

2013 C L D 58

Securities and Exchange Commission of Pakistan

Before Imtiaz Haider, Commissioner (SMD) and Mohammed Asif Arif, Commissioner (Insurance)

OLYMPIA SPINNING AND WEAVING MILIE: LIMITED---Appellant

VERSUS

EXECUTIVE DIRECTOR (ENFORCEMENT)---Respondent

Appeal No. 1 of 2010, decided on 13th July, 2012.

Muhammad Anas Makhdoom. Barrister-at-law and Waqar Monnoo, CEO for Appellant.

Shahzad Afzal, Joint Director (Enforcement) and Haris Bin Tippto, Deputy Director (Enforcement) for Respondent.

Date of hearing: 20th April, 2012. A

ORDER

Appeal dismissed

Companies Ordinance (XLVII of 1984)---S. 492---False statement--Contravention of S.492 of Companies Ordinance, 1984 was not a criminal offence, but contravention of S.492 would attract imposition of penalty by the Commission---Ingredients of criminal offence, need not be established in order to impose penalty under S. 492 of Companies Ordinance, 1984, it was sufficient to prove that the contravention was made knowingly.

AIR (36) 1949 Madras 657, [1967] 37 Com Cas. 790; AIR 1929 Bombay 443 and Messrs Gharibwal Cement Limited and others v. Executive Director (Enforcement and Monitoring), Securities and Exchange Commission of Pakistan 2003 CLD 131 ref.

This order shall dispose of Appeal No.1 of 2010 filed under section 33 of the Securities and Exchange Commission of Pakistan [the "Commission"] Act, 1997 against the order dated 26-11-2009 (the "Impugned Order") passed by the respondent.

2. The facts leading to the case are that in February 2008, an Extraordinary General Meeting ("EOGM") of the Olympia Spinning and Weaving Mills Ltd. (the "Company") was called to seek approval of shareholders in terms of section 208 of the Companies Ordinance, 1984 (the "Ordinance"). EOGM was called to approve a transaction, wherein, the Company had provided cross corporate guarantee (the "Bank Guarantee") to Bank Alfalah Limited (the "Bank") in respect of a long term finance facility availed by Olympia Power Generation (Pvt.) Limited ("OPGPL"), an associated company with common directorship. The Commission while examining the notice of EOGM cautioned the directors ,of the Company that the proposed business should not be undertaken as section 195 of the Ordinance expressly bars such an arrangement, unless relationship between the two entities is that of parent and subsidiary companies. In order to regularize the aforesaid arrangement, each of the three directors of OPGPL who were also directors in the Company, gifted 3000 shares of OPGPL to the Company, thereby establishing a parent-subsidiary relationship between the two companies. On 27-06-2009 the Board of Directors ("BoD") of the Company, however, acting on behalf of the Company resolved to gift back to themselves 9000 shares of OPGPL held by the Company and entered deeds for declaration and confirmation of oral gift dated 27-06-2009. The fact was intimated to the Karachi Stock Exchange on 29-06-2009 and a copy was sent to the Commission. The aforesaid events raised concerns about the manner in which the Company affairs were being conducted by the directors of the Company and it was considered necessary to investigate the entire events along with the underlying documents to identify any violations of law including any ultra vires acts. The

examination of the underlying documentary evidence revealed that the Bank Guarantee had in fact been given in January 2007 and was still outstanding. Moreover, the Board of Directors ("BoD") meeting for returning back the shares of OPGPL to themselves was held in the absence of quorum as three out of the five directors approving the aforesaid business were interested in it and this fact was neither disclosed nor did they refrain from casting their vote in accordance with the provisions of the Ordinance. The aforesaid acts indicated violation of provisions of sections 214, 216, 193, 492 and 496 of the Ordinance. 3. Show cause notice dated 27-8-2009 (the "S'CN") was issued to the directors. The reply was submitted by M. Waqar Monnoo, Chairman and Chief Executive of the Company and hearing in the matter was held. The respondent dissatisfied with the response of the directors passed the Impugned Order and imposed total penalty of Rs.35.80,000 for violation of sections 492, 193, 214 and 216 of the Ordinance.

4. The appellant dissatisfied with the Impugned Order has preferred the instant appeal. The appellant counsel argued that:-

- (a) the majority shareholders of the Company decided to establish a captive power project namely OPGPL of a capacity of 8 MW for exclusive supply of electricity to the Company. The application was made to National Electric Power Regulatory Authority, which was pleased to grant license to OPGPL for generation of electricity. Each of the three directors of OPGPL subscribed to 5000 shares and all three directors of OPGPL were also elected as directors of the Company. In order to finance the establishment of the power plant, OPGPL arranged financing from the Bank on Islamic financing basis. In order to avail the benefit of concessional rates of interest available under the State Bank of Pakistan scheme for long term export oriented finance (LFT) for textile industry, OPGPL requested the Bank to transfer financing to the LFT Scheme. The Bank required OPGPL to provide certain security for the swap of outstanding liability from Islamic financing to the LFT Scheme, including the execution of Bank Guarantee from the Company. The aforesaid Bank Guarantee was signed on 15-1-2007 to order to convert the LFT Scheme. It was an time that the Bank effect after the legal law are fully met. The cover the paper work in outstanding finance into the accepted position at that Guarantee shall come into requirements set out in the Company in accordance with the requirement of section 208 of the Ordinance convened an EOGM and the shareholders of the Company authorized the Company to provide Bank Guarantee to OPGPL on 12-02-2008:
- (b) the directors of the Company did not make any misstatement as observed by the respondent in the Impugned Order. The Bank Guarantee was actually executed on 12-02-2008 and not on 15-01-2007 as contended by the Respondent. Reliance was placed on letter dated 01-09-2007, Wherein, the Bank did not mention the Guarantee as contingent liability of OPGPL. Further it was contended that section 492 of the Ordinance is a criminal offence and one of the ingredients of the offence is mens rea i.e. guilty mind, which has not been proved by the respondent. Section 628 of the Companies Act, 1956 of India was quoted and it was argued that section 492 of the Ordinance is similar. Reliance was placed on AIR (36) 1949 Madras 657, [1967] 37 Com Cas.790, wherein it was held that in order to sustain an action under section 628 of the Companies Act, the prosecution must show that false statements were made in the balance-sheet knowing them to be false and with a dishonest intention. AIR 1929 Bombay 443 was relied upon, wherein, section 228 of the Companies Act 1913 was discussed section 492 of the Ordinance) and it was where a criminal offence is involved, has to be proved. Moreover, in order to penalty for false statement, loss caused to (similar to held that 'mens rea' attract the shareholders has to be proved; and

(c) the resolution to gift back 9000 shares of OPGPL held by the Company to the directors passed on 27-6-2009 was not acted upon and the shares were not transferred back in the names of the directors. The Company continues to hold 60% of the issued share capital of OPGPL and OPGPL is still a subsidiary of the Company. The penalty was imposed under sections 193, 214, 216 of the Ordinance despite the fact that the resolution was not implemented, therefore, the Impugned Order be set aside on this ground alone.

5. The department representatives argued that it is an admitted fact that the Bank Guarantee was signed on 15-1-2007. The Bank Guarantee took effect from the date of its signing and post facto approval was taken by the Company to comply with the requirement of section 208 of the Ordinance. The Company concealed the fact of furnishing Bank Guarantee in the financial accounts of the Company. The Bank Guarantee was not the liability of OPGPL, rather, it was liability of the Company, as such, the letter dated 1-9-2007 sent by the auditors of OPGPL was declared irrelevant by the respondent in the Impugned Order. Further, the resolution passed by the directors on 27-6-2009 was in contravention of sections 193, 214 and 216 of the Ordinance; as the Ordinance requires express disclosure of interest, which should have been documented in the minutes. 6. We have heard the parties and have gone through the record. Our findings on the issues are as under:--

(a) & (b) the Bank Guarantee was signed on signed on 15-01-2007. The directors of the Company had to show that Bank guarantee took effect from the date of EOGM and not from the date of signing. The directors of the Company have failed to demonstrate that the Bank Guarantee took effect from the date of EOGM, as such, the approval of EOGM can at best be treated as post facto approval. The law on the issue of prior approval of the shareholders in a general meeting was laid down in the case of Messrs Gharibwal Cement Limited and others v. Executive Director (Enforcement and Monitoring), Securities and Exchange Commission of Pakistan, 2003 CLD 131, where our predecessors decided the question on whether or not prior approval is required and have made a comparative analysis of the provision with the Indian Companies Act 1956; the relevant extract is reproduced for ease of reference:

“We have considered the arguments and rationale from both sides and closely examined the provision of section 208 under the Ordinance and section 372(4) under the Indian Companies Act. It needs to be appreciated that the principle of plain and ordinary meaning from reading of section 208 of the Ordinance appears none other than seeking prior permission of both the shareholders as well as the Commission. In our view the two provisions are distinguishable. The words "under the authority" as used in section 208 of the Ordinance are much stronger than the word "sanctioned" used in section 374 of the Indian Companies Act. In our view, by no stretch of imagination an act can be termed as "under the authority" when the authority is subsequently acquired. The appellant has also submitted his arguments regarding the interpretation and relevance of the word "prior" and "previous" "approval" which does not appear convincing to us. The expression "approval" has nowhere been used in section 208 of the Ordinance, therefore, applying the principle of plain and ordinary meaning and the principle of redundancy we should not read into a statute words that are not provided for. It is relevant to see the context in which a word is used and only then a word should be interpreted or a meaning can be assigned to it. To us, the plain and ordinary meaning of the words "under the authority" means having consent of the shareholders prior to investment.

On the issue of nature of liability under section 492 of the Ordinance, we have compared the provisions of section 492 of the Ordinance with section 628 of the Companies Act, 1956. The sections are reproduced for ease of reference:-

492. Penalty for false statement.---Whoever in any return, report, certificate, balance sheet, profit and loss account, income and expenditure account, prospectus, offer of shares, books of accounts, application, information or explanation required by or for the purposes of any of the provisions of this Ordinance or pursuant to an order or direction given under this Ordinance makes a statement which is false or incorrect in any material particular, or omits any material fact knowing it to be material, shall be punishable with fine not exceeding five hundred thousand rupees.

628. Penalty for false statement.--if in any return, report, certificate, balance sheet, prospectus, statement or other document required by or for the purposes of any of the provisions of this Act, any person makes a statement-

(a) which is false in any material particular, knowing it to be false;

(b) or which omits any material fact, knowing it to be material;

he shall, save as otherwise expressly provided in the Act, be punishable with an imprisonment for a term which may extend to two years, and shall also be liable to fine.

The contravention of section 492 of the Ordinance is not a criminal offence and contravention of the aforesaid section attracts imposition of penalty by the Commission, whereas, contravention of section 628 of the Companies Act, 1956 of India is criminal offence for which imprisonment in addition to fine is provided. In order to impose penalty under section 492 of the Ordinance, it is sufficient to prove that the contravention was made knowingly and ingredients of criminal offence need not be established; and

(c) the contention of the appellants counsel that the resolution to gift back 9000 shares of OPGPL held by the Company to the directors passed on 27-06-2009 was not acted upon and the shares were not transferred back in the names of the directors, as such the contravention of sections 193, 214, 216 of the Ordinance did not take place has been examined in light of the aforementioned sections, Which, have been reproduced for ease of reference:

193. Proceedings of directors.---(1) The quorum for a meeting of directors of a listed company shall not be less than one-third of their number or four, whichever is greater.

214. Disclosure of Interest by director.---(1) Every director of a company who is in any way, whether directly or indirectly, concerned or interested in any contract or arrangement entered into, or to be entered into, by or on behalf of the company shall disclose the nature of his concern or interest at a meeting of the directors:

216. Interested director not to participate or vote in proceedings of directors.---(1) No director of a company shall, as a director, take any part in the discussion of or vote on, any contract or arrangement entered into, or to be entered into by or on behalf of the company, if he is in any way, whether directly or indirectly, concerned or interested in the contract or arrangement, nor shall his presence count for the purpose of forming a quorum at the time of any such discussion or vote; and if he does vote, his vote shall be void.

The directors of the Company resolved in the BOD meeting dated 27-6-2009 that the 9000 shares of the OPGPL be gifted back to them. The resolution was passed in the BOD meeting where three out of five directors were interested in the resolution. The directors in complete

disregard of the legal provisions stated above not only failed to disclose their interest but also exercised their voting rights and passed the proposed resolution. The directors have not been penalized for non-implementation of the resolution; in fact the respondent in the Impugned Order had restrained the directors from implementing the aforesaid decision till such time the Bank guarantee given to the Bank is outstanding. The aforementioned sections were contravened at the time of passing of resolutions.

In view of the above, We do not see any reason to interfere with the Impugned Order. The appeal is dismissed with no order as to cost. The directors of the Company shall pay the penalty from their personal resources and not from the coffers of the Company.