

**Before Dr. Sajid Qureshi, Executive Director (CL)**

**In the matter of**

**M/S Noon Textile Mills Limited**

**Under Section 208 Read With Section 472 Of Companies Ordinance, 1984**

Number and date of notice	No. EMD/233/164/2002-7073-7079 dated December 30, 2005
Date of hearing	March 15, 2006
Present	Mr. M. Azam Khan, Company Secretary, Mr. Fahim Ahmed, Consultant
Date	May 15, 2006

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**ORDER**

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This order shall dispose of the proceedings initiated through Show Cause Notice No.EMD/233/164/2002-7073-7079 dated December 30, 2005 against Noon Textile Mills Limited (the “Company”) under the provisions of Section 208 of the Companies Ordinance, 1984 (the “Ordinance”).

2. The Company was incorporated as a public company limited by shares in the year 1966. The shares of the Company are listed on the Karachi and Lahore Stock Exchanges. The paid up capital of the Company is Rs. 20 million divided into 2 million ordinary shares of Rs. 10 each. The Company is principally engaged in the manufacture and sale of cotton yarn. Its mills are located in Sargodha District. The Company has 549 shareholders comprising individuals, joint stock companies, private limited company, financial institutions etc. and as per its pattern of shareholding annexed to the Directors’ Report in the accounts for the year September 30, 2004, Associates, directors, their spouses and minor children hold 92% of the total shareholding. Board of Directors of the company as per its annual report for the year ended June 30, 2005 comprises the following persons:

**SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN**  
*Enforcement Department*

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1.	Ch. Muhammad Tariq, Chief Executive
2.	Ch. Muhammad Nasir Ali, Director
3.	Ch. Muhammad Aamir, Director
4.	Mrs. Shazia Tariq, Director
5.	Mrs. Mussarat Ayyaz, Director
6.	Mrs. Khadija Begum, Director
7.	Ch. Muhammad Boota, Director

3. Brief facts of the case are that the examination of audited accounts of M/s Noon Textile Mills Limited (the “Company”) for the year ended June 30, 2005 (the “Accounts”) revealed that Rs. 13.757 Million is shown as due from associated undertakings M/s Neelibar Textile (Pvt) Mills Limited and M/s Qadri Textile Mills Limited. Perusal of prior years’ accounts revealed that the amount has been outstanding since long. It was also noted that the amount was separately disclosed for the first time in the accounts for the year 2001 and comparative figures for the year 2000 were shown as restated. While no disclosure about the names of these undertakings was given till the year 2002. The balance outstanding at various points in time was as follows:

Year	2000 (Restated)	2001	2002	2003	2004	2005
Advances to Associates	8,473,852	17,387,837	15,242,277	13,627,155	11,163,154	13,757,839

4. It was also observed from the notes to the accounts that no markup was being charged by the Company on these balances since inception, while the Company’s borrowing cost as per accounts for the year 2005 was 20% p.a. Moreover, the aforesaid investment was made by the Company without obtaining approval of its shareholders.

5. A Show Cause Notice (the “Notice”) was issued to the Chief Executive and directors of the Company on December 30, 2005 as to why a penalty under Section 208 of the Ordinance may not be imposed on them for aforesaid violations. The company replied to the Notice vide its letter dated February 01, 2006. In this context following submissions were made:

- The amounts due from Associated Undertakings do not represent advances within the meanings of investments under section 208 of the Companies Ordinance, 1984. Infact, these represent normal business transactions including trading of goods.
- The borrowing cost of 20% mentioned in the notice, taken from Note No. 11 relates to Short Term Loan of Rs.890,000 from National Industrial Co-operative Finance Corporation Limited (NIFCL). This loan is outstanding since around 1992 and has been utilized by the Company at that time. NIFCL is under liquidation and no claim of the said loan or markup has so far been made. This loan has not been utilized by the company in the current assets in the financial years ended on September 30, 2000 to June 30, 2005. Therefore the Company has no borrowing cost against current assets in these years.
- All steps are being taken to adjust all outstanding balances due from associated undertakings as early as possible.
- Since these advances do not represent investments, it has therefore been requested that proceedings be dropped.

No comments were made as regards the non-disclosure of names of these undertakings till the year 2002.

6. The Company's reply to the issues raised in the Show Cause Notice was not satisfactory. Their representation that the advances were outstanding due to normal business transactions including trading of goods with the associates was also not supported by evidence, as no sales were reported in the Company accounts during the period perused since 1992. Further, the contention that no markup is charged on the grounds that the Company has no borrowing cost other then frozen balance of only one interest bearing liability, payable to a financial institution which is currently under liquidation is also not valid. Interest free advancing to associates clearly violates the provisions of Section 208. In order to give an opportunity to the management of the Company to clarify their position, a hearing was fixed on February 27, 2006, which was adjourned on Company's request and was refixed on March 15, 2006.

7. On the date of hearing Mr. Mr. M. Azam Khan, Company Secretary and Mr. Fahim Ahmed, Consultant appeared on behalf of the Chief Executive and directors of the Company.

8. During the hearing, it was submitted that Noon textile Mills Limited was a sick unit which was acquired by M/s AMI Ginning and Oil Mills (Private) Limited, and it currently holds 80% share holding in the Company. AMI Ginning and Oil Mills (Private) Limited is related to both the associates i.e. *M/s Neelibar Textile Mills (Pvt) Limited* and *M/s Qadri Textile Mills (Pvt) Limited* by virtue of common directorship and major shareholding. The Company has been mainly run by the funds injected by AMI Ginning and Oil Mills (Private) Limited. Out of the funds advanced by the parent the Company has made payments on behalf of other associates. As a result balances receivable from these associates are appearing in the books of the Company. Due to location of these mills it is convenient to route the financing arrangements through the Company. However, subsequent to the year end these balances have been recovered from the associates. As regards failure to obtain approval of the shareholders for the authorization of these advances, request was made for condoning of the default.

9. I have analyzed the facts of the case and observed that no resolution was ever passed by the Company under the provisions of Section 208 of the Ordinance. These advances to associates come under the definition of investment within the meaning of Section 208 because the company has not entered into any sale transactions with its associates. After having considered the arguments of the representative of the directors and Chief Executive of the Company and also having examined documents of the Company on record and produced before me, I am of the opinion that the Company cannot provide loans to its associated company without any return thereon. The provisions of Clause (b) of proviso to Sub-section (1) of Section 208 are mandatory and require that the return on loans shall not be less than the borrowing cost of the Company. The aforesaid provision of law is reproduced hereunder:

***“the return on investment in the form of loan shall not be less than the borrowing cost of the company”.***

The aforesaid provisions of law were brought about through Finance Act, 1995 to prohibit the provision of mark up free loans to associated companies. In my view, the spirit of the aforesaid provisions of law is that the companies must receive return on their investments in associated companies. The reference to borrowing cost has been made to set a benchmark for the determination of rate of return to be received on loans to associated companies. Advancing of loans without any return amounts to passing of undue benefit to the associated company, which is a loss to the lending company and its shareholders. The law, therefore, does not envisage loans without any return to associated companies.

10. In the case in hand, as the Company had no loans, therefore, it was wrongly presumed that the Company could provide loans without any return to its associated company. The provision of loans without any return thereon indicates that the directors have acted in the interest of associated companies. Thus, this is a case where the directors holding interest in more than one company have tried to pass on the benefits to one company at the cost of shareholders of other company. Due to 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 providing advances to associated concerns. I have, however, noted that the Directors of the Company have admitted the default and are in a process of rectifying the default by recovering the balance due from its associated companies. Further, I have also considered that, compared to general public, the directors directly and through the holding company have a higher stake in the Company and Chief Executive and the Directors of the Company have also assured that they would ensure strict compliance to the provisions of the Ordinance in future.

11. In view of the above, I, instead of imposing maximum penalty as prescribed by Sub-section (3) of Section 208 of the Ordinance, I impose a fine of Rs.100,000 on the Chief Executive Ch. Muhammad Tariq. He is directed to deposit the aforesaid fine in the designated bank account maintained in the name of Securities & Exchange Commission of Pakistan in the Habib Bank Limited within 30 days of the date of this order and furnish a receipted challan to the Commission in this regard.

The Chief Executive and Directors are also directed to recover the entire outstanding amount along with markup thereon from the associated undertakings by June 30, 2006 and pass a fresh resolution under Section 208 and SRO 865(I)/2000 dated December 6, 2000 before making any such advances in future. An auditor certificate confirming the total recovery of the amount from the associated undertakings shall be furnished to the Commission by July 2006.

***Dr. Sajid Qureshi***  
Executive Director (CL)