

Before

Amir M. Khan Afridi, Director/Head of Department

In the matter of

Colony Textile Mills Limited

Date of Hearing

December 15, 2021

Order-Redacted Version

Order dated March 14, 2022 was passed by Director/Head of Department (Adjudication-I) in the matter of Colony Textile Mills Limited. Relevant details are given as hereunder:

Nature	Details
1. Date of Action	Show Cause Notice dated September 27, 2021
2. Name of Company	Colony Textile Mills Limited
3. Name of Individual*	The proceedings were initiated against the Company and its Board of Directors of the Company.
4. Nature of Offence	The Company extended said loan to *** without agreement in writing and without any return. Moreover, the Company did not provide any detail regarding the return against the aforesaid loan. Hence, the loan amounting to Rs. 21.111 million extended to *** without any agreement in writing, <i>prima facie</i> , is in violation of Section 199(2) of the Companies Act, 2017 (the Act) read with the Companies (Investment in associated companies) Regulations, 2017 (the Regulations). Keeping in view the said violation, SCN was issued to the Respondents, under Sections 199 and 479 of the Act read with the Regulations.
5. Action Taken	Key findings are given as hereunder: I have gone through the facts of case, relevant provisions of the law and record placed before me. In this regard, the following legal objections taken by the learned counsel for the Respondent need to be addressed first:

(i) As far as the legal objection taken by the learned counsel for the Respondent that Commission is not validly constituted and this Office could not assume and exercise jurisdiction resulting in the issuance of the SCN; in my view argument of learned counsel for the Respondent is misconceived due to fact that Securities and Exchange Commission of Pakistan Act, 1997 (SECP Act) was amended by the Securities and Exchange Commission (Amendment), Act of 2013, and under Section 5(5) of the Act, acts decisions and proceedings of the SECP were saved and validated. For ready reference provisions of Section 5(5) of the Act are as under:

“No act, proceeding or decision of the Commission shall be invalid by reason only of the existence of a vacancy in, or defect in the constitution of the Commission.”

So, plea of the learned counsel for Respondent that at the time of issuance of SCN the Commission was not properly constituted or this office does not have jurisdiction does not hold merit. I do not find any merit in this objection.

The next legal objection taken by the counsel of the Respondent that this office lacks jurisdiction for issuance of SCN is misconceived regarding the authority, power or jurisdiction to issue the instant SCN. It is pertinent to note that Section 10 of the Securities and Exchange Commission of Pakistan Act, 1997 exclusively empowers the Commission to delegate any of its functions or powers under the SECP Act or any administered legislation to one or more commissioners or any officer of the Commission. Accordingly, the authority has been validly delegated by the Commission to the Head of

Department (HOD) Adjudication-I being an officer of the Commission through S.R.O.1545(I)/2019 Dated 6th December 2019 under clause 33 of subject SRO and subject notification has been duly published in the Gazette of Pakistan. Therefore, the instant Show Cause notice was lawfully issued by the Head of Department Adjudication-I in accordance with the delegated powers. In view of above I do not find any merit in this objection.

(ii) As regards to Respondents' stance that the Act does not fall in the ambit of administered legislation in terms of first schedule to the SECP Act, 1997, the same is not tenable. As in terms of sub-section (4) of Section 509 of the Act the expression Companies Ordinance, 1984 provided in first scheduled to the SECP Act, 1997 is to be read as the Act unless the context requires otherwise. Relevant provision of Section 509(4) of the Act states that: *"After the commencement of this Act, the expression Companies Ordinance, 1984 (XLVII of 1984) and any referring sections thereof, used in any law for the time being in force including all administered legislations and rules, regulations and guidelines made thereunder, shall be read as Companies Act, 2017 along with corresponding provisions of Companies Act, 2017 unless the context requires otherwise."*

(iii) Section 199(1) of the Act clearly stipulates that the company cannot make investment in associated company or associated undertaking except under the authority of special resolution, which shall indicate the nature, period, the amount of the investment and the terms and conditions thereof. Hence, authority of special resolution of shareholders of a company is mandated by law for making any such investments, loans, advances etc., to associated companies or undertakings. The

explanation added to Section 199(1) provides that the term “investment” shall include equity, loans, advances, guarantees, by whatever name called, except for the amount due as normal trade credit, where the terms and conditions of trade transaction(s) carried out on arms-length and in accordance with the trade policy of the company.

The exemption provided by the Commission vide SRO 1239(I)/2017 dated December 6, 2017 is to the extent of a special resolution, wherein the Commission specified the classes of companies to which the restriction provided under sub-section (1) of Section 199 of the Act shall not apply. It has specifically been provided by clause (a) of sub-section (3) of Section 199 of the Act that, *“the Commission may be notification in the official Gazette, specify the class of companies or undertakings to which the restriction provided in sub-section (1) shall not apply.”*

Section 199(2) of the Act provides that the company shall only invest in its associated company or associated undertaking by way of loans or advance in accordance with an agreement in writing and such agreement shall include the terms and conditions, specifying: (i) the nature, purpose and period of loan, (ii) rate of return on loan; (iii) fees or commission; (iv) repayment schedule for principal amount and return; (v) penalty clause in case of default or late repayments; and (vi) security, if any, for the loan in accordance with the approval of the members in the general meeting. Furthermore, the return on such investment shall not be less than the borrowing cost of the investing company or the rate as may be specified by the Commission whichever is higher and shall be recovered on regular basis in accordance with the terms of the

agreement, failing which the Company/directors shall be personally liable to make the payment. The requirements of Section 199(2) of the Act are applicable irrespective of the fact that exemption allowed in terms of S.R.O is applicable. Hence, the arguments of the Respondents that the requirements of Section 199(2) are not applicable in view of exemption of Section 199(1) Act, however, the same are not tenable.

(iv) As per available information, the Company has extended an amount of loan of Rs. 21.111 million (2019: Nil) to ***. The aforesaid transpires that an amount of Rs. 21.111 million was extended to wholly owned subsidiary company without charging any interest thereof and without any agreement in writing. I am of the view that the Company cannot extend 'loan' or 'advance' to its wholly owned subsidiary company without any return thereon. In view of the aforesaid, the Respondents have contravened the requirements of Section 199(2) of the Act.

(v) In terms of Regulation 5(4) of the Regulations, the rate of return on loans, advances may not be less than Karachi Inter Bank Offered Rate for the relevant period or the borrowing cost of the investing company, whichever is higher, and rate of return or interest or mark-up at rate to be determined, as specified, on such amounts from the date of transfer of funds was not charged. The aforesaid regulation and the requirements provided in terms of Section 199(2) of the Act make it obligatory on the part of the Respondents to charge and recover mark-up periodically for the amount of loan extended to SPL, however, in absence of any evidence of compliance, they

	<p>contravened the requirements of Section 199(2) of the Act and of regulation 5(4) of the Regulations.</p> <p>(vi) The Respondents have not placed before me any documentary evidence of any compliance of the requirements of Section 199(2) of the Act and regulation 5(4) of the Regulations.</p> <p>From the above discussion and after careful consideration of all the facts of the case, I am of the view that provisions of Section 199(2) of the Act read with regulation 5(4) of the Regulations have been contravened and for this contravention, the Respondents are liable under sub-section (6) of Section 199 and Section 479 of the Act. In exercise of the powers conferred under the said provision, I hereby impose aggregate penalty of Rs. 700,000/- (Rupees Seven Hundred Thousand only) on the Respondents.</p> <p>The aforesaid fines must be deposited in the designated bank account maintained with MCB Bank Limited in the name of the Securities and Exchange Commission of Pakistan within thirty days of the date of this order and furnish receipted bank vouchers to the Commission. In case of non-deposit of the said penalty, proceedings under Section 485 of the Act will be initiated for recovery of the same as arrears of land revenue. It may also be noted that the said fines are imposed on Respondent in personal capacity, therefore, is required to pay the said amount from personal resources.</p> <p>Nothing in this Order may be deemed to prejudice the operation of any provision of the Regulations/Act providing for imposition of penalties in respect of any default, omission or violation of the Regulations/ Act.</p>
6. Penalty Imposed	Rs. 700,000/-
7. Current Status of Order	Appeal has been filed (17/2022)