

IN THE HIGH COURT OF SINDH AT KARACHI

(Companies Jurisdiction)

~~30-5-2001~~  
*[Signature]*

J. Misc. Petition No. 29 of 2001

Additional Registrar (C&J)

IN THE MATTER OF

Sections 284, 285, 286, 287 and 288 of the Companies Ordinance 1984

AND IN THE MATTER OF

**PFIZER LABORATORIES LIMITED**

a company incorporated in Pakistan,  
having its registered office at

12, Dockyard Road, West Wharf, Karachi ..... Petitioner No 1

AND

**PARKE DAVIS & COMPANY LIMITED**

a company incorporated in Pakistan,  
having its registered office at

B-2, S.I.T.E., Karachi ..... Petitioner No 2



ORDER SHEET  
IN THE HIGH COURT OF SINDH, AT KARACHI

J.M. No.29of 2001

Date order with signature of Judge

For further arguments in CMA No.1725/2003.

- (i) C/A in CMA No.1725/2003.  
(ii) Statement filed by Mr. Muhammad Ali Sayeed Advocate.  
(iii) Additional Affidavit filed by Advocate for the petitioner.

Dates of hearing : 25.10.2005, 18.10.2006, 08.11.2006, 28.11.2006,  
07.12.2006 & 22.12.2006

Petitioners through : Mr. Qazi Faez Issa, Advocate.

Objector through : M/s Muhammad Ali Sayeed & Shehnsah  
Hussain Advocates.

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GULZAR AHMED. J. : This is an application under section 151 CPC filed by the objector praying for setting aside of the valuation report of Pfizer Laboratories Ltd (PLL) prepared by M/S Ford Rhodes Sidat Hyder & Co. (the auditors), in terms of order dated 14.10.2002 and to order for preparing fresh valuation report of PLL as an on going concern and in the alternative dividend growth model suggested by the auditors in their report may be applied in its entirety with all its ramifications and the date of acceptance of offer i.e. 31.8.2003 contained in letter dated 9.8.2003 be extended and fixed on the disposal of the application. PLL has filed counter affidavit to which rejoinder is filed. An additional affidavit is also filed by the objector.

2. Learned counsel for the parties have made extensive submissions while the counsel for the objector has also filed a comprehensive note of written arguments.

3. The controversy arises from the fact that a petition under section 284 read with section 285 to 288 of Companies Ordinance 1984 was filed jointly by Pfizer Laboratories Limited as petitioner No.1 and Parke, Davis & Company Limited as petitioner No.2 seeking sanction of the scheme of arrangement providing for amalgamation of petitioner No.1 into the petitioner No. 2 with usual transfer of whole of the undertaking, business, assets, properties, rights, liabilities and obligations and consequential prayers. This petition came to be contested by minority share holders of both the companies and ultimately vide judgment dated

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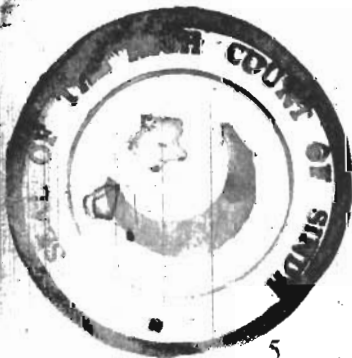


26.6.2002 the scheme of arrangement was declined and while disposing off the petition the following directions were given:

1. The exercise of valuation be conducted afresh through an independent auditor, who should evaluate the petitioners as on going concern and for the purpose of valuation the factors such as tangible and intangible assets and every factors that concern the valuation be taken into consideration.
2. On the basis of fresh valuation, by independent auditors, the majority share holders of PLL to purchase the share from minority share holders who are willing to part with their share on reasonable price and.
3. The scheme be put to the members in the extra ordinary general body meeting for their approval to be convened under Court directions.

4. On 14.10.2002 the court passed the following further order:

“In view of consent for the appointment, M/S Ford Rhodes Sidat Hyder & Co., the said firm appointed as Auditors at the cost of the petitioner to evaluate the Petitioners as “on going concern” and for the purpose of evaluation the factors such as tangible and intangible assets and every factors that concern the valuation be taken into consideration. The evaluators would be at liberty to summon any documents, material or information from relevant quarters for such valuation. A copy of the judgment dated 26.6.2002 may also be provided to the Evaluators in this regard and every factor that has been considered by this Court be considered for such valuation.”



5. On the basis of this order the auditors have prepared the valuation report, a photocopy of which is filed as annexure 'B' to the application.-

6. Pursuant to this report, counsel for the petitioners through his letter dated 09.8.2003 has offered the objectors/minority shareholders to purchase their entire shareholding in PLL at Rs.37.42 per share providing terminal date of offer as 31.8.2003 on which the objectors have filed this application and by an order dated 25.8.2003 the effect of this letter was suspended.

7. Learned counsel for the objector has attacked the valuation report of the auditors and submitted that the report does not comply with the court order dated 14.10.2002 as the auditors have not valued the company as an on going concern and not taken factors into consideration provided in the said order.

8. Learned counsel for the petitioners has objected to the maintainability of the application filed by the objector on the grounds that the order dated 14.10.2002 did not provide for filing of objection to the valuation report of the auditors and on pronouncement of judgment the court became functus officio. It was further submitted that the application is based upon malafide inasmuch as the wife of attorney of objector has subsequent to valuation report acquired 50,000 shares of PLL and that auditors have given their fair opinion substantially favouring the objector.

9. I have considered the submissions of learned counsel and have also considered the report of the auditors in the face of the order passed by this court.

10. So far the objections of learned counsel for petitioner on the maintainability of the application that the order dated 14.10.2002 did not provide for objecting to the valuation report and that on announcement of judgment dated 26.6.2002 the court has become functus officio, suffice it to note that when the court in its order requires anything to be done providing parameters, a party to the proceeding is always entitled to agitate that the thing done is not consistent with the court order and may seek compliance of it in its true terms and spirit. This is so because the thing done under the court order remains justiciable until it reaches its logical conclusion of either being accepted by the parties or operates as an acceptance by law. Neither of the two conditions in the case in hand are pointed out. As regards the question of functus officio pressed without citing law, I find that after the judgment dated 26.6.2002, the petitioners themselves have given consent on the basis of which order dated 14.10.2002 was passed. At that point of time, the petitioner did not raise such objection and I am unable to discover the rationality of this argument at this stage of the proceeding. As regards the ground of malafide, I do not consider that merely purchasing of share by the wife of the attorney of the objector will lead to any such inference except that in the first place, it may be assumed that while purchasing the shares she was familiar with value of shares determined by the auditors report and at best a plea of estoppel may be raised against her. I can not however, expect that she may not be aware of the dispute regarding the valuation of the shares and if she has ventured to purchase the shares, she may have done so as a business risk to herself but it could not be, from any angle, based upon malafide. The last mentioned objection from the side of petitioner could be dealt with while dealing with the arguments of the objector counsel.



11. As it appears from the record, that the exercise of valuation of PLL was undertaken earlier by M/S Taseer Hadi & Company, a firm of Chartered Accountants in their report have valued the share of PLL as on 31.12.2000 at Rs.1.37 on the basis of fair value of net assets and worked out swap ratio of 264 shares of PLL to 1 share of Parke, Davis & Company Limited. The court in its judgment has rejected such valuation of shares on the premises that PLL has not been valued as an on going concern and its goodwill, patent and trademark being tangible assets have not been considered by the Chartered Accountants in making of such valuation pursuant to which directions as noted above were given in the judgment and further these aspects were also drawn in the order dated 14.10.2002, which was passed by consent.

12. The auditors in the report which is being attacked by the objector have followed the formula of dividend growth model whereby per share value of Rs.37.42 has been advised to be the reasonable price of share of PLL at which the majority may acquire from the minority shareholders. Swap ratio of 376 shares of PLL to 1 share of Parke, Davis & Company Limited has been concluded.

13. The objector do accept the formula of dividend growth model on which the value of PLL as an on going concern has been worked out to Rs.2,716.98 million, but raise objection that in dividing this value on issued subscribed and paid up shares, the right shares issued by PLL to its holding company be excluded whereupon true value of shares held by him will crystallize. The objector claims that right shares have been acquired by the holding company of PLL in dubious manner inasmuch as the holding company has forced upon the management of PLL to acquire raw material from it which entails the concept of transfer pricing which has robbed profitability to PLL rather it has become indebted to its holding company which indebtedness, the holding company has injected into PLL in acquiring the right shares thereby not only made PLL which was a profitable concern into loss making concern but also diluted investment of the minority shareholders and in the same way goodwill and tangible assets of PLL are being camouflaged as it is being worked out by the mechanism of transfer pricing. These facts are not controverted by the petitioners counsel.

14. Perusal of the auditors report shows that they have repeatedly made observations regarding the management policy of adhering to the mechanism of transfer pricing and at page 6 of their report have said as follows:

“ It may be argued that the financial position of PLL is a direct consequence of the decision of its management



to operate in the manner described, and that such management decisions have been in the interest of its majority shareholder, which is also its principal supplier of raw materials. It may further be argued that had the majority shareholders not considered it viable to operate in this manner, they would not have funded the financial deficits of PLL by equity injections and would have wound up the operations of the company in Pakistan - the underlying assumption being that such investment would be expected to yield profits commensurate with the risks of such an investment.

It may also be argued that the interest of Pfizer Inc's presence in the Pakistan market may lie not only in profitability derived from its operations in the country but also from Pfizer Inc. maintaining its presence in the Pakistan market as part of its global strategy.

However, notwithstanding the above, the ultimate decisions taken with respect to the operations of PLL do not appear to have been in the interests of the minority shareholders. The minority shareholders have not received any return on their investment during the last ten years and their investment has also diluted over time as PLL issued rights shares from time to time, which were only taken up by its parent company. These minority shareholders now hold only 0.68 percent of the total shareholding (492,976 shares)."

15. At page 7, the auditors have stated that:

"Since the values determined under the scenario that active ingredients could have been procured at significantly lower prices if the alleged transfer pricing would not have been restored to, is subjudice at various legal and appellate forums, we have opted not to base our recommendation taking cognizance of this scenario."

16. The auditors then proceeded to undertake the exercise by concluding at page 9 of their report as follows:

"It is neither possible, nor part of the scope of our work, to determine the impact of the decision of the management of PLL to procure its raw material from parties other than its parent/affiliated companies, would have on the value of the company. We assume (refer fundamental business assumptions below) that the existing arrangements will continue for the company as a going concern."



17 The auditors report further shows that PLL is having steady increase of sale of its products for over five years period i.e. 1998 to 2002 and such growth on an average is around 4% per annum. At page 26 of report, it states as follows:

"The company generates its revenues from a portfolio of 22 brands of which five products of the company contribute around 70 percent to the total revenues. However, the top two products of the company are being sold at a gross loss even though both these products i.e. Norvase and Vibramycin are well established products and hold the second and first positions respectively in terms of market share in their respective drug categories. These products have become controversial in various related Government departments, primarily due to issues raised by the Income Tax authorities relating to the purchase cost of the respective active ingredients of these products. These active ingredients are being purchased by the company from its parent company Pfizer Inc. and the tax authorities have assessed these transactions as not being at arms length. The MoH is also cautious while taking any decisions with respect to increasing the prices of these products.

PLL, however, is paying Income Tax to the tune of around Rs. 55 million every year for the last five years under the Presumptive Tax Regime.

18. Page 74 of the report demonstrates import price and alternate source price of raw material imported by MNCs and as regards PLL it has noted as follows:

Name of material	US\$	
	Import price per KG	Alternate source price per KG.
Amlodipine Besylate	30,000	500
Piroxicam	8,750	125
Doxicycline	700	60

19. The report states that approximately 75 percent of raw material used by PLL are imported from different parts of the world. Around 75 to 80 percent of these imports (approximately 60% of total purchase) are from Pfizer Inc. or other affiliated companies. The auditors in the scenario, as noted above, have based their opinion fixing the swap ratio and reasonable price of the shares which are noted above. This exercise, the auditors have conducted on the basis of going concern asset valuation and have stated that valuation so arrived at includes the value of goodwill implicitly inherent in the business. I may also take note of the aspects of shareholding funds noted by the auditors at page 42 of their report which runs as follows:



#### “ Share capital

The capital invested by the shareholders of the company stood at Rs.726.2 million and comprises around 119 percent of the total assets of the company. Pfizer Inc. has made repeated capital injections in PLL amounting to Rs.88.8 million, Rs.54.3 million and Rs. 331.8 million in the FYsE 1998, 1999 and 2000 respectively. These equity injections have been through right issues which were fully taken up by Pfizer Inc.

#### Advance against equity.

Owing to the dismal liquidity situation of the company, the management has been borrowing funds from its parent company, Pfizer Inc. to finance its working capital as well as capital expenditure requirements. Funds in this regard have been borrowed every year during the five year period under review except for FYE 2000 where no borrowing was made. These funds were converted to equity through issues of right shares from time to time. However, no right shares have been issued subsequent to FYE 2000. Advance against equity stands at 37 percent of the paid up share capital of the company as at December 31, 2002.

#### Accumulated losses

As a result of continuing net losses, the accumulated losses of the company have mounted to Rs. 930.3 million in the FYE 2002 as compared to Rs.336.7 million in FYE 1998; an increase of almost 176 percent. These accumulated losses are equal to 152 percent of the total assets of the company. The persistent accumulation of losses has resulted in a wipeout of more than 90 percent of the equity invested by the shareholders; the positive equity figure primarily being as a result of repeated equity injections and funds disbursed by Pfizer Inc. as advances against equity which are eventually to be converted to equity. Further, the company has also not distributed any dividend since the last 10 years.”

20. Whatever, the figures in the auditors report may reflect, the glaring fact on the basis of which the auditors have proceeded with the exercise provided by the order dated 14.10.2002 seems to be based on assumptions and acceptance of the fact of the transfer pricing and its financial standing on PLL and its impact on shareholding funds which is all negative to PLL and to its minority shareholders. The objector has agitated before me that the minority shareholders should get a fair value of their shares from PLL minusing the elements of transfer pricing and the right shares acquired on its basis by the holding company of PLL. There appears to



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good deal of law on the point as to how the directors are required to conduct the affairs of a company. Holding company having 99.32% shares in PLL ought to be having its own nominated board. Section 214 & 216 of the Ordinance requires directors to conduct themselves in a fiduciary behavior and their acts have to be bonafide and for the benefit of the company as a whole. The motivated interest of the board of PLL to look after the benefits of its own employer i.e. the holding company to the detriment of minority shareholders is not legally permissible and may bring the affairs of PLL within the scope of section 265 of the Ordinance which, inter alia, provides for an investigation of the company's affairs by the Commission in the circumstances suggesting that the business of the company have been conducted or managed as to deprive the members thereof a reasonable return or that the affairs of the company are not being managed in accordance with sound business principles or prudent commercial practices. But, this is not what the objector has sought from the court. This, however, does not affect the applicability of the legal provision which remains to be adhered.

21. Though there may be disputes pending with the Income Tax authorities in respect of tax liabilities of PLL, I am not much concerned with those proceedings as the jurisdiction being exercised by me is that of a Company Judge and the matters and things that are brought to the notice of the court is in respect of its company jurisdiction. I am required to address them as the law requires it to be done.

22. The aspect of transfer pricing and its impact on the financial standing of PLL and resultant marginalizing of minority share-holders is very much admitted in the auditors report, that their investment have been diluted overtime by issuance of right shares to the parent company. The funds used by the parent company for this acquisition, is not a direct investment by it in PLL but from chunk developed on selling of its products to PLL at the price which otherwise is altogether unconscionable from the stand point of the comparative chart of same products being obtainable from other sources. It is amazing that PLL though having excellent sales is unable to show profits and for this the auditors themselves have squarely blamed the element of transfer pricing which the management of PLL is unable to avoid. Though business realities may be relevant, but at the same time, law requires directors to exercise their power in a fiduciary capacity and to conduct the business of the company on sound business principles or prudent commercial practices and not to deprive its members of reasonable return on their investment.



23. In the case of Scottish Co-Operative Wholesale Society Ltd. V/s Meyer and another {1959} AC 324 the House of Lords dealt with a case where the holding company took decisions regarding its subsidiary company which were oppressive and brought it to a pass where the subsidiary was on the verge of liquidation resulting decline in value of shares of subsidiary. seriously affecting its minority shareholders and relief was granted to them by fixing enhanced price of the shares by way of compensation and the company was allowed to operate and continue its business. His Lordship Viscount Simonds, in his opinion adopted the views of Lord President Cooper that "In my view, he said, the section warrants the court in looking at the business realities of a situation and does not confine them to a narrow legalistic view. Truth is that, whenever subsidiary is formed as in this case with an independent minority of shareholders, the parent company must, if it is engaged in the same class of business, accept as a result of having formed such a subsidiary an obligation so to conduct what are in a sense its own affairs as to deal fairly with its subsidiary." Same view was adopted by His Lordship Keith. He further quoted from Lord Sorn's, that "The society as majority shareholders controlling the company "made use of its control to ensure that the company remained passive under the attack and did not have an opportunity to struggle for its existence"; that they failed in their duty of raising "the question of looking for another source of supply as an urgent question of policy"; and that, when the policy of liquidation had been expressly approved by the society's board "the nominee directors still did nothing and let the company drift towards the rocks." His Lordship Denning, in his opinion expressed his view as to how a nominee directors are to conduct the affairs of the subsidiary company and stated thus:

"What, then, is the position of the nominee directors here? Under the articles of association of the textile company the co-operative society was entitled to *nominate three out of the five directors, and it did so. It nominated three of its own directors and they held office, as the articles said, "as nominees" of the co-operative society. These three were therefore at one and the same time directors of the co-operative society - being three out of 12 of that company - and also directors of the textile company - three out of five there. So long as the interests of all concerned were in harmony, there was no difficulty. The nominee directors could do their duty by both companies without embarrassment. But, so soon as the interests of the two companies were in conflict, the nominee directors were placed in an impossible position. Thus, when the realignment of shareholding was under discussion, the duty of the three directors to the textile company was to get the best possible price for any new issue of its shares (see per Lord Wright in Lowry v. Consolidated*



African Selection Trust Ltd.<sup>11</sup>), whereas their duty to the co-operative society was to obtain the new shares at the lowest possible price – at par, if they could. Again, when the co-operative society determined to set up its own rayon department, competing with the business of the textile company, the duty of the three directors to the textile company was to do their best to promote its business and to act with complete good faith towards it; and in consequence not to disclose their knowledge of its affairs to a competitor, and not even to work for a competitor, when to do so might operate to the disadvantage of the textile company (see *Hivac Ltd. V. Park Royal Scientific Instruments Ltd.*<sup>12</sup>), whereas they were under the self-same duties to the co-operative society. It is plain that, in the circumstances, these three gentlemen could not do their duty by both companies, and they did not do so. They put their duty to the co-operative society above their duty to the textile company in this sense, at least, that they did nothing to defend the interests of the textile company against the conduct of the co-operative society. They probably thought that “as nominees” of the co-operative society their first duty was to the co-operative society. In this they were wrong. By subordinating the interests of the textile company to those of the co-operative society, they conducted the affairs of the textile company in a manner oppressive to the other shareholders.”

24. His Lordship further goes on say that:

“ One of the most useful orders mentioned in the section which will enable the court to do justice to the injured shareholders – is to order the oppressor to buy their shares at a fair price: and a fair price would be, I think, the value which the shares would have had at the date of the petition, if there had been no oppression. Once the oppressor has bought the shares, the company can survive. It can continue to operate. That is a matter for him. It is, no doubt, true that an order of this kind gives to the oppressed shareholders what is in effect money compensation for the injury done to them: but I see no objection to this. The section gives a large discretion to the court and it is well exercised in making an oppressor made compensation to those who have suffered at his hands.”

25. In citing the provision of the Ordinance, the principles of conduct and dealings of the parent company with its subsidiary which affects the latter's business and its minority shareholders, my emphasis is that it should be based on good faith and in the interest of subsidiary company and upon sound business principles or prudent commercial practices and not be oppressive to the minority shareholders of depriving them of a reasonable return on their investment. The



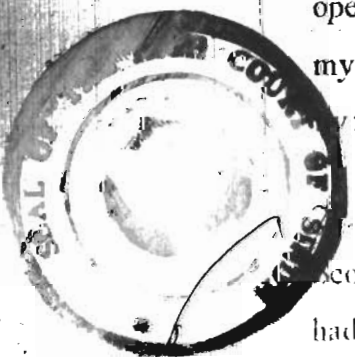
concept of on going concern and the valuation of tangible and intangible assets of PLL. as ordered by the Court on 14.10.2002 did not provide in its context, factors extraneous but only bonafide in the interest of PLL and its members based upon sound business principles or prudent commercial practices. Though, the auditors have done enormous work and have given their fair opinion about the affairs of PLL; but at the same time <sup>they</sup> ~~what~~ assumed that they were confined in their exercise to only whims and wishes of the management of PLL.

26. The grievance of the objector is that the value of their shares may be derived on dividend growth model value of Rs.2.717 million by excluding the right shares issued to the parent company. Apparently such an exercise will not be possible, for the reason that there is no proceeding before the court for the ratification of the register and it is not made clear as to on what principle of law, this can be done in this proceeding.

27. As the facts and circumstances do show oppressive treatment to minority shareholders of PLL inasmuch as they have not been paid return on their investment and the value of their shares have receded overtime for reasons already noted above, they seem to be entitled to some measure of compensation on acquiring from them their shareholding.

28. Apart from the arguments that right share be excluded in arriving at per share value on dividend growth model, no other mode was suggested. Be that as it may, the record shows that in the first report of the Chartered Accountants, per share value of PLL was worked out at Rs.1.37 as on 31.12.2000 on net asset value. The auditors, in their report, have worked out per share value at Rs.1.67 as on 31.12.2002 on net asset value. On dividend growth model, value per share is worked out at Rs.37.42 based upon an on going concern inclusive of goodwill and value of tangible and intangible assets and this is despite the fact that PLL is in loss to the tune of Rs.930.3 million for the year ending 2002. As it appears, the loss in the books of PLL, in reality may not be loss to the parent company but is a result of diversion of PLL funds to it by way of transfer pricing to use such funds either to enhance its own equity in PLL or to have it as its own profit derived from operation of PLL and to distribute it among its own members as dividend. This, in my view, is an oppressive conduct of the subsidiary and its minority shareholders by the parent company.

Thus in what form the objector could be compensated, in the cited case of Scottish Society, it was done by pricing the shares on the date of petition, if there had been no oppression. The date or dates on which the objector acquired the



shares of PLL will be relevant and the dates on which oppression seem to have taken place and the quantum and effect of such oppression on the objector's shares. The price of the objector's share may be worked out by the auditors minusing the element of oppression on the dividend growth model which model is accepted by the objector. The auditors will hear the objector and the PLL and accordingly give their report as early as possible.

30. The application in the above terms stands disposed of.

Karachi.  
Dated : 21.5.2007

*Sl. Gulzar Ahmad  
Judge*



CERTIFIED TO BE TRUE COPY.

*Sl. Gulzar Ahmad  
29/5/07*

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*25th May 07  
28th May 07  
29-5-2007*

ASSISTANT REGISTRAR

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*29/5/07*

*Sl. Gulzar Ahmad  
29/5/07*

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