



**BEFORE APPELLATE BENCH NO. III**

In the matter of

**Appeal No. 38 of 2006**

1. S.M. Ahmed  
2. Asim Ahmed  
3. Zubaida Khatoon  
4. Sohail Ahmed  
5. Saba Sohail  
6. M. Rafiq Dawood  
7. Rafiq Ahmed  
(Directors of S.G. Power Limited) ..... Appellants

Versus

Executive Director (Enforcement)  
Securities and Exchange Commission of Pakistan ..... Respondent

**ORDER**

Date of hearing ..... 22/12/11

**Present:**

**For the Appellant:**

Mr. Javed Panni, Chief Executive, MJ Panni & Associates

**For the Respondent Department:**

Ms. Amina Aziz, Director



## SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

SECP

1. This order shall dispose of appeal No. 38 of 2006 filed under section 33 of the Securities and Exchange Commission of Pakistan (the "Commission") Act, 1997 (the "SECP Act") against the order dated 06/04/06 (the "Impugned Order") passed by the Respondent.
2. Facts leading to the case are that on examination of annual audited accounts for the year ended 30/06/04 (the "Accounts") of S.G. Power Limited (the "Company"), it was observed that as per Note 9 and 11 to the said Accounts, the Company had receivable balances of Rs.194,497,933 and Rs.28,694,388 as 'trade debts' and 'other receivables' respectively from S.G. Fibre Limited (the "associated company") which were not falling in the nature of 'normal trade credit' in terms of section 208 of the Companies Ordinance, 1984 (the "Ordinance"). Moreover, The 'trade debts' amounting to Rs.194,497,933 far exceeded the annual sales of the Company which amounts to Rs. 191,862,245, thus resulting in trade debt collection period of 374 days which appeared to be an abnormal trade credit period.
3. Show cause notice dated 01/03/05 ("SCN") was issued to the Appellants under sub-section (3) of section 208 read with section 476 of the Ordinance. Reply to the SCN was submitted and hearing in the matter was held on 17/02/06. The Respondent taking a lenient view enforced penalty of Rs. 100,000 on each Appellant after the directors of the Company admitted default and began process of rectifying the default by recovering the said receivables due from the associated company. The Respondent gave further directions to the Appellants under section 473 of the Ordinance to recover the balance receivables as outstanding interest from the associated company; to recover the electricity sales from the associated company and to calculate and recover the interest as return on its previous years' credit which was not in the nature of 'normal trade credit'.



4. The Appellants preferred to file the instant appeal against the Impugned Order. The Appellants' counsel argued that:

(a) for the financial year ended 30/06/04, the Company had the following receivables from its associated company:

- |                         |                |                                |
|-------------------------|----------------|--------------------------------|
| (i) 'trade debts'       | Rs.194,497,933 | (sale of electricity)          |
| (j) 'other receivables' | Rs.28,694,388  | (outstanding interest on loan) |

The 'trade debts' resulted from the normal business operations whereby the Company had sold electricity to the associated concern that was the sole buyer of the said commodity, as such, the transaction was a 'normal trade credit'. Further, the Respondent has erred by treating 'outstanding interest on loan' to the associated company as 'other receivables'. The original loan has been repaid and it was not an extension of any type of credit to the associated company. The 'trade debts' and 'other receivables' do not fall under the category of "*investment*" in terms of section 208 of the Ordinance;

(b) the Board of Directors (the "Board") after keeping in view the financial hardships faced by the associated company and the Company's long term-interests, allowed soft payment terms of 12 months credit to the associated concern. Since, the directors of both the companies were the same and the trade credit was allowed by the Board, keeping in view business conditions prevailing at that time, the directors had not failed to exercise due diligence and care in discharge of their duties.



5. The Respondent argued that:

(a) the 'trade debts' amounting to Rs.194,497,933 far exceeded the annual sales of the Company which amounts to Rs.191,862,245, thus resulting in trade debt collection period of 374 days which is an 'abnormal trade credit period'. There was no recovery in the year 2004 with respect to 'outstanding interest on loan' which was recoverable from the associated concern. The amount receivable is not a 'normal trade credit' and is an "investment" in terms of sub-section (1) of section 208 of the Ordinance. Moreover, during the year ended 30/06/04, instead of recovering the said 'trade debts', the Company further extended financial help to the associated concern in the form of 'open ended credit' which is evident from the accounts of the Company;

(b) the Commission was informed by the Company that the Board had agreed and had passed a resolution for soft payment terms of 12 months credit to the associated concern. The aim of the Company was to provide financial benefit and assistance to its associated company; hence, if trade credit facilities are provided with the intention to provide financial benefit, then, it will not be termed as 'normal trade credit'.

6. We have heard the parties. Section 208 of the Ordinance has been reproduced for ease of reference:

**Section 208. Investments in associated companies and undertakings-**

*(1) [Subject to sub-section (2A) a] company shall not make any investment in any of its associated companies or associated undertakings except under the authority of a special resolution which*



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*shall indicate the nature, period and amount of investment and terms and conditions attached thereto:*

*Provided that the return on investment in the form of loan shall not be less than the borrowing cost of investing company.*

*Explanation.- The expression 'investment' shall include loans, advances, equity, by whatever name called, or any amount which is not in the nature of normal trade credit.*

### Emphasis added

- (a) From the perusal of the documents and financial statements of the Company, it is evident that the Company's paid up capital for the years 2004 and 2005 is Rs.178.332 million whereas the 'trade debts' due from the associated company during the years ended 30/06/04 and 30/06/05 was Rs.194.498 million and Rs.242.515 million respectively. The said 'trade debts' far exceeded the paid up capital of the Company, as such, the said credit facility extended to the associated company, cannot be termed as a 'normal trade credit'. Providing 'open ended trade credit' falls under the ambit of section 208 of the Ordinance. The aforesaid credit was extended to the associated company without seeking prior approval of the shareholders through a special resolution. For the foregoing reasons, it is established that the Chief Executive and the directors have violated the provisions of section 208 of the Ordinance and have not exercised due care while extending the said credit to the associated concern;



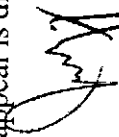
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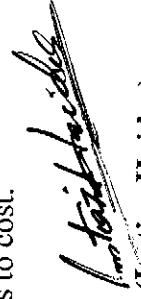
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(b) In the instant matter, the aim of the Company was to provide financial assistance to its associated concern. Approval through special resolution in general meeting of shareholders is required for such finances to be provided to associated companies. Credit facilities have been provided to the associated company which is greater than the whole year's sale of the Company and the 'trade debts' for both the years are far exceeding the paid up capital of the Company. The resolution for soft payment terms of 12 months cannot be termed as 'normal trade credit' as it was meant for financial assistance to the associated company.

In order to ascertain the affairs of the Company, the Auditors' Report for the year 2011 has been perused. The Company is non-operational and the financial statements has further disclosed that an amount aggregating to Rs. 176,112,583 are still receivable from the associated company which has also shut down its plant and is running into huge losses. No compliance has been made in pursuance of the directions issued by the Commission through the Impugned Order. No mark-up has been provided in the current financial year against the aforementioned liability.

In view of the above, we see no reason to interfere with the Impugned Order. The appeal is dismissed with no order as to cost.

  
(Mohammed Asif Arif)  
Commissioner (Insurance)

  
(Imtiaz Haider)  
Commissioner (SM)

Announced on: 01/03/12