that express approval from the other shareholders having 53% shareholding has not been obtained for issuance of the Option. The Respondent also contended that the disclosures made in the prospectus and financial statements regarding the Option cannot be construed as obtaining approval of shareholders. Moreover, the Company failed to justify the specific benefits accrued to the shareholders rather in consequence of the Option, the dilution of shareholding has been acknowledged by the Appellant.

4. The facts of the case are interlinked with two factors or reasons which compelled the Respondent to pass the Impugned Order i.e. the Resolution passed by the Appellant being an unlisted company whereby the Option was granted to the CEO and other is dilution of the shareholding of existing shareholders as consequence of issuance of the Option. The Respondent is of the view that a fresh special resolution of the existing shareholders of the Appellant is required to allow the Option. The Respondent also consider the Option against the shareholders and Appellant interest. On the other hand, the Appellant has vehemently denied said two factors or reason and stated that the listing cannot redundant the Resolution passed by the shareholders prior to listing, therefore, fresh special resolution is not required and existing shareholders are well aware about the Option and dilution of their shareholding because said factor has been disclosed in the prospectus of and in all audited financial statements since 2011. The Appellant also contended that the existing shareholders have never objected the Option and they have never taken it as surprise.

5. In view of the arguments advanced by the parties and in the light of applicable legal framework, the assertions of the Respondent with respect to the Resolution cannot be acceded to. The Resolution was passed without any defect therefore, it cannot be invalidated on the ground that it was passed by the Appellant prior to acquiring the listing status. While questioning the validity of the Resolution the Respondent has failed to refer

any law or provision to declare it void or defective. The Bench is of the view that the disclosures made by the Appellant in its prospectus and audited financial statements of seven years have turned the fortune in Appellant's favor. Therefore, we find no reason to support an apprehension that the approval of the Option would be detrimental to the rights of the Appellant's shareholders. We believe that the sanctity is attached with Resolution therefore, it should be honored.

6. The Bench finds it appropriate to discuss the analysis of the Respondent about the current status of the shareholders and who passed the Resolution. The conclusion drawn by the Respondent in this regard is erroneous in nature. As per record eleven shareholders including the CEO passed the Resolution and they had 100% shareholding and currently only six out of eleven are the shareholder with 47% shareholding. Respondents' observation that the express consent of the new shareholders having 53% shareholding is necessary to execute Option, is not based on legal reasoning, therefore, we do not accept this observation. The Bench wants to make it clear that the Agreements entered by the Appellant are binding on it and for their execution, presence of all or any one of the shareholders who consented for such agreements through a special resolution is not required. Therefore, decrease in shareholding and number of shareholders who passed the Resolution and inclusion of new shareholders having majority shareholding cannot be construed as nullity of the Resolution.

7. The perusal of the record has revealed that the Appellant has made appropriate disclosure in prospectus whereby it has been clearly mentioned that the issuance of shares against the Option would result in dilution of shareholding of the existing shareholders. In note III at page 24 of the prospectus the disclosure has been made in the following manner;

> *"……to issue shares against the exercise of option by Mr. Najam, interest of the shareholders may be adversely affected in the form of dilution of their shareholding and decrease in the breakup value per share……"*

Furthermore, under the heading of "Risk Factor: at page 40 of the prospectus the impact of the Option has been explained in the following manner;

RISKS	DESCRIPTION	MITIGANTS
Dilution	Risk of dilution in case of Stock Option exercised by Mr. Najam Ali. For instance, if Stock Option will be exercised to the maximum of 2 million shares, the dilution will be 8.16% of the total paid up shares of 24.5 million.	No mitigant exists for dilution in shareholding with the exercise of the stock option. However, the effect of dilution will be insignificant and the exercise of the option would reflect confidence in the Company enabling shareholders to benefit from the future growth.

In addition to above, the Appellant has also explained about the Agreements under the heading "8.12 MATERIAL CONTRACTS/DOCUMENTS" at page 59 to 61 of the prospectus. The Appellant has also made the disclosure about the Option in note 26.2 at page 38 of the Annual Report 2016.

8. The record manifest that in response to the Appellant's application for approval of the Option in 2011, the Commission advised the Appellant to file an application once the BOD had decided to issue the Option. However, the Commission had not imposed any other condition. Therefore, in view of the disclosures made in the Prospectus, audited financial statements and BOD decision dated 02/02/17, we hereby set aside the Impugned Order and allow the Appeal as per prayer contained in para seven of the Appeal.

9. Parties to bear their own cost.

(Fida Hussain Samoo)
Commissioner (Insurance)

(Tahir Mahmood)
Commissioner (CCD-CLD)

Announced on: 26 SEP 2017