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**SECURITIES & EXCHANGE COMMISSION OF PAKISTAN
APPELLATE BENCH REGISTRY**

BEFORE APPELLATE BENCH NO. II

In the matter of

Appeal No. 02 of 2010

1. Muhammad Omar Amin Bawany
2. Ahmed Ali Muhammad Amin
3. Muhammad Amin Ahmed Bawany
4. Iqbal A Rehman
5. Abdul Wahid A Ghaffar
6. A. Wahid Jalianawala

All directors of

Farhan Sugar Mills Limited

..... Appellants

VERSUS

Executive Director (Enforcement)

Securities and Exchange Commission of Pakistan

..... Respondent

Date of hearing

02-04-10



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN
APPELLATE BENCH REGISTRY

ORDER

Present:

For the Appellant:

Khalid Mehmood Siddiqui

Advocate

For the Respondent Department:

Amina Aziz

Joint Director

1. This order shall dispose of appeal No. 02 of 2010 filed under section 33 of the Securities and Exchange Commission of Pakistan (the "Commission") Act, 1997 against the order dated 26-11-09 (the "Impugned Order") passed by the Respondent.
2. Joint Venture Agreement ("JVA") was entered between M/s Rogasa Holdings with Mehran Sugar Mills Limited and Mirpurkhas Sugar Mills Limited for setting up a joint venture company in the name of Unicol Limited ("Unicol"). Farhan Sugar Mills Limited (the "Company") purchased the entire shareholding of M/s Rogasa Holding and stepped in as JVA partner in its place.
3. On examination of annual accounts of the Company for the year ended 30-09-08, it transpired that the Company had made sales of Rs. 213.178 million to Unicol. The Commission called information and documents regarding sales of molasses and baggasse (the "by-products") to Unicol by the



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Company. The documents revealed that the Company had been selling the by-products to Unicol on credit basis against the industry norms. The by-products have ready cash market and are sold either on advance or cash basis. The credit period with respect to by-product sales to Unicol by the Company was 103.5 days calculated on average of opening and closing monthly balances outstanding against these sales.

4. Show cause notice dated 15-07-09 ("SCN") was issued under section 196 and 208 read with section 476 of the Companies Ordinance, 1984 (the "Ordinance") to the directors of the Company. The Company filed reply to the SCN and hearing was held. The Respondent, dissatisfied with the reply to the SCN and the arguments made before him, passed the Impugned Order and imposed a penalty of Rs. 250,000 each on the Chairman, Vice-Chairman and Chief Executive Officer; Rs. 150,000 each on the directors, whereas, the nominee directors were reprimanded.
5. The Appellants have preferred appeal against the Impugned Order. The Appellants' counsel argued that:
 - a) The Company entered into an agreement with Unicol for sale of the bye-products with approval of its Board of Directors ("BoD"). The credit period was not specified in the agreement, however, sale of the bye-products to Unicol was made by the Company on average credit period of 95 days.
 - b) The amount received from Unicol cannot be treated as investment in terms of section 208 of the Ordinance. Reliance was placed on *Societe Generale De Surveillance S. A vs. Pakistan, cited at 2002 SCMR 1694*. It was argued that 'sale' cannot be treated as 'investment' as such the



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'credit sale' does not come under the ambit of section 208 of the Ordinance. Section 208(1) of the Ordinance relates to the transfer of money only and does not encompass 'credit sales'. It was further argued that transfer of money is the '*sin qua non*' to attract the application of section 208(1) of the Ordinance.

- c) The Appellants did not take any personal benefit from the proceeds of the sales to Unicol. Unicol earned higher profits as result of the sale by the Company and the Company earned additional dividend which was distributed amongst the share holders of the Company. It was further argued that the Commission allowed other JVA partners with similar credit period to operate, whereas, the Appellants have been discriminated by imposition of penalty.
6. The departmental representative stated that the Company made an investment in its associated company namely Unicol, by allowing abnormal credit terms in violation of section 208(1) of the Ordinance. The Appellants ought to have passed a special resolution before making an investment in Unicol. It was argued that the market practice for sale of the bye-products is that it is either sold in advance or credit period of up to 10 days, whereas, the Appellants allowed credit period averaging 103.5 days to Unicol. On the issue of discrimination it was argued that the other JVA partners, if found involved in violation of the Ordinance, shall also be proceeded against in accordance with law.
7. We have heard the parties. Section 208(1) of the Ordinance is reproduced for ease of reference:



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208. Investments in Associated companies and undertaking. - (1) *Subject to sub-section (2A) 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.*

Emphasis added

In terms of section 208(1) of the Ordinance, a company is required to pass a special resolution before making investment in an associated company. In the instant case no such resolution was passed by the Company. The term 'investment' has been defined in explanation to section 208(1) of the Ordinance. The term 'investment' does not necessarily involve transfer of money as suggested by the Appellants' counsel. We have gone through the case *Societe Generale De Surveillance S. A vs. Pakistan*, cited at 2002 SCMR 1694 presented by the Appellants' counsel in support of his contention. The case law is not relevant as it defines 'investment' in the context of 'bilateral investment treaty'. For the purposes of section 208 of the Ordinance, the term 'investment' includes 'loans', 'advances', 'equity' by whatever named called, or any amount, which is not in the nature of normal trade credit. In the instant case, the trade credit granted by the Company to Unicol cannot be termed as normal trade credit. In the Impugned Order, the Respondent has set out the by-product average trade credit in the industry, which has been reproduced for ease of reference:



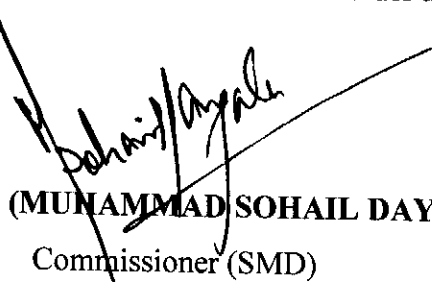
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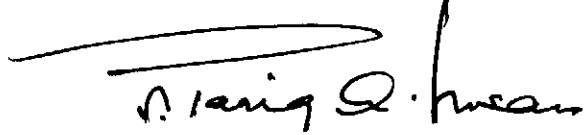
Company	Shahtaj Sugar	Al-Noor Sugar	Thal Industries	Tandlianwala Sugar	Sanghar Sugar
Terms of sale of Molasses	Advance Payment	Advance Payment/ Credit period of up to 10 days	Advance Payment	Advance Payment	Advance Payment

The Appellant has neither challenged nor denied the industry norm referred to in the Impugned Order. We therefore accept the position of the normal practice prevailing in the trade as referred to in the table above.

In the instant case, the Company admitted that it had given a credit period of up to 95 days to Unicol. In our view, the abnormal trade credit given to Unicol caused loss to the Company as it could have sold the bye-product in open market on advance basis. The Company failed to pass a special resolution in terms of section 208(1) of the Ordinance before making 'investment' in its associated company and the penalty was rightly imposed.

In view of the above, we see no reason to interfere with the Impugned Order. The appeal is dismissed with no order as to cost.


(MUNAMMAD SOHAIL DAYALA)
Commissioner (SMD)


(S.TARIQ ASAF HUSAIN)
Commissioner (LD)

Announced on: 30.04.10