



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Enforcement Department

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

**In the matter of**

**Zeal Pak Cement Factory Limited**

**Under Section 208 read with Section 476 of the Companies Ordinance, 1984**

No. and date of Notice	EMD/Co.233/388/2002 dated July 18, 2007
Date of hearing	November 29, 2007
Present	Mr. Shafiq Ahmad, Legal Counsel

***Order***

This order shall dispose of the proceedings initiated against all the directors including the Chief Executive of Zeal Pak Cement Factory Limited (hereinafter referred to as the “Company”) vide show cause notice dated July 18, 2007 under the provisions of Section 208 read with Section 476 of the Companies Ordinance, 1984 (hereinafter referred to as the “Ordinance”).

2. The Company was established as a public limited company on May 9, 1957 and is currently listed on Karachi Stock Exchange. Its authorized and paid-up capital, as per annual audited accounts for the year ended June 30, 2006 (hereinafter referred to as the “annual accounts”), was Rs.1,800 million and Rs.1,700 million respectively. The principal activity of the Company is manufacturing and sale of cement and clinker. The Company has 5,008 shareholders comprising individuals, financial institutions, joint stock companies etc., as per the pattern of shareholding annexed to the Directors’ Report on the annual accounts.

3. Brief facts leading to this case are given hereunder:

- i) The examination of annual accounts for the year ended June 30, 2004 (hereinafter called as “first annual accounts”) of the Company revealed that during the year 38,853 metric tons of clinker was sold to Pakistan Slag Cement Industries Limited (hereinafter called as “PSCIL”), an associate company, for a total consideration of Rs.110.490 million.



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- ii) This sale was made at a loss of Rs.432 per metric ton resulting into loss of Rs.16.784 million on this transaction;
- iii) The examination of annual accounts for the year ended June 30, 2005 (the “second annual accounts”) revealed that 24,477 metric tons of clinker was sold to PSCIL for total of Rs.45.884 million;
- iv) This sale was again made at a loss of Rs.105 per metric ton resulting into loss of Rs.2.570 million on this transaction;
- v) The examination of annual accounts for the year ended June 30, 2006 (the “third annual accounts”) revealed that an amount of Rs.198.898 million was receivable from PSCIL;
- vi) It appeared that aforementioned transactions of sale of clinker to PSCIL were not carried out at arm’ length and also does not fall within the ambit of normal trade credit and undue benefit was given to PSCIL;
- vii) The Company was advised vide letter dated March 01, 2007 to provide ledger accounts of PSCIL maintained in the books of the Company from July 01, 2005 to June 30, 2006;
- viii) The Company submitted requisite ledger accounts vide letter dated July 05, 2007 after several reminders. The ledger accounts of PSCIL were examined and it was observed that an amount of Rs.412.041 million is receivable from PSCIL as per following details:

**(Receivable from PSCIL)**

<b>Account Number</b>	<b>Amount (Rs.)</b>
181200008	44,251,072.00
192300003	360,802,796.00
180100002	6,987,065.00
<b>Total</b>	<b>412,040,933.00</b>

4. The facts narrated in the preceding paras indicated that the Company *prima facie* has contravened the provisions of Section 208 of the Ordinance by entering into transactions with its associated company i.e. PSCIL which cannot be termed as normal trade credit as these transactions were carried out at huge losses and also an amount of Rs.412.041 million is receivable from PSCIL since June 30, 2005. The Company had not charged any mark-up on the outstanding amount. It was, therefore, considered



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necessary to probe the details of these transactions, therefore, proceedings through a show cause notice (hereinafter referred to as the “SCN”) dated July 18, 2007 under the provisions of Section 208 read with Section 476 of the Ordinance were initiated against all the directors of the Company namely:

- i. Mr. Mazhar Ali Jatoi, Chairman;
- ii. Mr. M.A. Jameel, Chief Executive;
- iii. Mr. Shahzad Ali Jatoi, Director;
- iv. Mr. Nawab Ali Jatoi, Director;
- v. Mr. Muhammad Moosa, Director;
- vi. Mr. Mushtaq Ali Shah Bokhari, Director; and
- vii. Mr. Nawab Ahmed Khanzada, Director.

5. The SCN was responded by the Chief Executive of the Company vide his letter dated August 21, 2007 and made the following submissions:

- (a) The Company uses wet process instead of dry process for production of cement thus its fuel cost is almost double than the fuel cost of dry process. The Company had no alternative but to sell the cement on the than prevailing market price, which was lower than its cost of production. To reduce financial constraints and inventory cost, management decided the sell surplus clinker. Consequently, efforts were made to sell clinker at a reasonable rate to various cement manufacturers but all of them have their own clinker production facility so the only purchaser was PSCIL which is a cement grinding plant without having the facility for clinker production. Being the only purchaser of clinker, PSCIL was in a better position to negotiate the purchase price suitable to it;
- (b) With regard to applicability of Section 208 of the Ordinance, the Company has submitted that Zeal Pak and PSCIL are not associated companies and they do not meet any of the criteria specified in Section 2(2)(i) of the Ordinance as; (i) none of the directors of the Company is a director of PSCIL and there exists no common directorship between these two companies; (ii) none of the directors of the Company, either directly or indirectly, hold 20% voting shares in PSCIL. Similarly none of the directors of PSCIL, either directly or indirectly, hold 20% voting shares in the Company;



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- (c) The net amount receivable from PSCIL is actually Rs.126.329 million instead of Rs.412.041 million as the Company also owes Rs.285.711 million to PSCIL as on June 30, 2006. Further, the Company has not been classified the aforesaid receivable as 'receivable from associated company' but has been classified differently.

6. In order to provide an opportunity of personal hearing the case, after two adjournments on the request of the Company, was fixed on November 29, 2007. Mr. Shafiq Ahmad, advocate of Nuruddin Sarki & Company appeared as legal counsel on behalf of all the directors (hereinafter called as the "Counsel") to argue the case. During the course of hearing, the Counsel reiterated the same facts as were narrated in response to the SCN. In addition, he submitted that the amount receivable from PSCIL cannot be termed as 'investment' in terms of Section 208 of the Ordinance, as this was a transaction carried out in the normal course of business and according to the terms and conditions already settled between the Company and PSCIL. He also referred a case law in support of his argument explaining the term investment in associated companies. Text of the case law titled [1993 MLD 42 (a)] Central Cotton Mills Limited vs. Naveed Textile Mills Limited was provided vide letter dated December 5, 2007.

7. I feel it appropriate to quote here the relevant provisions of the Ordinance. Sub-section (1) of Section 208 of the Ordinance provides that:

*A company shall not make any investment in any of its associated companies or associates 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.*

Sub-section (2) of Section 2 of the Ordinance defines the associated companies as follows:

*"associated companies" and "associated undertakings" mean any two or more companies or undertakings, or a company and an undertaking, interconnected with each other in the following manner, namely: —*



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- (i) *if a person who is the owner or a partner or director of a company or undertaking, or who, directly or indirectly, holds or controls shares carrying not less than twenty per cent of the voting power in such company or undertaking, is also the owner or partner or director of another company or undertaking, or directly or indirectly, holds or controls shares carrying not less than twenty per cent of the voting power in that company or undertaking; or*
- (ii) *if the companies or undertakings are under common management or control or one is the subsidiary of another; or*
- (iii) *if the undertaking is a modaraba managed by the company;*

*and a person who is the owner of or a partner or director in a company or undertaking or, who so holds or controls shares carrying not less than ten per cent of the voting power in a company or undertaking, shall be deemed to be an "associated person" of every such other person and of the person who is the owner of or a partner or director in such other company or undertaking, or who so holds or controls such shares in such other company or undertaking;*

8. I have analyzed the written submissions made by the Company, verbal submissions of the Counsel and relevant provisions of the law. My observations in the case are hereunder:

- a. The Company never provided evidence such as quotations, tenders, advertisements which could indicate that the Company has made efforts to sell clinker to other cement manufacturers and the Company was forced to sell the clinker to PSCIL at a loss and it has not given an undue advantage to its associated company;
- b. With regard to applicability of Section 2(2)(i) the Ordinance, it is pertinent to mention here that Sardar Mohammad Ashraf D. Baluch & Co. (Pvt.) Limited (hereinafter called as "SMADBL") holds 143,726,282 (84.54%) shares in the Company and the CEO of this company, Mr. Sikandar Ali Jatoi holds 3,200,000 (50%) shares in PSCIL. Further, the CEO and directors of PSCIL hold only 500 shares each in PSCIL which also gives an indication that they are merely working directors elected through proxies and PSCIL is in fact controlled by SMADBL through its CEO. Therefore, it is viewed that the Company and PSCIL are associated undertakings being under common control.



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- c. Both, the Company and PSCIL have classified each other as associated companies in their annual accounts;
- d. The Company has submitted that the actual net amount receivable from PSCIL, after adjusting Rs.285.711 payable to PSCIL, is Rs.126.329 as on June 30, 2006 whereas the annual accounts for the year ended June 30, 2006 reflect an amount of Rs.198.898 million as receivable from PSCIL;
- e. No movement in receivable balance of Rs.412.041 has been observed in the ledger accounts for the year ended June 30, 2006 provided by the Company, indicating that the Company has not received any money from PSCIL against sale of clinker and cement in this year. However, payable balance of Rs.285.711 (payable to PSCIL) has shown a movement (payment) of Rs.24.024 million to PSCIL by the Company during the year ended on June 30, 2006. Further, the Company has not classified 'receivable from PSCIL' differently as the same has been classified as 'due from associated undertaking' as per note 16.1 of the annual accounts for the year ended June 30, 2006;
- f. The proviso of Sub-Section (1) of Section 208 of the Ordinance is very clear. It explains that expression investment shall include loans, advances, equity, by whatever name called, or any amount which is not in the nature of normal trade credit. The Company has given an open ended credit to PSCIL with no time frame for recovery as has been observed from the ledger accounts for the year ended on June 30, 2006. Such transaction cannot be termed as normal trade credit, hence, falls within the explanation of investment as given in Sub-section (1) of Section 208 of the Ordinance. The normal trade credit is a credit which the Company extends to its customers against the sale of goods in the normal course of business and most of times it is based on industry norms and such credit extended should be a current liability for the receiver. An open ended credit without specific purpose cannot be termed as normal trade credit, hence, falls in the definition of investment in terms of Section 208 of the Ordinance;
- g. The case law provided by the Counsel is self explanatory. In first para, it explains that a company would not make any investment in any of its associated companies or associated undertakings except under the authority of a resolution indicating nature and amount of investment and conditions attached thereto. The



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terms investment has been explained in the proviso of Sub-section (1) of Section 208 of the Ordinance as 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. In view of this explanation, it can be concluded that the Company has not entered into normal trade credit transaction with PSCIL - an associated company. The second para of the case law has no relevance to the case under review which pertains to investment in associated company through extending abnormal trade credit whereas the case law explains that disinvestment is outside the scope of Section 208 of the Ordinance, as the case under review is not a disinvestment, so it has no relevance to court case quoted by the Counsel.

9. From the above discussion, submissions of the Company and argument put forward by the Counsel, I am of the 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 instead of imposing a maximum penalty of one million rupees on each director impose a fine aggregating to Rs.800,000 (Rupees eight hundred thousand only) which will be paid by the Chief Executive and directors in the following manner:

<b>Name</b>	<b>(Rs.)</b>
Mr. Mazhar Ali Jatoi, Chairman	100,000
Mr. M.A. Jameel, CEO	200,000
Mr. Shahzad Ali Jatoi, Director	100,000
Mr. Nawab Ali Jatoi, Director	100,000
Mr. Muhammad Moosa, Director	100,000
Mr. Mushtaq Ali Shah Bokhari, Director	100,000
Mr. Nawab Ahmed Khanzada, Director	100,000



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The above named CEO and directors of the Company 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 under the Land Revenue Act, 1967 will be initiated for recovery of the fines as an arrear of land revenue. It may also be noted that the said penalties are imposed on the CEO and directors in their personal capacity; therefore, they are required to pay the said amount from their personal resources.

11. Before departing with the order, I hereby invoke provisions of Section 473 of the Ordinance and direct Chief Executive and all the directors of the Company to get the outstanding balance of receivable from PSCIL verified by the statutory auditors of the Company and submit auditor certificate to the Commission within thirty days from the date of this order. The CEO and directors are further directed to recover the aforesaid amount as verified by the statutory auditor till June 30, 2008 and submit evidence of receipt of funds from PSCIL to the Commission within 7 days from the date of full recovery, failing to fulfill aforesaid directions the Commission shall be constrained to initiate proceedings under Section 495 of the Ordinance.

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**Tahir Mahmood**  
Executive Director (Enf.)

**Announced**  
**December 12, 2007**  
**Islamabad.**