



Securities and Exchange Commission of Pakistan

BEFORE APPELLATE BENCH NO. III

In the matter of

Appeal No. 38 of 2011

1. Mr. Habib Ahmad

2. Mr. Muhammad Rafiq

3. Mr. Zahid Rafiq

4. Mr. Khalid Rafiq

5. Mr. Shahid Rafiq

6. Mr. Sajid Rafiq

(All directors of Habib Rafiq (Pvt.) Ltd Appellants

Versus

Director (Enforcement) Respondent

ORDER

Date of hearing

11/12/13

Present:

For the Appellants:

Mr. Zafar Ullah Shah, FCA

Ms. Nudrat Sultana Alvi, Advocate

Department representatives: (through video conference)

Mr. Shahid Javed, Deputy Director (Enforcement)

Mr. Haroon Abdullah, Deputy Director (Enforcement)



Securities and Exchange Commission of Pakistan

1. This order shall dispose of appeal No. 38 of 2011 filed under section 33 of Securities and Exchange Commission of Pakistan (the "Commission") Act, 1997 against the order dated 20/12/10 (the "Impugned Order") passed by the Respondent.
2. The Enforcement Department (the "Department") of the Securities and Exchange Commission of Pakistan (the "Commission") while examining the annual audited accounts dated 30/06/09 (the "Accounts") and other information and explanations provided by Habib Rafiq (Pvt.) Ltd (the "Company") observed that a loan of Rs. 39.7 million was receivable from LAFCO (Pvt.) Limited ("LAFCO"), associated undertaking of the Company. The Board of Directors ("BOD") of the Company passed a resolution on 30/03/09, wherein, it was resolved that an amount of Rs. 39.7 million receivable from LAFCO may be converted into long term loan. It was also resolved to charge markup at the rate of KIBOR +200 basis, while amount of markup and principal will be paid by LAFCO on availability of funds. The Company failed to pass a special resolution for its investment in LAFCO.
3. Show cause notice dated 23/09/10 ("SCN") under the provisions of section 208 read with section 476 of the Companies Ordinance, 1984 (the "Ordinance") was issued to the directors including the Chief Executive Officer of the Company. The reply of SCN was submitted by the Appellants on 12/07/10 and hearing in the matter was held. The Respondent, dissatisfied with the response of the Appellants, passed the Impugned Order and imposed penalty of Rs 100,000 on each Appellant.



Securities and Exchange Commission of Pakistan

4. The Appellants' counsel argued that:

a) LAFCO was incorporated under joint venture MOU dated 24/10/03 by and between promoters, partners, shareholders including the Company. In terms of the joint venture MOU, the percentage of paid up capital in LAFCO with no of directors and participation was agreed as:

	Percentage	Director
1. Frontier Works Organization	65%	4 (four)
2. Khalid Rauf & Co (Pvt.) ltd	20%	1 (One)
3. Habib Rafique (Pvt.) Ltd	10%	1 (One)
4. Sachal Engineering Works (Pvt.) Ltd	5 %	1 (One)

the Company has less than 20% shareholding in LAFCO and was not an associated undertaking, as such, the requirements of section 208 of the Ordinance were not applicable on the Company;

b) it was a routine business transaction and the amount of Rs 40,050,416 was receivable from LAFCO against the work carried out by the Company. The Company entered into a loan concessional agreement on 31/03/07, whereby, the amount of Rs 40,050,416 representing amount of work done by the Company and balance due from LAFCO was converted into long term loan. The conversion of the amount receivable from LAFCO into long term investment was before 30/06/07 and at that time section 208 the Ordinance was not applicable to private companies; and



Securities and Exchange Commission of Pakistan

- c) the Commission vide its notification *No 704(I)/11* dated *13-07-11* has exempted a private limited company, which is not subsidiary of a public limited company from the application of section 208 of the Ordinance. Reliance was placed on *Commissioner of Income Tax vs. Shahnawaz Ltd and Others* cited at *1992 SC 920*, wherein, Crawford's statutory construction has been cited and it is stated that a statute relating to remedial law may properly, in several instances, be given retrospective operation. It was argued that the exemption from application of section 208 of the Ordinance available to the private companies from 13/07/11 should also be applicable to cases pending at the time of issuance of the said notification.

5. The department representative argued that:

- a) the Company and LAFCO have a common director namely; Mr. Zahid Rafiq, as such, both the companies were associated undertakings at the time of passing the board resolution dated 30/03/09 in terms of section 2(2) of the Ordinance;
- b) the Impugned Order was passed on the basis of observations made in the annual account for the year ended 30/06/09 and at that time section 208 of the Ordinance was applicable to all private limited companies. Further, the amendments made through Finance Act 2007 do not relieve a private limited company from the compliance of the provisions of section 208 of the Ordinance; and
- c) the exemption granted to the private companies was extended through notification *SRO. No 704(I)/11* dated 13/07/11, which was much after



Securities and Exchange Commission of Pakistan

the cognizance taken in the year 2009, as such, the benefit of the aforementioned notification should not be given to the Appellants.

6. We have heard the parties. Our para wise findings on the issues raised in the appeal are as under

a) Section 2 (i) and (ii) of the Ordinance is reproduced for ease of reference:

(2) *"associated companies" and "associated undertakings" mean any two or more companies or undertakings, or a company and an undertaking, interconnected with each other in the following manner, namely: —*

(i) *if a person who is the owner or a partner or director of a company or undertaking, or who, directly or indirectly, holds or controls shares carrying not less than twenty per cent of the voting power in such company or undertaking, is also the owner or partner or director of another company or undertaking, or directly or indirectly, holds or controls shares carrying not less than twenty per cent of the voting power in that company or undertaking; or*

(ii) *if the companies or undertakings are under common management or control or one is the subsidiary of another; or*

Emphasis added

In terms of section 2 (i) of the Ordinance, a company is an associated company of another company, even in a case where there is a single common directorship on the board of the two companies. The word 'or who' followed by a 'comma' has been used to set out two separate conditions under which a company shall be treated as an associated company.

The Respondent in para 9 of the Impugned Order has observed that "..... *The Company and LAFCO have a common director namely; Mr. Zahid Rafiq, so due to the fact both companies were associated undertaking at the time of the transaction....*" The department representative at the time of hearing relied on



Securities and Exchange Commission of Pakistan

definition of associated companies given in section 2 (ii) of the Ordinance. Section 2 (ii) of the Ordinance states that where the companies are under common management or control, they are deemed as associated companies. In the instant case only Mr. Zahid Rafiq is the director in both the companies. The companies cannot be deemed as working under a common management on the basis of one common director, however, the companies would still be considered associated companies in terms of section 2(i) of the Ordinance, as discussed above.

- b) the contention of the Appellant that the Company entered into a loan concessional agreement on 31/03/07, whereby, the amount of Rs 40,050,416 representing amount of work done by the Company and balance due from LAFCO was converted into long term loan, as such, section 208 of the Ordinance as at the time of the said agreement should be taken into consideration is examined. Section 208 of the Ordinance was amended after the said agreement to include private limited companies in its preview. We are not in agreement with the contention of the Appellants' counsel stated above, as the financial impact of the agreement was in the accounts for the year ended 30/06/09 and the resolution of board of director dated 30/03/09 also supports the contention of the Respondent that the conversion of the balance due from LAFCO into long term loan was undertaken in the year 2009. The Respondent rightly proceeded under section 208 of the Ordinance, as after the amendment in 2007, the Appellant had to comply with the requirements stated; and
- c) the Commission vide its notification *SRO. No 704(I)/11* dated 13/07/11 has exempted a private limited company, which is not subsidiary of a public limited company from the application of section 208 of the Ordinance. The applicable law as of today does not require the Company to pass a special resolution while making investment in their associated concern. We have perused the case law cited by the Appellants' counsel on the subject. In the matter of *Income Tax vs. Shahnawaz Ltd and Others* cited at 1992 SC 920, reported in *Complete Supreme Court cases on Income Tax (1947-1997), Volume II, published by S.A. Salam Publications, 1997/ [(1992) 66 Tax 126 (S.C.Pak.)]*, wherein, Crawford's

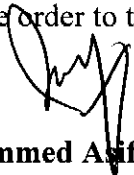


Securities and Exchange Commission of Pakistan

statutory construction has been cited and it is stated that a statute relating to remedial law may properly, in several instances, be given retrospective operation. It was argued that the exemption from application of section 208 of the Ordinance available to the private companies from 13/07/11 should also be applicable to cases pending at the time of issuance of the said notification. In the aforementioned judgment, the honorable judge of the Supreme Court also quoted the judgment of the High Court in the same matter, wherein, it was observed that the retrospective operation could extend only to such:

"cases which were pending at the time of amending law was enacted i.e. cases which had not been finally determined or processing(')s which had not attained finality. The retrospective effect of the amending law would therefore, apply only to those cases where assessment had not been made by the I.T.Os or where an appeal was pending before the Tribunal or reference was sub-judice before the High Court, at the time the amending law was enacted. The cases which had finally been determined or had attained finality i.e. which were past and closed transactions, could not be reopened under amending legislation as there are no express words to that effect employed in the amending law."

The notification SRO No. 704(I)/11 dated 13/07/11 was not in field at the time of passing the Impugned Order, however, it is in force at the time of passing the instant order. We are in concurrence with the views expressed by the honorable Supreme Court/ High Court and hereby extend the benefit of the exemption from the requirement at the Appellate stage to the Appellants by setting aside the order to the extent of the penalties.


(Mohammed Asif Arif)
Commissioner (Insurance)


(Imtiaz Haider)
Commissioner (SCD)

Announced on: 30/1/14