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SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

BEFORE APPELLATE BENCH NO. II

In the matter of

Appeal No. 13, 14 and 15 of 2007

- 1 S.M Ehtishamullah - Director
- 2 Ahsan M Saleem - Chief Executive Officer
- 3 Mazhar Karim - Chairman

of Crescent Steel and Allied Product Limited Appellants

Versus

Executive Director (Enforcement) Respondent

Date of hearing 05/01/11

Present:

For the Appellant:

Dr. Pervez Hassan - Advocate

Majid Jehangir - Advocate

For the Respondent Department:

Amina Aziz Director

Ayesha Riaz - Director



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1. This order shall dispose of appeal No. 13, 14 and 15 of 2007 filed under section 33 of the Securities and Exchange Commission of Pakistan (the "Commission") Act, 1997 against the order dated 23-05-07 (the "Impugned Order") passed by the Respondent.
2. Crescent Steel and Allied Product Limited (the "Company") was asked to clarify its position with regard to total investment of the Company in Altern Energy Limited ("AEL") and evidence of compliance with SRO 865 (1)/ 2000 dated 06-12-00 made under following resolutions tabled before the shareholders:

| Date of EOGM | Resolution | Purpose of Investment in accordance with SRO 865 (1)/ 2000 | Amount (Rs. in Million) |
|--------------|--|--|-------------------------|
| 28-01-06 | Approval of the Company be and is hereby accorded to make potential equity investment up to Rs.60.4 million in Altern Energy Limited, an eventual associated concern. | Balance Diversification | 60.40 |
| 28-04-06 | Approval of the Company be and is hereby accorded to make an additional equity investment of Rs. 570.3 in Altern Energy Limited, an associated company, by way of rights subscription of Rs 57.028 million ordinary shares of Rs. 10 each be and is hereby approved. | Balance Diversification | 570.30 |
| 14-07-06 | Approval of the Company be and is hereby accorded to make an additional long term equity investment up to Rs.379 million in Altern Energy Limited, an associated company, by way of right subscription of Rs. 37.9 million ordinary shares of Rs. 10 each as per Right Issue announced by the Altern Energy Limited to Finance its own | The purpose of present issue is to invest in shares of Altern Energy which in turn will use these funds to acquire 59.984% of shares of an independent power | 379.00 |



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| | |
|---|---|
| expansion and also to finance the acquisition of Rouch Power (Pakistan) Limited is hereby accorded" | project, Rouch Power (Pakistan) Limited ("RPPL"). RPPL is the owner of a power generation plant with a dependable capacity of 395 MW operating on natural gas. The revenues of RPPL is based on a 30 years take or pay power purchase agreement with WAPDA. Altern Energy itself is also revamping and enhancing company's assets." |
|---|---|

3. The Company replied that the investment of the Company in AEL would amount to Rs. 1.047 billion. The Company had already advanced a sum of Rs. 60.4 million against potential equity investment approved in Extra Ordinary General Meeting ("EOGM") dated 28/01/06 and Rs. 34.7 million against Rs. 570 million approved by the shareholders in EOGM dated 28/04/06. The total investment of the Company would be Rs. 1.047 billion in the AEL. The detail for cost of Rs. 1.047 billion together with the number of shares and their face value was given as under:

| Particulars | No. Of Shares | Face Value@ Rs. 10 per share Rs. (in Million) | Cost Rupees in Million | Source of Payment |
|--|---------------|---|------------------------|------------------------------|
| Acquisition under listed Companies (Substantial Acquisition of Voting Shares and Takeover) Ordinance, 2002. From sponsor shareholders (Sponsors) @ Rs. 12.50 | 7,735,000 | 77.40 | 96.70 | Internal Generation of Funds |



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| per share | | | | | |
|--|--------------------|-----------------|-----------------|--|--|
| From 1 % public offering to existing shareholders @ Rs. 12.50 per share | 1,295,000 | 1.20 | 1.60 | -do- | |
| Approved Shareholders in EOGM dated April 28, 2006 by Shareholders in EOGM | 57,030,000 | 570.30 | 570.30 | Internal Generation of Funds and Realignment of Investment portfolio | |
| Approved Shareholders in EOGM dated July 14, 2006: by Shareholders in EOGM | 37,900,000 | 379.00 | 379.00 | -do- | |
| Total | 102,794,000 | 1,027.90 | 1,047.60 | | |

4. The reply of the Company was not found satisfactory and the Company was asked to explain as to why it had given loan to AEL amounting to Rs.95.1 million, when the shareholders had not given any approval to the Company for the aforesaid loan. Moreover, the exact sources of funding for meeting the proposed investments had not been explained at any point of time in the earlier EOGMs. It also appeared from the representation given by the Company that the requirements of SRO 865(I)/2000 dated 06/12/00 for investment in associated concerns had not been complied; with regard to the earlier resolutions passed on 28/01/06 and 28/04/06. It is required that in case any decision to make investment under authority of a resolution is not implemented till the holding of a subsequent general meeting, its status including: a) reasons for not having made investment so far; and b) major change in financial position of investee company since date of last resolution must be explained to the shareholders in the statement of material facts annexed to the notice of the meeting.



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5. The Company replied that Rs. 95.1 million was not given as loan and it had been given as advance for purchase of proposed right shares (to be issued by AEL). This advance carried mark-up of 11% per annum as approved in EOGM held on 28/01/06. Apart from the initial investment of Rs. 98.3 million already made, investment in right issue of AEL, will be Rs. 949.3 million (Rs.570.3 +379) which will be funded as under:

| | <u>Rs. (In million)</u> |
|---|-------------------------|
| • Already paid to AEL out of internal generation | 95.10 |
| • Acquisition by way of settlement with CSIBL | 131.00 |
| • Internal generation and realignment of portfolio / sale of some investment | <u>723.20</u> |
| Total | <u>949.30</u> |

6. The facts and circumstances narrated in the preceding paragraphs showed that the investments of the Company made in its associated undertakings were not in accordance with the resolutions approved by the shareholders. The Company invested an amount of Rs. 95.1 million as advance while right was yet to be offered by AEL and Rs. 131 million taken over by way of settlement with CSIBL was not approved by the shareholders.

7. Show Cause Notice dated 07/08/ 06 ("SCN") was issued to the Company and its directors highlighting the prima facie violation of section 208 of the Ordinance. The Company and the directors submitted reply to the SCN and hearing in the matter was held. The Respondent, dissatisfied with the response of the Appellant, passed the Impugned Order and imposed penalty of Rs 100,000/- each on the Chairman, CEO and the executive director of the Appellant and the non-executive directors of the Company were reprimanded.



8. The Appellant has preferred to file the instant appeal against the Impugned Order. The Appellant's counsel argued that:

- a) the Respondent's allegations are factually untenable: i) with regards to the EOGM held on 28/01/06, the observations of the officers of the Commission made in various letter addressed to the Appellant were responded and all necessary disclosures were made. The Appellant issued addendum to the shareholders of the Company in response to the observations made with regard to the EOGM held on 28/01/06 and the benefits accrued to the shareholders of the Company were discussed in the aforementioned EOGM and was minted as summary of projected financial performance of AEL. Members' approval was also taken for making potential equity investment up to Rs. 60.4 million in AEL by way of advance against issue of right shares and AEL was obligated to pay mark up of 11% per annum. ii) with regard to the EOGM held on 28/04/06, the Company approved additional equity investment of Rs 570.3 million in AEL by way of right subscription of 57.028 million shares. c) with regard to the EOGM held on 14/07/06, the Company made long term equity investment up to Rs 379.0 million in AEL by way of right subscription of 37.9 million shares. The Company also provided the information regarding the aforementioned investment called by the officer of the Commission from time to time;

- b) the Respondent's objections are legally untenable as section 208 of the Ordinance allows making of investment in associated companies and



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the word investment includes both loans and advances. Reliance was placed on 2010 CLD 75, 2010 CLD 36 and 2006 CLD 1055 to show the permissive character of section 208 of the Ordinance vis-à-vis loan/advances. The allegations that the requirements of SRO 865 (1)/ 2000 dated 06/12/00 were not complied with are baseless as all requirements communicated to the Appellant were met forthwith. Further, no objection has been taken by the shareholders of the Appellant till date on the investments made in AEL;

c) The fine imposed on the Appellants is discriminatory as there is no exclusive nexus between the Appellants and the factum of investment in AEL. Reliance was placed on 2008 CLD 17, 2009 CLD 1639, 2006 CLD 1150 and 2009 CLD 65 to show that the fine is generally imposed on the entire Board of Directors ("BoD"), whereas, in the instant case cherry picking has been done by the Respondent by imposing fine on three directors out of the entire BoD. In other cases cited at 2008 CLD 786, 2006 CLD 458 and 2008 CLD 809, fine was imposed on either CEO or one of the directors and CEO, however, the reasons were stated in the orders for imposing fine. In the instant case Appellant No 2 and 3 did not attend the EOGM in which investment in AEL was approved, as such, the imposition of fine on the aforementioned Appellants was arbitrary;

d) The default by the directors, if any, was not done 'knowingly or wilfully'. Reliance was placed on 1990 CLC 1008, 1984 CLC 2456 to show that the act of the Appellants were not intentional and should the Appellate Bench (the "Bench") come to the conclusion that the default was made, it was nevertheless without any ill intention.



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9. The departmental representatives argued that the advance given to AEL was not in compliance with the approval granted by the shareholders. The Company advanced an amount of Rs 60.4 million for ten months and an amount of Rs. 34.7 million for five months, implying that the Company was acting as a financier for AEL. In the EOGM held on 28/04/06 and 14/07/06, the shareholders of the Company approved the transaction to invest in the equity of shares through subscribing the right shares. The management instead advanced loan to AEL at a date when no right was announced by AEL. Moreover, the Appellants did not comply with the requirements of SRO 865(I)/2000 dated 06-12-00 which specifically requires that where the decision to make investment under authority of a resolution is not implemented till the holding of a subsequent general meeting, its status including i) reasons for not having made investment so far and ii) major changes in financial position of the investee company since the last resolution, shall be dispatched to the shareholders through a statement under section 160(1) of the Ordinance. The department representatives also argued that the fine is imposed on the CEO, Chairman and one of the directors as they were the principle officers of the Company. There is plethora of case law where fine has been imposed on CEO or any one of the directors of the Company, as such, the contention that the CEO, Chairman and one of the directors were cherry picked is baseless.

10. We have heard the parties and have gone through the record. Our para-wise findings on the issues raised by the Appellants' counsel are as under:

- a) our observations in each of the EOGM held are: i) in the EOGM held on 28/01/06, the approval was taken for potential equity investment of Rs 60.4 million and the observations of the department were addressed in the addendum issued to the shareholders of the Company,



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, thereafter, the investment in AEL was made in terms of the said resolution as such there was no violation of section 208 of the Ordinance in respect of the said meeting; ii) in the EOGM held on 28/04/06, equity investment of Rs 570.30 million was approved by way of right subscription of 57.028 million shares of Rs 10 each, out of which 34.7 million was advanced to AEL. The making of advance of Rs 34.7 million to AEL was not approved by the shareholders, as such, it was violation of section 208 of the Ordinance in terms of the said meeting; iii) in the EOGM held on 14/07/06, equity investment of Rs 379.00 million was approved by way of right subscription of 37.9 million shares of Rs 10 each, and no sum was advanced, as such, there was no violation of section 208 of the Ordinance. The Appellants in making advance to AEL before actual issue of right shares had acted beyond the authority conferred to them by the shareholders in the EOGM held on 28/04/06. The interest charged on the advances does not absolve the Appellants for the said violation;

- b) Section 208 of the Ordinance stipulates that the company shall not make investment in any of its associated companies or associated undertakings except under the authority of a special resolution, which indicates the nature, period and amount of investment and terms and conditions attached thereto. The Appellants sought approval for making 'equity investment' in the EOGM held on 28/04/06 and approval for 'advance' was not sought through a special resolution, therefore, the argument of the Appellant that it complied with the requirement of section 208 of the Ordinance is not tenable. Moreover, the failure on part of the Appellants' to make the required disclosure in terms of SRO 865(I)/ 2000 dated 06/12/00 cannot be condoned on the ground that the disclosure was made in the EOGM held on 14/07/06;



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- c) the contention of the Appellants' counsel, that the Respondent has cherry picked the directors while imposing fine has been examined. The Respondent has imposed fine on the Chairman, CEO and one of the directors. It is pertinent to mention that SCN was issued to the Chairman, CEO and all directors of the Company. Respondent in the penultimate para of the Impugned Order taking a lenient view imposed penalty on the Chairman, CEO and the director/CFO and reprimanded the non-executive directors of the Company to be careful in future. The lenient view taken by the Respondent was based on clear distinction between the directors directly responsible for the default as principle officers of the Company, whereas the non-executive directors were let off with warning;
- d) the argument that the acts of the Appellants were not willful are not substantiated with the facts of the case. The Appellants were fully cognizant of the fact that the advance made to AEL was without the shareholder's approval, as such, the default cannot be condoned on the ground that the acts were not willful. We place our reliance on the definition of 'willful' as reproduced in 1984 CLC 2456 from Black Law Dictionary as an act done with stubborn purpose, but not with malice, as done intentionally, knowingly and purposely as distinct from an act done carelessly, thoughtlessly, heedlessly or inadvertently. It is in fact the act, and the circumstances surrounding such act which points towards the intention of a person committing an offence and as has been illustrated, the act of the Appellants were willful.


In view of the findings of para 10 (a) above, we are of the view that the violation of section 208 of the Ordinance was only in respect of the




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EOGM held on 28/04/06 and at the same time, we find no reasons to interfere into the order of the Respondent but are of the view that Appellants be penalized and held responsible only to the extent of violation committed by them. We, therefore, taking a lenient view, waive the penalty imposed through the impugned order and the Chairman, Chief Executive and the Executive director namely Mr. S. M. Ehtishamullah of the Company are hereby reprimanded and warned to be careful in future and act in accordance with the requirements as envisaged under the law and comply with the resolution of the general meeting in letter and spirit so that the resolutions passed by the general meeting are completely adhered to as passed by the shareholders. Accordingly, the said appeals are hereby disposed of.


(Mohammed Asif Arif)
Commissioner (Insurance)


(Imtiaz Haider)
Commissioner (SMD)

Announced on: 01/03/12