



# SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

**Before Tahir Mahmood  
Commissioner (CLD)**

**In the matter of**

**Elahi Cotton Mills Limited**

Number & date of the notice: EMD/TO/26/2009-2415-2418 dated September 02, 2010  
Date of hearing: December 13, 2010  
Present: 1. Mr. Javed Panni, MJ Panni & Associates  
2. Mr. M. Ayub Qureshi, MJ Panni & Associates

## **ORDER**

### **Under Section 26 read with Section 25 of the Listed Companies (Substantial Acquisition of Voting Shares and Takeovers) Ordinance 2002**

This Order shall dispose of proceedings initiated vide Show Cause Notice No. EMD/TO/26/2010/2415-18, dated September 02, 2010 (the "SCN") issued in the matter of acquisition of substantial shares of Elahi Cotton Mills Limited ("Company or Target Company") pursuant to provisions of Section 26 read with Section 25 of the Listed Companies (Substantial Acquisition of Voting Shares and Takeovers) Ordinance 2002 ("Takeovers Ordinance"):

2. The facts of the case are that the cumulative review of the statutory returns, documents filed with Securities and Exchange Commission of Pakistan (the "Commission") and pattern of shareholding annexed with annual reports for the year ended June 30, 2007, June 30, 2008 and 30, 2009 of the Company revealed that shareholding of Mr. Mahboob Elahi (*the "Acquirer"*), the Chief Executive / Director of the Company has increased substantially from 8.92 % to 28.54% in the paid up capital of the Company in the aforesaid periods. This substantial increase in shareholding was attributed, in the information provided by the acquirer, to the acquisition of 255,000 shares through broker as well as through the purchase of physical shares against cash, between August 8, 2007 to May 29, 2008.

3. As is evident from the above information provided by the acquirer and the perusal of records available/submitted with the Commission that as on June 30, 2008, the acquirer has increased his



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 2 -

shareholding from 8.92 % to 28.54%, thereby crossing the threshold level of 25 % holding of voting shares in the Company which requires the compliance of section 5 of the Takeovers Ordinance, which includes the disclosure to the Target Company and to the stock exchange on which the voting shares of the Target Company are listed, as well as the making of a public announcement of offer.

4. Moreover, the aforesaid cumulative review further revealed the increase in the shareholding of the following four directors of the Company (together the "Acquirers") from 26.26 % (year 2007) to 48.19 % (2008), and subsequently to 78.59 % was mainly due to the increase in holding of three directors, all of them are forming a group being a family.

Year-wise comparison of shareholding of the directors						
Categories of Share Holders	June 30, 2007		June 30, 2008		June 30, 2009	
	Number of shares	% of holding	Number of shares	% of holding	Number. of shares	% of holding
Mr. Mahboob Elahi, CEO	116,000	8.92 %	371,000	<u>28.54 %</u>	548,200	42.17 %
Mr. Mahfooz Elahi, Director	77,675	5.98 %	77,675	5.98 %	199,675	<u>15.36 %</u>
Mr. Mahmood Elahi, Director	74,250	5.71 %	104,250	8.02 %	200,250	<u>15.40 %</u>
Mrs. Samina Begum w/o Mr. Mahboob Elahi	73,500	5.65 %	73,500	5.65 %	73,500	5.65 %
Director, CEO & their spouse & children	341,425	26.26 %	625,425	<u>48.19 %</u>	1,021,625	<u>78.59 %</u>

5. The aforesaid comparison indicate that the group while acting in concert has steadily consolidated its holding from 26.26 % to 48.19 % and finally 78.59 % in years 2007, 2008 and 2009 respectively, which requires compliance of section 6 provisions of Takeovers Ordinance that includes the disclosure to the Target Company and to the stock exchange on which the voting shares of the Target Company are listed, as well as the making of a public announcement of offer.

6. To ascertain whether the Acquirer(s) have complied with the applicable provisions of the Takeovers Ordinance, the Commission vide its letter dated July 19, 2010 advised the Acquirers to provide documentary proof of compliance with the requirements of the Takeovers Ordinance before the acquisition/consolidation of holding in the Target Company. The acquirers individually replied to



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 3 -

the said letters while stating that the compliance of the applicable provisions of the Takeovers Ordinance have been made. In addition to this, the information for acquiring of shares has also been communicated to the Commission as and when acquired in the form of submission of return/Form 31 and 32 under section 222 and 224 of the Companies Ordinance, 1984. Salient points extracted from the said replies are stated below:

- a. *Dates and mode of acquisition of shares.*
- b. *Name of sellers will be submitted if desired by you.*
- c. *Compliance was not applicable as there was no change in management control nor in influence on the board of Target Company.*
- d. *The latest information of the number of shares held*

7. The aforesaid replies were found unsatisfactory since the Acquirers were unable to justify that the mandatory provisions of the Takeovers Ordinance were not applicable on them. Therefore, an SCN dated September 2, 2010 was served upon the acquirers as to why action may not be taken against the Acquirers and persons acting in concert under Section 25 and sub-section (3) of Section 26 of the Takeovers Ordinance for non-compliance under the Takeovers Ordinance.

8. The Acquirers submitted their response through MJ Panni & Associates, Corporate and Capital Market Consultants (*"the Authorised Representative"*) vide November 5, 2010. The submissions of the Respondents' Representative are summarized below:

- a. The Target Company was initially established at Dacca that was shifted to Pakistan in a plant location at Tehsil Gojar Khan, District Rawalpindi and was installed in 1973. The mills comprising of 12,432 spindles at one point of time, could not go through BMR program due to financial losses and was reduced to 6,216 spindles at the end of 2009 and is operating with almost forty years old machinery.
- b. Mr. Mahboob and family acquired complete management and control of the Company in 1980, and had following shareholding at that time that has been increased over a period of time in the coming years;



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 4 -

<i>Pattern of shareholding of the Company</i>										
<i>Name of shareholder</i>	1980		As on Dec 31, 2002		As on Oct 24, 2007		As on Oct 27, 2008		As on Oct 28, 2009	
	<i>Shares</i>	<i>%</i>	<i>Shares</i>	<i>%</i>	<i>Shares</i>	<i>%</i>	<i>Shares</i>	<i>%</i>	<i>Shares</i>	<i>%</i>
Mr. Mahboob Elahi	48,000	7.38	96,000	7.38	186,000	14.34	386,500	29.72	558,200	42.94
Mr. Mahfooz Elahi	-	-	74,250	5.71	77,675	5.98	77,675	5.98	199,675	15.36
Mr. Mahmood Elahi	-	-	74,250	5.71	104,250	8.02	104,250	8.02	200,250	15.40
Mrs. Samina Begum	86,750	13.35	73,500	5.65	73,500	5.66	73,500	5.66	73,500	5.66
<b>Total</b>	<b>134,750</b>	<b>20.73</b>	<b>318,000</b>	<b>24.66</b>	<b>441,500</b>	<b>34.00</b>	<b>641,925</b>	<b>49.38</b>	<b>1,031,625</b>	<b>79.36</b>
<i>Financial Institutions</i>										
ICP	85,900	13.20	158,867	12.22	-	-	-	-	-	-
HBL	95,450	14.70	190,900	14.68	79,000	6.07	78,400	6.03	-	-
Salim Sozar Securities (Pvt) Ltd.	-	-	-	-	-	-	-	-	149,006	11.47
General Public	333,900	51.37	632,233	48.64	779,000	59.93	579,675	44.59	119,369	9.13
<b>Total</b>	<b>650,000</b>	<b>100</b>	<b>1,300,000</b>	<b>100</b>	<b>1,300,000</b>	<b>100</b>	<b>1,300,000</b>	<b>100</b>	<b>1,300,000</b>	<b>100</b>

- c. Elahi Family acquired 134,750 shares (21 % shareholding) from the previous management, and the management control was exercised with voting power of ICP and HBL. However the process of purchase of shares continued over long period of 29 years, from 1980 to 2009, in a consistent, regular and gradual manner. The Elahi Family's shareholding rose to 24.46 % by Dec 31, 2002.
- d. The sponsor's family never faced any threat to its absolute control over affairs of the Target Company, since its assuming management and control. The mills, because of multifarious reasons, like being a very small spinning unit, located in non-cotton producing region, facing textile sector related problems was never an economically viable proposition and a failed enterprise from the very outset unlike the composite textile unites. The Company had been confronted with huge financial losses during most of its history and even now has six times negative equity as of June 30, 2009. The aforementioned factors prove that the Target Company could have been least attractive for any prospective investor in any sense.
- e. The so called group comprising three directors of the Company namely Mr. Mahboob Elahi, Mahfooz Elahi and Mahmood Elahi; and Mrs. Samina Begum cannot be categorized as "Acquirer" as per the definition of the law, as the group, purchased



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 5 -

134,750 shares out of total 650,000 along with complete management and full control of the Company way back in 1980. As such the group cannot be characterized as purported acquirer of their own Company.

- f. The close examination of the relevant definitions of Acquirer makes it amply clear that the acquirer be it an individual, an organization or a corporate body for all practical purpose is to be an outsider, who is striving to acquire shares by offering attractive share price to allure shareholders of the Target Company to sell their shareholding to him/her. The objective is intended to wrest management and control of the target companies/entities which are selected as Target Company. The Target Company is one whose shares are directly or indirectly acquired or intended to be acquired. Thus it cannot be implied that a Company already managed and controlled for a long period of time i.e. three decades could be a Target Company for the existing management which hold the management and also control the same. The definition of Control states that the control envisages right to appoint majority of directors or to control management or policy decisions etc and if this right exists, then there is no question of getting such right afresh.
- g. The focus of aforesaid definitions is on acquirers who intend to wrest control of companies. For the purpose only such companies/entities are assumed to be the Target Company who perform far below their optimum potential due to various factors and the potential acquirer is confident to turn them around and made significant profit. However, in the present scenario, the group is in full and absolute control since 1980, having the board of directors comprising of Elahi Family, and available with continued support by the financial institutions i.e. ICP and HBL. The Elahi Family, even if, had not purchased a single share, had no threat to their control or management. Infact, their periodic purchase provided a golden opportunity to the small shareholders to en-cash their investment. Secondly, no investor in his right mind could select such a losing concern, viewing the precarious financial position of the Target Company.
- h. The categorization of sponsoring group as "Acquirers" is against the spirit of law as they had acquired management and control of the Company in 1980 that is much before the promulgation of the Takeovers Ordinance. The group had unequivocal and absolute control over the affairs of the Company, and the BOD comprises of family members elected by the group. The purchase of shares over the period of 30 years has been consistent, gradual and quite unrelated to taking control and management. The fact of matter is that as sufficiently evident from definitions analyzed , discussed and examined



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 6 -

in the preceding paragraphs that the provisions of the Takeovers Ordinance i.e. 5 and 6 mentioned in the SCN did not apply to the Company and its sitting group exercising control over the management.

9. In order to provide the opportunity of personal representation to the Acquirers, hearing in the matter was fixed on December 6, 2010. Mr. Javed Panni and Mr. Ayub Qureshi from MJ Panni & Associates (*the "Authorized Representative"*), appeared before me and reiterated the same views as were given in the written response, in addition to the following;

- a. *The section 4, 5 and 6 of the Takeovers Ordinance are to be read together as they provide different threshold for acquisition of share and infact Takeovers Ordinance is focusing the acquisition of Control through acquisition of shares and they cannot be read separately.*
- b. *The Company is sick unit and hence cannot be an attractive proposal for an acquirer.*
- c. *Acquirer is essentially an outsider and the sitting management cannot be termed as acquirer.*

10. I have considered the facts and record of the case, relevant provisions of the Takeovers 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. At the outset it is crucially important to address the foremost issues surrounding the contents of SCN. The contentions raised by the respondents that pertain to the interpretation and focus of the provisions of the Takeovers Ordinance, are considered by me and I am of firm view that the intention of the legislature is that the mandatory provisions of the Takeovers Ordinance are applicable in case of breach of either prescribed thresholds or acquisition of control of the Target Company. The statute cannot be read to interpret that the breach of shareholding threshold is made conditional to acquisition / change in control of the Target Company. Infact the focus of the Takeovers Ordinance is mainly covering both the issues in an exclusive manner i.e. acquisition of shares beyond prescribe threshold; and the acquisition of control, a process which is organized and conducted by the Takeover Ordinance, and is evident from the plain reading of section 5 and 6 of the Takeovers Ordinance.



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 7 -

- b. Having read out the admitted facts and the objective of legal provisions, I now address the first issue that is whether Mr. Mahboob Elahi, has violated section 5 of the Takeovers Ordinance. The relevant portion of Section 5 of the Takeovers Ordinance reads as under:

**5. Additional acquisition of voting shares.** — (1) *No person shall, directly or indirectly, acquire—*

- a) *voting shares, which (taken together with voting shares, if any, held by such person) would entitle such person to more than twenty five per cent voting shares in a listed company; or*
- b) *control of a listed company, unless such person makes a public announcement of offer to acquire voting shares or control of such company in accordance with this Ordinance.*

(2) *Before making announcement under sub-section (1), such person shall make disclosure in the manner specified in section 4.*

- c. A plain reading of the above quoted provisions of law make it abundantly clear that any person who acquires more than 25 percent of shares in a listed company must make a public announcement of offer to acquire voting shares as well as to the Target Company and to the stock exchange on which the voting shares of the Target Company are listed.
- d. Mr. Mahboob Elahi, the director of the Company has substantially increased his shareholding in the Company from 8.92 % to 42.17% during the period June 30, 2007 to June 30, 2009 that is attributed to the acquisition of 255,000 shares as per the information provided by the acquirer, through broker as well as through the purchase of physical shares against cash, between August 8, 2007 to May 29, 2008. In view of the aforesaid discussion and as stated in section 5(1)(a), it is evident that as on May 29, 2008, the acquirer who held 28.54% shareholding, thus crossing the threshold level of 25 % holding of voting shares in the Company which requires the compliance of section 5(1)(a) of the Takeovers Ordinance, has contravened the section 5(1)(a) of the Takeovers Ordinance by not making a public announcement and requisite disclosure.
- e. Now addressing the applicability of section 6 of the Takeovers Ordinance, and for such determination it is to be shown that the respondents (each being a person) did in fact 'cooperate' for purposes of acquiring/consolidation of 78.59 % 'voting shares' in the Target Company in contravention of the said Section 6. This is an admitted position of the respondents who increased their shareholding, that all of them belong



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 8 -

to the Elahi Family, a fact which has been repeatedly presented in the tables included in or Annexure attached to the reply to the SCN. The aforesaid summarized pattern of shareholding clearly shows that "Elahi Group" or "Sponsoring Group" has breached the shareholding threshold defined in the Law. Hence the question whether the respondents acted 'in concert' with each other being a group in the matter of acquisition of the shares in contravention of Section 6 of the Takeovers Ordinance is accordingly established.

- f. The respondents' observation that the increase in the shareholding position has been gradual is not supported by the factual position as it can be observed from the above table presented that out of the total increase of 58.66 % recorded in the Elahi Family's shareholding, merely 3.93 % has been increased in twenty two (22) years (from 1980 to 2002), whereas within a span of last three (3) years, an increase of 45.36 % has been marked.
- g. Secondly, another equally important question that needs to be addressed, being consistently relied by the respondents in their contentions, is to see whether the respondents' claims of retaining absolute and unequivocal control of the Company qualify for the definition of control in true spirit and meaning or its is just a presumptuous control. The acquirers along with sponsors / directors were holding less than 51% shareholding and decisive control has to be exercised due to the support given by the financial institutions (*the HBL and ICP*) and the remaining shareholders. The underlying factors to acquire and retain control as defined in the Takeovers Ordinance includes the right to appoint majority of directors or to control management or policy decisions, exercisable by a person individually or through any person acting in concert, directly or indirectly, whether by virtue of his shareholding, management right, shareholders agreement, voting agreement or otherwise; The respondents' argued that they have been effectively exercising the control over the matters of Company with the support of financial institutions (*HBL & ICP*) having a shareholding of 27.90 @% (*in 1980*), in addition to the respondents shareholding. This support, as stated, is extended to them from the financial institutions, drawn from a notion that financial institutions have never intervened in the functional control of the sponsors over the matters of Company and the appointment of directors on the Board of Directors, as well as no threat of takeover mustered by the general public who held more than 51 % shares till December 31, 2002. However that non-





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 9 -

contractual/un-documented support by the financial institutions could have been withdrawn at any time thus the respondents clearly felt a need to consolidate its shareholding from 24.66 % (as on Dec 31, 2002) to as high as 79.36 % (as on Oct 28, 2009) due to the very fact that the control it has exercising over a period of time was defective and the sponsors were not certain whether how long will it be able to retain the control with below the threshold of substantial shareholding of 51 %. However, in the absence of any demonstrable proof supporting this presumption of continued support by the financial institutions to the sponsors for retaining control over the Company, the control asserted by virtue of electing directors on the Board of Directors may only be tagged as defective control as long as the financial institutions or general public were satisfied/dormant in terms of exercise of their voting rights. Hence the very nature of the control claimed by the respondents, in the absence of holding of substantial shareholding individually or jointly with others and directly or indirectly may only be a defective control and not qualifying to be valid till the time the sponsors actualized it by acquiring the required threshold of substantial shareholding of 51 % of the Company shares.

- h. The definition of Control explained by respondents that the control envisages right to appoint majority of directors or to control management or policy decisions etc and if this right exists, then there is no question of getting such right afresh, is not valid due to the inherent weakness in the nature of control being a defective one as this had been based on weak grounds of less than required threshold of substantial shareholding and assumed support of financial institutions. This is evident from the fact that had the control was assured to be consistently available to the respondents through some solid arrangement with the financial institutions/ others and the Elahi family has not been exposed to any threats of hostile takeover, they would not have been so much keen to show their interest in picking more shares of such Company that is termed as loss making and poor in their own representations.
- i. Now, reverting back to the applicability of section 6 of the Takeovers Ordinance, the very fact that shareholding of the respondents who while acting in concert with each other being members of Elahi family, has increased their shareholding from 26.26 % (2007) to 48.19 % (2008) and then subsequently increased to 78.59 % mainly due to increase in holding of three directors, all of them are forming a group being a family. The aforesaid acquisition of shares required compliance of section 6 of Takeovers



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

Continuation Sheet - 10 -

Ordinance in the form of making of public offer and the disclosure requirement, which were not complied by the respondents. Accordingly, all of the respondents are held liable for contravention of the mandatory provisions of Section 6 of the Takeovers Ordinance.

11. It is imperative here to revert to the main purpose of the Takeovers Ordinance which is to provide for a fair and equitable treatment to all the investors and to provide a transparent and efficient system for substantial acquisition of voting shares and control of listed companies. In this particular case, the Acquirers have failed to comply with any of the provision of the Takeovers Ordinance. For the above stated purpose the statute provide wide ranging powers to the Commission to issue directions and impose penalties on the Acquirers who fail to fulfill the prescribed requirements. However, I am of the firm view that while deciding such cases judicious use of these wide ranging powers must be ensured keeping in view the specific circumstances of each case.

12. I am convinced that the Acquirers have violated the provisions of the Takeovers Ordinance. However, while deciding the case it cannot be ignored that since inception of the Company the effective control of the Target Company has always been vested with the Acquirers and their sponsors. Therefore, taking a lenient view and keeping in view the circumstances of the case, I hereby impose the fines, under Section 26(3) of the Takeovers Ordinance, on the Acquirers for violating the respective provisions of the Takeovers Ordinance, in the following manner:

Sr. No.	Names	Amount of Penalty in Rupees
(i)	Mr. Mahboob Elahi for violation of Section 5 of the Takeovers Ordinance.	Rs.200, 000 (Rupees two hundred thousand).
(ii)	For contravention of Section 6 of the Takeovers Ordinance. 1. Mr. Mahboob Elahi 2. Mr. Mahfooz Elahi 3. Mr. Mahmood Elahi 4. Mrs. Samina Begum	Rs.5, 00,000 (Rupees five hundred thousand) <u>each</u> .

13. The Acquirers are hereby directed to deposit the aforesaid fine in the designated bank account maintained in the name of Securities and Exchange Commission of Pakistan with MCB Bank Limited



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
*Enforcement Department*

Continuation Sheet - 11 -

within thirty days from the date of this Order and furnish receipted challans to the Commission failing which proceedings for recovery of the fine as arrears of land revenue under the Land Revenue Act 1967 will be initiated.

**Tahir Mahmood**  
**Commissioner (CLD)**

Announced:  
December 15, 2010  
ISLAMABAD