

No.19 (701) CF/ISS/92-
SECURITIES & EXCHANGE COMMISSION OF PAKISTAN
(Enforcement & Monitoring Division)
NIC Building, Jinnah Avenue, Blue Area

**IN THE MATTER OF INVESTIGATION INTO THE AFFAIRS OF
M/S CHAKWAL CEMENT COMPANY LIMITED**

No.& date of Show Cause Notice : No.19(972)CF/ISS/92 dated 25-07-2000.
Date of final hearing : 19-12-2001 -
Appearance : Mr. Irfan Ahmad Shèikh, Advocate
Date of Order : 01-02-2001

**ORDER UNDER SECTION 265 OF THE COMPANIES
ORDINANCE, 1984**

M/s Chakwal Cement Company Limited was incorporated as a Private Limited Company on May 23, 1993. Later on the status of the Company was converted from Private to Public through special resolution dated October 18, 1994. The main object of the Company is to carry out the business of the production and sale of cement. The paid up capital of the company as on June 30, 1999 was Rs.5 .624 billion. The company made public offer of its shares in Oct. 1995 amounting to Rs 602.72 million which was fully subscribed. The company could not start its operations as undertaken in the prospectus and did not pay any return to its shareholders after listing and presently its shares of Rs. 10/- per share are being quoted below Rs.1/-.

2. Several complaints were received from the shareholders that the company had never paid any return on their investments since November 1995. Shareholders further complained that they did not receive any information regarding the development of the company, financial statements or any other correspondence from the company. Institutional investors i.e. National Investment Trust (NIT) and State Life Insurance Corporation of Pakistan (SLIC) also complained about the adverse performance of the company in the last few years. SLIC

further complained that the company had defaulted on payment of guaranteed interest @16% per annum right from the first maturity of interest payments which accumulated to Rs.64 million as on 22.08.99 against which SLIC had already filed a suit in Sindh High Court against the Chief Executive of the company. Humanity Foundation and Geoffery & Khitran, Advocates also filed complaints that the management of the company has been defrauding national exchequer by forging property registration documents. After series of correspondence between the company and erstwhile CLA in 1998, the company was required to file monthly progress reports of the development in the commissioning of the project. However, the said reports were never received by KSE nor by the CLA.

3. The company published a notice on 7-12-99 in newspapers that in its AGM the management of the company will move a resolution to seek authorization of the members for re-export and sale of the plant and machinery for such consideration and on such terms and conditions as the directors may consider beneficial to the company. Further, the Directors report annexed to the financial statements for the period ended on June 30,1997 indicated that in case necessary financing to complete the project could not be arranged, export and or sale of the plant and machinery would be inevitable to save the machinery from deterioration.

4. On enquiry from the company regarding the rationale behind disposing of most of the plant and machinery eventually leading to the liquidation of the company, the company replied that the idea was coined after an auction "Notice" was published by Collector Custom, Karachi in the daily Nation in Aug. 1999 with regard to the machinery lying at Custom Warehouse or Karachi Port to recover the import duties and other dues leviable on plant and machinery amounting to Rs. 1 billion approximately. The company had not disclosed this material fact in the statement u/s 160(l)(b) annexed to the notice of meeting dated 7-12-1999 nor in the Directors' report annexed thereto. These facts seriously incited the apprehension of the Commission regarding the conduct of the affairs of the company and necessitated detailed review of the affairs of the company since its listing.

5. On examining of the record of the company it was noticed that the company which undertook to start the commercial production in October 1997 in its Prospectus, has not completed its project even to-date. On inquiring the reasons for delay in completion of the project and start of commercial production, the company had informed erstwhile CLA in 1998 that certain commitments from various financial institutions viz M/s. Faisal Bank and Citibank N.A. to meet part of the financing of the project to the tune of Rs.700 million could not materialize due to restrictions imposed by the State Bank of Pakistan which pushed the company into adverse financial

constraints thus delaying the project. The company further explained that the benefit of exemption from import duties and sales tax available through SRO 484(1)/92 expired in 1995 putting additional burden on the company. The company also argued that increasing inflation necessitated the need for additional funds to bridge the escalation in the project cost which could not be arranged.

6. It was further observed that company made false and/or incorrect statements in material, particular knowingly and willfully in the directors' reports for various years. In the Directors' Report for the period ended 30.06.96 signed on November 11, 1996 it was stated that the project implementation is progressing well, foreign and local machinery suppliers are progressing as per schedule and it is expected that the project shall commence commercial production in October, 1997. The Directors' Report on the financial statements for the half year ended 31-12-1996 issued on 26-2-1997 stated that major imported/local plant and machinery has been shipped/manufactured and has also reached at the plant site: There was no indication in the report of directors that the completion of project was being delayed. In the Directors' Report for the year ended 30.6.1997, the delay in the implementation of the project was mentioned to some extent but Directors assured to bridge the gap of additional funds for completion of the project. Then contrary to the statement made in Directors' Report for the half year ended December 1996 (where it has been stated that major imported machinery had reached the site), it was stated in this report that substantial part of machinery was still lying at Karachi Port for want of heavy storage charges. However, it was claimed that due to continuous efforts of the management of the company, Government had taken lenient view and allowed release of machinery at minimum concessional rates.

7. In the Directors' Report for subsequent year the directors primarily focused to assure to the shareholders that if the project is completed it would be most viable project of the country. This report again concealed this aspect from the shareholders that the company could not even get the plant and machinery cleared from the port where it was turning into a junk. The report rather again assured that the management would be able to bridge the gap of funds required for completion of the project. This way shareholders were continuously kept in dark about the fate of the project of the company, where as, the law enjoins the company to give a true and fair view of its, state of affairs.

8. In view of the above a Show Cause Notice under Section 265 of the Companies Ordinance, 1984 was issued to the company requiring them to explain that why an Inspector should not be appointed to investigate into the affairs of the company.

9. The company in response to the show cause notice referred to above filed an interim reply stating that complaints of Humanity Foundation as well as of Geoffrey & Khitran, manifest that these are instruments of black mailing and nothing else.

10. It was further argued by the authorized representative of the company;

- a) That there is no allegation of any mismanagement of the company by any of the above persons;
- b) That there is no material, on the basis of which it could be alleged that the company has not conducted or managed its affairs according to sound business principles or prudent commercial practices; and
- c) That the only grievance is lack of payment of dividend.

11. The company's reply was examined in detail and found vague and/or irrelevant in the circumstances avoiding explanation on the specific issues involved in the case. The issues were examined in detail and the following emerged:-

- (a) The company's claim that the project could not be completed due to failure of some of financial institutions in timely providing their part of the financing is not tenable as the funds of Rs.700 million constitute about 10% of total cost of the project. It is strange that for want of only this minor amount of funds, the project was stuck up to the extent that its machinery could not be cleared from the port. The Management has repeatedly been assuring in the Directors Report to be able to fill this gap of funds. It was stated in one report that even suppliers have agreed to contribute funds to fill the financing gap. It is not understandable that how a prudent management can prefer to let the investment of billions of rupees go down the drain only due to disputes on regulatory duties. It appears that the management was never serious in implementing the project.
- (b) The Directors continued to make false statements and concealed material facts from shareholders that the company was not able to even get the plant and machinery cleared from the custom authorities and the same was still lying at the port.
- (c) The company continued to prepare the financial statements on the going concern assumption on the

basis of the continued financial support of its sponsors and its lending agencies. However, no such financial support from the sponsors was ever received by the company making the whole basis incorrect and making a misstatement in the financial statements.

12. The company was allowed opportunity to explain its viewpoint and Mr. Irfan Ahmad Sheikh, Advocate High Court, company's authorized representative, after obtaining various adjournments finally appeared on 19.12.2000 and argued the case in line with the matters raised by him through his letter dated 15.12.2000. Mr. Sheikh preferred not to touch the facts and merits of the case and took very innocent defense that since the company has not commenced the business it cannot be said that affairs of the company are not being conducted in accordance with sound business principles. He stressed that conducting of business means business of the company after its project has gone into commercial operations. He has further shown his anger on the Commission for issuing notices to a company which according to his arguments has been/is doing wonderful jobs for shareholders. The authorized representative of the company preferred not to say even a single word on the facts concerning the case but through his written reply and arguments at the time of hearing confined himself to irrelevant issues i.e. that in absence of rules framed by the Commission for conducting proceedings u/s 265, the Commission is not authorized to carry out explorative reading of accounts filed with Commission as such accounts are filed only for record purposes, that total acts of the Enforcement Division are unlawful and the Commission is not an organ of state, that its employees are non-civil servants and non-civilians cannot adjudicate matters under the Companies Ordinance, 1984, that Commission at present is deficient in representation of industrialists, and that notice has been issued without appreciating the untoward climate in commercial circles. He suggested that the company should not be kept under baseless strain and harassment and sponsors should be allowed to complete their project for the uplift and welfare of the industry and the country. While arguing that the management should be allowed to complete the project he has forgotten that the company has already proposed resolution to re-export most of the plant and machinery eventually leading to liquidation of the company. Appointment of inspector u/s 265 is in no way a punitive action but only requires a fact finding exercise. It cannot be denied that in case of this company, situation is not quite normal. The imported plant has not even reached the destination and is being re-exported. Small shareholders to whom the company and its management owe fiduciary obligations are crying that their investment is sinking. In these circumstances, it becomes obligatory on the Commission to at least dig out facts through independent sources. If Inspector, in his report, holds that the company has reached this stage, due to fault of none of the promoters/directors thereof, the report will rather be helpful to the management than being detrimental to their interests. I fear that if at this stage the Commission does not even arrange a fact finding exercise, the Honourable Court and also the

shareholders will tomorrow hold the Commission responsible for not having timely acted to safeguard the shareholders' interests.

13. Now therefore, in the public interest and in exercise of the powers conferred upon me under Section 265 (b) of the Companies Ordinance, 1984 (XLVII of 1984), I hereby appoint Mr. Abdur Rahman Mir, FCA of M/s Rahman Sarfaraz & Co., Chartered Accountants, 2nd Floor, Nawai-e-Waqt Building, Shahrah-e-Fatima Jinnah, P.O. Box 51, Lahore to act as Inspector to investigate into the affairs of M/s. Chakwal Cement Limited on a remuneration of Rs. 150,000/- (Rupees one hundred fifty thousands only) which shall be paid by the company.

14. Without, in any way limiting the scope of investigation, the Inspector shall conduct investigation on all aspects of the operations of the company and shall after scrutiny of the entire record and books of accounts furnish reports, inter alia, on the followings matters:

- (i) Reasons for non-completion of the project and start of commercial production as undertaken in the prospectus.
- (ii) Determination of false and incorrect statements made in the Prospectus and the Directors' Reports.
- (iii) Whether or not funds raised through public offer were utilized in the manner as undertaken in the Prospectus.
- (iv) Whether or not proper records have been kept by the company as required by Sections 230 and 234 of the Companies Ordinance, 1984.
- (v) Whether or not an adequate system of internal controls exists/existed so as to prevent misappropriation and misapplication of companies assets.
- (vi) Whether or not expenses have been properly incurred, sanctioned, vouched and allocated and whether these were for exclusive purpose of the company.

(vii) To report any lapse or other delinquency detected during the course of investigation.

15. The Inspector shall submit a detailed report along with supporting documents/evidence to the Commission (in quadruplicate) within 60 days from the date of this order.

16. Proceedings with reference to the Show Cause Notice dated February 15, 2000 under Sections 60, 66 and 492 of the Companies Ordinance, 1984 will be finalized after receipt of the Inspector's Report.

(M. Zafar - ul - Haq Hijazi)
Commissioner (Enforcement)