



Securities and Exchange Commission of Pakistan
Company Law Division
(Enforcement Department)

[Islamabad]

Before Mr. Tahir Mahmood, Executive Director (Enforcement)

Order

In the matter of

M/s SOUTHERN NETWORKS LIMITED

Under Section 226 Read With Section 229 And Section 472
Of The Companies Ordinance, 1984

Show Cause Notice No. and Date: EMD/233/652/2004-8828, dated 7.03.2006

Date of final hearing: 16.07.2007

Present: Mr. Nisar Ahmed, Director on behalf of Chief Executive of M/s Southern Networks Limited

Date of Order: 1.08.2007

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The case before me pertains to the proceedings initiated against the Chief Executive of M/S Southern Networks Limited (the "Company") under Section 226 of the Companies Ordinance, 1984 (the "Ordinance").

2. In order to dispose of the aforesaid matter, it is necessary to have a quick glance into the background facts leading to the issue of the Show Cause Notice by the Enforcement Department of the Commission. Examination of Company's Annual Audited Accounts for the year ended June 30, 2005 (the "Accounts") and further enquiry from the Company revealed that:

- a) As per Note 8 (Long Term Security Deposits) an amount of Rs.15.55 million (2004: Rs.27.2 million) was disclosed as mark-up free security deposits given by the Company's Dealers (the "Dealers") and were stated as refundable after the termination of contract.
- b) These deposits were received from Dealers for the purpose of granting agencies for collection of monthly subscription from the customers and sale of company's Set Top boxes to the customers.
- c) The deposits obtained were in the normal course of carrying out business of the Company as such no separate bank account was opened being not required.



Securities and Exchange Commission of Pakistan

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3. The Enforcement Department being un-satisfied with the explanation furnished by the Company, issued a Show Cause Notice dated 7.03.2006 for violation of Section 226 of the Ordinance to Mr. Tahir A. Khan, Chief Executive of the Company.

4. In reply to the Show Cause Notice, the Company through its various replies while admitting the default made following submissions:

- a) The Company is engaged in the business of Cable TV operations through satellite. To receive service of the Company at the subscribers' end, an expensive item is imported like Special Antenna and Set Top Boxes (the "Equipment") which is required to be installed at the subscriber site against which subscription of Rs.350 per month is charged by the Company.
- b) The marketing, installation and collection of monthly subscription was channelised by the Company through territorial distributors appointed through Dealership Agreement.
- c) The deposits were obtained under the agreements from the Dealers and refunded whenever Dealership Agreement was terminated or altered.
- d) These deposits were obtained in the normal course of business in order to secure the payment due from the Dealers against sale/supply of equipment and monthly subscription and as such no separate bank account was opened being not required.
- e) With regard to direction under section 472 of the Ordinance to deposit whole outstanding amount on account of Dealers' Deposit, almost whole amount of the Security Deposit has already been adjusted, refunded till date with the exception of Rs.1 million (as per letter dated 9.09.2006) which was expected by the Company to be refunded before 31.12.2006 and this amount is also in the process of adjustment/refund as the Company has changed policy for marketing, installation and collection of subscription through Dealers
- f) The provisions of section 226 and 229 of the Ordinance are not attracted in the case because of the reasons, necessity and facts given narrated above and therefore proceedings be dropped.

5. After granting of various adjournments to the Company against their requests, the case was finally fixed for hearing on 16.07.2007. On the date of hearing, Mr. Nisar Ahmed, Director who appeared on behalf of Chief Executive of the Company, reiterated the same arguments as were earlier stated by the Company in its afore stated written replies and requested for a lenient view in the matter. Mr. Nisar also provided, as a sample, a copy of one of the dealership agreements ("Agreement") of the Company.

6. Before proceeding further, it is necessary to advert to the provision of law, which has been violated by the Chief Executive of the Company. These are contained in Section 226 of the Ordinance and are, to the extent relevant, reproduced as follows:

"226. Securities and deposits, etc.-

No company, and no officer or agent of a company, shall receive or utilise any money received as security or deposit, except in accordance with a contract in writing; and all moneys so received shall be kept or deposited by the company or the officer or agent concerned, as the case may be, in a special account with a scheduled bank:



Securities and Exchange Commission of Pakistan

Company Law Division
(Enforcement Department)

Provided that this section shall not apply where the money received is in the nature of an advance payment for goods to be delivered or sold to an agent, dealer or sub-agent in accordance with a contract in writing.”

7. The aforesaid provisions of law are clear and explicit. The objective of these provisions is to secure the amounts collected from the dealers of the Company from being mis-utilized. The Company was required to act like a trustee of the dealers through the mechanism of:

- a) Receiving or utilizing any money received as security or deposit, only in accordance with a contract in writing.
- b) Keeping the deposits in a separate bank account.

Such amounts are unsecured if kept in Company's own bank accounts as if the Company goes insolvent, the dealers would be the worst sufferers.

8. The arguments extended by the authorized representative of the Company have been analyzed and not found satisfactory due to the following reasons:

- a) Note 8 to the Accounts discloses the following:

“This represents mark-up free deposits by the dealers and are refundable after the termination of contract.

It appears from the above that this represented security deposits and not advances.

- b) The following extracts from the Agreement endorse the fact that the sum was in the nature of security deposit and that Company failed to comply with the provisions of Section 226 of the Ordinance.

16.b. Any unutilized Security deposit paid by the Distributor hereunder will be returned to the Distributor after termination or expiry of the Agreement provided, if upfront commission has been paid on any connection, charge backs have been processed for those connections and deduction of all outstanding amount the Distributor owes to Sun TV.”

It is clear from the above that the deposits received by the Company were in fact security deposits and the Company failed to fulfill the requirement of the aforesaid provision of the Ordinance to keep the deposits of the Dealers in separate bank accounts and wrongly assumed that the Company is exempt from the requirements as laid down in Section 226 of the Ordinance

9. For the foregoing, I am of the considered view that the Chief Executive has breached the mandatory requirements of Section 226 of the Ordinance. An action, therefore, is necessary under Section 229 of the Ordinance, which provides that whosoever contravenes or authorizes or permits the contravention of any of the provisions of Section 226 shall be punished with a fine which may extend to five thousand rupees and shall also be liable to pay the loss suffered by the depositor of security on account of such contravention. However, considering the fact that the Company has made effort to rectify the default in response to issuance of Show Cause Notice by the Commission which is evident from the reduction in the amount of security



Securities and Exchange Commission of Pakistan
Company Law Division
(Enforcement Department)

deposits from Rs.15,550,000 on 30.06.2005 to Rs.397,273 on 30.06.2006, I am inclined to take a lenient view of the default. I, therefore, instead of imposing maximum penalty, impose a fine of Rs.2,000 (Rupees two thousand only) on the Chief Executive of the Company under Section 229 of the Ordinance.

10. The Chief Executive of the Company is hereby directed to deposit the aforesaid fine in the designated bank account maintained in the name of Securities and Exchange Commission of Pakistan with Habib Bank Limited within thirty days from the receipt of this order and to furnish receipted challan to the Commission in this regard failing which proceedings for recovery of the fines as an arrear of land revenue will be initiated. It should also be noted that the said penalty is imposed on the Chief Executive in his personal capacity and he is required to pay the said amount from his personal resources.

11. In view of the above, the Chief Executive of the Company is advised to undo the above irregularities by ensuring that all moneys so received as security deposit from Dealers should be kept or deposited by the Company in a special account with a scheduled bank in accordance with Section 226 of the Ordinance and submit a compliance report within 30 days of the date of this Order.

Tahir Mahmood
Executive Director (Enforcement)

Ali Azeem Ikram
Director (Enforcement)

Announced
1.08.2007
Islamabad