No. Co. 265/3/EM/2000-
SECURITIES & EXCHANGE COMMISSION OF PAKISTAN
(Enforcement & Monitoring Division)
State Life Building, 7-Blue Area
Islamabad

**IN THE MATTER OF INVESTIGATION INTO THE AFFAIRS OF M/S. UDL INDUSTRIES LIMITED**

| | | |
|---|---|---|
| Date of Show Cause Notice | : | 16-05-2000 |
| Date of hearing | : | 26-06-2000 |
| Present | : | None |
| Date or Order | : | 15-08-2000 |

**ORDER UNDER SECTION 265 OF THE COMPANIES ORDINANCE, 1984**

M/s. UDL Industries Limited was incorporated in 1965 and listed on Karachi Stock Exchange in 1970. At present its paid up capital is Rs. 12 million. The main object of the company is the manufacturing/assembling and trading in the electrical domestic appliances. On examination of the financial statements of the company for the last few years, it was revealed that the company which was earning reasonable profits till June 30, 1995 incurred losses of Rs. 6.9 million and Rs. 40.9 million for the years ended June 30, 1996 and June 30, 1997 respectively. Moreover, the fixed assets of the company bearing cost of Rs. 2.512 million and Rs. 4.573 million were sold/written off out of the total fixed assets of Rs. 12.364 million as on 1st July, 1996. To turn the affairs from bad to worst, the fixed assets decreased to Rs. 1.6 million as on 30.06.1998 and to Rs. nil as on 30.06.1999. The company finally ceased to operate since July 1, 1997, however, the Chief Executive continued to draw his salary and other benefits. The company repaid Rs. 23.116 million to its associated undertaking in the year 1996 & 1997 by borrowing short-term loans and from the proceeds realized on sale of assets of the company. It was further noted that assets of the company were disposed off without approval of shareholders in terms of Section 196 (3) of the Companies Ordinance, 1984.

2. The performance of the company from 1993 to 1996 is tabulated as follows:-

**(Rs. In million)**

| | **31.12.1997** | **31.12.1994** | **30.06.1995 (Six months)** | **30.06.1996** |
|---|---|---|---|---|
| Sales | 180.082 | 102.029 | 81.383 | 141.253 |
| Gross Profit | 36.616 | 22.001 | 15.984 | 25.176 |
| Net Profit (After tax) | 4.342 | 0.207 | 0.59 | (6.888) |
| Dividend | 20% | Nil | Nil | Nil |
| Assets (Depreciated value | 8.917 | 7.634 | 6.617 | 6.071 |
| Paid up capital | 12.000 | 12.000 | 12.000 | 12.000 |

3. However, the company's performance deteriorated significantly since July 1, 1996. The financial performance of the company thereon is summarized as follows:-

**(Rs. in Million)**

| | **30.06.1991** | **30.06.1998** | **30.06.1999** |
|---|---|---|---|
| Sales | 65.484 | 8.074 | - |
| Gross profit/(Loss) | 3.864 | 0.036 | - |
| Net Profit/(Loss) | (40.863) | (2.156) | 1.957* |
| Accumulated loss | (44.087) | (12.888) | (10.930) |
| Paid up capital | 12.000 | 12.000 | 12.000 |
| Value of Fixed Assets | 2.429 | 1.599 | Nil |

* Profit represents income on sale of Assets.

4. In view of above, a show cause notice under section 265 of the Companies Ordinance, 1984 served upon the company on May 16, 2000, requiring it to explain that why an inspector may not be appointed to investigate into the affairs of the company, as in the opinion of the Commission the affairs of the company were not being managed in accordance with sound business principles and prudent commercial practices and apparently there was non-compliance of the provision of section 196(3) also. The company furnished its reply through its Chief Executive taking position as follows:-

**QUOTE:-**

(i) section 196 (3) requires that directors will take consent of shareholders before selling of whole undertaking or major part thereof.

(ii) maximum total assets stood at Rs. 110.4 million as on 30.06.1995. Out of this, Rs. 103.8 million (94%) comprised of current assets like stock-in-trade, debtors etc.

(iii) in view of erosion of our gross profit (and foreseeing further losses on imports), we stopped making imports in 1997. Stock in trade and other current assets were realized and converted in bank balance in due course of time and was utilized in repayment of trading liabilities and interest based borrowings;

(iv) the assets were:-

- movable assets like Motor vehicles etc. (Rs. 2.1 million)
- land and Hub Industrial Trading Estate (HITE) (Rs.2.2 million). This land was purchased in 1983 but was not utilized since. concessions available were withdrawn.
- Plant & machinery (Rs. 1.7 million) which was installed in Mingora, Swat in a rented premises for assembling Black & White TV's.

**UNQUOTE**

5. The company further explained that disposal of moveable assets like stock in trade and Motor vehicles etc., is a normal business activity and no approval from shareholders was required. Land at HITE was surrendered to HITE at surrender value i.e., Nil. The plant and machinery was disclosed at the realizable value estimated at Nil value and therefore, the balance in accounts was written off. The company further argued that section 196 (3) becomes applicable where the company dispose off a major part of its manufacturing facilities or right to manufacture and situation in this case was not such. The company further argued that the fact of cessation of company operations was communicated to erstwhile CLA. As far salary drawn by Chief Executive, the company

argued that a salary of Rs. 261,104 was drawn by the Chief Executive only during the year 1996-97 which was approved by the shareholders. Explaining the reasons for huge losses suffered by the company, it was stated that company has suffered losses due to various measures taken by Govt. and the continuous depreciation of Rupee against US$, due to which the cost of sales increased. Further, the smuggled TVs remained available in the market at lower prices. In view of this and due to general slump in the market, the company was not able to increase its selling prices to the extent of increased cost. This resulted in erosion of gross profit. The company was also forced to book Rs.10.9 million expenses on account of tax liability of earlier years arising due to Supreme Court decision on writs of 80C and 8OD of the Income Tax Ordinance. All these factors combined together, resulted in non-viability of the company's operations and therefore, the directors have decided to cease the company's operations.

6. The arguments forwarded by the Chief Executive were considered and not found satisfactory. As regards the management's contention that the fixed assets disposed off are 6% of the total assets, the same is not maintainable, because the assets referred in Section 196 (3) of the Companies Ordinance, 1984 do not include current assets which arise as consequence to the normal course of business. Their contention that the manufacturing facility or the right to manufacture is not surrendered, is again not understandable as the manufacturing facility does not seem to be in existence any more, in view of the nil value of the fixed assets and surrender of factory premises to HITE. As regards the reasons of huge losses the reply of the company is of general nature and the Chief Executive has attributed the loss to external factors only i.e., increase in cost of sales owing to stringent measures adopted by the Government, smuggling and depreciation of Rupee against US$ and accrual of tax liability of Rs. 10.9 million etc. The factor responsible for collapse of the company as mentioned by Chief Executive, are perhaps cause of concern for many industries which managed to survive. It may be emphasized that appointment of Inspector is not a punitive action on the part of regulator but only a fact finding exercise and in case of this company where minority shareholders appears to have lost all of their investments, there is no reason that only for management's comfort this exercise should not be carried out. Such explanation may be offered to Inspector who may analyse them in-depth and report.

7. In view of the unsatisfactory reply, a final opportunity of hearing was provided through our letter No. Co.

265/3/EM/2000, dated June 6, 2000 & June 26, 2000 but inspite of various adjournments granted on Chief Executive's request, neither the Chief Executive Officer nor his authorize representative appeared before me. Instead, the Chief Executive through his letter dated July 20, 2000 requested for dropping the proceedings in view of the company being intended to be taken over by a new managements. In this regard a letter was also received from M/ s. Israil A. Menai & Associates, Attorney at law, Karachi, on behalf of the proposed buyer namely Mr. Firoz S. Shroff, to allow them an opportunity to make presentation before the Commission. Accordingly they were advised to make presentation before the Commissioner (Enf.) alongwith Chief Executive or director of the company on 12.08.2000. No one appeared. However, a fax message was received stating that they are engaged in the process of negotiations with the company's management and as soon as a clear picture emerges, they will request for presentation. In this uncertain situation I think investigation should not be delayed as investigation means inquiry into past acts of the company and has to do nothing with change of management. This company has ceased its manufacturing activities and sold/written off its assets and minority shareholders appear to be loosing everything and in these circumstances it will not be un-reasonable if a fact finding exercise is carried out in order to ascertain facts/ reasons behind the total collapse of a profitable company.

8. In view of foregoing I, in the public interest and in exercise of powers conferred upon me by Section 265 of the Companies Ordinance, 1984, hereby appoint Mr. Aziz Hussain, C-172, Navy Housing Scheme, Zamzama Link Road, Clifton, Karachi-75600 to act as Inspector to investigate into the affairs of M/s. UDL Industries Limited on remuneration of Rs. 100,000/- to be paid by the company.

9. Without in any way limiting the scope of investigation, the Inspector shall conduct investigation on all aspects of the operations of the company and shall after scrutiny of the entire record and books of accounts, furnish his reports, inter alia, on the following matters

(i) Identification of factors due to which a profitable enterprise has been completely ruined and report about mismanagement and oppression of minority shareholders, if any.

(ii) Reasons and genuineness of heavy losses after the year 1995.

(iii) Analyse the rationale and justification behind selling the assets and ceasing the company's operations.

(iv) To report about mismanagement/misappropriation and to fix responsibility.

(v) An inventory be made about the assets owned, assets sold by the company to discharge the liabilities and the assets still left with the company.

(vi) Whether or not proper records have been kept by the company as required by Section 230 and Section 234 of the Companies Ordinance, 1984.

(vii) Whether or not an adequate system of internal control has been existing/exist so as to prevent misappropriation and misapplication of company's assets.

(viii) Compliance with statutory requirements in the operations of the company indicating that the business was conducted and expenditure were incurred in accordance with the objects and for purposes of the company.

(ix) To report lapses/irregularities detected during the course of investigation.

10. The Inspector shall submit a detailed report alongwith supporting documents/evidences to the Commission (in quadruplicate) within 60 days of the date of this Order.

**(M. Zafar - ul - Haq Hijazi)**
**Commissioner (Enforcement)**