

Appellate Bench Orders

Before Appellate Bench No. 3

January 22, 2003

Before Appellate Bench No. 3 (Re-Constituted)
In the matter of
Appeal No. 71 of 2002

Quality Steel Works Ltd.
D/22, S.I.T.E
Manghopir Road
Karachi – 75700

..... Petitioner

Versus

Executive Director (EMD) SEC

..... Respondent

Date of Impugned Order

November 04, 2002

Date of Hearing of Revision

January 07, 2003

Present:

For the Company

1. Dr. Muhammad Azam Chaudhry, Advocate
2. Mr. Farooq Akhtar
3. Mr. Muhammad Ziauddin
4. Mr. Masood Ali

For the Respondent

1. Mr. Ashfaq Ahmed Khan (Director)
2. Mr. Mubasher Saeed (Joint Director)
3. Ms. Amina Aziz (Deputy Director)
4. Ms. Sumaira Siddiqui (Deputy Director)

Order

This order will dispose off the present revision petition filed under section 484 of the Companies Ordinance, 1984 (the "Ordinance") by the Petitioner against the Order dated November 04, 2002 (the "Impugned Order") passed by the Executive Director (Enforcement & Monitoring).

1. Brief facts leading to this revision petition are that a notice dated April 08, 2002 was issued by the Commission to the Company (Petitioner herein) and its Chief Executive calling upon them to show cause as to why an inspector under clause (b) of section 265 of the Ordinance may not be appointed to investigate into the affairs of the Company. The past history of the Company showed that it had not held its Annual General Meetings (the "AGM") for the calendar years 1999, 2000 and 2001 and had also failed to present therein its annual audited accounts for the year ended June 30, 1999, 2000 and 2001. The Company had also failed to comply with the statutory requirements of holding of election of directors, appointments of its Chief Executive and the appointment of auditors. The latest available financial statements of the Company at the time of issue of show cause notice were for the year ended June 30, 1998, which gave a dismal financial picture of the Company. The Company, as of June 30, 1998, had accumulated losses to the tune of Rs.214.309 million against its paid up capital of Rs.17.717 million, which meant that its current liabilities exceeded its current assets. The auditors of the Company had given serious observations, which indicated imprudent management of the affairs of the Company. They had raised their doubts about the Company's ability to continue as a going concern in view of the accumulated losses, which were more than 12 times its equity.

2. An opportunity of hearing before the Respondent (the "Executive Director") was provided to the Company on June 05, 2002. The Chief Executive of the Company in its defence contended that the Company was technically insolvent when it was handed over to the present management by the Privatization Commission, however, due to policies of the present management, the Company was making a turn around. The Executive Director, not being convinced by the contentions of the Company, held that circumstances provided a substantial basis for an investigation by an inspector under;

(a) Sub-clause (i) of Clause (b) of Section 265 - The business of the Company is being conducted in a manner oppressive to its members.

(b) Sub-clause (iii) of Clause (b) of Section 265 - The affairs of the Company have been conducted or managed as to deprive the members thereof of a reasonable return.

(c) Sub-clause (iv) of Clause (b) of Section 265 - The members of the Company have not been given all the information with respect to its affairs, which they might reasonably expect.

(d) Sub-clause (vi) of Clause (b) of Section 265 - The affairs of the Company are not being managed in accordance with sound principles and prudent commercial practices.

(e) Sub-clause (vii) of Clause (b) of Section 265 - The financial position of the Company is such as to endanger its solvency.

3. Aggrieved by the Impugned Order, the Company has preferred this revision petition under section 484 of the Ordinance before this Bench. The Petitioner Company also filed an application under Order 39, Rule 1 & 2 read with section 151 of CPC for suspension of the Impugned Order till the final decision of the main revision petition. We were told by Mr. Mubasher Saeed, Joint Director appearing on

behalf of the Executive Director that the Company had initiated multiple proceedings in different High Courts against the Impugned Order, some of which were still pending. The Company had made an identical plea for stay of the Impugned Order till the final decision of the revision petition before us in the Hon'ble Sindh High Court, which was denied by the court. The main petition though was still pending before the Court.

4. Mr. Farooq Akhtar, appearing before us on behalf of the Company on the date of hearing, pleaded that the Company's stay application should be heard by the Bench before the main petition. The counsels were asked by the Bench to plead the application and the main petition together on the same date of hearing. In support of the stay application the counsels for the Company pleaded that if a stay against the Impugned Order was not granted by the Bench, the Company's right of appeal/revision would become infructuous as the investigation by the inspector may have been completed by the time the main petition is decided by the Bench. We are told by Mr. Ashfaq Ahmed Khan appearing on behalf of the Executive Director that the investigation by the Inspector is required to be completed by February 19, 2003. As the Bench intended to dispose of the main petition much before the said date, we found that there is no merit left in the contention of the Company. This order therefore will dispose off both, the application and the main petition.

5. In support of the revision petition the counsels for the Company argued that the Executive Director had imposed the severest penalties on the Company for defaults under other statutory provisions of the Ordinance, which would result in strangulation of the Company. They further stated that most of the grounds for appointment of the inspector provided under the provisions of the Ordinance were either not there at the time of passing of the Impugned Order or had been removed since then. They alleged that the reason why an inspector has been appointed is to dig out additional violations or defaults of the Company and the management in order to punish them further. They contended that the present management was not responsible for most of the defaults, which have been made the ground for action by the Executive Director. They also stated that the Company's losses of Rs.148.471 million incurred during the last two years under the Government control were restricted to Rs.104.670 million after take over by the present management which proved that the financial position of the Company is not such as to endanger its solvency. They argued that the business of the Company has never been conducted in a manner oppressive to its members and the Company has not deprived its shareholders of reasonable returns.

6. The counsels for the Company stated that the Impugned Order has been passed with mala fide motive of supporting the ex-owner of the Company namely Mr. Akbar Abdullah who holds only 0.2% of the shares of the Company. They contended that the proceedings against the Company were started only on the behest of and to please Mr. Akbar Abdullah. They stated that they have been refused the inspection of the complaints against the Company kept with the Commission in violation of section 20(6)(f) of the Securities & Exchange Commission of Pakistan Act 1997 to find out the details of the applications filed by Mr. Abdullah. They also objected to the appointment of a Lahore based Chartered Accountant as an inspector to investigate the affairs of the Company. The counsels also contended that the Executive Director does not have the authority to appoint an inspector and the Appellate Bench does not have the power to hear the matter as winding up proceedings were pending against the Company in the High Court.

7. Mr. Ashfaq Ahmed Khan appearing on behalf of the Executive Director contended that the action of appointment of inspector was taken suo moto by the Executive Director keeping in view the worst financial position of the Company and serious observations made by the auditors. He stated that Mr. Akbar Abdullah has no nexus with the instant matter. The shortcomings and legal violations are the ingredients for mismanagement and are sufficient grounds for investigation of the Company. The accusation of the Company that all these actions are done to facilitate Mr. Akbar Abdullah, a shareholder of the Company is totally irrelevant. In fact, the Company is trying to shift the attention of the Bench from the actual issue and trying to defame the Regulator and its senior officers. He argued that the penalties imposed for various defaults committed under the provisions of the Ordinance itself indicate that the affairs of the Company have not been managed in accordance with sound business principles. He argued that the members of the Company have not been given information with respect to its affairs, which they might reasonably expect, which meant that the business of Company is being conducted in a manner oppressive to its members. He contended that the appointment of inspector is only a fact-finding exercise and it may be helpful in highlighting the areas, which need improvement.

8. We have heard both the parties and also examined the relevant provisions of the Ordinance and the material placed before us. As far as the Company's allegation of mala fide against the Executive Director is concerned, we note that the Company has, other than alleging the same, not provided any sort of evidence in support of his allegations. We therefore reject this allegation and would like to express our disapproval to the management and counsels of the Company for making such false and unsubstantiated allegations.

9. We also do not agree with the contention of the counsels of the Company that there exists no other reason for the appointment of the inspector other than to please a small shareholder of the Company. It is a matter of fact that the Company had failed to prepare and present its accounts to its shareholders since 1999 and failed to hold its AGM on time for four consecutive years since 1999. It is a matter of fact that the Company had failed to pay any dividend to its shareholders since its privatization other than in 1999. The Company can also not deny the fact that the auditors of the Company had reported serious irregularities committed by the management, which proved that the Company was not being managed in accordance with sound business principles and in a prudent commercial manner. The decision to appoint an inspector to investigate the affairs of the Company was made in light of all of this and not on the whims of any one person. It is also clear that the Executive Director is authorized to make such a decision suo motto under the provisions of clause (b) of section 265 of the Ordinance.

10. With regards to the counsels' contention that the Executive Director has denied inspection of the record of the Company kept with the Commission, we are of the view that the complaints filed against the Company do not constitute public record and the Commission is not required to show those documents to the Company. In any case, we cannot comprehend how the refusal to show these documents affects the Company's working or its ability to conduct itself in a prudent commercial manner. Nor, in our opinion, does it help the Company in any way to defend itself better before us. This issue is therefore, irrelevant to these proceedings.

11. As for the counsels' contention that due to pending winding up proceedings against the Company before the Hon'ble High Court, the Appellate Bench does not have the power to hear this matter, we are of the view that it is best that this matter is taken up before the Hon'ble High Court.

12. In our opinion, the appointment of an inspector to investigate the affairs of a Company does not amount to a penalty or punishment. We cannot help but agree with the opinion of the Executive Director that the investigation is only a fact-finding exercise to reach the truth of the matter. In fact it is our considered view that this investigation will help the Company and its management in improving the working of the Company.

In light of the submissions of the parties, examination of records and the above findings, we uphold the order of the Executive Director (Enforcement & Monitoring) dated November 04, 2002.

This revision petition is accordingly dismissed.

(ETRAT H. RIZVI)
Commissioner (Insurance)

(SHAHID GHAFAR)
Commissioner (Securities Market)

Islamabad

Announced: January 22, 2003