ORDER SHEET

IN THE HIGH COURT OF SINDH AT KARACHI

SUIT No. 1102 / 2015

DATE	ORDER WITH SIGNATURE OF JUDGE

Plaintiff: **KASB Corporation Ltd & others through Mr. Basil Nabi Malik Advocate.**

Defendant: **Bank Islami Pakistan Limited through Mr. Arshad Tayyebaly Advocate.**

1) For examination of parties / settlement of issues.
2) For hearing of CMA No. 9828/2015.
3) For hearing of CMA No. 9829/2015.
4) For hearing of CMA No. 8530/2016.
5) For hearing of CMA No. 9243/2016.
6) For hearing of CMA No. 10735/2016.

Date of hearing: **12.02.2018.**
Date of hearing: **18.04.2018.**

Muhammad Junaid Ghaffar, J. All listed applications are being dealt with through this common order. Application at Serial No.2 has since become infructuous and has not been pressed any further. Application at Serial No.3 is for restraining the Defendant from declaring the advance made by Plaintiff No.1 to the erstwhile (**"KASB Bank"**) now Defendant as a doubtful liability in its account. Application at Serial No.4 is a contempt application in respect of alleged violation of order dated 1.7.2015. Application at Serial No.5 has again become infructuous and has not been pressed. Whereas, Application at Serial No.6 is under Order 39 Rule 1 & 2 red with Order 38 Rule 1 & 5 and further read with Section 94 and 151 CPC, seeking directions to the Defendant to deposit an amount of Rs. 981,410,000/-with the Nazir of this Court and to invest the same in some interest bearing instrument.

In fact this is the application which is the bone of contention for the present purposes.

2. This is a Suit for Declaration and Injunction filed by Plaintiff No. 1 & 2. The Plaintiff No.1 is a listed public limited company which was formed upon the merger of KASB Finance (Private) Limited into Sigma Corporation Limited pursuant to order dated 24.9.2013 passed by the Islamabad High Court. The Plaintiff No.2 is the Chief Executive Officer of Plaintiff No.1 and is also a majority shareholder. It is the case of the Plaintiffs that Plaintiff No.1 was the owner of 83.62% of the total issued and paid up share capital of KASB Bank, till such time it was allegedly ousted as a shareholder upon amalgamation of KASB Bank into the Defendant Bank. For the present purposes the amalgamation *per-se* is not under challenge; but in fact it is pending in Constitutional Petition bearing No. D-3076/2015. It is the case of the Plaintiffs that prior to amalgamation an amount of US$ 10 million in four Tranches was advanced to KASB Bank and was reflected in the audited financial statement for the year ending 31.12.2013 as “Advance against future issue of rights shares” in the equity section of the Balance Sheet of KASB Bank. According to the Plaintiffs, the said advance was made pursuant to letter dated 4.12.2012 issued by State Bank of Pakistan which stated that the competent authority is allowed that KASB Bank may treat the advance towards issue / subscription of right shares for compliance of minimum capital requirement / capital adequacy ratio. It is the case of the Plaintiffs that the said amount of advance has been misappropriated and is not being properly reflected in the accounts of Defendant after amalgamation as a liability of the Plaintiffs and therefore, till such time this Suit is finally adjudicated, the Defendant be directed to deposit the said amount with the Nazir of this Court.

3. Learned Counsel for the Plaintiffs has contended that insofar as the amount given as advance is concerned, the same has not been denied by the Defendant and further admitted that such amount was given as an advance against future issue of right shares. According to the learned Counsel, on 1.7.2015 when this Suit was filed an order was passed by this Court whereby, it was observed "that the statement of financial position be filed disclosing that where the amount is available and keep the amount in same position". However, such order was only complied with belatedly; whereas, the account statement reflects that the said amount is not kept in the same position as directed on 1.7.2015 and therefore, contempt has been committed. Per learned Counsel the accounting standards which are applicable have been notified by the Securities & Exchange Commission of Pakistan vide SRO No. 633(I)/14 dated 10.7.2014 wherein, International Accounting Standard 32 (**IAS 32**) are to be considered as fundamental documents on the basis of which the assets and liabilities are to be determined. According to the learned Counsel, as per IAS 32, financial liability has been defined as a contract that will or may be settled in the entity's own equity instruments, and is, or a derivative, that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. According to the learned Counsel, in terms of Para 16 of IAS 32 it is further provided that when an issuer applies the definitions in paragraph 11 ibid to determine whether a financial instrument is an equity instrument rather than a financial liability, the instrument is an equity instrument if, and only if, both conditions at (a) and (b) of Para 16 are met, which according to the learned Counsel is not the case here. Learned Counsel has also referred to Para 9 of IAS 39 i.e.

(definition of a derivative) and contended that the transaction shall be designated as an equity instrument only when a fixed number of shares are given for a fixed amount of cash and in the accounting terminology, the test is referred to as the "Fixed to Fixed Test". Per learned Counsel the contract between the Plaintiffs and the Defendant is a derivative contract and an amount of US$ 10 million was disbursed to KASB Bank for an undetermined number of shares which may have changed according to various factors, including prevailing market interests rates, foreign exchange fluctuations, discounted share price determined by the Defendant as well as the share price at that point of time. Learned Counsel has further contended that even as per letter dated 4.12.2012 of SBP the advance in question was treated as a liability and it was only required to show equity for the purposes of compliance with minimum capital requirement as well as capital adequacy requirements. Per learned Counsel till such time the Plaintiffs were forcibly ousted through amalgamation, the said advance was shown in the audited accounts i.e. Annual Report 2013 in the "represented by" column and according to the learned Counsel the treatment was given with specific designated issue of right shares. According to the learned Counsel, this advance against issue of right shares, after scheme of amalgamation is not reflected it in a proper place in the financial statements, by the Defendant, thereby, depriving the Plaintiffs from recovering the said amount as liability. According to the learned Counsel, as per International accounting terms, equity is not composed of merely share capital, but is a composite of different categories, and each transaction / category of equity is an independent source of equity than the other. Per learned Counsel this financial liability in terms of international accounting practices, as well as all other liabilities of KASB Bank,

whether present or future, or contingent, were transferred to the Defendant for the purposes of fulfillment, and the extinuishment of Rights and Interests in the shares of the Bank, as reflected in the amalgamation scheme would have no effect on the advance in question as it is only the share capital which was extinghuised, whilst the remaining cateqoires of equity remained intact. Per learned Counsel, the Plaintiffs entire case is premised on the fact that after amalgamation the Defendant unnecessarily and so also in violation of the Court's order, subsequently removed the said amount of advance from its financial statements by giving an impression that it had no obligation to return the same or to issue any share(s) in lieu thereof. Learned Counsel further contended that in the supporting affidavit to CMA No. 10735/2016 in Para 28 an assertion was made to the effect that such amount of advance is being fully utilized by the Defendant and this has not been specifically denied which in terms of Order 8 Rule 3 & 5 CPC is required to be specifically denied and failing to do so amounts to an admission. In support he has relied upon ***M/s Sports World and others V. Latees Fabrics and others (1995 MLD 1707).*** Learned Counsel has further contended that the order dated 1.7.2015 was never complied within time and in the meantime, the Defendant changed the statement of financial position in the quarterly report of September, 2015 as well as in its Annual Report of 2015; and after doing that they filed such statement before the Court and the financial position reflecting the illegal changed status of the advance which in fact defeats the very purpose of order passed on 1.7.2015; hence, prima facie contempt has also been committed. In view of such position, the learned Counsel contended that a prima facie case has been made out, whereas, the Defendant has admittedly misappropriated the amount of

advance, and therefore, till such time the Suit is finally decided, the Defendant be directed to deposit the said amount with the Nazir of this Court with further directions to invest the same in some profit bearing instrument.

4. On the other hand, learned Counsel for the Defendant at the very outset has contended that the prayer made in these applications in fact amounts to grant of the entire final relief claimed in the Suit, and it is settled law that through an injunction application, no final relief sought in the main Suit can be granted. Per learned Counsel the letter of State Bank of Pakistan dated 4.12.2012, whereby, directions were given to inject money in KASB Bank was clearly in terms that it was for the purpose of maintaining a minimum capital requirement under the prevailing prudential regulations and therefore, it was shown under the head of capital instead of liability. Learned Counsel has further contended that the relief being sought in this Suit is already a part of the claim made in C.P. No. 3076/2015, whereby, the entire amalgamation scheme has been impugned; hence, the entire Suit is incompetent. According to the learned Counsel, at the time of amalgamation the entire share capital had wiped out and was in negative; therefore, the valuators determined Rs. 1000/- as the entire value of shares, hence, the claim of the Plaintiffs is even otherwise unjustified. According to the learned Counsel after advancement the said amount and before the order of amalgamation, it was treated by the Plaintiffs management as capital; and now when they are no more controlling the management they want this Court to treat the same as a liability. Per learned Counsel this change of stance does not warrant any exercise of discretion by the Court for the relief being sought. Learned Counsel has submitted that the very purpose of making such

advance was to fulfill the capital requirement and at no stage of the proceedings, any repayment was to be made, except right shares, which in the given facts are no more available. Finally, learned Counsel contended that no prima facie case has been made out, and even otherwise, the Defendant is a banking company working satisfactorily within the jurisdiction of this Court and therefore, even if any final decree is passed, it can be satisfied and presently there is no apprehension that the final decree would be avoided. Insofar as the contempt application is concerned, learned Counsel has contended that necessary compliance has already been made and as alleged no order of this Court has been violated. Learned Counsel has placed on record letter dated 6.12.2017 addressed to State Bank of Pakistan by the Plaintiffs through which they have sought clarification and according to the learned Counsel as per contents of the said letter, the Plaintiffs have already approached State Bank of Pakistan; hence, instant Suit as well as all applications have become infructuous. He has further submitted that such letter was responded by State Bank of Pakistan on 26.1.2018, wherein, the Plaintiffs have been informed that all equity had been wiped out and was determined at a value of Rs. 1000/- as compensation, therefore, no money is due to the Plaintiffs. Learned Counsel has also relied upon Module 22 (Liabilities and Equity) issued by the IFRS (International Financial Reporting Standards) and has contended that in terms of Module 22.7(b) if any entity receives cash or other resources before the equity instrument are issued, and the entity cannot be required to repay the cash or other resources received, the entity shall recognize the corresponding increase in equity to the extent of consideration received. In these circumstances, learned Counsel has prayed for dismissal of all the listed applications.

5. While exercising the right of rebuttal, learned Counsel has contended that the Plaintiff's letter dated 6.12.2017 was without prejudice and was only in respect of Article 9.02 of the scheme of amalgamation and was only to the extent of seeking a clarification as to the advance in question being a liability in the scheme of amalgamation or not, whereas, the said clarification has no bearing on the maintainability of this Suit as well as the applications as according to the learned Counsel, the Plaintiff is only seeking preservation of the corpus for the purposes of final determination of the nature of advance i.e. a liability or not. Per learned Counsel even otherwise, the final relief being sought is a matter of evidence and State Bank of Pakistan would have no jurisdiction nor can it decide the issue in hand. Insofar as relevance of Module 22 as above is concerned, learned Counsel has contended that in fact it is wholly inapplicable to the facts and circumstances of this case as the said Module is in respect of Small and Medium Enterprises (SME's) for which the accounting standards, including IAS 32 have different parameters. Even otherwise, according to the learned Counsel on facts also this does not apply to the case of the Plaintiffs. As to the merits of the application under Order 38 Rule 5 CPC and its consequences, learned Counsel has contended that without prejudice this Court has ample powers under Section 94 and 151 CPC to provide proper relief for advancement of justice and in support he has relied upon ***PLD 1989 Karachi 635 (Nazar Muhammad V. Ali Akbar), PLD 1990 Karachi 1 (Baslagamwala Oil Mills (Pvt.) Ltd. V. Shakarchi Trading A.G. an 2 others), PLD 2011 Karachi 605 (Muhammad Ather Hafeez Khan V. Messrs SsangYong & Usmani JV), PLD 1962 SC 119 (Mohiuddin Molla V. The Province of East Pakistan (2) Abdus Sobhan and (3) Ketab Ali, 2013 CLC 1220 (Ms.***

Afshan V. Syed Kamran Ali Shah & 6 others) and 2015 CLC 1223 (Pakistan Railways Employees Cooperative Housing Society Ltd. V. Karachi Building Control Authority and 9 others).

6. I have heard learned both the Counsel and perused the record. The Plaintiffs through listed application(s) is somewhat seeking two reliefs. One is to the effect that pending final determination of this Suit the Defendant be directed to deposit the amount of advance before the Nazir of this Court and shall also accord proper treatment to the said advance in the financial statements by showing it as a liability instead of equity. Additionally contempt proceedings be initiated for alleged violation of order dated 1.7.2015.

7. The facts have been already discussed briefly hereinabove and from the perusal of the record, it reflects that instant Suit has been filed against the Defendant only in respect of the amount in question which was given as advance by the Plaintiffs to KASB Bank prior to the amalgamation. Since the approval of the amalgamation scheme is already under challenge before a learned Division Bench in a Constitutional Petition, therefore, for this Court it would not be appropriate to go into the minute details of the scheme of amalgamation lest if may prejudice the case of any of the parties. It is not in dispute that the said amount of advance was injected in erstwhile KASB Bank pursuant to letter dated 4.12.2012 issued by the State Bank of Pakistan to the Plaintiffs and it would be advantageous to refer to the said letter (**Emphasis Supplied**) which reads as under:-

"STATE BANK OF PAKISTAN
BANKING SURVEILLANCE DEPARTMENT
I.I. CHUNDRIGAR ROAD
KARACHI

No. BSD/CS/14315/12 December 04, 2012

The President/CEO

KASB Bank Limited,
Business & Finance Centre,
I.I. Chundrigar Road,
Karachi.

Dear Sir,

KASB CAPITAL PLAN

Please refer to KASB bank Finance Ltd's letter dated November, 16, 2012 regarding placement of US$ **30 million advance toward the issue of right shares by KASB Bank Ltd**. and email dated November, 30, 2012 of KASB bank's CFO.

In this regard, it is advised that the competent authority has allowed **that KASB Bank may treat the advance towards issue / subscription of right shares for compliance of MCR/CAR requirements and report the same amount in the equity section of its Balance Sheet**. However, this will be subject to the following conditions:-

i) The advance may be maintained in US$ provided the foreign currency is kept in interest free mode with the SBP, and the same will be converted into Pak rupee at the ruling exchange rate on the actual date of subscription by KASB Finance / sponsor shareholders towards the KASB Bank's share issue or on 1st April, 2013 whichever is earlier.

ii) The advance share deposit will be placed by sponsors of KASB Bank by December, 31, 2012:

iii) **The advance will be subordinated to all other liabilities including deposits of the bank and will be utilized only for the capitalization of the bank** and will not be withdrawn by KASB Finance. Further no mark up / return will be paid on this advance.

iv) The instructions by KASB Finance / sponsor shareholders for deposit of US$ 30 million should provide valid authority to the bank for placing of funds in shares subscription account and treating it as subordinated advance toward future right issue;

v) The advance will be extended by the sponsors from their own sources they should not borrow (or subsidiary of Pakistani bank to generate funding for the advance;

vi) The bank and KASB Finance / sponsor will ensure compliance with all applicable laws, rules and regulations in respect of the issuance, and subscription, of right shares; and

vii) **The right issue process should be completed by March 31, 2013 and detailed schedule of the right issue process with clear timeline will be provided to SBP.** It is advised that all efforts should be made to complete the process within the given timeframe.

Please acknowledge receipt.

Yours sincerely,

Sd/-
(Amer Hassan)
Joint Director"

8. Perusal of the aforesaid letter reflects that it was in response to Plaintiffs earlier letters regarding placement of US$ 30 million advance towards the issue of right shares by KASB Bank. The State Bank of Pakistan advised that the competent authority has allowed KASB Bank to treat the advance towards issued / subscription of right shares for

compliance of MCR (minimum capital requirement) /CAR (capital adequacy ratio) requirements and *report the same amount in the equity section of its balance sheet*. It further provided that the advance will be subordinated to all other liabilities including deposits of the bank and will be utilized only for *the capitalization of the Bank and will not be withdrawn by KASB Finance* and further no mark- up / return will be paid on this advance. It further provides that there shall be a valid authority to the bank for placing of funds in shares subscription accounts and treating it as subordinated advance towards future right issue and finally it further provided that the right issue process should be completed by 31.3.2013 and detailed schedule of the right issue process with clear time line be provided to State Bank of Pakistan with further advise that all efforts should be made to complete the process within the given time frame. Now it is an admitted position that, firstly according to SBP's directions, the advance amount was supposed to meet the MCR/CAR requirements, and secondly, it was to be shown in the equity section of the Balance Sheet. It is an admitted fact that after advancing money as above, and till such time the amalgamation scheme was notified, there was enough and ample time for the Plaintiffs / subscribers of KASB Bank to have their right shares issued but for unexplained reasons the same was not done and subsequently, this plea has been raised. In fact there was no one to stop them from making a right share issue. According to them the advance money was there's and there was no stopping them at least from issuing right shares. But this could not have been done and the simple reason being, KASB Bank was never in a position to do so. The overall structure of the financial affairs didn't permit them to issue right shares. And for this also they had to approach SBP as this could have an effect on MCR /

CAR limits and requirement. So all in all, the thing which could not have been done practically and financially, was not done, but now a stance has been taken, that it ought to have been done or shall now be done by the defendant. This does not seems to be justifiable and at least at this stage of the proceedings, when the evidence is yet to be led by the plaintiff for justifying its stance, this Court in the given facts would not go to the farthest of the extents as contended. All said and done, I may reiterate that this is a tentative view on the basis of record presently before me, as I am mindful of the fact that at this injunctive stage the Court should refrain from given any final adjudication on this aspect of the case; but certainly for deciding these applications this question is crucial as to pass the litmus test for making out a prima facie case for injunction, as well as for attachment before the judgment. Repeatedly, the learned Counsel was confronted as to why during the interregnum, the Plaintiffs failed to comply with such procedure (i.e. issuance of right shares) and if that had been done, perhaps, this issue would not have come before this Court and to this there wasn't' any satisfactory response forthcoming. Therefore, the conduct of the Plaintiffs even otherwise does not justify exercise of discretion while deciding the application at this stage.

9. It is also a very important aspect of the case that how the advance being made for issuance of any rights shares is to be classified at the very initial stage. It is not in dispute that when this advance was made the Plaintiffs were having the management control of KASB Bank and continued with it, for at least more than two years (from 4.12.2012 till moratorium dated 14.11.2014 & amalgamation dated 7.5.2015). The IAS 32 which has been relied upon by the Plaintiffs' Counsel is one of the Accounting Standards issued and adopted by the International Accounting

Standards Board (IASB) and the idea of such recognition of standards is to understand the company accounting across the International Boundaries, especially when companies are operating worldwide or are seeking investment from outside the country. IAS 32 relates to presentation of Financial Instruments and the objective of this Standard is to establish principles for presenting financial instruments as liabilities or equity and for offsetting financial assets and financial liabilities. It applies to the classification of financial instruments, from the perspective of the issuer, into financial assets, financial liabilities and equity instruments; the classification of related interest, dividends, losses and gains; and the circumstances in which financial assets and financial liabilities should be offset. The above definition regarding presentation of liabilities and equity outlines the accounting requirement for the presentation of financial instrument, particularly as to the classification of such instruments into financial assets, financial liabilities and equity instruments. The standard also provides guidance on the classification of related interests, dividends and gains / losses and when financial assets and financial liabilities can be offset. It enables in clarifying the classification of a financial instrument issued by an entity as a liability or as equity prescribing the accounting for treasury shares (an entity's own repurchased shares) and also prescribes strict conditions under which assets and liabilities may be offset in the balance sheet. Para 15 thereof provides certain guidelines and directions insofar as "Presentation" of "Liabilities and Equity" is concerned. The same reads as under:

> 15 The issuer of a financial instrument shall classify the instrument, or its component parts, **on initial recognition** as a **financial liability**, a **financial asset** or an **equity instrument** in accordance with the substance of the contractual arrangement and the definitions of a financial liability, a financial asset and an equity instrument.

10. The above definition encompasses a fundamental principle and that is a financial instrument should be classified as either a *financial liability* or an *equity instrument* according to the substance of the contract, not its legal form, and the definitions of financial liability and equity instrument. The two exceptions from this principle are certain puttable instruments meeting specific criteria and certain obligations arising on liquidation; but it is certain that the entity must make the decisions at the time the instrument is *initially recognized*. The classification of such instrument made at the initial stage cannot be subsequently changed or based on changed circumstances. This clearly reflects that insofar as the applicability of IAS 32 is concerned, (without prejudice to any objections of the defendant at the trial stage), even if the said standard is or was applicable, by its nature, the advance made to the company was initially, (and could not have been treated otherwise as per SBP's directions), treated as an equity instrument, and not as a liability. This by its own on the basis of IAS 32.15 could not be changed subsequently and this rests the case of the plaintiff at naught.

11. These are two crucial points which are to be considered at the injunction stage and both goes against the Plaintiffs. Whether the advance is to be treated as a capital / equity or as a financial liability is a matter of evidence and need not be decided at this stage of the proceedings. But for deciding these applications at the interim stage, in my view both the aforesaid issues do not corroborate or support the Plaintiffs stance. Undoubtedly, they were at the helm of affairs and when the advance was made, they were required to follow the mandate of SBP, whereby, such advance was required to be shown as "equity" and not as "liability"; secondly, and without prejudice to this, they ought to have issued the right shares by 31.03.2013 which was not

done for unexplained reasons. They were under certain directions of State Bank of Pakistan to meet the minimum capital requirements as well as capital adequacy ratio and for that they could not have shown this advance as a financial liability but as a capital requirement which at the time of amalgamation had completely wiped out and was in fact in negative. In view of such position, there appears to be no justifiable or arguable case as contended on behalf of the plaintiffs to grant the relief being sought through these applications, which otherwise is definitely a very harsh order to be made against the defendant for deposit of the entire amount being claimed in this Suit with the Nazir of this Court. In granting such relief the Court has to be satisfied that plaintiff's cause if of a prima facie nature, based on an unimpeachable averment / claim in the plaint, and Court must have reasons to believe on the basis of material before it, that unless jurisdiction is exercised and orders as solicited are not passed, there is a real danger that defendant may remove itself from the territorial jurisdiction of the Court and an intent to avoid passing of a decree must be clearly shown with reasonable clarity. In fact the provisions of Order 38 Rule 1 & 5 as well as Section 94 and 151 CPC as relied upon on behalf of the plaintiff in a case like this are not to guarantee the plaintiff availability of an asset to satisfy the decree which ultimately be passed, but to ensure non abusing of process of Court by a defendant. Moreover, it is not the case of the plaintiff that the defendant in order to frustrate the decree which may ultimately be passed in this Suit, is running away or for that matter, is selling its assets. In fact there appears to be no such real danger in hand in this case. And these ingredients I am afraid are completely lacking in the plaintiffs case as placed before this Court. It is also a settled law that order of this nature definitely burdens the

defendant for a variety of reasons, and if there is any ambiguity or doubt in the case of the plaintiff, then such benefit of doubt must go in favor of the said defendant.

12. In view of hereinabove facts and circumstances of this case I am of the view that no prima facie case is made out on behalf of the plaintiff, nor the balance of convenience lies in its favor, and no irreparable loss would be caused if the orders as solicited are refused. Accordingly, application(s) at Serial No.3 (**CMA No.9829/2015**) and at Serial No.6 (**CMA No.10735/2016**) are dismissed. Whereas, applications at Serial No.1 & 5 (**CMA Nos.9828/2015 & 9243/2016**) are dismissed as not presses. As to application of contempt at Serial No.4 (**CMA No.8530/2016**) let the same be taken up along with Final Arguments after evidence, as presently the same cannot be finally adjudicated by this Court.

Dated: 18.04.2018

J U D G E

ARSHAD/