



# Securities and Exchange Commission of Pakistan

## **BEFORE THE APPELLATE BENCH**

IN THE MATTER OF

### **APPEAL No. 84 OF 2019**

(Against Order Dated 30-09-2019 passed by ED-CSD, SECP)

**DIRECTORS OF CHAKWAL SPINNING MILLS LIMITED**

**... APPELLANT(S)**

**V E R S U S**

**EXECUTIVE DIRECTOR, CORPORATE SUPERVISION DEPARTMENT, SECP**

**... RESPONDENT(S)**

**Date of hearing:**

October 14, 2021

**Present: (Via Video-Link)**

**For the Appellant(s):**

Mr. Nadeem Anwar, Company Secretary, Chakwal Spinning Mills Limited

**For the Respondent(s):**

Mr. Amir Saleem, Additional Director, Adjudication Department – I, SECP

## **ORDER**

1. This Order shall dispose of Appeal No. 84 of 2019, filed by the Directors of Chakwal Spinning Mills Limited (the “**Appellants**”), under Section 33 of the Securities and Exchange Commission of Pakistan Act, 1997 (the “**Act**”), against Order dated 30-09-2019 (the “**Impugned Order**”), passed by the Respondent, where the Appellants are aggrieved.



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2. Brief facts of the case are that review of the financial statements, for the period ended on 31-12-2017 of Chakwal Spinning Mills Limited (the “**Company**”), revealed that the Company leased out the entire production facility to M/s. Yousuf Weaving Mills Limited (“**YWML**”), an associated company, without obtaining prior approval of the shareholders in terms of section 183(3)(a) of the Act.
3. Furthermore, the minutes of the meeting of the Board of Directors of the Company held on 10-11-2017 (the “**Board Meeting**”) revealed that five of the eight directors, who attended the said Board Meeting, were interested directors by virtue of common directorship and shareholding. Out of these five interested directors, three directors (Khawaja Mohammad Kaleem, Khawaja Mohammad Jawed and Mohammad Tariq Sufi) disclosed their interest and did not participate in discussion or voting. However, the remaining two directors (Khawaja Mohammad Jahangir and Khawaja Mohammad Tanveer) neither disclosed their interest, nor abstained from voting while approving the lease arrangement with YWML, hence, contravened the requirements under section 205 and 207 of the Act.
4. Moreover, since five of the eight directors in the Board Meeting were interested directors, therefore, the quorum was also insufficient in terms of section 176 of the Act.
5. It is also noted that a post-facto approval / ratification from the shareholders of the Company was obtained for the lease arrangement of the entire production facility with YWML in the Annual General Meeting (**AGM**) held on 27-11-2018.
6. As a consequence of the proceedings initiated through the Show Cause Notice (**SCN**) dated April 26, 2019, penalties were imposed through the Impugned Order on all the 8 Appellants in terms of Section 183 of the Act. The Appellants, being aggrieved by the Impugned Order, preferred this Appeal.
7. Learned representative for the Appellants mainly pressed upon the point that the Company in its AGM held on 17-11-2018, obtained approval of the lease arrangement with YWML from members of the Company, hence, fully complied with section 183(3)(a) of the Act. Thus, the imposition of penalty, when the members have consented to the lease arrangement with YWML,





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is unjustified. Since members of the Company endorsed the earlier decision of the Board in relation to the lease arrangement with YWML, therefore, the directors concerned must not be held accountable.

8. Learned representative of the Appellants also argued that since the Company had closed its operations and production had ceased, therefore the directors acted promptly to save the machinery from deterioration and keep the Company assets in operation. Such actions of the directors not only saved jobs of a large number of workers and employees of the Company, but also strengthened confidence of the suppliers and shareholders. Hence, since earlier decision of directors regarding the lease arrangement with YWML did not cause any damage or loss to the Company, and in the presence of a valid approval of the members in accordance with the requirements of the Act, it was prayed that the penalty imposed on the directors be set aside.
9. On the other hand, learned representative for the Respondent rebutted arguments of the Appellants, *inter-alia*, that the Appellants were non-compliant with the requirements of section 183(3)(a) of the Act which makes it mandatory upon the board of a company not to sell, lease or dispose of the undertakings, unless it has obtained consent of members in the general meeting.
10. In the present case, the Appellants being directors of the Company, failed to seek approval of the shareholders thereby clearly violating the provisions of section 183(3)(a) of the Act. Subsequently, the Appellants placed the matter for ratification / validation of the lease agreement in its AGM held on 27-11-2018 i.e. after a lapse of one year from the date of the lease arrangement. This also shows that the Appellants were aware of the requirements and the requisite approval, which they obtained subsequently rather than the mandatory prior consent required under the Act. Hence, the Appellants were non-compliant with the explicit requirements of section 183(3)(a) of the Act by failing to obtain prior approval of shareholders for the subject lease arrangement with YWML.
11. Learned representative of the Respondent further submitted that quorum of the Board Meeting, comprising of the Appellants, held on 10-11-2017, where the subject lease arrangement with YWML was approved, was incomplete in terms of section 176 of the Act. The lack of quorum was based upon the fact that out of eight directors, five were interested directors by virtue of



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common directorship and shareholding. Moreover, it was submitted that the Appellants contravened sections 205 and 207 of the Act, as section 205 requires disclosure of interest by directors and section 207 of the Act pertains to interested directors not to participate or vote in proceedings of the Board. In the instant matter, two of the directors neither disclosed their interest, nor abstained from voting while approving the lease arrangement with YWML. Section 207 of the Act also states that if majority of the directors are interested in any contract or arrangement entered into on behalf of the company, the matter shall be laid before the general meeting for approval. Hence, section 207 was also not complied as the matter was not placed before the members in a general meeting.

12. In light of the arguments put forth by the representative of the Respondent, it was contended that the assertion of the Appellants that the Board of directors was empowered to approve the subject lease arrangement with YWML is misconstrued and the Board of Directors had failed to obtain prior approval from members of the Company and other requirements of the provisions under the Act. Hence, a token penalty was imposed after considering the post facto approval / ratification from the shareholders upon the Appellants for violating the provisions of section 183 of the Act only, is reasonable and appropriate.
13. **The Appellate Bench** (the “**Bench**”) has heard the parties and perused the record. Representatives of the Appellants and the Respondent reiterated their grounds of appeal and rebuttal thereof.
14. The basic contention in the instant matter relates to the penalty imposed upon the Appellants under section 183 of the Act only. Therefore, the matter was reviewed in light of the facts and arguments put forth by the Appellants and the Respondent, as to whether there was any contravention of this section which subsequently led to imposing of the penalties.
15. There is no denying the fact that the lease arrangement with YWML by the directors during the Board Meeting held on 10-11-2017 without approval of the shareholders was in clear contravention to the provisions under section 183 of the Act. Contention of the Appellants that subsequent approval from the shareholders of the Company was obtained, cannot be considered as a defense to the violations already committed. The mandatory prior approval of the members





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within the four corners of section 183 of the Act for any lease arrangement was a prerequisite which was not complied with in the present case. Hence, without the need to go into any further details, the fact of the matter remains simple, which is that section 183 of the Act was contravened and the Appellants were penalized accordingly.

16. It is pertinent to mention here that, generally, directors have a fiduciary responsibility to show utmost loyalty and care towards the company and its shareholders. Directors are required to put the interests of the company and its shareholders over their own personal interests while making decisions for and on behalf of the company. Thus, wherever personal interests of the directors come in conflict with the affairs of the company, strict implementation of the given laws must be adhered.

17. In light of the above, this appeal has no merits which is hereby dismissed. Impugned Order dated 30-09-2019 is maintained and upheld for the penalty imposed under section 183 of the Act.

(Sadia Khan)  
Commissioner

(Farrukh Hamid Sabzwari)  
Commissioner

Announced on: **24 NOV 2021**