

2013 C L D 28

Securities and Exchange Commission of Pakistan

Before Muhammad Ali, Chairman and Mohammed ASIF Arif Commissioner (Insurance)

GHULAM MUHAMMAD MALKANI-Appellant

VERSUS

DIRECTOR (ENFORCEMENT), SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN---

Respondent

Appeal No. 57 of 2011, decided on 31st May, 2012.

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[Companies Ordinance (XLVII of 1984)]----Sections 195, 196(3)(b) & 473---Securities and Exchange Commission of Pakistan Act (XLII of 1997), S.33---Powers of the Directors of the company to give relief or to give extension of time for the repayment of outstanding debt---Amount of Rs.33,674,564.00, was receivable from 'spouse' of appellant/Chief Executive of the company- She had traded in shares through her equity trading account which was maintained with the company--Show-cause notice was issued to the appellant under S.196(3)(b) of the Companies Ordinance, 1984, which had restricted the powers of the Directors of a public company to remit, give any relief or give extension of time for the repayment of any debt outstanding against their spouse and minor children without consent of the shareholders in a general meeting---Appellant had provided to the Commission an undertaking by spouse of the appellant regarding repayment of the outstanding amount in a minimum monthly installment of Rs.100,000---Said undertaking could not over-rule the requirement of law and the consent of the shareholders in general meeting, could not be dispensed with---Penalty imposed on the appellant/Chief Executive Officer, was upheld.

Ghulam Muhammad Malkani, Appellant present

Abid Hussain, Director for Respondent

Amir Saleem, Deputy-Director, Department Representative.

Date of hearing: 14th February, 2012.

ORDER

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This order is in Appeal No. 57 of 2011 filed under section 33 of the Securities and Exchange Commission of Pakistan (the "Commission") Act, 1997 against the Order dated 26-04-2011 (the "Impugned Order") passed by the respondent.

2. The facts leading to the case are that on perusal of the annual audited accounts of Messrs J.S. Global Capital Limited (the "Company") for the financial year ended 30-06-2009 (the "Accounts"), it was observed that an amount of Rs.33,674,564.00 was receivable from Mrs. Rubina Malkani, "spouse" of the then Chief Executive of the Company, Mr. G.M. Malkani (the "Appellant"). Mrs. Malkani had traded in shares through her equity trading account No.00858 which was maintained with the Company. Mrs. Malkani's equity trading account was opened on 19-08-2008 and on that day she had a debit balance of Rs.1,606,822.03.

3. Show cause notice ("SCN") dated 18-08-2010 was issued under section 196(3)(b) of the Companies Ordinance, 1984 (the "Ordinance"). The aforementioned provision restricts the powers of the directors of a public company or of a subsidiary of a public company to remit, give any relief or give extension of time for the repayment of any debt outstanding against their spouse and minor children, as specified in section 195(1) of the Ordinance, without consent of the

shareholders in a general meeting. In response to the SCN, the authorized representative of the appellant submitted a written reply dated 25-09-2010 that the Appellant has not given any loans or advances to his spouse nor any debt was outstanding against her as envisaged under section 196(3)(b) of the Ordinance. It was further argued that the amount was receivable against a normal business transaction which was not prohibited under the Ordinance. The reply to the SCN was not found satisfactory and hearing in the matter was held on 13-04-2011. The Respondent passed the Impugned Order and imposed a penalty of Rs.50,000 for violation of section 196(3)(b) of the Ordinance and directed the appellant in terms of section 473 of the Ordinance to undo the default by depositing the outstanding amount within 90 days from the date of the Impugned Order.

4. The Appellant preferred the instant appeal against the Impugned Order, The Appellant argued that:-

- (a) Mrs. Malkani had traded in shares through the Company and was maintaining an equity trading account No. 00858 with the Company since 18-02-2002. The account of Mrs. Malkani remained in credit right from the inception till 19-08-2008. No loan, advance or credit was ever granted by the Company to Mrs. Malkani for the purpose of trading in shares or otherwise;
- (b) the debit balance of Rs.33,674,564 as reflected in the financial statements of the Company for the year 30-06-2009 had occurred due to losses suffered by her on account of the application of Floor at the Karachi Stock Exchange and forced settlement of future contracts and Continuous funding system ("CFS") open positions. The amount was neither on account of any loan and advances, nor was a book debt. The debit balance had occurred only on 19-08-2008, when trading losses occurred abruptly due to reasons beyond anyone's control; and
- (c) Mrs. Malkani entered into an agreement with the Company to settle the outstanding amount of Rs.28,349,564. Mrs. Malkani has been making regular payments to the Company, in terms of the aforesaid agreement with the Company. The appellant was asked by the Appellate Bench (the "Bench") to present the agreement signed between Mrs. Malkani and the Company and the sub-ledger report of Mrs. Malkani maintained by the Company to show that the terms of agreement are being complied with.

5. The Respondent argued that the scheme of the law is very clear and section 196(3)(b) of the Ordinance prohibits directors of a public company or of a subsidiary of a public company to remit, give any relief or give extension of time for the repayment of any debt outstanding against any person, specified in section 195(1) of the Ordinance, without consent of the shareholders in a general meeting. The appellant as Chief Executive Officer of the Company should have recovered the outstanding amount from his wife as he was under a fiduciary duty not to give any relief for re- payment of debt without the consent of the shareholders in a general meeting. It was further argued that the loss. Incurred by Mrs. Malkani was not on account of the application of Floor at the Karachi Stock Exchange and forced settlement of future contracts and CFS open positions, instead. the loss was incurred as Mrs. Malkani traded during market closure and suffered loss as consequence of the trading activity. Reliance was placed on transactions after 25-08-2008 appearing in the sub-ledger report of Mrs. Malkani maintained by the Company.

6. We have heard the parties and have gone through the record. Section 195(1) and section 196(3)(b) are reproduced for ease of reference:--

195. Loans to directors, etc.-(1) Save as otherwise provided in subsection (2), no company, hereafter in this section referred to as "the lending company", shall, directly or indirectly, make any loan to, or give any guarantee or provide any security in connection with a loan made by any other person to, or to any other person by.—

- (a) any director of the lending company or of a company which is its holding company or any partner or relative of any such director;
- (b) any firm in which any such director or relative is a partner;
- (c) any private company of which any such director is a director or member;
- (d) any body corporate at a general meeting of which not less than twenty five per cent of the total voting power may be exercised or controlled by any such director or his relative, or by two or more such directors together or by their relatives; or
- (e) any body corporate, the directors or chief executive whereof are or is accustomed to act in accordance with the directions or instructions of the chief executive, or of any director or directors, of the lending company:

Provided that a company may, with the approval of the Commission, make a loan or give any guarantee or provide any security in connection with a loan made by any other person to a director who is in the whole-time employment of the company for the purpose of acquisition or construction of a dwelling house or land therefore or for defraying the cost of any conveyance for personal use or household effects or for defraying any expense on his medical treatment or the medical treatment of any relative as are ordinarily made or provided by the company to its employees.

Explanation.---"Relative" in relation to a director means his spouse and minor children.

196(3)(b) The directors of a public company or of a subsidiary of a public company shall not except with the consent of the general meeting either specifically or by way of an authorization, do any of the following things, namely.

- (a) sell, lease or otherwise dispose of the undertakings or a sizeable part thereof unless the main business of the company comprises of such selling or leasing; and
- (b) remit, give any relief or give extension of time for the repayment of any debt outstanding against any person specified in subsection (1) of section 195.

The appellant has correctly pointed out that Mrs. Malkani was trading shares through equity trading account No. 00858 with the Company since 18-02-2002. The contention of the appellant that the loss incurred by Mrs. Malkani was on account of imposition of Floor has been examined in light of the facts and the perusal of the sub-ledger report of Mrs. Malkani maintained by the Company. Mrs. Malkani had a credit balance of Rs. 1,590,303 on 02-09-2008 and the balance has remained in debit since 04-09-2008 till date. The Floor was imposed on 28-08-2008 and was lifted on 15-12-2008 and perusal of the sub-ledger report shows that during the imposition of Floor, the Appellant purchased securities including that of Jahangir Siddiqui and Co., as such, the contention that the loss was incurred merely due to the imposition of the Floor is not tenable.

Section 196(3)(b) of the Ordinance is attracted in cases where the directors of a public company without the consent of shareholders in the general meeting either specifically or by way of an authorization give relief or extension of time for the repayment of any debt outstanding against the directors spouse or minor children. The relief or extension of time for repayment of debt given to Mrs. Malkani could only have been allowed with the consent of the shareholders in the general meeting in terms of section 196(3) of the Ordinance. The Appellant has provided to the Bench an undertaking by Mrs. Malkani dated 26-07-2010 regarding repayment of the outstanding amount in a minimum monthly installment of Rs. 100,000. The undertaking cannot over rule the requirement of law, as such. the consent of shareholders in general meeting cannot be dispensed with.

In view of the above, the penalty on the CEO is upheld. In so far as the direction under section 473 of the Ordinance is concerned. we have been informed that the Company has instituted a recovery Suit No.334 of 2012 before the Sindh High Court, Karachi (the "Court"). Since, the issue of recovery from Mrs. Malkani has been taken up by the Court, the instant appeal is being disposed of Without dilating on the issue of recovery.