

***Before Tahir Mahmood,
Executive Director (Enforcement)***

In the matter of

Shakarganj Mills Limited

Number and date of show cause notice	EMD/233/363/2002 dated September 15, 2006
Date of hearing	May 24, 2007
Present:	<ol style="list-style-type: none">1. Mr. M. Javed Pannii (MJ Panni & Associates)2. Mr. Asif Ali (General Manager, Finance)3. Mr. Shahid Aziz, representing Mr. Muhammad Asif and Mr. Gulnawaz, Nominee Directors NIT

ORDER

Under Sub-Section (1) of Section 208 read with Section 476 of the Companies Ordinance, 1984

This order will dispose of the proceedings pertaining to contravention of the provisions of Section 208 of the Companies Ordinance, 1984 (hereinafter referred to as “the Ordinance”), which has arisen out of the show cause notice No.EMD/233/363/2002 dated September 15, 2006 served on all the directors including the Chief Executive of Shakarganj Mills Limited (hereinafter referred to as “Shakarganj”).

2. Shakarganj, is a public company limited by shares incorporated on September 20, 1967 having authorized capital of Rs.1,300 million divided into 80 million ordinary shares of Rs.10 each and 50 million preference shares of Rs.10 each and paid up capital of Rs.579.365 million divided into 57.936 million ordinary shares of Rs.10 each as per its audited financial statements for the year ended September 30, 2006. Shakarganj is listed on all the three Stock Exchanges in Pakistan and is engaged in the business of manufacture, purchase and sale of sugar, ethanol, building material and yarn.

3. The facts leading to this case are that the Enforcement Department (hereinafter referred to as “the Department”) of the Securities and Exchange Commission of Pakistan (hereinafter referred to as “the Commission”) issued a show cause notice number EMD/233/363/2002 dated September 15, 2006 under Sub-section (1) of Section 208 read with section 476 of the Ordinance to all the directors including the Chief Executive of the Company for making following investments in the Altern Energy Limited



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(hereinafter referred to as “the Altern”) without prior approval of the shareholders through a special resolution:

- a. An advance of Rs. 25,627,746 was made to Altern; and
 - b. Entered into underwriting agreement amounting to Rs. 46,730,222 with Altern on June 12, 2006.
4. The show cause notice was issued to all the directors of Shakarganj, namely:
- i) Mr. Mazhar Karim, Chairman
 - ii) Mr. Ahsan M. Saleem, Chief Executive
 - iii) Mr. Anjum M. Saleem, Director
 - iv) Mr. Gul Nawaz, Director
 - v) Mr. Khalid Bashir, Director
 - vi) Mr. Muhammad Anwar, Director
 - vii) Mr. Muhammad Arshad, Nominee Director (NIT)
 - viii) Mr. Muhammad Asif, Nominee Director (NIT)
5. Mr. M. Javed Panni of M/s MJ Panni & Associates (hereinafter referred to “the Counsel”) through his letter dated September 29, 2006, stated that he has been appointed as Counsel by five present directors and one ex-director of the Company, names of which are given at serial (i) to (vi) in para 4 above, to submit reply to the Commission on their behalf. He requested for extension up to October 15, 2006 for submitting the reply. Whereas, nominee directors of National Investment Trust (NIT), Mr. Muhammad Asif and Mr. Gulnawaz submitted their reply dated September 28, 2006 to the show cause notice explaining the following:
- i) The BOD of the Company in its 124th meeting held on April 04, 2006 approved equity investment of Rs. 307.500 million in Altern, as associated company, by way of right subscription of 30.75 million ordinary shares of Rs. 10 each.
 - ii) The shareholders of the Company in EOGM held on May 05, 2006 approved the aforesaid equity investment of Rs. 307.500 million in Altern by subscribing the 21.75 million right shares offered to Shakarganj plus additional 9 million shares.



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- iii) The BOD of the Company in its 125th meeting held on May 31, 2006 considered and approved the proposal from management to enhance the Company's stake in Altern by Rs.114.453 million and allowed the management to underwrite upto 7.1 million right shares of Altern.
- iv) The Board in its 126th meeting held on July 31, 2006 was apprised that the Company had been successful in reaching an agreement with Crescent Standard Investment Bank Limited ("CSIBL") to takeover its investment in Altern to set off the amount receivable from CSIBL. As a result of such settlement Shakarganj received Rs. 17,325,000 by purchase of 2,165,625 shares of Altern and Rs. 93,737,532 by taking over advance share deposit money paid by CSIBL to Altern for subscription of right shares offered by Altern to its shareholders. The BOD took note of the already executed settlement agreement by the management with CSIBL and ratified the same.
- v) Our nominee directors in their capacity of institutional representatives and non-executive directors have been playing important role to safeguard the interests of minority shareholders.

6. The Counsel submitted his reply on behalf of the rest of the directors vide his letter dated October 13, 2006 stating the following:

- i) The BOD had agreed to underwrite 7,100,000 shares of Altern. The matter was also placed before the shareholders in EOGM held on June 29, 2006 and was approved.
- ii) The underwriting of shares does not fall under the definition of 'Investment' as explained in Section 208 of the Ordinance.
- iii) Companies underwrite public issues/right issues if authorized by the objects of the companies. Underwriting commitments are not investments and may either lapse or be partially fulfilled to the extent the issue is unsubscribed.
- iv) On the basis of approval of the BOD, the Company had entered into an underwriting agreement with Altern as it had to line up other underwriters for the total issue of right shares.
- v) Shakarganj had wrongly entered into underwriting agreement for 46,730,222 shares as it included 39,630,222 right shares that were to be taken up as a pre-emptive exercise of the right. The actual commitment was for 7,100,000 shares only.



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- vi) The Company had given share subscription deposit of Rs.25,627,746 to Altern against the right shares to be allotted by that company. It is re-iterated that this amount is not given as a loan. It is further added that it is a common corporate practice that large stakeholders give subscription deposit in advance to enable the investee company to meet its cash-flow needs.
- vii) Altern and Shakarganj became associated companies when Mr. Anjum Saleem became director of Shakarganj on May 31, 2005. Earlier, he had become director of Altern on March 03, 2005. Investment of Rs. 19.425 million in Altern was made on February 15, 2005 which was prior to his becoming a director of Shakarganj on the date of investment therefore provisions of Section 208 of the Ordinance were not attracted.
- viii) As per Forms 29 filed with the Company Registration Office, Lahore, Shakarganj and Altern, remained associated companies due to having a common director namely Mr. Anjum till January 08, 2006.

7. In order to provide an opportunity of personal representation, a hearing in the matter was fixed on March 13, 2007. The hearing was attended by the counsel of the directors and Mr. Shahid Aziz representing nominee directors of NIT. The Counsel reiterated the same arguments as were given through written submissions in response to the show cause notice. He also submitted a letter dated March 13, 2007 pointing out that the figure of advance to Altern is Rs. 21,627,746 which was erroneously mentioned in earlier correspondence as Rs. 25,627,746 and this amount was paid as part of right shares subscription on March 31, 2006. The hearing was adjourned as following issues remained unsatisfied which were communicated to Shakarganj vide letter dated March 15, 2007:

- i) Exact amount and the date on which advance payment was made to Altern as the Counsel's letter dated March 13, 2007 states that Company has paid an amount of Rs. 21,627,746 on March 31, 2006 as subscription money to Altern whereas the Shakarganj vide its letter dated July 21, 2006 stated that an amount of Rs. 25,627,746 was deposited against right issue in two installments on January 11, 2006 and January 19, 2006.
- ii) Reasons for providing advance in January 2006, whereas the Altern announced rights issue @ 1450% at par on March 22, 2006.
- iii) Minutes of BOD meeting in respect of approval of aforesaid advance against the rights issue subscribed by the Shakarganj.



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- iv) Whether the advance given to the Altern was adjusted against the rights issue subscribed by the Shakarganj.
- v) Certified copy of related ledger account for the period January 2006 to February 2007.
- vi) Certified copies of bank statements highlighting the transaction.
- vii) Minutes of all BOD meetings of the Shakarganj regarding the right issue/investment in Altern.
- viii) Break-up of 46.73 million shares for which the underwriting agreement was made.
- ix) Dates at which the Altern remained an associated undertaking of the Shakarganj during the calendar year 2005 and 2006 along with the documentary evidences.
- x) Reasons for not-taking the full right of the Company in Altern's right issue despite approval of shareholders was already obtained. Who was allotted the balance of the right issue of the Shakarganj?
- xi) Benefits achieved with regard to benefits explained to the shareholders in the EOGMs conducted in this regard.

Similarly, the nominee directors of NIT were required through a letter dated March 14, 2007 to submit the minutes of the BOD meeting in respect of approval of advance of Rs. 25,627,746 as a deposit against right issue to Altern along with attendance sheet of directors.

8. The Counsel submitted his reply through letter dated April 05, 2007 stating as follows:

- i) The exact dates along with amounts paid to Altern are as below

No	Date	Amount
1	January 09, 2006	14,627,746
2	January 19, 2006	1,000,000
3	February 23, 2006	6,000,000
Total		21,627,746

- ii) The amount of Rs. 21,627,746 was paid to Altern in view of the proposed right issue at the specific request of the Altern's management to meet their immediate liquidity requirements for implementation of the revival plan. This was done to protect the existing investment of the Company and to facilitate Altern for its smooth revival leading to



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acquisition of another profitable IPP, Roush Pakistan Power Limited, which in longer run would greatly benefit the Company and the shareholders.

- iii) The decision to provide the advance was made by the Chief Executive of the Company under the powers delegated to him by the BOD of the Company under the General Power of Attorney.
- iv) The advance was not adjusted against the right issue but was refunded to the Company by Altern after the completion of the right issue on November 28, 2006. This was done because the KSE had advised Altern through its letter dated July 04, 2006 not to issue shares against this advance.
- v) Altern was an associated company due to common directorship during May 31, 2005 to January 08, 2006.
- vi) Keeping in view the current and future market conditions, the Company has re-aligned and restructured its investment portfolio and this was the main reason for reduction of exposure of the Company in Altern.
- vii) The benefits were potential dividend income and capital gain that would increase the shareholder's value.
- viii) As per the minutes of the BOD provided by the Counsel and NIT vide its letter dated March 31, 2007, the issue of investments in Altern was first came to the notice of the board in its meeting held on April 04, 2006.

Copies of bank statements, relevant vouchers, copies of forms 29, general power of attorney given to the Chief Executive, and ledger accounts of the amount of advance granted were also provided.

9. Final hearing in the matter was fixed for May 24, 2007 before the Executive Director, Enforcement, at Head Office, Islamabad. The Counsel was advised to bring the certified copy of bank statements showing the value dates for the period January 1, 2006 to February 9, 2006, certified copy of the cheque amounting to Rs. 14,627,746 issued to Altern and certified copies of signed vouchers of the bank payments made to Altern. The hearing was held as per schedule. The hearing was attended by the Counsel of the Company along with Mr. Asif Ali, General Manager, Finance of Shakarganj and Mr. Shahid Aziz, representative of the nominee directors of NIT. The requisite documents provided by the Counsel reflected that the Shakarganj issued a cheque amounting to Rs. 14,627,746 dated January 03, 2006 which was cleared by the bank on January 05, 2006 as evident from the bank statement. Record



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provided during the course of this proceeding proves that the Shakarganj and Altern were associated companies as on the date of the transaction. The fact has been accepted by the Counsel.

10. I have gone through the facts of the case, record of the Company, relevant provisions of the Ordinance, arguments by the directors and their counsels in the hearings and written submissions given in response to the show cause notice. I feel it appropriate to quote here the relevant provisions of the Ordinance. Sub-section (1) of Section 208 of the Ordinance provides that:

- (1) A company shall not make any investment in any of its associated companies or associated undertakings except under the authority of a special resolution which shall indicate the nature, period and amount of investment and terms and conditions attached thereto.*

Provided that the return on investment in the form of loan shall not be less than the borrowing cost of investing company.

Explanation: *The expression 'investment' shall include loans, advances, equity, by whatever name called, or any amount, which is not in the nature of normal trade credit.*

To sum up, it has been established that both Shakarganj and the Altern were associated companies till January 08, 2006. Shakarganj advanced an amount of Rs. 14,627,746 to Altern when both the Companies were associated companies. The advance was granted without the approval of the shareholders in the general meeting as required under the provisions of Section 208 of the Ordinance. Shakarganj in its correspondence dated July 07, 2006, July 21, 2006, March 13, 2007 & April 05, 2007 submitted varying statements regarding grant of this advance. As per the minutes submitted, it is pertinent to mention here that the Board of Directors of Shakarganj discussed the issue of making investments in Altern in its meeting held on April 04, 2006, whereas it had already advanced the said amount to subscribe the right issue of the associated company. As per the argument presented by the Counsel that the Chief Executive was authorized to make such advance or investment, it can easily be inferred from the aforesaid provision of law that shareholders approval is necessary before grant of such advance / investment and the provisions of law cannot be by passed by entering into an agreement or by giving power of attorney to any director of the Company. It has further been observed from the record obtained from the auditor of Altern that Shakarganj has placed its funds with Crescent Standard Business Management (Pvt.) Limited ("CSBM") and CSBM has balances receivable from Altern amounting to Rs.68,910,240 and accrued



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markup thereon. CSBM transferred receivables of Rs. 10 million from Altern in favor of Shakarganj through an agreement dated May 06, 2006. The fact that the Shakarganj has made an advance of Rs. 25,627,746, including the above mentioned investment of Rs. 10 million, has been confirmed by the Shakarganj's letter dated June 26, 2006 addressed to the auditor of the Altern. However, the shareholders were never informed about the aforesaid investment of Rs. 10 million. As regards, the underwriting of 7.1 million (Rs. 71 million) right shares of Altern, I am convinced that the shareholders of the Company had granted a blanket approval of Rs. 307.500 million in their meeting held on May 05, 2006 for investment in Altern, whereas the Company made an underwriting agreement with Altern on June 12, 2006, and in the subsequent meeting of the members dated June 29, 2006, again there was a resolutions passed of right subscription of 7.1 million (Rs. 71 million) shares.

11. From the above discussion, facts of the case and arguments put forward by the Counsel, I am of a considered view that the provisions of Section 208 of the Ordinance have been violated and directors are liable for the penalties as defined in Sub-section (3) of the aforesaid provisions of the Ordinance. Sub-section (3) of Section 208 of the Ordinance provides that if default is made in complying with the requirements of this section, every director of the company who is knowingly and willfully in default shall be liable to fine which may extend to one million rupees and in addition the directors shall jointly and severally reimburse to the company any loss sustained by it in this respect. I have observed from the correspondence took place with the Company that the directors tried to conceal the correct information from the shareholders and the Commission with regards to advance given to Altern at number of occasions which is against the good governance practices. I have a strong belief that the shareholders and the regulatory bodies should be provided correct and timely information with all fairness. The directors of the Company therefore deserve no sympathy on this account however keeping in view the track record of Shakarganj I instead of imposing maximum fine impose an aggregate penalty of Rs. 600,000 (Six hundred thousand rupees only) i.e. Rs. 100,000 (one hundred thousand rupees only) each on i) Mr. Mazhar Karim ii) Mr. Ahsan M. Saleem iii) Mr. Anjum M. Saleem iv) Mr. Muhammad Anwar v) Mr. Khalid Bashir and vi) Mr. Muhammad Arshad who involved themselves in such an illegitimate transaction. The above named directors of Shakarganj are hereby directed to deposit the aforesaid fine in the designated bank account maintained in the name of the Commission with Habib Bank Limited within thirty days from the receipt of this order and furnish receipted bank vouchers to the Commission. In case of non-deposit of the penalty, proceedings for recovery of the fines as an arrear of land revenue will be



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initiated. It may also be noted that the said penalties are imposed on the directors in their personal capacity; therefore, they are required to pay the said amount from their personal resources.

Mr. Muhammad Asif and Mr. Gulnawaz, nominee directors of NIT are hereby strictly warned to be vigilant in playing their role as independent non-executive director as I expect that the independent directors are the main element of transparency in the decisions of the Board of Directors of a Company.

12. Further, in terms of the provisions of Section 473 of the Ordinance I hereby direct the directors of the Company to submit a report to the Commission covering the following aspects of the above case within thirty days of this order:

- i) Reasons why varying statements were submitted to the Commission regarding payment of advance for right shares subscription;
- ii) Exact detail of the amount paid to the Altern as advance along with the value dates; and
- iii) How much amount was settled with the associated companies for subscription of right shares.

Tahir Mahmood
Executive Director

Announced
June 14, 2007
Islamabad