

**Before Dr. Sajid Qureshi, Executive Director (CL)**

**In the matter of**

**M/S Pak Elektron Limited**

**(Under Sub-Section (5) of Section 495 Of the Companies Ordinance, 1984)**

No. and date of show cause notice	233/463/2002-2133-2142 dated August 31, 2005
Date of final hearing	November 15, 2004
Present:	Syed Manzar Hasan, Chief Financial Officer Mr. Aziz-ur-Rehman, General Manager Mr. Amir Sattar, Finance Manager
Date of Order	November 21, 2005

**Order**

This order will dispose of the proceedings initiated against the Chief Executive and Directors of M/s Pak Elektron Ltd. (the “Company”) for not complying with the directions of Commission in respect of recovering the unauthorized investments, the investments made without complying with the requirements of the section 208 of the Companies Ordinance, 1984 (the “Ordinance”). The non-compliance of aforesaid directions of the Commission attracts the penal provisions under Section 495 of Ordinance and for which show cause notice was issued to the Chief Executive and Directors of the Company

2 The Company is a public company limited by shares, incorporated on March 03, 1956. Its shares were listed on the stock exchanges in 1988 following the public issue of its shares on July 11, 1988. It has authorized and paid up share capital of Rs.2,500 million and Rs.1,136 respectively, as per its audited Balance Sheet for the year ended June 30, 2005. The object for which the Company was established and its powers are contained in its Memorandum and Articles of Association. It is principally engaged in production and sale of electrical capital goods and domestic appliances. The manufacturing facility of Pak Elektron is located at 14



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K.M. Ferozepur Road, Lahore and Registered Office at 17-Aziz Avenue, Canal Bank, Gulberg-V, Lahore. The Company has 2,152 shareholders comprising individuals, joint stock companies, public sector institutions, financial institutions etc. as per pattern of shareholding annexed to the Directors' Report on the accounts for the year June 30, 2005. Associated companies, directors and their spouses hold around 43% of the paid up capital. This indicates that there is a substantial public interest in the shares of this Company.

3. The Board of Directors of Pak Elektron, as per its Financial Statements for the year ended on June 30, 2005 comprises of the following individuals

Mr. M. Naseem Saigol, Chief Executive

Mr. M. Azam Saigol, Director

Mr. Shahid Sethi, Director

Mr. Haroon Ahmed Khan, Director

Mr. Murad Saigol, Director

Mr. Homaeer Waheed, Director

Mr. Gul Nawaz, NIT Nominee

Mr. Javed Mahmood, NBP Nominee

Mr. Tajamal H. Bokaree, NBP Nominee

Mr. Wajahat A. Baqai, NBP Nominee

4. The brief facts leading to this case are that the Chief Executive and Directors made unauthorized investments in the associated concerns, the investments were made without obtaining requisite approval of the shareholders for which the Commission passed an Order on May 09, 2003 penalizing the Chief Executive and Directors of the Company for non-complying with the mandatory requirements of Section 208 of the Ordinance and were directed to recover the entire outstanding amount along with the markup from the associated undertakings by May 09, 2005. However, the Chief Executive and Directors of the Company afterwards made further unauthorized investments in its associated undertaking namely, M/s PEL Daewoo Electronics Ltd. and M/s Saigol Qingqi Motors Ltd. The Commission passed another Order on December 30, 2004 penalizing the Chief Executive and Directors of the Company and again directed them to recover the entire outstanding amount along with the markup from the associated undertakings by June 30, 2005.



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5. The Commission vide its letter dated July 22, 2005 asked the Company to provide the status of Compliance with the directions issued vide order dated May 09, 2003 and December 30, 2004 for recovery of unauthorized investments in its associated concerns. It was observed from the reply of the Company that the aforementioned directives of the Commission were not complied with and instead of recovery; the Company made a request for extension in the time period for recovery of investment from the associated concerns.
6. In reply to letter dated July 22, 2005 of the Commission the Company stated that;
- i. By virtue of Joint venture agreement between the Company and Daewoo Electronics Company Limited-Republic of Korea, additional contribution / loan to PEL Daewoo Electronics Limited (PDEL), if required was to be made in ratio of 60:40. Daewoo Electronic Limited has not made any investment since incorporation, other than share capital. In absence of further contribution from joint venture Partners, it became necessary for the Company to meet its contractual obligations arising out of corporate guarantees and other commitments.
  - ii. Company has negotiated a settlement with Daewoo Electronics Company Limited as a result of which it is expected that shares held by Daewoo Electronics Company Limited will be acquired by PEL for total consideration of Rs.1 only.
  - iii. In past due to indifferent attitude of joint venture partner the business operation of PDEL were hampered. But Now Pakistan Daewoo Electronics Ltd. with assistance of the joint venture partners will be able to revive its operations.
  - iv. It was prayed even in the course of hearing that sufficient time may be given for recovery of the amount involved.
  - v. The Company has further stated that
    - a) A case is filed in court of senior civil judge, Islamabad against Daewoo Electronics Company limited- Republic of Korea for appointment of arbitrator. The Company is seeking to recover of 40% losses of PDEL.
    - b) The Company will introduce manufactured/ assembled TV using the facility of PDEL.
    - c) The Company is considering proposal of merger of PDEL into the Company.



- vi. A former associated concern PEL Appliances Limited (PAL) was also subject to the proceedings of Section 208 of the Ordinance and was successfully merged into the Company with the approval of the Commission.
- vii. In last, the Company has requested to extend the recovery period for three years i.e. till June 30, 2008 during which the recovery will be made through steps '(a)' '(b)' or '(c)'.

7. The contents of the letter of the company disclosed that the concerns of the Commission have remained unaddressed and the directions remained unattended. The representation of the Company regarding the contractual obligations arising out of corporate guarantees and other commitments, settlement with Daewoo Electronics Company Limited as a result of which it is expected that shares held by Daewoo Electronics Company Limited will be acquired by PEL for total consideration of Rs.1 only and that PDEL with assistance of the joint venture partners will be able to revive its operations do not address the issue. The corporate guarantees and other commitments were related to a separate legal entity and do not form part of the obligations of the Company, as a result of the proposed settlement PEL would be just acquiring the liabilities toward the third parties as the equity is eroded and revival of unit is again a issue subjected to various risks. The authority in respect of investment under section 208 vests with the shareholders and this authority was abused by the Directors and they invested funds of the Company without taking approval of the shareholders into the associated concern, moreover the repeated directions of the Commission remained unattended The aforesaid situation required corrective action and in view of the these state of affairs a show cause notice under Sub Section (1) of Section 495 of the Ordinance dated August 31, 2005 was served to the Directors of the Company and its Chief Executive/Chairman of the Company.

8. The Company submitted reply on September 08, 2005 to the show cause notice dated August 31, 2005 in which it again reiterated the contents of the letter mentioned above and also informed about the further developments in respect of the recovery, which are as follows.

- i. Initiated Court proceedings against Daewoo Electronics Company limited- Republic of Korea (JV partner) for appointment of arbitrator. The Company is seeking to recover 40% losses of PDEL from JV partner.



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- ii. Carried out study for identification of possible way of recovery and figured out that merger is the best solution therefore the Company is considering proposal of merger of PDEL.
  - iii. The Company has plans to add the TV business to their existing products of appliances. The Company has already successfully marketed imported TV under their own brand name. The Company will introduce manufactured/ assembled TV using the facility of PDEL.
9. Since the Company failed to follow the Directions of the Commission and an amount of Rs.258 million, as on June 30, 2005, is still outstanding against M/s PEL Daewoo Electronics Ltd. The violation attracted the provisions of Sub Section (1) of Section 495 of the Ordinance provides that

*“Where any directive is given or order is issued by the Court, the officer, the Commission, the registrar or the Federal Government under any provision of this Ordinance, non-compliance thereof within the period specified in such direction or order shall render every officer of the company or other person responsible for non-compliance thereof punishable, in addition to any other liability, with fine not exceeding fifty thousand rupees and, in the case of a continuing non-compliance, to a further fine not exceeding two thousand rupees for every day after the first during which such non-compliance continues.”*

10. An opportunity of the hearing was given by the undersigned on November 15, 2005 to the Chief Executive and Directors of the Company. During the Course of hearing Syed Manzar Hussain, Chief Financial Officer stated that they are trying to recover the amount by way of the various options given in the reply to the Show cause notice, he further added that the most suitable option is merger, as the Company in previous case of PEL Appliances Limited has already adopted the same course of action. Moreover, the merger will be effective from June 30, 2005 therefore, the merged accounts will not reflect any outstanding amount and most importantly according to Finance Act, 2005 the accumulated losses of Pak Daewoo Electronics Limited amounting to Rs.354 million will bring in the tax advantage of approximately Rs.100 million to the Company. Syed Manzar Hussain further stated that the Directors, their spouses and Minor Children hold 50% of the shareholding and 10% is with the creditors i.e National Bank of Pakistan, hence with this majority they can easily pass a special resolution and can get approval from shareholders for merger, he claimed that the Company has already negotiated



with the creditors and the creditors will not object to the merger of the Company with Pak Daewoo Electronics Limited. The regulator had already vetted the case of merger with PEL Appliances Ltd therefore the Company see no hurdle in the process of merger.

11. The reply of the Company has been analyzed and is found unsatisfactory. The Company has been consistently making unauthorized investment in associated concern i.e. M/s PEL Daewoo Electronics Limited despite the fact that the Commission vides its order dated May 09, 2003 and December 30, 2004 had directed the Company to recover the investment from the said company. The investment in M/s PEL Daewoo Electronics Limited increased to Rs. 258 millions on June 30, 2005 from Rs. 172.589 million on June 30, 2003 and the rights of the shareholders were continuously abused.

12. Sufficient time has been given to the Company to recover the outstanding amount from associated undertakings. The first direction was given on May 09, 2003 and time given to the Company for recovery was two years but the Company instead of recovering the unauthorized investment, had made further investment. The Company did not take any corrective measures and never turned back to the Commission and the shareholders.

13. The proposals submitted by the Chief Executive and Directors of the Company have been considered and I am of the view that the proposal does not seem to be the effective solution of the breach committed by the Directors as all the proposed actions are directed toward correcting the situation by indirect means and none of the proposal has been given where the funds are pay backed to the Company the way the loans / advances are paid under normal trade terms i.e. by way of cash resources. Moreover the proposed solutions have their own limitations as explained below:

- i. With regard to recovery of 40% losses from JV partner, it is observed that PDEL is a limited Company and the liability of the members is limited. The recovery from JV partner is contingent and if through any arbitration they can get hold of any money the settlement of entire outstanding amount would not be possible.



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- ii. The merger requires approval from the Court and in the presence of the legal proceeding against the Company under Section 208 and 495 of the Ordinance, the possibilities of the approval of the merger scheme from the Court seems remote. The shares held by Chief executive, Directors their spouse and Minor Children are only 43% and 14% is held by the National Bank of Pakistan. Section 284 (2) of the Ordinance provides that approval of three-fourth i.e 75% majority of the shareholders is required to file an application for merger. The creditors and shareholders might also be having reservation on merger as the last financial statement of PDEL discloses accumulated losses amounting to Rs. 354.874 million. By way of merger, the Company would not be making any recovery rather it will be a book adjustments and instead it will be acquiring a loss making unit alongwith its outstanding liabilities.
- iii. The tax advantage available against the accumulated losses of the PDEL would be limited to only around Rs.100 million, as represented by the Company.
- iv. Financial glimpse of the PDEL, as at June 30, 2004, as highlighted reflects that it is a unit having an eroded equity and accumulated losses alongwith huge outstanding liabilities.

Figures in thousands (000)

Paid up capital	Rs. 70,000
Accumulated losses	(354,874)
Equity	(284,874)
Surplus	NIL
Long term liabilities	92,224
Current liabilities	241,578
Total liabilities	333,870
Payables to associates-PEL electronics	217,399
%age of shareholding of PEL-	PEL owned 60% of paid up capital
%age of shareholding of Korean associate-	Daewoo Electronic Co owned 40% of paid up capital



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- v. In case the Company opts to add TV business to its product by using the facility of PDEL the recovery of the outstanding amount will be very slow. The new product range would require time for settlement and would be subjected to market dynamics and risks.

14. The directors owe fiduciary duties to the Company they serve and its shareholders. They must discharge their statutory obligations in good faith with fairness, morality and honesty. The directors have failed to exercise reasonable care to see that mandatory provisions of law were being violated and have disrespect the mandate of the shareholders. Therefore, the directors have breached their fiduciary duties, which they owed to Pak Elektron and its shareholders. The Directors made repeatedly unauthorized transactions out the funds of the Company. Moreover, the directors have not complied with the directions of the Commission In fact Pak Elektron has been acting as a financier providing funds to them to fulfill their working capital requirements. I have been informed that the Directors are in a process of rectifying the default by recovering the balance due from its associated companies with interest over and above their borrowing cost and the representative of Chief Executive and the Directors of the Company has also assured that they would ensure strict compliance of the provisions of the Ordinance in future and will provide undertaking in respect of recovery plan of the Company

15. In view of the above, I, instead of imposing maximum penalty of Rs. 380,000 on the Chief Executive and each director as prescribed by Sub-section (1) of Section 495 of the Ordinance, impose a fine of Rs. 50,000 on each of the directors namely, Mr. M. Naseem Saigol, Mr. M. Azam Saigol, Mr. Shahid Sethi, Mr. Haroon Ahmad Khan, Sheikh Mohibullah Usmani and Mr. Homaeer Waheed. The afore-named directors 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.

16. The Chief Executive and Directors are also directed to recover the entire outstanding amount along with markup thereon from the associated undertakings by June 30, 2007. The Chief Executive and Directors are also directed to provide an undertaking that they will recover the amount along with mark-up from the associated concerns otherwise will be





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personally liable to make good the loss. The aforesaid undertakings shall be furnished to the Commission by December 31, 2005 along with the recovery plan fully supported by the facts and figures.

17. The Chief Executive and Directors of the Company are hereby directed to deposit the aforesaid fine totaling to Rs.300,000/- (Rupees Three hundred thousands 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.

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***Dr. Sajid Qureshi***  
Executive Director (CLD)