



Corporate Supervision Department
Company Law Division

Before Abid Hussain -Executive Director

In the matter of

Elmetec (Private) Limited

Number and date of notice: EMD/242/K/862/13-1167 dated April 21, 2014
Date of hearings: May 28, 2014, December 31, 2014, June 10, 2015, May 16, 2016
Present: Mr. Syed Amjad Kabir - Director

ORDER

UNDER SECTION 492 READ WITH SECTION 476 OF THE COMPANIES ORDINANCE, 1984

This order shall dispose of the proceedings initiated against the directors including the Chief Executive (the "respondents") of Elmetec (Private) Limited (the "Company") through show cause notice ("SCN") dated April 21, 2014 issued under the provisions of Section 492 read with Section 476 of the Companies Ordinance 1984 (the "Ordinance").

S#	Name of Respondent
1	Mr. Faisal Bilal Qureshi
2	Ms. Syed Amjad Kabir

2. Brief facts of the case are that examination of annual audited accounts for the period ended June 30, 2008, June 30, 2009, June 30, 2010, June 30, 2011, June 30, 2012 and June 30, 2013 of the Company revealed following:

- Statement of changes in Equity have not been annexed with the accounts for the year ended June 30, 2008, June 30, 2009 and June 30, 2010,
- Accounts submitted for the year ended June 30, 2008 do not represent calculation of deferred tax liability/asset on account balances as well as no deferred tax liability has been created on the Surplus on Revaluation of fixed Assets recognized during the year ended June 30, 2008,
- As per accounts submitted for the year ended June 30, 2013 deferred tax liability amounts to Rs 8,175,124/- (2012: 6,434,891/-) and deferred tax charge amounts to Rs 1,740,232/- (2012: 1,372,940/-).

3. Section 235 of the Ordinance provides:

(1) Where a company revalues its fixed assets, the increase in, or sums added by writing up of, the value of such assets as appearing in the books of accounts of the company shall be transferred to an account to be called "Surplus on Revaluation of Fixed Assets Accounts" and shown in the balance-sheet of the company after Capital and Reserves.



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(2) Except and to the extent actually realised on disposal of the assets which are revalued, the surplus on revaluation of fixed assets shall not be applied to set-off or reduce any deficit or loss, whether past, current or future, or in any manner applies, adjusted or treated so as to add to the income, profit or surplus of the company, or utilised directly or indirectly by way of dividend or bonus:

Provided that the surplus on revaluation of fixed assets may be applied by the company in setting-off or in diminution of any deficit arising from the revaluation of any other fixed assets of the company:

Provided further that incremental depreciation arising out of revaluation of fixed assets may be charged to Surplus on revaluation of fixed assets account.

(3) The requirements of sub-sections (1) and (2) shall also apply to any account representing any increase in or addition to the value of any asset as a result of any revaluation of any fixed assets done before the commencement of this Ordinance, howsoever described, to the extent of the amount thereof appearing in the books of account of the company on such commencement,

(4) After revaluation as aforesaid, depreciation on the assets so revalued shall be provided with reference to the value assigned to such assets before revaluation and surplus on revaluation may be amortized according to life of the assets.

4. Para 1.1 of Section 1 of Accounting and Financial Reporting Standards (the "AFRS") provides:

- 1.1 A complete set of financial statements includes the following components:
- (a) a balance sheet;
- (b) an income statement;
- (c) a statement showing either:
 - (i) all changes in equity; or
 - (ii) changes in equity other than those arising from capital transactions with owners and distributions to owners;
- (d) a cash flow statement; and
- (e) accounting policies and explanatory notes.

5. Para 3.24 of Section 3 of AFRS provides:

3.24 An amount equal to incremental depreciation for the period shall be transferred from 'Surplus on Revaluation of Fixed Assets Account' to unappropriated profit / accumulated loss through 'Statement of Changes in Equity' to record realization of surplus to the extent of the incremental depreciation.

6. Para 11.4 and 11.8 of Section 11 of AFRS provides:

11.4 A deferred tax liability shall be recognised for all taxable temporary differences, except to the extent that the deferred tax liability arises from:

- (a) the initial recognition of goodwill; or
- (b) the initial recognition of an asset or liability in a transaction which:
 - (i) is not a business combination; and
 - (ii) at the time of the transaction, affects neither accounting profit nor taxable profit (tax loss),

11.8 The measurement of deferred tax liabilities and deferred tax assets shall reflect the tax consequences that would follow from the manner in which the entity expects, at the balance sheet date, to recover or settle the carrying amount of its assets and liabilities,

7. The Company has failed to incorporate the above mentioned disclosures as required under section 235 of the Ordinance and AFRS. As a result, the annual audited accounts of the Company for



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the years mentioned above are, prime facie, misstated. The amount and effects of above referred observations are material. Therefore, SCN was issued on April 21, 2014 advising the respondents to explain their position within 14 days from the date of the notice as to why penal action may not be taken against him for contravention of provisions of Section 492 of the Ordinance. The respondents vide letter dated May 06, 2014 submitted:

- It is denied that the provisions of Section 492 of the Ordinance are attracted in the instant case as the omission was not made knowingly. It is noteworthy that the Securities and Exchange Commission of Pakistan (the "Commission") in the case reported as 2013 CLD 58 has held that "in order to impose penalty under section 492 of the Ordinance, it is sufficient to prove that the contravention was made knowingly and ingredients of criminal offence need not be established". It is not a willful default on behalf of the Company or the directors rather the relevant officers of the company were not aware of the recent developments in the law/accounting principles that resulted in such anomaly. What the law punishable is a false statement that is untrue or incorrect statement known to the framers of the balance sheet to be false,
- It is submitted that the effect of the mistake is not material. It is important for the Commission to take into account and evaluate the effect of the mistake before any order is passed. The Company submits that no tax liability has been evaded as a consequence of this anomaly in the accounts/balance sheet. The mistake does not give or present a false picture of the profits or profitability of the Company. The Company is a private company having two shareholders, who are the directors of the Company. No other individual/shareholders are involved who may get adversely affected through this mistake. It is submitted that the Company has not concealed any material fact rather the issue at hand is merely a presentation issue i.e. how the information has been presented. Such presentation issues in not misleading,
- Company has never been fined or penalized by the Commission. This is the first instance where the company has been issued a SCN. The Commission must consider that fact that this anomaly has resulted from a change in the applicable accounting principles and law that the relevant officers of the Company overlooked to take note of,
- The Commission has highlighted the anomaly and the Company and the directors have taken note of the same. As the mistake was not willful, an assurance has already been given to the Commission that steps shall be taken to rectify the errors(s)/anomaly as soon as possible,
- The statement/anomaly was not false or incorrect in any material particular or omits any material fact knowing it to be material, no fine or penalty should be imposed as the provisions of section 492 of the Ordinance are not attracted in the instant case,
- Commission has highlighted the anomaly and the Company has already started taking measures to rectify the anomaly. In such like circumstances, the commission is requested to



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take lenient view, as this is the first ever SCN issued to the Company and the alleged contraventions are not material and relevant officers of the Company ignored to take into consideration. Role of the regulators is to ensure that the companies comply with the relevant laws and not to generate income through imposing penalties on the companies. In circumstances where company has already assured compliance of the provisions of law that it was not aware of earlier, there is a good reason for the Commission to take a lenient approach in the matter,

- An appropriate case to impose penalty would have been where it could be shown that the Company or directors acted with mala fide, intentions. In the instant case, the company (its employees) or the directors were not aware of the applicable changes in the law and accounting principles. The Company and its Directors simply relied on the officers of the Company to prepare the accounts. Therefore, it is humbly submitted that imposition of penalty on the Company and its Directors shall not be appropriate in current circumstances.

8. In order to provide opportunity of personal hearing the case was fixed before the Head of Department on May 28, 2014 and then on December 31, 2014 and were held on the same dates. Subsequently the powers to adjudicate default under section 492 of the Ordinance were delegated to Commissioner. Accordingly, hearing in the matter was fixed for June 10, 2015. Company vide its letter dated June 08, 2015 requested to dispose of the case on the basis of hearings held on May 28, 2014 and December 31, 2014. The powers to adjudicate cases under section 492 of the Ordinance have again been delegated to the Executive Director (Corporate Supervision Department). To conclude the matter and to bring it to a logical end another hearing opportunity was provided to the Company on May 16, 2016. Company vide its letter dated May 12, 2016 requested to decide the matter on the basis of earlier submissions and hearings held on May 28, 2014 and December 31, 2014.

9. Before proceeding further, it is necessary to advert to the following relevant provisions of Section 492 of the Ordinance, which states as under:

"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."

10. In terms of the Commission's notification SRO 1003 (I)/2015 dated October 15, 2015, the powers to adjudicate cases under section 492 of the Ordinance have been delegated to the Executive Director (Corporate Supervision Department).



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11. I have analyzed the facts of the case, relevant provisions of the Ordinance, requirements of AFRS, arguments put forth by the Respondents in writing. My observations are that:

- In terms of section 233 of the Ordinance, it is responsibility of the directors of every company to lay before the company in annual general meeting a balance-sheet and profit and loss account or in the case of a company not trading for profit an income and expenditure account for the period not later than eighteen months after the incorporation of the company and subsequently once at least in every calendar year, in the case of the first account for the period since the incorporation of the company and in any other case since the preceding account, made up to a date not earlier than the date of the meeting by more than four months the directors of the company to lay accounts at the annual general. Section 234 of the Ordinance provides that balance sheet and profit and loss account should give a true and fair view of the financial statement. In view of the above, the responsibility of preparing true and fair financial accounts rest with the directors of the Company and it cannot be shifted to the accounting staff of the Company,
- The objective of financial statements is to provide information about the financial position, performance and changes in financial position of an enterprise that is useful to a wide range of users in making economic decisions. Above information is helpful for following purposes:
 - Prospective Investors need Financial Statements to assess the viability of investing in a company. Investors may predict future dividends based on the profits disclosed in the Financial Statements. Furthermore, risks associated with the investment may be gauged from the Financial Statements. For instance, fluctuating profits indicate higher risk. Therefore, Financial Statements provide a basis for the investment decisions of potential investors.
 - Financial Institutions (e.g. banks) use Financial Statements to decide whether to grant a loan or credit to a business. Financial institutions assess the financial health of a business to determine the probability of a bad loan. Any decision to lend must be supported by a sufficient asset base and liquidity,
 - Suppliers need Financial Statements to assess the credit worthiness of a business and ascertain whether to supply goods on credit. Suppliers need to know if they will be repaid. Terms of credit are set according to the assessment of their customers' financial health,
 - Employees use Financial Statements for assessing the company's profitability and its consequence on their future remuneration and job security
- A regulator is a public authority or government agency responsible for exercising autonomous authority over some area of human activity in a supervisory capacity. An independent regulator is a regulatory agency that is independent from other branches or arms of the government.



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- Regulator deal in the areas of administrative law, regulatory law, secondary legislation, and rulemaking (codifying and enforcing rules and regulations and imposing supervision or oversight for the benefit of the public at large),
- The Company has to follow AFRS prescribed for medium sized entities. Treatment of depreciation and surplus on revaluation of assets as defined under section 235 of the Ordinance and AFRS is vital for the fair presentation of the financial statements,
- Fair presentation of the financial statement is very helpful for the users as mentioned above to take decision regarding the company,

12. I have analyzed the facts of the case, relevant provisions of the Ordinance, arguments put forth by the respondent and the authorized representative and I am of the firm view that treatment of deferred tax liability, surplus on revaluation of fixed assets and presentation of financial statements in accordance with the section 235 of the Ordinance and AFRS was the responsibility of the directors and response given by the directors is found to be unsatisfactory. The aforesaid section does not give or provide any exception for omission of material facts presented before the shareholders and regulators. As regards the establishing intent, it is imperative to note that it has been held by superior courts that breach of fiduciary duty is considered willful. In case of City Equitable Fire Insurance Co. Ltd, Re, 1925 Ch 407, it was held that a default, in case of breach of duty, will be considered 'willful' even if it arises out of being recklessly careless, even though there may not be knowledge or intent. As per case law cited as 1987 MLD 3039, the legal duty or liability is always needed to be discharged by the person required by law and if not complied, the presumption will be that he has done so willfully. Therefore, when a requirement of a statute has been violated then there is no need to establish malafide or mens rea to prove the non-compliance of the provisions.

13. The accounts are considered to be as misstated. There is no reason to believe that the default of the respondent in compliance of the required AFRS was not willful. The respondents have made themselves liable under the provisions of Section 492 of the Ordinance. However, keeping in view that fact that the company is a private company, I am taking a lenient view in the matter and instead of imposing maximum fines on the respondents, impose a token fine of Rs. 30,000/- (Rupees Thirty Thousand only) in aggregate on respondents under the provisions of Section 492 of the Ordinance. The respondents are directed to deposit the fine in the following manner:

S#	Name of Respondent	Amount Rs
1	Mr. Faisal Bilal Qureshi	15,000/-
2	Ms. Syed Amjad Kabir	15,000/-



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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 from the receipt of this order and furnish receipted bank vouchers to the Commission. In case of non-deposit of fine, proceedings for recovery of the fines as arrears of land revenue will be initiated.

Abid Hussain
Executive Director (Corporate Supervision)

Announced:
December 29, 2016
Islamabad.

