

**Securities and Exchange Commission of Pakistan  
Enforcement and Monitoring Division  
7th Floor, NIC Building, Jinnah Avenue,  
Blue Area, Islamabad.**

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*June 17, 2002*

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**Before Rashid Sadiq, Executive Director**

**In the matter of**

**M/S Dadabhoy Cement Industries Limited**

Number and date of show cause notice No.

19(762)CF/ISS/2001

**dated**

January 18, 2002

**Date of hearings**

April 22, 2002

**Present:**

Mr. Abdul Samad

**ORDER**

This is a case where M/S Dadabhoy Cement Industries Limited (hereinafter referred to as "Dadabhoy Cement") has pledged its investment comprising 4,500,000 ordinary shares of Rs. 10 each of M/S Dadabhoy Energy Supply Company Limited (hereinafter called as "Dadabhoy Energy") with M/S National Development Finance Corporation Limited (the "NDFC") as security against financial assistance provided by NDFC to Dadabhoy Energy. This provision of security to Dadabhoy Energy *prima facie* was in violation of the provisions of Clause (d) and Clause (e) of Sub-section (1) of Section 195 of the Companies Ordinance, 1984 (the "Ordinance").

2. The brief facts of this case are that the examination of the audited accounts of Dadabhoy Cement for the year ended June 30, 2001 indicated that Dadabhoy Cement, a company limited by shares and listed on stock exchanges has placed its investments as security with NDFC in order to enable NDFC to provide finances to Dadabhoy Energy (an unlisted company). It was observed from the perusal of the record of both the Companies that the directors of Dadabhoy Cement held shares in Dadabhoy Energy,

which taken together constituted 43.21% of the total paid up capital of Dadabhoy Energy and accordingly not less than 25% voting power of Dadabhoy Energy could be exercised by the aforesaid directors of Dadabhoy Cement at a General Meeting of Dadabhoy Energy. It was also noticed that Mr. Muhammad Hussain Dadabhoy, Ms. Razia Hussain Dadabhoy, Mr. Muhammad Amin Dadabhoy, Ms. Humaira Dadabhoy, Mr. Fazl Karim Dadabhoy, Ms. Yasmeen Dadabhoy and Mr. Naseemuddin were common directors in both the Companies and as such there were reasons to believe that the Chief Executive of Dadabhoy Energy was accustomed to act in accordance with the directions or instructions of the Chief Executive or of any director or directors of Dadabhoy Cement.

3. The Auditors' of Dadabhoy Cement, M/s Sidat Haider Qamar & Co., Chartered Accountants have qualified their report on the aforesaid audited accounts in the following manner:

"the business conducted, investments made and the expenditure incurred during the year were in accordance with the objects of the Company except for the fact that the company has provided security and made advances as referred to in note 14.1 and 19.1 to the accounts."

4. Note no 14.1 being relevant in this case is reproduced hereunder:

"The Company has pledged 4,500,000 ordinary shares of Rs 10 each of Dadabhoy Electric Supply Company Limited (DESCL) with a financial institution as a security against the financial assistance extended by the financial institution to DESCL."

5. The directors' report attached to the accounts of the Company under Section 236 of the Ordinance did not give fullest information of the aforesaid qualification and instead contained only the following explanation:

"as far security is concerned, the shares are pledged since 1996 and same were given to meet the requirement. It is the routine practice in the Banking and Industrial Sector. Since 1996, Auditors had never raised any objection"

6. It was in the above circumstances that a detailed examination of this matter was necessitated to ascertain the extent of violation committed by Dadabhoy Cement and the potential risk to its shareholders.

7. Consequently, a notice dated January 18, 2002 was served upon every director including Chief Executive of the Company to show cause within seven days as to why an action may not be taken as provided under Sub-section (5) of Section 195 of the Ordinance.

8. In response to the Show Cause Notice the Company requested for more time vide its letters dated January 25, 2002 and January 31, 2002. Subsequently, a request was received on behalf of the Company from Mr. Anwar Mansoor Khan, advocate, for further

extension of two weeks to respond to the show cause notice. The request was accordingly allowed.

9. The Company responded the show cause notice through its letter dated February 21, 2002. It was averred in the reply that Dadabhoy Energy was in fact a subsidiary of Dadabhoy Cement. To substantiate the aforesaid averment, it was stated that the Company along with its seven directors, all of which are common with Dadabhoy Energy, owned or held more than 50% of the voting securities and had power to elect and appoint more than 50% of the directors of Dadabhoy Energy. A list of the shareholding was also provided according to which following are the shareholders of Dadabhoy Energy:

Sr. No.	NAME	SHARES HELD	% AGE
1	Mr. Muhammad Hussain Dadabhoy	700	0.002
2	Ms. Razia Hussain Dadabhoy	382,501	1.458
3	Mr. Muhammad Amin Dadabhoy	2,737,825	10.436
4	Ms. Humaira Dadabhoy	2,737,825	10.436
5	Mr. Fazl Karim Dadabhoy	2,737,825	10.436
6	Ms. Yasmeen Dadabhoy	2,737,824	10.436
7	Mr. Naseemuddin	500	0.002
8	M/s Dadabhoy Cement Industries Limited	5,000,000	19.058
	<b>SUB-TOTAL</b>	<b>16,335,000</b>	<b>62.264</b>
9	M/s National Development Finance Corporation	9,900,000	37.736
	<b>TOTAL</b>	<b>26,235,000</b>	<b>100.000</b>

10. The total shareholding of Dadabhoy Cement and its directors in Dadabhoy Energy constituted 62.26% on the basis of the aforesaid factual position. The Company, therefore, contended that Dadabhoy Energy was its subsidiary and clause (c) of Sub-section (2) of Section 195 was applicable. The said provision of the Ordinance is, to the extent relevant, reproduced below:

"Sub-section (1) shall not apply to:-

(c) Any guarantee given or security provided by a holding company in respect of any loan made to its subsidiary"

11. A declaration was also provided to the Commission by all the directors that Dadabhoy Energy is a subsidiary of Dadabhoy Cement. Additionally, a copy of the legal opinion obtained from Mr. Anwar Mansoor Khan, advocate was also placed on record to support the contention of the Company. I am in complete agreement with the said opinion that Section 195 of the Ordinance would not be applicable in view of its clause (c) of Sub-section (2), where, it has been stated that Sub-section (1) shall not apply to any guarantee given or security provided by a lending company, in respect of any loan to its subsidiary. This being the situation, the Company and its directors committed no default

under Section 195 of the Ordinance. In consequence thereof, no action is warranted and proceedings initiated against Dadabhoy Cement under Section 195 are hereby dropped.

12. Now it remains to be seen as to why the auditors have qualified their report on the accounts for the year ended June 30, 2001. In the circumstances, Mr. Abdul Samad was asked to explain as to whether this position was placed before the auditors at the time of audit of the accounts of the Company for the year ended June 30, 2001. He could not give a satisfactory response to this question.

13. As regard to why such objection was not raised in previous audits since 1997, I direct the relevant official in my office to take up this matter with the auditors of Dadabhoy Cement.

14. Before parting with this Order, I would like to record some observation. During the course of proceedings of this case, it has been brought to my notice that the Company has not prima facie followed the mandatory provisions of Section 237 of the Ordinance and the requirements of International Accounting Standard 27. It also appears from the record that majority of the directors of both the Companies were interested in the business of granting of security to NDFC by Dadabhoy Cement, in order to provide financial assistance by NDFC to its subsidiary, Dadabhoy Energy. The relevant officer of the Office is hereby directed to examine this case in the light of relevant provisions of the Ordinance.

**RASHID SADIQ**  
Executive Director (Enforcement & Monitoring)

**Announced:**  
June 17, 2002  
ISLAMABAD