



Securities and Exchange Commission of Pakistan

BEFORE APPELLATE BENCH NO. III

In the matter of

Appeal No. 20 of 2013

Syed Mohammad Rehan

...

Appellant

Versus

Head of Department (Enforcement)

...

Respondent

ORDER

Date of hearing

20/02/14

Present:

Appellant:

Mr. Syed Muhammad Rehan (S.M. Rehan & Co. Chartered Accountants)

Department representatives:

Mr. Bilal Rasul, Director (Enforcement)

Mr. Moeed Hassan, Assistant Director (Enforcement)



Securities and Exchange Commission of Pakistan

1. This order shall dispose of appeal No. 20 of 2013 filed under section 33 of the Securities and Exchange Commission of Pakistan (the "Commission") Act, 1997 against the order dated 04/03/13 (the "Impugned Order") passed by the Respondent.
2. The brief facts of the case are that the Enforcement Department (the "Department") of the Commission conducted an examination of accounts of Venus Chemicals Limited (the "Company") for the year ended 30/09/09 (the "Accounts") which revealed that S.M. Rehan and Co., Chartered Accountants (the "Auditor") issued an unqualified report (the "Report") on 05/01/10. The examination of the Accounts revealed that the Company had included sales of Rs. 324,000,000/- made to Trading Corporation of Pakistan ("TCP") including the advance received from TCP of Rs. 307,800,000/- against sale of 13,000 m. ton of sugar without raising sales tax invoice and in contravention to the adopted accounting policy of the Company and in contravention to the requirements of para 9.3 of Accounting and Financial Reporting Standard for medium-sized entities ("AFRS"). The disclosure made in Note 16.1 of the Accounts and the Accounting policy adopted by the Company is as follows:

"This includes sales to Trading Corporation of Pakistan of Rs. 324,000,000 (net of sales tax) including amounting to Rs. 307,800,000 of advance received from TCP against sale of 13,000 m. ton of sugar and this will be reported in sales tax return as per Chapter-V of the Sales tax Special Procedure Rules, 2007 at the time of removal of sugar from the mill premises. Sales tax is the responsibility of TCP."

The Company's policy regarding revenue recognition is as follows:

"Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be measured reliably."



Securities and Exchange Commission of Pakistan

Revenue is recorded on dispatch of goods. Income on investments, if any, is recorded on accrual basis. Profit from bank account is recognized on a time proportion basis."

3. The Company had recorded sales to TCP against the requirements of Para 9.3 of AFRS and the aforesaid accounting policy of the Company. The aforesaid cast doubt on the authenticity of the revenue reported in the Accounts and prima facie overstatement of profits of the Company. The Auditor had failed to report the aforesaid misstatement in his Report to the members and instead stated in his opinion that the Accounts give a true and fair view of the state of affairs of the Company and conform with the approved Accounting Standard as applicable in Pakistan.
4. Show Cause Notice dated 26/03/12 ("SCN") was issued to the Auditor requiring him to explain within fourteen days of the date of the SCN as to why necessary action may not be taken against him under section 260 of the Companies Ordinance, 1984 (the "Ordinance") for making defaults in complying with the provisions of section 255 of the Ordinance. The Auditor appeared for the hearing on 11/04/12 and submitted a written reply to the SCN at the time of hearing. In order to ascertain the facts, third party confirmation was obtained from TCP. In reply, TCP provided a contradictory statement and submitted that the TMK Sugar Mills is a project of Venus Chemicals (Pvt.) Ltd and TCP has dealt with them in purchase of sugar without any reference to Venus Chemical (Pvt.) Ltd. In order to obtain clarifications from the Auditor regarding the reply given by TCP, another hearing was fixed on 04/01/13. The Auditor appeared on the date of the hearing and submitted a written reply in which the submissions made by the Auditor vide his letter dated 11/04/12 were repeated. The Respondent, dissatisfied with the response of the Auditor, held that the Auditor had failed to perform the statutory obligations



Securities and Exchange Commission of Pakistan

by failing to report a material deviation from the Company's accounting policy and imposed a penalty of Rs.50,000 on the Auditor.

5. The Auditor has preferred to file the instant appeal against the Impugned Order. The Auditor argued that:

- a) the sale to TCP fully meets the criteria of sales (Bill and Hold) as contained in part B(1) of AFRS. Although, there is no requirement for any disclosure of "Bill and Hold" sale, still the same was done in order to provide complete knowledge to the users of the financial statements; and
- b) the Impugned Order is not maintainable in law as during the first hearing before the Respondent, a short judgment was announced in the form of a warning letter and the Impugned Order may be set aside on this ground alone.

6. The department representatives argued that:

- a) TCP has submitted to the department that the Company has failed to deliver sugar for which payment was already made. Further, the Company reversed the sales in subsequent year accounts for year ended 30/09/09 due to non-lifting of stock by TCP. Moreover, TCP informed the department that the Company was charging interest on outstanding balances due for stocks which it had failed to deliver. The Auditor has failed to perform alternative procedures and to bring the aforesaid to the knowledge of the members. The disclosure given by the Company in Note 16.1 of the Accounts depicts that the Company has recorded false sales to TCP which is against the requirements of Para 9.3 of Section 9: Revenue (Sale of Goods) of AFRS applicable on MSE's. Moreover, the Company's policy is silent on the "Bill and Hold"



Securities and Exchange Commission of Pakistan

sales. Therefore, the submission that the revenue of TCP is recognized on the basis of “Bill and Hold” is not acceptable; and

b) during the hearing before the Respondent on 11/04/12, a verbal warning was issued conditional upon confirmation received from TCP. However, the information provided by TCP contradicted the stance of the Appellant, thus, necessitating a further hearing in the matter, which was held on 04/01/13.

7. We have heard the parties. Our para-wise findings on the issues are as under:

- a) para 9.3 of Section 9: Revenue (Sale of Goods) of AFRS states, “ *Revenue from the sale of goods shall be recognized when all the following conditions have been satisfied;*
- a) *the entity has transferred to the buyer the significant risks and rewards of the ownership of the goods;*
 - b) *the entity retains neither continuing managerial involvement to the degree usually associated with ownership nor effective control over the goods sold;*
 - c) *the amount of revenue can be measured reliably; and*
 - d) *it is probable the economic benefits associated with the transaction will flow to the entity; and the costs incurred or to be incurred in respect of the transaction can be measured reliably.”*

The Company in its policy had disclosed the basis for the recognition of revenue in the books of accounts in accordance with Para 9.3 of Section 9: Revenue (Sale of Goods) of AFRS but had deviated from this policy rendering the accounts to be misstated. The Company policy states that, “...*Revenue is recorded on dispatch of goods...*” It had been confirmed by TCP to the department that revenue had been recorded in the Accounts



Securities and Exchange Commission of Pakistan

before the delivery was made to TCP. This has been further substantiated by reversal of sales in the subsequent year accounts for year ended 30/09/09. It is, therefore, affirmed that the Company had wrongly recognized sales in the Accounts and the Auditor had failed to report this in his Report to the members. The aforementioned overrides all the contentions of the Appellant with regard to the recognition of revenue on the “Bill and Hold” sales; and

- b) no order had been passed by the Respondent after the hearing on 11/04/12, only a verbal warning was issued which was conditional upon confirmation received from TCP regarding delivery of goods. However, the information provided by TCP contradicted the stance of the Appellant, thus, necessitating a further hearing in the matter, which was held on 04/01/13. The Impugned Order was passed only after the hearing was concluded on 04/01/13.

It is clear from the above that the Auditor had failed to perform his statutory obligations in violation of section 255 of the Ordinance by failing to report a material deviation from the Company’s Accounts. The penalty was, therefore, rightly imposed on the Auditor and we see no reason to interfere with the Impugned Order.

(Mohammed Asif Arif)
Commissioner (Insurance)

(Imtiaz Haider)
Commissioner (SCD)

Announced on: 14/7/14