

Before Tahir Mahmood, Commissioner (CLD)

In the matter of

Zahidjee Textile Mills Limited

(Under Section 492 read with 473 and 476 of the Companies Ordinance, 1984)

Number and date of notice:	No.EMD/233/209/2002/1710-1717 Dated: June 25, 2010
Date of hearing:	September 24, 2010
Present:	Mr. Shahab-ud-din, Company Secretary Mr. Atta Muhammad Khan, Advocate, Legal Counsel
Date of Order:	October 1, 2010

ORDER

This order will dispose of the proceedings initiated against the Chief Executive, following Directors and CFO / Company Secretary of Zahidjee Textile Mills Limited (*the "Company"*) under Section 492 read with Section 476 of the Companies Ordinance, 1984 (the Ordinance) which states;

"Whoever in any return, report, certificate, balance sheet, profit and loss account, income and expenditure account, prospectus, offer of shares, books of accounts, application, information or explanation required by or for the purposes of any of the provisions of this Ordinance or pursuant to an order or direction given under this Ordinance makes a statement which is false or incorrect in any material particular, or omits any material fact knowing it to be material, shall be punishable with fine not exceeding five hundred thousand rupees."

2. The brief facts leading to this case are that the examination of the annual audited accounts of Company for the year ended June 30, 2009 (*the "Accounts"*) revealed that Note 9 (*Other receivable*) to the accounts of the Company disclose receivable against disposal of short term investment in the amount of Rs. 34.264 million (2008: 17.913 million). The Company attributed the aforesaid receivable to the sale proceeds of 467,700 ordinary shares of Askari Commercial Bank Limited (*the "share sale proceeds"*), receivable from the Company's authorized broker M/s Invest Capital and Securities (Pvt) Ltd (*the "Broker"*). The above shares were sold in the open market, from July 24, 2008 to August 20, 2008.



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet 2

3. The Company further informed, upon query by the Commission regarding the delay in the repatriation of such share sale proceeds from the broker to the Company, that the share sale proceeds were kept with the broker with the object of reinvestment in more profitable shares to recover the loss as and when the market situation allows. The Company further stated that the aforesaid funds were later on received by the Company from Feb 01, 2010 to March 18, 2010.

4. However, the information called from the broker showed that the share sale proceeds were not remitted/settled by the broker directly to the Company rather they were transferred from the Company trading account No. K 0102 to the trading account maintained in the name of Muhammad Zahid, the Chief Executive of the Company (Account Code No. K 0107). The broker record provided to the Commission divulged that said transfer of share sale proceeds were instructed by Muhammad Zahid, who was the authorized representative/signatory to open and operate the trading account with the broker. It was also noted from the record provided that one of the officers of the Company, Mr. Muhammad Asif, Manager Finance has also advised the broker regarding the transfer of Rs. 17.613 million among the share sale proceeds. The broker further disclosed the following credit ledger balances of the Company trading account with the Company (i.e. *Amount due from the Company to the broker*);

- a. As on June 30, 2008: Rs. 299,286
- b. As on June 30, 2009: Rs. 399

5. It was noted from the ledger statements received from the broker that Muhammad Zahid was paying mark-up to broker as high as upto 20 % per year on the debit balances of his personal trading account. Thus he has benefited himself by reducing these debit balances and saving the interest costs through transferring and utilizing the aforesaid Company funds into his personal trading account. The Company however failed to comply with the mandatory provision of Section 492 of the Ordinance, by misstating the factual position of those outstanding funds as receivable in the accounts.

6. Consequently, a show cause notice dated June 25, 2010 (SCN) was issued to the Chief Executive, all the directors and the CFO / Company Secretary (*the "Respondents"*), calling upon them to show cause as to why penal action may not be taken against them under Section 492 read with Section 472 and 476 of the Ordinance for violating the statutory requirements of the Ordinance. The Respondents did not submit their reply in the allowed time of fourteen (14) days and were extended a hearing opportunity vide



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet 3

Commission letter dated July 7, 2010, to be held on July 12, 2010, for submission of Respondents' representations. However, the Respondents requested, vide their letter dated July 7, 2010, for extension in time line for submitting the reply to the SCN owing to the continued absence of the Company Secretary due to recent expiry of his mother as well as the engagement of the management in preparation of annual accounts due to year end. The hearing was deferred until July 15, 2010, however Mr. Muhammad Zahid, the Chief Executive of the Company informed, vide his letter dated July 14, 2010, that since he wanted to be represented by an authorized representative, who has just returned from his foreign tour and will need at least fifteen (15) days for thorough study of the case. He however further requested for another adjournment after July 30, 2010, vide his letter dated July 23, 2010. The Commission fixed the hearing opportunity on August 16, 2010, on which Mr. Atta Muhammad Khan, Advocate, the legal counsel of the Respondents and Mr. Shahab-ud-din, the Company Secretary appeared and submitted their written representations on behalf of the respondents. The hearing was deferred until September 24, 2010, on which the representatives appeared and put forward the same arguments as were submitted in their written representations, earlier on.

7. The submissions made by the Respondents in its replies to the show cause notice are summarized as under:

- i. The Company sold 545,700 shares from February 26, 2008 to June 20, 2008 and 467,700 shares from July 24, 2008 to August 20, 2008 of Askari Bank Limited through authorized broker and the total amount receivable as per accounts for the year ended June 30, 2009 was Rs. 34.264 million.
- ii. Factually there was no delay in repatriation of sale proceeds of shares from broker to the Company. Sale proceeds of 545,700 shares were kept with the broker with the object of reinvestment. Out of which 50,000 shares of Askari Commercial Bank were repurchased through the broker on June 25, 2008. But in view of unfavorable market situation the management decided to adjust the loan account of Mr. Muhammad Zahid. The loan adjusted was recouped by Mr. Muhammad Zahid from February 01, 2010 to March 18, 2010 as per requirement of the Company.



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet 4

- iii. Mr. Muhammad Zahid, the CEO as per agreement dated July 02, 2007 has provided interest free loan to the Company in his name as well as in the name of his dependents of which year wise detail is as under;

Year	Loan provided by Muhammad Zahid and his dependants <i>(Amount in Rs)</i>	Loan provided directly by Muhammad Zahid dependants <i>(Amount in Rs)</i>
2007	200,173,359	82,309,758
2008	182,797,171	59,940,280
2009	180,422,107	56,565,116

- iv. As per clause 6 of the loan agreement, the Company is entitled to re-pay the loan by way of adjustment of its receivable from third party subject to written confirmation by the third party. The Company disposed off shares of Askari Commercial Bank Limited and an amount of Rs. 34.264 million was receivable from broker. The Company instructed the broker to pay the receivable to Mr. Muhammad Zahid against his interest free loan to the Company. The adjustments of balances in the books of account of the Company were subject to written confirmations of the adjustment. The written confirmation of adjustment in terms of loan agreement was received by the Company on October 17, 2009. The balance receivable from broker was accordingly adjusted vide our voucher No. 199 dated October 17, 2009 and transferred to the loan account of Mr. Muhammad Zahid. However, keeping in view the requirements of the Company Rs. 33.949 million was recouped by Mr. Muhammad Zahid in loan account during the period from Feb 2010 to March 2010 in terms of loan agreement.
- v. The difference between the ledger accounts of the Company with the books of Invest Cap was due to the following pending adjustment;

Description	2009 <i>(Amount in Rs.)</i>	2008 <i>(Amount in Rs.)</i>
Balance as per books of account of the Company	34,263,886	17,912,775
<u>Less:</u> Pending transfer to the CEO's loan	34,263,388	17,613,388



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet 5

account due to the pending written confirmation		
<u>Less:</u> Credit vide JV 4553 dated June 25, 2008	(100)	(100)
Rounding off difference	1	1
Balance as per books of account of broker	399	299286

- vi. Mr. Muhammad has not benefited himself by transferring and utilizing the Company's funds into his personal trading account but the Company has repaid his loan by issuing instructions of adjustment. Factually the Company is benefited from the huge amount of interest free loan granted by Mr. Muhammad Zahid in his personal name and in the name of his dependents.
- vii. The provisions of section 492 are not attracted in this case as the Company and its management has strictly acted in accordance with the provisions of law and the contents of the loan agreement executed between the Company and Muhammad Zahid as borrower and lender. The instructions to the broker on behalf of the Company were issued in terms of loan agreement. The disclosure in the annual accounts were made as per substance of the events and accounting policy of the Company as the presentation of net position of Muhammad Zahid loan account was subject to written confirmation from the broker therefore, the gross amount of loan payable to Muhammad Zahid and amount receivable from Invest Cap was faithfully presented in the annual accounts.
- viii. The Company has not made any false or incorrect statement in the annual account. The balance receivable from Invest Cap was shown due to the fact that neither any remittance nor any confirmation of adjustment was received till closing of annual accounts

The provisions of section 492 are not applicable in the instant case as the non adjustment of receivable of Rs. 34.264 million against the liabilities out of total current assets of Rs. 1426.6 million is not material in the light of definition of "material" in International Accounting Standard-I. Furthermore, the Company has not provided undue benefits to Muhammad Zahid as the transactions were carried out in the normal course of business.



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet 6

- ix. Based on the facts summarized above, the provisions of section 492 of the Companies Ordinance, 1984 do not apply in our case as the transactions carried out were in the normal course as per Company's accounting policies and terms of the loan agreement signed with Mr. Muhammad Zahid.
8. I have considered the facts and record of the case, relevant provisions of the Ordinance, written submissions made in response to SCN and presented during the hearing, however, I do not find myself convinced with the arguments raised by the Respondents. My observations on the issue are as follows:
- a. The Company, first in its letter dated April 5, 2010, attributed the receivable from the broker in the amount of Rs. 34.264 million, to sale proceeds of ordinary shares of Askari Commercial Bank Limited, sold during July 24, 2008 to August 20, 2008. The Company further explained in its letter dated April 23, 2010, upon enquiry by the Commission regarding the reason and position of this outstanding receivable, that the funds were kept with the broker with the object of reinvestment in more profitable shares to recover the loss. It has also informed that the said funds were received by the Company through crossed cheques during Feb 1, 2010 to March 18, 2010, while attaching the copy of bank statements showing the said recovery.
- b. However, when the Company was called upon for the supporting documents to verify its position with regard to the sale of shares and receipt of funds including the bank vouchers and broker ledger statements vide Commission letter dated May 21, 2010, the same were not provided until July 14, 2010, much after the date of aforesaid show cause notice issued dated June 25, 2010, when the Respondents appeared with a different position than before. The Respondents presented a loan agreement dated July 2, 2006 executed between Mr. Muhammad Zahid, the CEO (*the Lender*) and the Company (*the Borrower*) and stated that the said receivables were utilized for adjusting the loan of Muhammad Zahid towards the Company in accordance with clause 6 of the Loan Agreement. The said loan adjustment was stated to be recouped by Muhammad Zahid during the period from Feb 01, 2010 to March 2010.



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet 7

- c. The respondent stated that the share sale proceeds were transferred to Muhammad Zahid in accordance with the clause 6 of the said loan agreement, which states that the borrower i.e. the Company is entitled to repay any amount by way of adjustment of its receivables from third parties. The clause further states that the amount of loan outstanding shall be adjusted in the books of account of the borrower with the amount realized by the lender from the third party on the written confirmation of offsetting arrangement by the third party. Since such written confirmations were received on October 17, 2009 hence were adjusted in the books of accounts on that date and accordingly the receivable could not be reduced by the aforesaid adjusted amount in the annual accounts for the period ended June 30, 2009.

The respondents' plea for not recording the transaction due to delayed receipt of written confirmation is not valid since the Company was regularly receiving the ledger/trading statement from the broker where all the relevant share sales and purchases were indicated along with the receivable/payable balance from/to the broker. Moreover, Mr. Muhammad Zahid was the Chief Executive of the Company who has instructed this transfer of funds from Company's trading account maintained with the broker to his personal trading account with the same broker and hence has sufficient knowledge of receipt of that credit in his account and the adjustment of receivable from the broker. All this is sufficient supportings for recording this transaction in the books of accounts of the Company, as per the accounting conventions. The argument presented that this transaction could not be recorded due to the absence of written confirmation from third party is merely an excuse since avoiding the accounting treatment of a transactions which otherwise has a serious impact due to the involvement of the CEO, on the pretext that certain clause of some loan could not be fulfilled is not a valid argument. The existence of such clause in loan agreement can not prevail upon the accounting treatment of recording of receivable by way of adjustment, as that loan agreement is purely a separate matter between Borrower and Lender and can not overrule the general accounting principles.

- d. Most importantly, when the copy of the aforesaid loan agreement was sent for verification of issue of underlying stamp paper (*bearing No. 9456 issued on 20-6-2006*), its particulars could not be verified from the Stamp Issue Register that was submitted to the General Record Room, Faisalabad, proving this agreement to be an invalid/fake document, and its execution



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet 8

at the declared date of agreement. The negative confirmation of the issuance of stamp paper and hence the loan agreement thus fundamentally excludes the justifications offered by the respondents for their defaults, which even otherwise don't carry rationale and are not tenable.

9. Moreover, the respondent's representatives, during the hearing, after witnessing the evidence to the above discussion, also admitted the default and requested for a lenient attitude.

10. From the above discussions, the submissions put forward by the Respondents and the vital information available on record, I am of the considered view that Section 492 of the Ordinance has been violated and directors are liable for the penalties as defined in aforesaid Section of the Ordinance. However, since substantial amounts of interest free loan have been provided by the respondent directors to the Company, I therefore impose a penalty aggregating to Rs. 17,50,000/- (Rupees Seventeen hundred and fifty thousand only) on the Chief Executive and the following directors of the Company.

The detail of the penalties imposed is as follows:-

S. No.	Name	Penalty (Rupees)
1	Mr. Muhammad Zahid, Chief Executive	250,000
2	Mrs. Muhammad Qasim, Director	250,000
3	Mst. Huma Zahid, Director	250,000
4	Mst. Fauzia Shahani, Director	250,000
5	Mr. Naveed Ahmed, Director	250,000
6	Mr. Asma Makhdoom, Director	250,000
7	Mst. Fiza Zahid, Director	250,000
	Total	1,750,000

13. The Chief Executive and aforesaid directors of the Company are hereby directed to deposit the aforesaid fines aggregating to Rs.1,750,000/- (Rupees Seventeen hundred and fifty thousand only) in the designated bank account maintained in the name of Securities and Exchange Commission of Pakistan with MCB 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



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Enforcement Department

Continuation Sheet 9

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.

Before departing with the order, I hereby invoke provision of section 473 of the Ordinance and direct the Chief Executive of the Company to deposit the mark up on the outstanding amount transferred to the personal trading account of Mr. Muhammad Zahid on a rate which shall not be less than the borrowing cost of the Company, from the date the funds were advanced till its repatriation. The directions are to be complied within 60 days of the date of this order and the Chief Executive is to submit a report to this Commission duly certified by the statutory auditor of the Company.

Tahir Mahmood
Commissioner (CLD)

Announced:
October 1, 2010, Islamabad