



Before Tariq Bakhtawar, Director (Enforcement)

In the matter of

Globe Textile Mills Limited

Under Section 196 Read With Section 472 Of The Companies Ordinance 1984

Number and date of notice	No. EMD/CO233/126/2002 dated March 20, 2008
Date of hearing	June 23, 2008
Present	Mr. Arif Habib, Chief Executive Mr. Mohammad Bashir, Company Secretary

INTERIM ORDER

This is an interim order in the show cause proceedings initiated vide notice No. EMD/233/126/2002/3684 dated March 20, 2008 under Section 196 read with Section 472 of the Companies Ordinance, 1984 issued to the chief executive and directors of Globe Textile Mills Ltd. ("GTML") namely: Mr. Arif Haji Habib, Ms. Farzana Arif, Ms. Gul Bano Haji Habib, Mr. Arshad Arif, Ms. Misbah Arif, Ms. Farzeen Fazl-e-Umar and Ms. Sameera Yasin Saya

2. Show cause notice (the "SCN") issued to the Directors of GTML required each of them to explain their position in writing within 14 days and appear in person on April 17, 2007 in respect of the following issues:

- a) Write-off of cotton stock worth Rs. 264.886 million, considered material, without approval of the Board of Directors by way of a resolution.
- b) Sale of stock worth Rs. 718.019 million, being sizable part of assets, without approval of the shareholders in a general meeting.
- c) Sale of balance and modernized machinery of Unit No. 1, being sizable part of assets, without prior approval of the shareholders in a general meeting.

3. The submissions by the respondents in writing or in person were not submitted at the given date and the written reply to the SCN was received on May 08, 2008 vide letter dated April 25, 2008 subsequent to issuance of reminders regarding non-receipt of response. Hearing of the case was held on June 23, 2008 wherein the Chief Executive and the Company Secretary appeared. The representations of the respondents on the aforesaid issues are as follows:



Write-off / sale of cotton stock:

The amount of Rs. 718.019 million relates to closing stocks and includes work-in progress and finished goods amounting to Rs. 42.609 million and Rs. 67.657 million respectively. As such the opening stock was Rs. 607.753 million. Further details are as under:

	Rs. in million
Opening Stock	607.753
Impairment of cotton	264.886
	342.867
Purchase of cotton (2006)	193.946
	536.813
Consumption (2006)	299.398
Closing stock as on 30-06-06	237.415
Sale of cotton (2007)	196.088
Loss on sale of cotton (2007)	41.327

The damaged cotton was sold as the Chief Executive was advised by the Technical Manager to dispose it off immediately otherwise it would damage the balance of good cotton. Thus the Chief Executive has taken the step to avoid further loss which definitely was in the interest of all the stakeholders of the Company. The loss on the sale of damaged cotton was reported as impairment of cotton.

The sale of damaged cotton could not be considered a write off. It was just like sale of waste or waste cotton. As such there was no need to have a resolution approved by the Directors under Section 196(2)(m)(i) of the Ordinance. The purchase of cotton, sale of yarn, sale of waste, sale of cotton and sale of damaged cotton does not fall under “the sale or otherwise dispose of the undertaking or a sizable part thereof” and as such there was no need for approval of the shareholders in the general meeting under Section 196(3)(a) of the Ordinance. The decision of disposal of damaged cotton was within the powers of the Chief Executive as it could not be termed as write off of inventories and other assets of the Company and is covered under the normal business of the Company.

Sale of machinery undergone BMR

In this connection it was pertinent to note that the unit was closed in first week of April 2006 and the resolution was passed on June 21, 2007 after a lapse of 14 months. It is obvious that the entire machinery had lost its efficiency. In the statement of material facts submitted under Section 160 of the Ordinance it was mentioned that the Directors be authorized to dispose off machinery and



equipment or part thereof as the Chief Executive and a Director deem fit. The resolution approved by the shareholders is very clear and does not restrict the authorized directors to limit the items of plant and machinery to be sold. BMR of the ring frames of the mills was undertaken, however the back process was not modernized, therefore the company could not benefit from it. Due to lay off the plant and machinery could not be restarted without a complete overhaul.

4. Before commenting on the submissions it would be beneficial to examine the scheme of law as regards the division of powers to be exercised on behalf of the Company. The statute establishes three distinct realms of authority in so far as running of the affairs of the company is concerned. The chief executive, the Board of Directors and the shareholders have been assigned specific powers and authorities. Moreover in case of the Board of Directors and the Shareholders the statute prescribes a particular manner through which these powers and authorities can be exercised. These three distinct realms of authority represent the levels of assurance required by particular transactions. The logical series of events in case the inventories lose their reported value would have been that their value would be brought down to reflect the net realizable value and the amount charged as impairment loss. Proceeds from subsequent sale of written down inventories would then be shown as gain/loss on sale. The authority to write-off the value of stocks to depict the net-realizable value fall under the powers assigned to the Board of Director as is clearly stated in Section 196(2)(m). Sale of written down stock then becomes routine business transaction falling within the powers of the Chief Executive. However, if even considered otherwise, the authority to decide on the sale/disposal of 30% of the assets of company, comprising its inventory, rest with the shareholders under Section 196(3)(a).

5. Reverting to the representation made that the Technical Manager advised to dispose it off immediately as otherwise it would damage the balance of good cotton, it has been observed that the report is not issued by an accredited institution and sole reliance regarding the certification of damage has been placed on the laboratory test report by the technical manager on the quality control. These reports have been examined and found to be non-specific as these provide no details about the damaged cotton bales. These test reports are unsigned and un-dated. The technical manager, himself is a graduate in textile engineering and does not possess certification/accreditation relating to the testing of cotton. Also otherwise, the reliance on these reports and any representation from the employees of GTML has to be much lower due to the weak internal controls and lack of governance. Moreover, the chief accountant of the company has stated that he did not inspect the damaged cotton personally and the amount and quantity of the impaired cotton were verbally conveyed to him by the chief executive.



6. It would be beneficial here to look into the importance of the statement of material facts annexed to the notice of general meeting. Its objective is that all members of the Company must know as to what was the exact nature of the business to be transacted at the meeting alongwith the material facts so that they can make a conscious decision by considering all important facts pertaining to the business. Material information are the facts, which have a bearing on the business to be transacted and which could influence the shareholders while making a decision of approving the business proposed or not.

7. The on-going BMR program of GTML can be evidenced from its audited financial statements. In a period of five years from 2002 to 2006 the audited financial statements of GTML shows that a total of Rs. 264.78 million was spent on additions to owned plant and machinery. GTML applies a 10% rate of depreciation on its plant and machinery thus estimating its useful life to be at least 10 years. The statement of material facts under Section 160 of the Ordinance clearly states that “*the company now proposes to sell the machinery and equipment which are outdated and unviable to operate*”. It may be pointed out that the criterion set forth for sale of machinery is the test of obsolescence and not of efficiency. It has been argued that resolution passed by the shareholders did not restrict the Chief Executive and Director from selling any part of plant and machinery of the GTML. However, the resolution cannot be read in isolation to determine the scope of the approval given by the shareholders. It has to be read jointly with the statement of material facts which defines the types of assets to be sold and limits the authorization for sale to only the assets that are outdated and unviable. The submission by the chief executive that the BMR, amounting to more than Rs. 264.78 million, was not beneficial for the company has added further ambiguity to the state of affairs of the company.

8. While reviewing the events/ transactions discussed earlier, the matter turns out to be more than obtaining the appropriate authorizations and approvals. The auditors report to the members on the financial statements for the years ended June 30, 2006 and 2007 were qualified on non-verification of impairment loss, disposal of impaired stock, mode of disposal of plant and machinery and related party liabilities. The inspection of books of accounts and records of the GTML carried out under Section 231 of the Ordinance reveal that the cotton stock impairment and its subsequent disposal, sale of machinery and short term loans from the related parties lack required level of transparency. Events and transactions, the way they have been executed, strongly raise our concern as deliberated below:

Damage and sale of Cotton Stock

Cotton stock comprising of 24,249 bales (out of a total stock of 48,480 bales), valuing Rs. 264.886 million was reported fully damaged due to rain water (Dec 2005-Feb 2006). Representation is not



substantiated by the virtual stock scene, stocks reported to the bank, vague profile and capacity of the buyer to consume / handle such a huge stocks. It is observed that:

- Single lot of cotton stock is tightly stacked over each other in layers of 5 to 8 bales that reach a height ranging between 8 to 20 ft, whereas at the time of peak flooding the water stood at approx 1 ft, making it virtually impossible for the rain water to surge up to the higher layers to cause the damage, except the cotton bales stacked at the bottom.
- The stock verification reports, submitted to bank, in respect of the cotton stocks that were pledged, certified that stock upto 35,056 bales was in good condition till March 31,2006, much later then the period of Dec 2005-Feb 2006 , when the damage was reportedly caused.
- Vague profile of the buyer of damaged cotton stocks and his questionable capacity to consume / handle such huge stocks. The stock was sold in a doubtful manner to one Mr. Abdul Sattar as waste at a price of Rs. 5.150 million only, in cash on April 29,2006.
- The report on the damaged stock is not issued by an accredited institutions and sole reliance regarding the certification of damage has been placed on the laboratory test report by the technical manager of the company. These test reports are unsigned and un-dated. The technical manager, himself is a graduate in textile engineering and does not possess certification/accreditation relating to testing of cotton.

Sale of Plant and Machinery

The management sought approval for sale of obsolete machinery and instead started selling the plant and machinery that had undergone BMR in 2004. The notice of Extra Ordinary General meeting held on June 21, 2007 seeking approval for the sale of assets was not submitted to the Commission. The statement of material facts, annexed with the notice, under Section 160 of the Ordinance did not provide complete and comprehensive information. The provisions of limited information regarding the assets proposed to be sold appears to have been designed purposely with the view to take advantage and empower the Directors to sell off balanced and modernized plant and machinery under the guise of obsolescence. The addition in plant & machinery in the recent years does not fit in this scenario and the question on the disposal of recent capital expenditure remains unanswered. The following additions to the plant and machinery have been disclosed in the financial statement of GTML:



Description	2006	2005	2004	2003	2002
	<i>Rupees in millions</i>				
Addition in Plant & Machinery					
Owned	67.892	95.925	0.761	83.502	16.700
Leased	15.000	-	-	18.965	94.200

Liabilities Payable to Related Parties

An amount of Rs. 160.5 million disclosed in the financial statements for the period ended on June 30, 2006 as short term loan from the related party was explained as loans from chief executive/director, injected in the company for repayment of bank loans that were borrowed from family sources. It is suspected that the funds were laundered through the accounts to disguise the source and it was observed that:

- Financial and commercial consideration of the lenders remain unexplained.
- Agreement / terms of reference governing the loans are not documented.
- The funds were injected subsequent to April 29, 2006, the date when stock had been wiped out. The chronology of the transactions raises suspicion that the stocks have been sold and part of the proceeds have been injected into the Company as short term loan.
- The pattern of the transfer of funds demonstrates that the accounts were used as a conduit to cover the identity.

9. Reviewing all the transactions i.e. (i) the impairment of stock and its subsequent sale (ii) sale of plant and machinery and (iii) short term loan from the related parties, it is apprehended that Directors have devised an elaborate scheme to obtain benefit for themselves and in doing so have deprived the shareholders of GTML.

10. An Agreement For Settlement Of Outstanding Liabilities was executed between M/S Globe Textile Mills Ltd (GTML), M/S Globe Textile Mills (OE) Ltd (GTMOL) and MCB Bank Ltd. Under the agreement the land and building of GTML will be transferred to the Bank at a price of Rs. 651.330 million. The sale price will be appropriated/ utilized in the following manner:

Settlement Proceeds	Rs. in million
Liability of MCB Bank Ltd	285.523
Liability of Askari Bank Ltd.	222.500
Payment to GTML	143.307



The amount of Rs. 285.523 million include Rs. 19.055 million being the liability of Globe Textile OE Ltd, an associated company however, it is not disclosed to the shareholders that assets / funds of the GTML would be used to settle the liability of the associated concern.

11. Under the terms of the Agreement for settlement of outstanding liabilities, a sum of Rs. 143.307 million will be paid to GTML on account of balance sale consideration after the transfer of the property / fixed assets in the name of MCB Bank Ltd.

12. The events and transaction suggest that an elaborate scheme has been devised to deprive shareholders of GTML and it is apprehended that funds may be siphoned out in a similar non-transparent way. Without prejudice to the powers/rights of the Commission to look into the potential losses caused to the company, it is imperative to ensure adequate protection to the shareholders. It is in line with the declared objective of the Commission that the interests of investors small or large shall be protected alike.

13. In the case of Sheikh Abdul Wahid & Others vs. Securities and Exchange Commission of Pakistan, M.A No.4 of 2007, it was held by the Honorable High Court of Sindh that it is one of the duties of Securities and Exchange Commission to ensure adequate protection of the investor by detecting unfair trade practices. In case any unfair practice is detected it should take all necessary measures to undo the wrong. This is necessary in order to maintain the confidence of ordinary shareholders of a company who are sitting at a distance waiting to reap fruit of their investments. They not being part of every decision making process of the company repose faith in the management which is expected to make sound commercial decisions for the collective benefit of all the shareholders. Such faith and trust cannot be allowed to be breached with impunity.

14. SECP has to rise to the occasion for taking appropriate measures to combat situations where unfair trade practices are noticed, which may or may not be conceived in advance. It was held by the Court that the power of SECP should be considered and interpreted in a way so as to see that the objects sought to be achieved by the Securities and Exchange Commission of Pakistan Act 1997 are fully served rather than being defeated on the basis of any technicality. The court went on to observe that SECP was entrusted with the power to make necessary measures as it thinks fit in order to discharge its duties and functions.

15. Therefore, the undersigned in the interests of the securities market and in exercise of powers under Section 196 of the Companies Ordinance 1984 directs as follows:



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

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- a) The GTML is hereby restrained from appropriating Rs. 143.307 million received on account of the balance consideration of sale of property under agreement for settlement of outstanding loan liabilities;
- b) The said amount will be kept in a separate remunerative bank / deposit account namely “The Globe Textile Mills Limited Shareholders Account” to be opened by the GTML with MCB Bank at MCB Bank, Main Branch, Karachi, till such time the concerns of the Commission are removed upon conclusion of the investigation proceedings pending under section 263 of the Ordinance. The MCB Bank is further instructed that the operational control of the said account will be under the instructions of the Commission.

Tariq Bakhtawar
Director Enforcement

Announced:
June 27, 2008