



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

Adjudication Department- I

Adjudication Division

ORDER	
Name of Company:	Zahur Cotton Mills Limited
Show Cause Notice No. & Date:	No. CSD/ARN/178/2015-402 dated September 05, 2024
Respondents:	(i) Mr. Imran Zaid, Chairman; (ii) Ms. Javeria Malik, Director; (iii) Ms. Sana Malik, Director; (iv) Mr. Muhammad Faheem Qureshi, Director; (v) Ms. Azra Perveen, Director; (vi) Mr. Muhammad Sheraz, Director; (vii) Syed Jawad Ali, Chief Executive; and (viii) Zahur Cotton Mills Limited
Date of Hearing:	November 07, 2024
Case represented by:	(i) Mr. Nadeem Mehmood Butt, CEO-FAPL; and (ii) Mr. Wasif Ali Rana, Director-FAPL
Provision of law involved:	Section 166(1), 169 & 512 of the Companies Act, 2017 and Regulation 6(1), 27 and 36(1) and 37 of the Listed Companies (Code of Corporate Governance) Regulations, 2019
Date of Order:	March 24, 2025

This Order shall dispose of the proceedings initiated by the Securities and Exchange Commission of Pakistan (the “**Commission**”) through the Show Cause Notice No. CSD/ARN/178/2015-402 dated September 05, 2024 (“**SCN**”) against Zahur Cotton Mills Limited (the “**Company**”) and its Directors/ CEO, hereinafter collectively referred to as the “**Respondents**”, issued under Section 166(1), 169 & 512 of the Companies Act, 2017 (the “**Act**”), Regulation 6(1), 27, 36(1) and 37 of the Listed Companies (Code of Corporate Governance) Regulations, 2019 (the “**CCG Regulations**”).

2. The brief facts of the case are that the Company was required to exercise its due diligence and select at least two or one-third of board members (whichever is higher) as independent directors on its board from the databank maintained by any institute, body or association, as may be notified by the Commission, in terms of Regulation 4(7) of the Companies (Manner and Selection of Independent Directors) Regulations, 2018 (the “**Directors’ Regulations**”), Regulation 6(1) of the CCG Regulations and Section 166(1) of the Act. A review of the annual audited financial statements of the Company for the year ended June 30, 2023 (the “**Accounts**”) revealed that the two independent directors on Board of Directors (“**BoD**”) of the Company namely Mr. Imran Zaid and Ms. Javeria Malik were not registered with the databank of Pakistan Institute of Corporate Governance (“**PICG**”).

3. Regulation 27 of the CCG Regulations mandates constitution of audit committee by the board of a listed company, and entails mandatory requirements concerning functioning of the said committee. In this respect, the auditor of the Company in his review report on the Statement of Compliance with the CCG Regulations *inter-alia* highlighted the following non-compliances of the Company with regulation 27 thereof:

Regulation No.	Non-Compliances
27	1. One of the members of audit committee is not financially literate as prescribed. 2. The audit committee did not hold required number of meetings. 3. The audit committee did not meet the external auditor and head of internal audit. 4. The term of reference of audit committee is not properly prepared and maintained.

4. In view of the foregoing, the Commission vide letter dated March 20, 2024 sought clarification from the Company and the auditor in the matter. The Company vide letter dated April 01, 2024 *inter-alia* submitted that the directors have been selected from PICG databank. On the other hand, the auditor vide email dated March 20,

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2024 *inter-alia* stated that as per regulation 6 of the CCG Regulations and Section 166 of the Act, a listed company is required to select independent directors from the specified database – since this compliance was not fulfilled, the observation was drawn up. The auditor pinpointed that as per regulation 27(1)(iii) of the CCG Regulations, a listed company is required to appoint at least one financially literate member on the Audit Committee of board; however, none of the members of audit committee were observed to be financially literate. The auditor further submitted that only two meetings of the audit committee were held during the financial year 2022-23 i.e. on October 05, 2022 and October 10, 2022; contrary to the requirements of regulation 27(2)(i) of the CCG Regulations to hold quarterly meetings.

5. As per the available record, the names of the aforesaid independent directors were included in the PICG databank after the observation was communicated to the Company by the Commission vide letter dated March 20, 2024, which reflects that the names of the said independent directors were not registered with the databank of PICG at the time of their appointment in the board meeting held on April 10, 2023.

6. Moreover, regulation 36(1) of the CCG Regulations obligates a listed company to publish and circulate a statement along with its annual report to set out its status of compliance with CCG Regulations. One of the requirements of such statement prescribed under the aforesaid regulation 36 is to confirm that the listed company has *inter-alia* complied with regulation 27 of the CCG Regulations. However, review of the Statement of Compliance published by the Company *prima-facie* revealed that the Company did not disclose/ confirm the same.

7. The aforesaid indicated that the Respondents, *prima facie*, contravened the provisions sub-section (1) of Section 166 of the Act, regulations 6, 27(1), 27(2) and 36(1) of the CCG Regulations and regulation 4(7) of the Directors' Regulations, which attracts penal action as provided under Section 169 and 512(2) of the Act read with regulation 37 of the CCG Regulations. For ease of reference, the same are reproduced hereunder:

"Section 166(1) of the Act:

166. Manner of selection of independent directors and maintenance of databank of independent directors.- (1) An independent director to be appointed under any law, rules, regulations or code, shall be selected from a data bank containing names, addresses and qualifications of persons who are eligible and willing to act as independent directors, maintained by any institute, body or association, as may be notified by the Commission, having expertise in creation and maintenance of such data bank and post on their website for the use by the company making the appointment of such directors:

Provided that responsibility of exercising due diligence before selecting a person from the data bank referred to above, as an independent director shall lie with the company or Government, as the case may be, making such appointment.

Section 169 of the Act:

169. Penalties.- Whoever contravenes or fails to comply with any of the provisions of sections 154 to 168 or is a party to the contravention of the said provisions shall be liable to a penalty of level 2 on the standard scale and may also be debarred by the authority which imposes the penalty from becoming or continuing a director of the company for a period not exceeding three years.

Section 512 (2) of the Act:

512. Power to make regulations.- (2) Any regulation made under sub-section (1) may provide that a contravention thereof shall be punishable with a penalty which may extend to five million rupees and, where the contravention is a continuing one, with a further penalty which may extend to one hundred thousand rupees for every day after the first during which such contravention continues.

Regulation 4(7) of the Directors' Regulations:

Every company shall be responsible for exercising its due diligence before selecting an individual from the data bank or appointment as independent director. In particular, every company shall require such individual to submit an undertaking on a non-judicial stamp paper that he/ she meets the requirements of sub-regulation (1) of this regulation along with relevant supporting information supporting the same.

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Sub-regulation (1) regulation 6 of CCG Regulations:

6. Independent Director. - (1) It is mandatory that each listed company shall have at least two or one third members of the Board, whichever is higher, as independent directors.

Regulation 27 of CCG Regulations:

27. Audit Committee.- (1) It is mandatory that the audit committee shall be constituted by the Board keeping in view the following requirements,-

- (i) the Board shall establish an audit committee of at least three members comprising of non-executive directors and at least one independent director;
- (ii) chairman of the committee shall be an independent director, who shall not be the chairman of the Board;
- (iii) the Board shall satisfy itself that at least one member of the audit committee shall be "financially literate";.

Explanation:- for the purposes of this clause the expression, "financial literate" means a person who,-

- (a) is a member of a recognized body of professional accountants; or
- (b) has a post graduate degree in finance from a university or equivalent institution, either in Pakistan or abroad, recognized by the Higher Education Commission of Pakistan; or
- (c) has at least ten (10) years of experience as audit committee member; or
- (d) at least twenty (20) years of senior management experience in overseeing of financial, audit related matters.

- (iv) the Audit Committee of a company shall appoint a secretary of the committee who shall either be the company secretary or head of internal audit.

(2) It is mandatory that meetings of the audit committee shall be held as per the following requirements,-

- (i) the audit committee of a company shall meet at least once every quarter of the financial year. These meetings shall be held prior to the approval of interim results of the company by its Board and after completion of external audit;
- (ii) a meeting of the audit committee shall also be held, if requested by the external auditors, head of internal audit or by chairman of the audit committee;

Sub-regulation (1) regulation 36 of CCG Regulations:

36. Compliance Statement and Auditor Review.- (1) It is mandatory that the company shall publish and circulate a statement, as given under Annexure A to these Regulations, along with their annual reports to set out the status of their compliance with the requirements of these Regulations and the said statement shall be specific and supported by necessary explanations.

Regulation 37 of CCG Regulations:

37. Penalty.- Whoever fails or refused to comply with, or contravenes regulation 3, 6, 7, 8, 27, 32, 33 and 36 of these Regulations, shall be punishable with penalty as provided under sub-section (2) of section 512 of the Act.

8. Taking cognizance of the aforementioned non-compliances, SCN was served upon the Respondents, requiring them to show the cause as to why penal action as provided under Section 169 of the Act, and regulation 37 of the Regulations read with sub-section (2) of Section 512 of the Act may not be taken against them for the aforementioned contravention of the law. However, the Respondents did not submit any reply in response to SCN.

9. In order to meet the ends of justice and provide an opportunity of being heard to the Respondents, hearing in the matter was fixed for November 07, 2024, which was attended by Mr. Nadeem Mehmood Butt, CEO-Frontier Advisory (Private) Limited ("FAPL") and Mr. Wasif Ali Rana, Director-FAPL on behalf of the

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Respondents as their Authorized Representatives. The Representatives *inter-alia* submitted that both the independent directors were not registered with PICG at the time of their appointment; however, their names are now registered in the said databank; while one of the members of audit committee namely Mr. Faheem meets the eligibility criteria of being financially literate. The Authorized Representatives further submitted that the meeting of audit committee for the third quarter could not be held due to non-availability of the half yearly reviewed financial statement.

10. Subsequently, the CEO of the Company vide letter dated November 11, 2024 *inter-alia* reiterated the aforesaid submissions of the Authorized Representatives and further submitted that one of members of audit committee namely Mr. Muhammad Faheem Qureshi holds a bachelor of commerce degree and a master degree in faculty of Arts and has over 40 years of senior management experience – demonstrating that Mr. Faheem holds appropriate qualification and experience to be a member of audit committee as per criteria stipulated under regulation 27 of the Regulations. The Representatives further informed that the Terms of Reference of audit committee are prepared in compliance with the regulatory requirements and the same were duly made available to the statutory auditors.

11. I have gone through the provisions relevant to the instant proceedings and considered the facts of the case, written and verbal submissions of the Respondents. I have also perused Section 169 of the Act and regulation 37 of the Regulations read with sub-section (2) of Section 512 of the Act, which stipulate penal provisions for contravention of the afore-referred provisions of law. I have noted that sub-section (1) of Section 166 of the Act and regulation 4(7) of the Directors' Regulations requires the companies to select and appoint an independent director from the databank maintained by the PICG once the company has exercised due diligence prior to making such selection. Registration in the databank of independent directors is imperative in that the due diligence of selection of independent directors from its databank synchronizes details of experienced directors as well as newly qualified candidates which reinforces the best governance practices in listed companies. It is observed that both Mr. Imran Zaid and Ms. Javeria Malik were appointed as independent directors on board of the Company with effect from April 01, 2023 and at that time, their names were not registered in PICG databank of independent directors.

12. In 2024 CLD 740 [Appeal No. 85 of 2022 decided on February 13, 2024], it was held by the Appellate Bench of the Commission that *"it is quite clear that subsection (1) of section 166 of the Act inter alia recognizes the requirement of appointment of an independent director in a company under any law, rules, regulations, or code, whereas, subsection (3) ibid provides the manner of election of an independent director of a listed company. Going forward, subsection (5) ibid is an enabling provision whereby the Commission is empowered to specify the manner and procedure of selection of independent directors through regulations and thus in this context CCG Regulations contain therein provisions pertaining to independent directors, such as regulation 6... Regulation 6 of the CCG Regulations when read with sub-sections (3) and (5) of the Act, as reproduced above, makes it incumbent upon a listed company to elect independent directors. The use of words 'shall' (in subsection (3) of section 166 of the Act) and 'mandatory' (in Regulation 6 of the CCG Regulations) leave no room for any ambiguity that the legislative intent behind the said provision is to have independent directors on the Board of a listed company and the same is not directory in nature..."*

13. As evidently admitted by the Respondents themselves, the names of the aforesaid directors were included/registered in the databank subsequent to the observation and deficiency was communicated to the Company by the Commission on March 20, 2024. Accordingly, the non-compliance of the Respondents with the requirements prescribed under sub-section (1) of Section 166 of the Act, regulation 6(1) of the CCG Regulations and regulation 4(7) of the Directors' Regulations is established.

14. The argument put forward by the Respondents that the meeting of audit committee during the third quarter could not be held due to non-availability of half yearly reviewed financial statements of the Company is not considered plausible, since firstly, the questioned allegation does not merely revolve around non-holding of meeting of audit committee for the third quarter; instead, it has been observed that the audit committee only held two meetings during the month of October 2022 and no other meeting of the committee was held during any other quarter of the financial year 2022-23. It is important to note that the provisions of regulation 27 of the CCG Regulations are mandatory in nature, are explicit & unambiguous, and require the audit committee of a

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listed company to meet at least once in each quarter of the financial year of the company. The want of law is required to be met in entirety and any element of legal framework cannot be demeaned in criticality where each element is supplementary and complimentary to the overall framework. The audit committee, being part of the whole fabric of the corporate compliance, is a linchpin entrusted to deal with external auditors, Board and internal management, hence its cardinality and cruciality cannot be undermined.

15. The framework requires the audit committee to meet at least once in each quarter to effectively undertake its role in ensuring effective and vigilant oversight on the Company's financial reporting, internal control, compliance and internal audit processes. Clear guiding reference can also be drawn from sub-regulation (4) of regulation 27 of the CCG Regulations, which enunciates numerous businesses, in addition to review of financial statements, that require consideration and review by the audit committee. Hence, by meeting regularly, the committee would be able to identify any critical matter in a timely manner and could promptly address the same. Hence, the non-compliance of the Respondents with regulation 27(2)(i) of the CCG Regulations is established.

16. As far as the requirements of regulation 27 of the CCG Regulations about meeting with the external auditor & head of internal audit and determination of terms of reference are concerned, it is observed that the Respondents have failed to submit any documentary evidence to substantiate that the audit committee duly held meetings with the external auditor and head of internal audit. More so, no documentary evidence has been submitted by the Respondents to substantiate the claim made by the Respondents that the terms of reference of the audit committee are properly determined, prepared and maintained. Thus, contravention of regulation 27(2)(ii) and 27(3) of the CCG Regulations is established.

17. The contention of the Respondents that Mr. Muhammad Faheem meets the specified criteria for being financially literate as provided in explanation to regulation 27(1)(iii) of the CCG Regulations is not based on the facts on record. It is clearly evident from the submissions made by the Respondents that Mr. Faheem is neither a member of recognized body of professional accountants/ holds a post graduate degree in finance nor has 10 years' experience as audit committee member or 20 years' senior management experience in overseeing finance or audit related matters.

18. The applicable regulatory framework prescribed under the CCG Regulations is plain and unambiguous, and sub-regulation (1) of regulation 36 of the CCG Regulations clearly declares it mandatory for the companies to publish and circulate a statement to set out the status of their compliance with the requirement of the CCG Regulations, duly reviewed and certified by their statutory auditors. The Respondents were clearly non-compliant with the aforesaid provisions of regulation 27 of the CCG Regulations and also failed to disclose this fact in its Statement of Compliance for the financial year 2022-23 annexed with the Accounts; which is clearly in contravention of the requirements of regulation 36(1) of the Regulations. In 2006 CLD 1577 [Wali Oil Mills Limited], it was rightfully observed that "...Directors of the Company, being a listed-company, should fulfil their responsibilities laid down in the Code of Corporate Governance and follow good financial practices, which in the present case are very much lacking. I am of the view that for a healthy corporate culture, which the Commission aims to achieve, it is expected that the Directors of the listed-companies would endeavor to bring in more transparency and enhancing confidence of the investors in the listed-companies..."

19. Based on the above, the non-compliance of the Respondents with the requirements of sub-section (1) of Section 166 of the Act, regulations 6, 27 and 36(1) of the CCG Regulations and regulation 4(7) of the Directors' Regulations has been established, which attracts penal action as provided under Sections 169 and 512(2) of the Act read with regulation 37 of the Regulations. Therefore, I, in exercise of the powers conferred upon me under Section 169 read with Section 512 of the Act and regulation 37 of the CCG Regulations in terms of S.R.O. 1545(I)/2019 dated December 06, 2019, hereby:

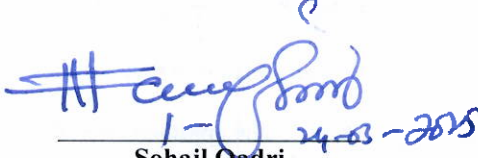
- (i) Impose an aggregate penalty of **Rs. 220,000/- (Rupees Two Hundred and Twenty Thousand Only)** on the Respondents in the following manner:

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Sr. #	Names	Penalty for Violation of			
		Section 166	Regulation 27(1)	Regulation 27(2)	Regulation 36(1)
		Pak. Rupees			
1.	Zahur Cotton Mills Limited	20,000	-	-	-
2.	Mr. Imran Zaid, Director	Warning	10,000	-	10,000
3.	Ms. Javeria Malik, Director (Member BAC)		10,000	15,000	10,000
4.	Ms. Sana Malik, Director		10,000	-	10,000
5.	Mr. Muhammad Faheem Qureshi, Director (Member BAC)		10,000	15,000	10,000
6.	Ms. Azra Perveen, Director (Member BAC)		10,000	15,000	10,000
7.	Mr. Muhammad Sheraz, Director (Member BAC)		10,000	15,000	10,000
8.	Syed Jawad Ali		10,000	-	10,000
	Total	20,000	70,000	60,000	70,000

- (ii) Advise all the Respondents to ensure meticulous compliance with the applicable legal and regulatory framework in future.

20. The Respondents are, hereby, directed to deposit the aforesaid amount of penalty in the designated bank account maintained in the name of the Commission with MCB Bank Limited or United Bank Limited within thirty (30) days from the date of this Order and to furnish a receipted bank challan to the Commission forthwith. In case of failure to deposit the penalty, the proceedings under Section 485 of the Act will be initiated for recovery of the fines as arrears of land revenue pursuant to provision of Section 42 of the SECP Act.


 1-24-03-2025
 Sohail Qadri
 Director/ HOD
 Adjudication Department-I

Announced:
 March 24, 2025
 Islamabad.