Securities and Exchange Commission of Pakistan
Enforcement and Monitoring Division
NIC Building, Jinnah Avenue, Blue Area, Islamabad

Before Rashid Sadiq, Executive Director

In the matter of

M/S M. A. ALAM & CO. CHARTERED ACCOUNTANT

Number and date of notice	19(975)CF/ISS/2001 January 18, 2002
Date of hearing	June 26, 2002
Present	Mr. Rizwan Badar

Order

This Order will dispose of the show cause proceedings initiated against Mr. Muhammad Akbar Alam under Section 260 of the Companies Ordinance 1984 (the "Ordinance") and the Companies (General Provisions and Forms) Rules, 1985 (the "Rules").

2. Mr. Muhammad Akbar Alam is an Associate Member of the Institute of Chartered Accountants of Pakistan (the "ICAP'). He was registered on February 11, 1990 under the Registration Number 1780. He is a practicing Chartered Accountant and conducting his business under the name and style **"M/S M.A. Alam & Company"** at 1/7-B, Mohammad Ali Housing Society, Karachi.

3. The facts relevant to this case, briefly stated, are that M/S M.A. Alam & Company, Chartered Accountant was appointed as Auditor of M/S Carvan East Fabrics Limited (the "Company") in its Annual General Meeting held on March 24, 2000 to hold office from the conclusion of the said meeting until the conclusion of next Annual General Meeting.

4. The Commission has conducted an examination of the financial statements of the Company for the year ended June 30, 2000 (the "Accounts") to determine, among other things, as to whether the Auditors' Report pertaining to the aforesaid financial year has been made in conformity with the requirements of Section 255, is otherwise true, contained no statement, which is materially false and that there is no omission of material facts about the affairs of the Company.

5. The aforesaid examination of the Company's Accounts revealed that the Audit Report signed by Mr. M.A. Alam on November 30, 2000 was not on the prescribed Form 35-A as notified vide SRO No. 594(1)/2000 dated August 25, 2000. This is because of the fact that the Auditor has not audited the statement of changes in equity and has not given any opinion on the truth and fairness of the said statements as well as observance of the approved accounting standards as applicable in Pakistan.

6. The Auditor of the Company, however, has not drawn attention of the members in their Audit Report towards the aforesaid non-disclosures in the Accounts. The Auditor has also failed to draw attention of the members towards possible going concern problem. The Company has incurred loss of Rs. 29.942 million during the year and has accumulated losses of Rs. 160.750 million, which not only eroded the equity but resulted in negative equity of Rs. 60.750 million. Current liabilities have exceeded its current assets by Rs. 100.704 million and lenders have filed recovery suits in the banking courts against the Company.

7. It was also noticed from the Accounts that the Company has not observed the following requirements of the International Accounting Standards (IAS) and Fourth Schedule of the Ordinance in regard to the accounts and preparation of the Balance Sheet and Profit and Loss Account for the year ended June 30, 2000:

- Disclosure of financial instruments has not been made in the accounts as per requirements of Para 56, 66 and 77 of IAS 32 (Financial instruments: Disclosure and Presentation).

- No provision for employees' retirement benefits has been made contrary to Para 25 of IAS 1 (Presentation of Financial Statements).

- Statement of changes in equity has not been prepared and annexed to the accounts contrary to the requirements as per Para 7 of IAS 1(Presentation of Financial Statements).

- Number of employees has not been disclosed as per requirements of para 102(d) of IAS 1 (Presentation of Financial Statements).

- Earning per Share has not been disclosed in the accounts as per IAS 33 (Earnings Per Share).

- Disclosure of liabilities against assets subject to finance lease has not been given according to Para 23(b) of IAS 17.

- Gain on disposal of fixed assets has been offset against administrative expenses contrary to Para 34 of IAS 1.

- The Company did not disclose accounting policies of staff retirement benefits and trade debts contrary to Para 97 of IAS 1.

- The company failed to comply with the provisions of Clause (ii) of Para 2 of Part I of Fourth Schedule to the Ordinance regarding disclosure of non-following of fundamental accounting assumption, namely going concern and accrual in preparation of the financial statements.

- Advances and prepayments have not been separately disclosed in the accounts as per Clause (A) of para 6 of 4th Schedule of the Ordinance.

- Disclosure of long-term loan has not been made in accordance with the requirements of sub-clause (b) of Clause (E) of Para 8 of 4th Schedule of the Ordinance. Further current maturity of long term loans has not been disclosed contrary to Sub-clause (b) of Clause (B) of Para 12 of Part II of 4th Schedule of the Ordinance.

- Disclosure of cash and bank balances is not in accordance with Sub-clause (xii) of Clause (A) of Para 6 of Part II of Fourth Schedule to the Ordinance.

8. In view of the above, a notice dated January 18, 2002 was issued to Mr. Muhammad Akbar Alam of M/S M.A. Alam & Company, Chartered Accountants to show cause as to why action under Section 260 of the Ordinance and Rule 35 of the Rules may not be taken against them for the contraventions of the mandatory provisions of the Ordinance and Rules. The reply to the show cause notice was received through letter dated April 11, 2002. In order to provide an opportunity of personal hearing, the case was fixed on June 26, 2002. On the date of hearing Mr. Rizwan Badar, Assistant Supervisor, appeared on behalf of Mr. Muhammad Akbar Alam.

9. In the written submissions as well as at the time of hearing, it was contended that the aforesaid revised Form 35-A was circulated by the Institute of Chartered Accountants of Pakistan (ICAP) on September 13, 2000 with the instruction that the same would be applicable with immediate effect except to those draft format which had been initialed for identification purposes and sent by the auditors to their clients. The report in this case was stated be sent before September 13, 2000. A copy of letter dated August 18, 2000 addressed to Mr. Shamim Rizwan, Director of the Company was also placed on record. It was contended that ISA 23 required that if the financial statements were not prepared on going concern assumption that fact should be disclosed in the financial statements. The net loss sustained by the Company during the year was less than the loss of last year. Moreover, said losses were being faced by the whole textile industry. The Company was utilizing 85% of its total production capacity, the credit worthiness of the Company had improved and the management was hopeful for rescheduling of loans for repayment. So far as para 25 of IAS 1 was concerned, the Company had no policy regarding employee's retirement benefits. Whereas the accrual basis of accounting was concerned, the annual accounts had been prepared on the same basis. Regarding other disclosures, it was stated that the same were inadvertently overlooked and would be taken care in the future audits. Mr. Rizwan Badar, however, admitted the defaults and requested for lenient view.

10. I have given careful consideration to the arguments advanced on behalf of Mr. Muhammad Akbar Alam, however, the most of them are found unsatisfactory. In view of the fact that the auditor has initialed his report before the September 13, 2000, the issue raised in this regard is hereby dropped. The omission of expression of opinion on the disclosure requirements of International Accounting Standards as well as Fourth Schedule to the Ordinance cannot be ignored. It is ironical that the auditor has not modified his report on the issue of going concern. In this regard, I would like to refer to para 16 of Auditing Standard 23 (Going Concern) which requires that if adequate disclosure is made in the financial statements, the auditor should ordinarily express an unqualified opinion and modify the auditor's report by adding an emphasis of the matter paragraph that highlights the going concern problem by drawing attention to the note in the financial statements that discloses the matters set out in paragraph 15. The accounts neither include such disclosure nor auditors have given any opinion in this regard. Moreover, they have failed to provide the audit evidence gathered to resolve the question regarding the company's ability to continue as going concern in operation for the foreseeable future. The other replies of the auditors are also unsatisfactory as they had not been able to give any justifiable excuse for the contraventions. The carelessness of the auditors is obvious, and it is abundantly clear that the Auditors have failed to perform their duties with reasonable degree of care and skill. There could be no other opinion except that the auditors have been grossly negligent in the performance of their duties. The Audit report, therefore, has been made otherwise than in conformity with the requirements of Section 255 of the Ordinance.

11. The Ordinance laid down provisions regarding several matters to be followed by the company in regard to the preparation of the accounts. The International Accounting Standards have been adopted to improve the quality of the financial statements and to improve increased degree of comparability. It is the responsibility of directors to ensure that these provisions of law are followed in letter and spirit. At the same time, it is the duty of the Auditor to bring to the notice of the members the major breaches observed in the financial statements. The International Accounting Standards and Auditing Standards must be followed by the Auditors to ensure that financial statements are prepared in accordance with the Generally Accepted Accounting Principles and that the auditors carry out their responsibilities in accordance with the Generally Accepted Auditing Standards. M/S M.A. Alam & Company, has not followed the prescribed practices and above stated mandatory requirements of law.

12. The shareholders are the ultimate entity to whom the auditors are responsible. They are supposed to keep this in mind while auditing the accounts of a company and reporting thereon. Keeping in view the shareholding structure of most of the listed companies, the sponsoring directors manage to appoint auditors of their own choice in the annual general meetings. It would have a devastating affect, if the auditor signs a clean report on the misleading accounts or otherwise breach the mandatory requirements while auditing accounts and reporting thereon.

13. In view of the foregoing, the undersigned is convinced that an action against the Auditor is necessary. As the Auditor has admitted the default and have not been able to give any justifiable excuse for the same, therefore, I consider it a deliberate act on the part of Mr. M.A. Alam who were under legal obligation to perform its duties, in the course of audit of Accounts of the Company and reporting thereon, in accordance with the provisions of the Ordinance, International Accounting Standards and Auditing Standards.

14. For the reasons stated above, I impose a fine of **2,000** (Rupees two thousand) under Sub-section (1) of Section 260 of the Ordinance on Mr. Muhammad Akbar Alam.

15. Mr. Muhammad Akbar Alam is directed to deposit the above stated fine in the designated Bank Account of Securities and Exchange Commission of Pakistan maintained with Habib Bank Limited within 30 days of the date of this Order and furnish a receipted challan to the Securities and Exchange Commission of Pakistan.

RASHID SADIQ
Executive Director (Enforcement & Monitoring)

Announced
June 28, 2002
ISLAMABAD