

Securities and Exchange Commission of Pakistan
Enforcement and Monitoring Division
7th Floor, NIC Building, Jinnah Avenue, Blue Area, Islamabad

Before Rashid Sadiq, Executive Director

In the matter of
MR. MUHAMMAD KALEEM RATHOR, FCA

Number and date of show cause notice	19 (624) CF /ISS/2001 dated November 13, 2001
Date of hearing	November 20, 2001
Present	Mr. Irfan Ahmed Bhatti, ACA

**ORDER UNDER SUB-SECTION (1) OF
SECTION 260 OF THE COMPANIES ORDINANCE, 1984**

Mr. Muhammad Kaleem Rathor is a Fellow Member of the Institute of Chartered Accountants of Pakistan (the "ICAP"). His Registration Number is 487 and the date of registration with ICAP is October 15, 1968. He is a practicing Chartered Accountant and is conducting his business under the name and style of '*Kaleem & Co.*' at 3rd Floor, Hafeez Chambers, 85-Shahrah-e-Quaid-e-Azam, Lahore. Kaleem & Co., was appointed as auditor of M/S Brothers Textiles Limited, a listed company (hereinafter referred to as the "Company") in its Annual General Meeting held on March 29, 2000 to hold office from the conclusion of the said meeting until the conclusion of next Annual General Meeting.

2. The Audited Accounts for the year ended June 30, 2000 (the 'Accounts') of the Company were examined and it was found that the Company has issued a corporate guarantee to Bank Al-Falah Limited on behalf of its associated undertaking namely, M/S Brothers Engineering (Private) Limited in

contravention of the provisions of Sub-section (1) of Section 195 of the Companies Ordinance, 1984 (the “Ordinance”)

3. It was also noted from the Accounts that the Company has not followed several requirements of the following International Accounting Standards (IAS) in regard to the accounts and preparation of the Balance Sheet and Profit and Loss Account for the year ended September 30, 2000:

- i) IAS-1 (Presentation of Financial Statements)
- ii) IAS-17 (Leases)
- iii) IAS-32 (Financial Instruments: Disclosure and Presentation)

4. It was further discovered from the perusal of the Accounts that the Company has not complied with the several mandatory requirements of the 4th Schedule to the Ordinance.

5. Mr. Muhammad Kaleem Rathor, the Auditor of the Company, however, has not drawn attention of the members in his Audit Report signed on March 08, 2001 towards the aforesaid contraventions/non-disclosures in the Accounts and instead has given a clean report to the members of the Company as is evident from the following paragraphs of his Audit Report:

QUOTE

“the balance sheet and profit and loss account together with notes thereon have been drawn up in conformity with the Companies Ordinance, 1984.”

“in our opinion and to the best of our information and according to the explanations given to us, the balance sheet, profit and loss account, cash flow statement, statement of changes in equity together with notes forming part thereof conform with the approved accounting standards as applicable in Pakistan, and, give the information required by the Companies Ordinance, 1984 in the manner so required and respectively give a true and fair view of the state of the company’s

affairs as at September 30, 2000 and of the profit, its changes in equity and cash flows for the year then ended.”

UNQUOTE

6 The Commission, through its letter dated August 13, 2001, brought the aforesaid contraventions/non-compliances of the law to the notice of the Auditor in response to which, Mr. Imran Bhatti, ACA, acting on behalf of Mr. Muhammad Kaleem Rathor stated as under:

“Cross Company Guarantee

The point was ignored on the basis of our understanding that the company due to circumstances beyond its control had to issue the guarantee and the audited accounts had fully disclosed the particulars of this guarantee.

**Requirements of International Accounting Standards
and 4th Schedule of the Companies Ordinance, 1984**

You must be aware of the fact that many amendments in the existing International Accounting Standards and a series of new International Accounting Standards have been introduced in last couple of years. These amendments/additions in International Accounting Standards have caused the omissions of these requirements.”

7. The above quoted comments show a clear admission and acknowledgement of the failure of the Auditor to report contraventions and non-compliances to the members of the Company. It also indicates that the Accounts of the Company do not conform to all approved accounting standards and also do not give all the information required by the Ordinance in the manner so required. It appeared that the Auditor has not performed his duties with reasonable degree of care and skill. The Commission felt concerned about the quality of the Audit of Accounts of the Company conducted by Kaleem & Co. Chartered Accountant and, therefore, it was decided to examine this matter further.

8. Consequently, a Show Cause Notice No.19 (624) CF/ISS/2001 dated November 13, 2001 was issue to Mr. Muhammad Kaleem Rathor to show cause, in writing, and to appear before the undersigned on Tuesday, November 20, 2001 at the Companies Registration Office, Associated House, Egerton Road, Lahore to explain as to why penalty may not be imposed on him as provided under Sub-section (1) of Section 260 of the Ordinance for the aforesaid contraventions.

9. On the date of hearing, Mr. Irfan Ahmed Bhatti appeared on behalf of Mr. Muhammad Kaleem Rathor and submitted his arguments. He also filed a reply to the show cause notice. He, however, admitted the defaults and requested for a lenient view of the said defaults. He also assured that all the requirements of law would be properly fulfilled in future.

10. Summary of the verbal and written contentions of Mr. Muhammad Kaleem Rathor, briefly stated, are as follows:

- i) The issue of corporate guarantee was ignored on the basis of understanding that the Company beyond its control had to issue the guarantee and the audited accounts fully disclosed the particulars of this guarantee.
- ii) Many amendments in International Accounting Standards and a series of new International Accounting Standards have been introduced in last couple of years, which have caused the omissions of these requirements.
- iii) All the requirements of the Ordinance were fulfilled except a few, which were not material on shareholders' point of view.
- iv) The Audit was conducted on test basis and there is always a risk of omission to some extent.
- v) The defaults were not willful and deliberate.

11. Before proceeding further, it would be beneficial to discuss the relevant provisions of law and their violation by the Auditor of the Company. Clause (i) of Sub-section (2) of Section 234 requires that the Balance Sheet and Profit and Loss Account or the Income and Expenditure Account:

“in the case of a listed company, comply with the requirements of the Fourth Schedule so far as applicable thereto.”

12. The provisions of Clause (i) of Sub-section (3) of Section 234 of the Ordinance requires that in the case of a listed company:

“such International Accounting Standards and other Standards SHALL be followed in regard to the accounts and preparation of the balance sheet and profit and loss account as are notified for the purpose”

13. Sub-section (3) of Section 255 requires that the Auditor SHALL make a report to the members of the company stating, among others, as to whether the Balance Sheet and Profit and Loss Account together with notes thereon have been drawn up *in conformity with the Companies Ordinance, 1984* and as to whether the Balance Sheet, Profit and Loss Account, Cash Flow Statement, Statement of Changes in Equity together with notes forming part thereof *conform with the approved accounting standards as applicable in Pakistan* and, *give information require by the Companies Ordinance, 1984 in the manner so required.*

14. The above stated provisions of the Ordinance are mandatory and it is the responsibility of the Auditor to ensure that the Audit is conducted in the manner provided in the Ordinance and to report non-compliances/contraventions of the mandatory requirements of the Ordinance to the members of the company. The arguments that the point was ignored, the requirements were not material on shareholders point of view and the risk of omission are not justifiable reasons and are not acceptable. I am also shocked at the argument that many amendments in International Accounting Standards and a

series of new International Accounting Standards have caused omissions of the requirements. Instead of improving the level of his skills and professional competence required to enable him to perform his duties with due care, he has put blame on the frequency of the new Standards and amendments therein. I impress upon Mr. Kalem Rathor to go through Auditing Standard AS-7 (Quality Control for Audit Work) and ensure to establish standards and quality control policies and procedures. ICAP should also look into this matter because such remarks by a practicing Chartered Accountant bring discredit to ICAP and the profession of Accountancy.

15. The Company has violated the aforesaid provisions of the Ordinance as is apparent from the above discussion. It was, therefore, incumbent on the Auditor to have drawn attention to the members of the Company towards these major non-compliances/contraventions in his Audit Report. The statement in the Audit Report that the accounts give the information required by the Ordinance in the manner so required and further the Accounts conform with the approved accounting Standards is incorrect and misleading. The Audit Report, therefore, is made than otherwise in conformity with the provisions of Section 255 of the Ordinance. Thus, the Auditor has made himself liable for punishment under Sub-section (1) of Section 260 of the Ordinance.

16. Failure of the Auditor to discover that the Company has issued a corporate guarantee of the value of Rs 40 million on behalf of its associated company in contravention of the provisions of Section 195 of the Ordinance could have been resulted into loss to the Company. However, through its timely action, the Commission has directed the Company to cancel of the said guarantee and the Company was saved from a major loss, which could have been caused in case of encashment of the said corporate guarantee. This having not been done, the Auditors Report has failed to bring this material fact about affairs of the Company to the attention of the members. On this issue also, the Auditor has made himself liable for punishment under Sub-section (1) of Section 260 of the Ordinance.

17. 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. 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 establish standards, which are required to 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 his responsibilities in accordance with the Generally Accepted Auditing Standards. Mr. Kaleem Rathor has not followed the prescribed practices and above stated mandatory requirements of law. ICAP has the responsibility as frontline regulator to look into such serious issues and ensure that its members strictly follow the mandatory statutory requirements.

18. In view of the foregoing, it is established that Auditors Report on the Accounts is made otherwise than in conformity of the requirements of Section 255 of the Ordinance and also the Audit Report has failed to bring material fact, as stated above, about the affairs of the Company. As the Auditor has admitted the defaults and has not been able to give any justifiable excuse for the same, therefore, I consider it a deliberate act which is certainly more than mere omission and default on the part of Mr. Muhammad Kaleem Rathor who was under legal obligation to perform his 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. Mr. Muhammad Kaleem Rathor has, therefore, made himself liable for punishment under Sub-section (1) of Section 260 of the Ordinance.

19. For the reasons stated above, I impose a fine of **Rs 2,000** (Rupees two thousand only) on Mr. Muhammad Kaleem Rathor under Sub-section (1) of Section 260 of the Ordinance read with Section

476 of the Ordinance. The manner in which audit Report has been made involves a serious breach of trust by Mr. Muhammad Kaleem Rathor, FCA for which the penalty imposed on him is both justified and necessary.

20. In addition, I also consider it necessary to issue a WARNING to Mr. Muhammad Kaleem Rathor to be more conscious, careful, and mindful in future and perform his duties with a reasonable degree of care and skill. His performance has brought disgrace to the noble profession of Accountancy. Such kind of professional negligence in the performance of duties is undesirable and unacceptable for practicing Chartered Accountant. The quality of services to the users of the financial statements can be improved only when the practicing members of ICAP implement quality control policies and procedures, which ensure that all audit are conducted in accordance with the Auditing Standards, International Accounting Standards and the provisions of the Ordinance.

21. Mr. Muhammad Kaleem Rathor is directed to deposit the above stated fine in the following Bank Account of Securities and Exchange Commission of Pakistan within 30 days of the date of this Order and furnish a receipted challan to the Securities and Exchange Commission of Pakistan.

Account N0. 10464-6
Habib Bank Limited
Habib Bank Plaza, Shahrah-e-Quaid-e-Azam
LAHORE.

RASHID SADIQ
Executive Director (Enforcement & Monitoring)

Announced
December 28, 2001
ISLAMABAD