

Before Dr. Sajid Qureshi, Executive Director (CL)

In the matter of

M/S Wali Oil Mills Limited

Under Section 86(3) read with Section 492 of the Companies Ordinance, 1984

Number and date of notice	No. CO.233/123/2002 dated October 28, 2005
Date of hearings	February 27, 2006 July 28, 2006
Present	Mr. Irfan Malik, Consultant Mr. M. Farooq Akhtar, Attorney
Date	August 24, 2006

ORDER

This order shall dispose of the proceedings initiated through Show Cause Notice No. CO.EMD/233/123/2002 dated October 28, 2005 against Wali Oil Mills Limited (the "Company") under the provisions of Section 86(3) read with Section 492 of the Companies Ordinance, 1984 (the "Ordinance").

2. The Company was incorporated in Pakistan as a private limited company under the Companies Ordinance, 1984 and converted into public limited company on April 14, 1991. The shares of the Company are listed on the Lahore Stock Exchange. The paid up capital of the Company is Rs.144 million divided into 14.4 million ordinary shares of Rs.10 each. The Company is principally engaged in the business of extracting manufacturing, refining and sale of edible oil. The Mill is located at District Sheikhpura, Punjab. The Company has 265 shareholders comprising individuals only and as per its pattern of shareholding annexed to the Directors' Report in the accounts for the year ended June 30, 2005, directors, their spouses and minor children hold 88% of the total shareholding increased from 75% after the right issue in 2004. This indicates that there is considerable public interest in the Company. Board of Directors of the company as per its annual report for the year ended June 30, 2005 comprises the following persons:

SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet - I -

1.	Haji Muhammad Bashir, Chief Executive
2.	Mr. M. Farooq Asghar, Director
3.	Mr. Muhammad Aamir, Director
4.	Mr. Badar Muneer, Director
5.	Mr. Fayyaz Ahmed, Director
6.	Mr. Ahmed Bilal, Director
7.	Mr. Zafar Iqbal, Director

3. Brief facts of the case are that during examination of annual accounts of the Company for the year-ended June 30, 2005 it was observed that share capital of the Company was increased from Rs.48 million in 2004 to Rs.144 million in 2005 as a result of 200 % right issue at par on April 05, 2004 under the Companies (Issue of Capital) Rules, 1996 (“Rules”). Further, it was noticed from note 3.1 to the accounts that the Company on April 05, 2004 offered right shares at par which have been subscribed by the directors of the Company and balance taken up by underwriters to the issue as at September 13, 2004. Directors’ loan to the extent of Rs. 93.930 million was shown as adjusted against the issue of right shares. Moreover, on perusal of the underwriting agreement it was discovered that Mr. Badar Muneer and Mr. Fayyaz Ahmed, directors of the Company were joint underwriters to the issue in the ratio of 50% each. The appointment of directors as underwriter was in violation of the Balloters, Transfer Agents and Underwriters Rules, 2001 which attracts penal provisions contained in Section 22 of the Securities and Exchange Ordinance, 1969.

4. It was noticed that the letter of rights dated April 14, 2004 sent to the shareholders and filed with the Registrar pursuant to Sub-section (3) of Section 86 of the Companies Ordinance, 1984 (the “Ordinance”) revealed the following as purpose of the right issue:

The funds are required to meet the need of working capital of the Company, to utilize full working capacity of the mill and improve the liquidity position, to pay off long term liabilities and for financial capital expansion being planned in the coming years.

Moreover the benefits likely to accrue from the proposed issue were stated as follows:

- ***Increase in the production capacity of the Company.***
- ***Improvement of the liquidity position of the Company and to pay off long term liabilities.***
- ***Increase in revenue and profitability of the Company and resultantly enhancing the expected returns to the shareholders.***

5. From perusal of financial projections prepared pursuant to Rule 5 of the Rules it was noticed that the project implementation was altogether in contrast with the financial projections. It was observed that the proceeds of the right issue were not utilized for the purposes disclosed in the financial projections submitted to the shareholders at the time of approval of right issue; instead these appeared to have been utilized for repayment of directors' loan. The post right issue scenario presented before the shareholders through the aforementioned circular was also not visible; rather the latest financial results depicted the adverse financial position of the Company, as the loss for the year amounted to Rs. 27.866 million compared to the projected profit of Rs. 7.980 million.

6. The above observations raised concerns about the state of affairs of the Company, a Show Cause Notice (the "Notice") was then issued to the Chief Executive and directors of the Company on October 28, 2005 asking them to explain the violation of Balloters, Transfer Agents and Underwriters Rules, 2001 and why penal action under the provisions of Section 492 of the Ordinance may not be invoked against the Company for making incorrect statements in the circular filed with the registrar pursuant to Sub-section (3) of Section 86 of the Ordinance.

7. The company submitted reply to the notice on November 18, 2005. Wherein, following submissions were made:

- With market value of the shares of the Company continuously being under par, it was not possible to find corporate underwriters making it necessary instead, to resort to other willing underwriters, the directors of the company. Further, Section 86(7) of the companies Ordinance, 1984 gives complete discretion to the directors to allot and issue unsubscribed shares in such manner as they may deem fit.
- The objective as envisaged for issue of right shares including utilization of proceeds thereof are the same as observed in your notice. The subsequent circumstances, due to depressed market condition resulted in reduction in actual production. The Company, instead of producing oil themselves by seed crushing was forced to engage in refining edible oil purchased in raw form. Despite adverse circumstances the Company paid off the long term liabilities of Rs. 37.5 million outstanding as on June 30, 2004 and short term borrowings have been reduced from Rs. 499.6 million to Rs. 177.1 million as at June 30, 2005.
- The Directors further injected Rs. 18 million during the year ended June 30, 2005 and total outstanding interest free loan from directors and associated amounts to Rs. 114 million as on June 30, 2005.

SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet - 3 -

8. The submissions of the Company as regards its actual performance in comparison with projections was not well supported, and on the basis of an examination, limited to the extent of information disclosed in the financial statements of the Company, the following facts were revealed:

- Effect of right issue vis a vis the production and performance of the Company was analyzed as follows:

	Before right issue	After Right issue
Production (Metric Tons)		
<i>Cotton Seed</i>	-	-
<i>Sunflower Seed</i>	11,192	886
<i>Rape Seed</i>	62,210	33,154
<i>Soybean Seed</i>	10,079	-
Revenue	1,919,096,044	1,520,341,011
Profitability		
<i>Net result after tax</i>	9,602,047	(27,865,595)

It was noted that none of the commitments made with the shareholders was materialized; rather a bleak effect was visible on the overall financial position of the company. Main reason being the fact that right issue did not result in fresh injection of funds in the Company, as merely a book adjustment was made in the accounts whereby the directors' loans were converted into equity. Share capital of the Company increased from Rs. 48 million in 2004 to Rs. 144 million in 2005 which was all taken up by the directors and as a result holding of ordinary shareholders was diluted drastically.

- Moreover, the departure of actual results from those projected and submitted to the regulator cannot be attributed merely to the effect of adverse market conditions alone. The repayment/offsetting of directors' loan is in absolute violation of financial projections which when compared to actual cash flow disclosed as follows:

Cash flow from financing activities	Projected (2005)	Actual (2005)
Redeemable capital	22,500,000	-
Long term loan-Directors	110,900,113	(109,623,588)
Lease liability	16,427,519	(7,240,916)
Increase in capital	96,000,000	96,000,000
Short term borrowing	241,881,627	(322,553,532)

Cash flows also show an outflow of Rs. 5.2 million as dividend in the year 2006, which is clearly not foreseeable in the present state of affairs. The directors' loan was projected to be injected in year 2005 in addition to the right issue proceeds. Instead the directors actually withdrew these funds from the Company. Thus through misstatement of facts the directors managed to convert their long stuck loans into equity.

- The circular sent to the members along with the notice offering new shares pursuant to the requirements of Section 86 (3) did not mention anything about the planned conversion/repayment of loan against the right issue. Thus the facts appeared to have been misrepresented before the shareholders.
- The repayment of short term financing has been effected out of the funds generated from operations. The arguments regarding effect of depressed market condition on the results can not be considered as the financial plan submitted at the time of right issue was supposed to remain valid for relevant period and any revision, duly substantiated, should have been submitted to all stakeholders.
- It is also observed that out of right issue of Rs.9,600,000 ordinary shares 9,930,000 shares were taken up by the directors on account of underwriting and by subscribing to the right. Holding of ordinary shareholders in the Company diminished as directors increased their shareholding from 75% to 88%.

9. In order to give an opportunity to the management of the Company to clarify their position, a hearing was fixed on January 03, 2006, which was adjourned at the request of the Company and was re-fixed on January 25, 2006.

10. On the date of hearing Mr. Irfan Malik, Consultant appeared on behalf of the Chief Executive and directors of the Company.

11. During the hearing, submissions made in the written reply were reiterated. Violation of the Balloters, Transfer agents and Underwriter Rules, 2001 was not discussed as the issue had already been referred to the office of Executive Director (SM) due to transfer of power of adjudication to his office. As regards the lack of any visible improvement in the financial results of the Company when compared to the financial projections and benefits of right issue not being tangible, it was stated that the management foresees better results in the near future. It was stated that the directors have been advancing loans to the

Company from time to time and their commitment can be judged from the fact that total outstanding interest free loan from directors and associated amounts to Rs. 114 million as on June 30, 2005. Regarding the misrepresentation in projections with respect to directors' loan no satisfactory answer could be submitted.

12. While the department was in the process of finalizing the case, a letter was received from the Company intimating that it has been decided to pursue the case through M/s Yousuf Adil Saleem & Co. Chartered Accountants for submission of additional grounds. The request was accepted by the Commission and the case was fixed for hearing on April 18, 2006 which was subsequently adjourned and finally fixed on July 28, 2006.

13. On the date of hearing Mr. M. Farooq Akhtar represented the directors and submitted his written representations with the note that these arguments may be treated as in addition to, and not in substitution of, submissions made in written reply. Relevant extracts are reproduced below:

- *Circular under section 86 is required to be filed with concerned Company registration Office and not with SECP (HQ). It is a "return for CRO" and CRO has found it correct and, accordingly accepted and acknowledged it. Circular 86 is not a "prospectus" and hence, beyond the jurisdiction of SECP (HQ). Similarly "Notice of Right Issue" is not a "Return" prescribed by the Companies Ordinance or SECP. It is also not prospectus. SECP has no jurisdiction to question notice of Right Issue.*
- *Why reliance is not made on the disclaimer by the management in the "Notice of Right Issue"*
- *All the steps for right issue were taken by the Company under the nose and eyes of SECP and SECP did not point out any anomaly in the process that was nor rectified. SECP is privy to the whole proceedings in this regard.*
- *Right issue was made in April/ May 2004. Penal proceedings after two years of its occurrence, erodes the sub-stratum of Show Cause Notice. It renders the whole proceedings as nullity in the eyes of Law. It smacks of malafide / malicious proceedings especially as no one at all was injured or harmed by the right issue.*

Finally it has been prayed that impugned Show Cause Notice, may graciously be withdrawn and the Management of the Company be allowed to complete delisting process so as to enable it to concentrate on its business for the development and prosperity of Pakistan. The learned Council also stated that the order may be passed on the basis of his afore-mentioned written representations.

14. I have taken into consideration the submissions, made in writing as well as those at the time of hearings of this case and observed that the circular communicating right offer to the shareholders filed with the Registrar and shareholders pursuant to Section 86 (3) of the Ordinance did not disclose the actual intentions of the Directors that the right issue proceeds would be utilized towards conversion of directors' loan into equity. Moreover, the material variances between the financial projection and actual results reflect that necessary due diligence was not done while making investment decisions. This resulted in the Company failure to translate the projected results into reality and raises concerns about the managements' representations made before the shareholders and the Commission from time to time. The fundamental information regarding capital inflow, directors' loan, and operating results provided in the projections for the offer of the right issue was thus rendered inaccurate and material facts were omitted. Moreover, it was also felt that the preparation of financial projections and their submission to the regulator was not given due seriousness by the Company as a result of which the financial impact of the right issue was miscalculated and hence misrepresented. It is further viewed that representations given in any public document are in effect management's undertaking and in the subject case these were incorrect and remained unfulfilled. The financial projections are part of the financial controls and current situation reflect lapses in the financial controls of the company.

15. Written representations submitted in second hearing were noticed to be silent regarding the misstatement by the management in financial projections and instead unnecessary questions regarding the jurisdiction issues have been raised. It is pertinent to point out that the Securities and Exchange Commission of Pakistan has been established for the beneficial regulation of capital markets, superintendence and control of corporate entities and for matters connected therewith and incidental thereto. The document in question i.e. the right issue projections, is not just a return, it is a fundamental tool that gives an insight into the existing financial position of the Company, the level of commitment of its management and its future outlook. The information contained in it, forms the basis of investment decisions of general public, its preparation and submission to the regulator and shareholders is therefore a sensitive issue. Accordingly, any commitments made by the Company to its shareholders are therefore watched by the Commission, in order to monitor the sanctity of management commitments and safeguard shareholders' interests. Moreover, incase due to changed circumstances, actual results deviate from those planned, unless those are disclosed appropriately before the stakeholders, these remain in effect and cannot be disregarded on the grounds that these were duly filed and submitted to the regulator. The financial year 2005 was the first financial close of the Company after the right issue and prompt action was taken by the Commission. It was noted that lack of professionalism and ill planning of the management resulted in the misstatement. The directors of the company, being a list company, should fulfill their responsibilities laid down in the Code of Corporate Governance and follow good financial

SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet - 7 -

practices, which in the present case are very much lacking. I am of the view that for a healthy corporate culture, which the Commission aims to achieve, it is expected that the directors of the listed companies would endeavor to bring in more transparency and enhancing confidence of the investors in the listed companies.

16. In view of the above, I instead of imposing maximum penalty of Rs.100,000 on the Chief Executive and each director as prescribed by Section 492 of the Ordinance, impose a ~~token~~ fine of Rs.50,000 on each of the following Directors and Chief Executive:

1.	Haji Muhammad Bashir, Chief Executive
2.	Mr. M. Farooq Asghar, Director
3.	Mr. Muhammad Aamir, Director
4.	Mr. Badar Muneer, Director
5.	Mr. Fayyaz Ahmed, Director
6.	Mr. Ahmed Bilal, Director
7.	Mr. Zafar Iqbal, Director

The afore-named persons are directed to deposit the aforesaid fine in the designated bank account maintained in the name of Securities & Exchange Commission of Pakistan in the Habib Bank Limited within 30 days of the date of this order and furnish a receipted challan to the Commission in this regard.

17. The Chief Executive and Directors of the Company are hereby directed to deposit the aforesaid fine totaling to Rs.350,000 (Rupees Three hundred and Fifty thousand only) 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 furnish receipted vouchers or pay by a DD/pay order issued in the name of Commission for information and record, failing which proceedings under the Land Revenue Act,1967 will be initiated which may result in the attachment and sale of movable and immovable property. It may also be noted that the said penalties are imposed on the Chief Executive and other Directors in their personal capacity who are required to pay the said amount from their personal resources.

Dr. Sajid Qureshi
Executive Director (CLD)