



Securities and Exchange Commission of Pakistan

BEFORE APPELLATE BENCH NO. III

In the matter of

Appeal No. 26 of 2010

1. Fakhruddin Usmani
2. Quamruddin Usmani
3. Muhammad Farooq Usmani
4. Mahmood Wali Muhammad
5. Muhammad Atiq
6. Ali Muhammad Usmani
7. Muhammad Shahzad Fakir

All directors of Hafiz Textile Mills Limited Appellants

Versus

Executive Director (Enforcement)

Securities and Exchange Commission of Pakistan Respondent

Date of hearing

18/09/12

ORDER

Present:

Appellant:

Mr. Quamruddin Usmani, Director

For the Appellants:

Muhammad Moin Khan, FCA

Department representatives:

Mr. Amir Saleem, Deputy Director (Enforcement)

Mr. Rohail Ahmed Abbasi, Assistant Director (Enforcement)



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1. This order shall dispose of appeal No. 26 of 2010 filed under section 33 of the Securities and Exchange Commission of Pakistan (the "Commission") Act, 1997 against the order dated 20/05/10 (the "Impugned Order") passed by the Respondent.
2. On the examination of the audited accounts of Hafiz Textile Mills Limited (the "Company") for the year ended 30/06/08 (the "Accounts") and previous audited accounts filed with the Commission, it was revealed that the Company had following outstanding balances of advances from customers and creditors.

Financial Year	Outstanding Advances from Customers (Rs)	Outstanding Creditors (Rs)
2008	60,093,050	8,105,364
2007	61,505,034	9,116,651
2006	63,231,189	9,702,737
2005	63,504,079	9,822,416
2004	62,338,079	9,933,655
2003	62,757,324	10,133,655
2002	62,257,074	10,276,155
2001	64,425,994	10,933,813
2000	66,552,494	10,968,813
1999	52,917,710	13,217,727
1998	53,156,290	11,843,423

The Commission, vide letter dated 17/09/08, required the auditors of the Company M/s Moochhala Gangat & Co. Chartered Accountants (the "Auditors") to explain audit procedure adopted for verifying creditors of Rs. 8,105,364 and advances of Rs. 60,093,050. In response, the Auditors replied vide letter dated 18/11/08, that the advances from suppliers and creditors were outstanding since the year 1997 and confirmation sent to the concerned creditors and suppliers remained unanswered.

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3. The accounts of the Company for the period ended 31/12/08 and annual audited accounts for the period ended 30/06/09 revealed that the Company paid Rs. 65,744,966 to aforesaid unverified creditors and suppliers, furthermore, long term loan from directors also increased by Rs. 56,634,905. The Commission, vide letter dated 26/08/09, required the Company to provide certified copies of bank statements showing receipt of directors' loan and payment to creditors and suppliers. The authorized representative of the Company, vide letter dated 11/09/09, replied that: *"The creditors have been paid off out of the pin money in possession of the families of the director to increase the capital of the company. The matter may not be pleased looked into through Company Law, this is an exceptional case"*, and vide letter dated 10/10/09 stated that: *"We have already informed you that it was a novel case, so, if the directors have made any mistake in making entry, you are therefore, requested to kindly advise them to make the correction in this respect"*. In order to ensure independent verification of Company's claim, requests for confirmation were sent by the Commission to the concerned creditors and suppliers on 27/08/09; almost all of the cases were received back marked *"No such consignee at given address"*.

4. Show cause notice ("SCN") under section 492 of Companies Ordinance, 1984 (the "Ordinance") was issued to the Appellants. The Appellants filed reply to the SCN and hearing in the matter was held. The Respondent, dissatisfied with the response of the Appellants, passed the Impugned Order and imposed a penalty of Rs. 300,000 each on the Appellants for misstatements in the Accounts and directed the Appellants under section 473 of the Ordinance to reverse the directors' loan of Rs. 57,790,720 and write back advances from suppliers/creditors to the profit and loss account of the Company in

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accordance with International Accounting Standard-8 (Accounting policies, Changes in accounting Estimates and Errors).

5. The Appellants preferred appeal against the Impugned Order. The Appellants' representative argued that the Respondent failed to point out any false or incorrect statement or error committed by the Appellants which fall under the ambit of section 492 of the Ordinance. It was argued that allegations on the Appellants regarding failure to prove the authenticity of advances from suppliers/creditors is neither justified nor based on any solid grounds. The fact remains that sufficient evidences in this regard were furnished during course of hearing before the Respondent. Complete details of amount received from creditors showing date of amount received, name of party and the bank in which amount was deposited, copy of cheque collection voucher, copy of deposit slip of the bank, copy of receipt issued by the Company and copies of bank statements were furnished to the Commission. It is abundantly clear that these amounts were actually received and utilized for the purpose of business of the Company. The Respondent failed to point out any specific discrepancy in these details and documents furnished by the Appellants. It was argued that mere non receipt of confirmation from respective creditors does not mean that these amounts were not received. The Respondent failed to appreciate that when it is established from all the documents furnished by the Appellants that amounts in question were received and recorded in the books of accounts and inflow of funds was duly incorporated in the books of accounts then naturally the same liabilities were required to be repaid and settled. The long outstanding creditors of the Company were paid by the directors of the Company from their personal resources and correct accounting entries were passed in the accounts of the Company. The directors had in fact paid a sum of Rs 57.791 million to the long outstanding creditors out of personal resources.

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6. The department representatives argued that the Appellants failed to provide satisfactory evidence to verify the payments to creditors and almost all requests for confirmation sent by the Commission to the creditors were returned as 'No such consignee at given address'. Further, the evidence provided by the Appellants regarding receipt of advances from creditors were not found satisfactory. The receipt vouchers of these advances revealed that the advances were on account of yarn sales. It was observed from documents provided by the Appellants' counsel that these advances were received in cash through installments. In cases where payments were received through cheques the copies of cheques were not provided to verify their authenticity. The Appellants also failed to provide any documents which support the contention that the amount shown in bank statements was actually received from the creditors. The contention of the Appellants regarding re-payment by the directors on behalf of the Company of an amount of Rs 57.791 million is a misstatement in the accounts, as the creditors were unverified and fictitious. The so called creditors could not be identified despite the efforts of the auditors and the Commission.
7. We have heard the parties. Section 492 of the Ordinance is reproduced for ease of reference:

"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 a fine not exceeding five hundred thousand rupees."

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The Appellants have failed to provide satisfactory evidence to verify the payments to creditors. Almost all requests for confirmation sent by the department to the creditors were not received and we find it peculiar that the Company does not have authentic addresses and CNIC of creditors with whom the Company had outstanding advances since the year 1998. Further, most of the advances by creditors were received through cash and where payments were received through cheques, copies of the cheques were not provided to verify authenticity of creditors. There is no evidence available with the Appellant which could support the argument of the Appellants that the amount shown in bank statements was actually received from the creditors. We, therefore, concur with the view of the Respondent that the payment recorded in the Company's accounts regarding advances received from creditors does not appear to be authentic.

One of the main objectives and intent of section 492 of the Ordinance is to protect the users, which may include investors, shareholders, creditors, bankers, customers etc. of financial statements against misstatements so that reliable financial information which is vital for making a well informed decision is available to them. In the instant case, the Appellants have not provided satisfactory evidence about the authenticity of both the accrual of directors' loan as well as settlement of advances from creditors. It is evident that the Appellants have contravened the provisions of section 492 of the Ordinance by misstating in the Accounts regarding repayment of Rs. 57,790,720 by the directors on behalf of the Company to unverified creditors/ suppliers. The Appellants are the real beneficiaries of misstatement as huge amount has been recorded in the Company accounts as payable to them without any underlying evidence. The Appellants in their capacity as

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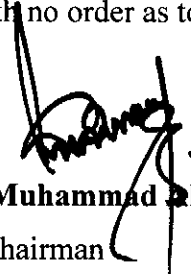



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directors of the Company are responsible for the misstatement in the Accounts.

The penalty imposed on the Appellants is in the personal capacity and ought to be paid by the Appellants from the personal resources and not from the coffers of the Company. We have considered, whether the quantum of penalty imposed is propionate to the offence. The maximum penalty provided for violation of section 492 of the Ordinance is Rs 500,000 on each Appellant, as such, the Respondent has already taken lenient view in the matter by imposing lesser penalty.

In view of the above, the Impugned Order is upheld. The appeal is dismissed, with no order as to cost.


(Muhammad Ali)
Chairman


(Mohammed Asif Arif)
Commissioner (Insurance)

Announced on: 07/12/12