



Securities and Exchange Commission of Pakistan

BEFORE APPELLATE BENCH NO. IV

In the matter of

Appeal No. 01 of 2016

JS Bank Limited

Appellant

Versus

(i) Commissioner Company Law Division, Securities and Exchange
Commission of Pakistan

(ii) Chenab Limited

Respondents

Date of Hearing

16/05/16

Present:

For the Appellants:

Rashid Sadiq, CEO RS Corporate Advisory (Pvt.) Limited

For Respondent No. 1:

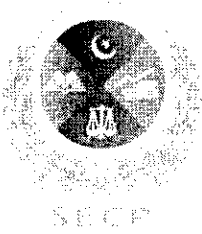
- (i) Mr. Abid Hussain, Executive Director (CSD)
- (ii) Ms. Ayesha Riaz, Additional Director (CSD)
- (iii) Ms. Khalida Perveen, Joint Director (CSD)

For Respondent No. 2:

- (i) Mr. Babar Sattar, Advocate High Court (AJURIS, Advocates & Corporate Counsel)
- (ii) Mr. Anique Salman Malik, Advocate (AJURIS, Advocates & Corporate Counsel)

ORDER

1. This order is in appeal No. 01 of 2016 filed under section 33 of the Securities and Exchange Commission of Pakistan Act, 1997 against the order dated 13/10/15 (Impugned Order) passed by the Respondent No.1.



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2. Brief facts of the case are that the Chenab Limited (Respondent No.2) issued 80 million non-voting cumulative preference shares (CPS) of Rs.10 each with preferential dividend of 9.25% per annum (including a public offer of 16 million shares) with approval of the Commission pursuant to the provisions of section 57 of the Companies Ordinance, 1984 (Ordinance) and Rule 5 of the Companies Share Capital (Variation in Rights and Privileges) Rules, 2000 read with section 90 of the Ordinance. JS Bank Limited (Appellant) subscribed 13.357 Million CPS and as per terms of the Prospectus exercised two consecutive Put Options for 1/3rd of the CPS each year on 29/09/08 and 30/09/09 respectively. Thereafter, upon non-redemption by the Respondent No.2 a notice for conversion of the CPS into ordinary shares was served upon the Respondent No.2 on 02/04/10 by the Appellant but Respondent No.2 failed to perform. The Appellant filed an application against the Respondent No.2 under section 474 of the Ordinance which was decided by the Director Enforcement vide letter dated 23/05/11. The Appellant preferred an appeal before the Appellate Bench under section 33 of the SECP Act against the decision of Director Enforcement. The Appellate Bench heard the appeal and remanded the matter to the Respondent to consider the submissions of the Appellant in view of the observations made by the Appellate bench vide order dated 11/10/12. The matter was initially heard by the Director (Enforcement) on 27/03/14, thereafter, during pendency of the proceeding, as a result of delegation of adjudication powers vide S.R.O.154(1)/2015 dated 19/02/15 the matter was finally decided by the Respondent No.1 vide the Impugned Order dated 13/10/15. The Appellant was advised to approach relevant forum for resolution of long outstanding matter in the interest of all stakeholders.
3. The Appellant's representative has preferred the instant appeal against the Impugned Order on the following grounds:

Appellate Bench No. IV

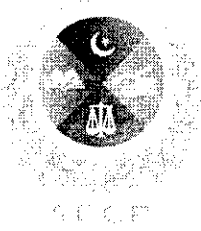
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- i. The Respondent No.1 has failed to provide adequate reasoning for declaring the application of Section 59 to be outside the scope of powers of the Commission contrary to the requirements of Section 22 of SECP Act 1997 and Section 24A of the General Clauses Act 1897.
- ii. The Respondent No.1 has failed to discuss the implications of the price manipulation on the business of the Appellant, particularly the loss suffered by the Appellant which is a banking company and has erred in implying that discussions on the issue of price manipulation are barred due to institution of criminal proceedings in the Court. Applying the fact of price manipulation towards providing justice to the Appellant would not constitute contempt of court or violation of Article 13 (Protection against double punishment and self-incrimination) of the Constitution of Pakistan. Reliance is placed on the judgement of the Supreme Court of Pakistan in the matter of Arif Ghafoor versus Managing Director cited at PLD 2002 SC 13 and in the matter of Shri Mehra, Senior Supdt versus Unknown cited at AIR 1962 MP 72.
- iii. The Respondent No.1 has failed to consider the application of legal principles established by the higher judiciary of Pakistan and acknowledged and adopted by the Commission in various decisions by it regarding violation of fiduciary duties in relation to the exercise of powers by Directors pursuant to Section 196 of the Ordinance.
- iv. The Respondent No.1 has failed to recognize the availability of powers of the Commission pursuant to Section 472 of the Ordinance. This requires the Company to make amendments of the share conversion price which was wrongfully inflated in breach of the established fiduciary duty provided under Section 196 of the Ordinance. The Respondent No.1 has failed to consider the application of Section 63 of the Ordinance when considering whether the statement included in the Prospectus regarding the 'Sinking Fund' would constitute a 'misleading' statement for the purposes of Section 59 of the Ordinance. It is submitted that the statement about the Sinking Fund being set-up primarily for the redemption of the Preference Shares was inserted in the Prospectus as a reassurance to prospective investors with the express intent to



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induce investors into purchasing the Preference Shares. The fact that the Preference Shares were not redeemed despite the existence of the Sinking Fund establishes that the said statement in the Prospectus was a misleading one for the purposes of Section 63 of the Ordinance which in turn leads to the application of Sections 59 and 60 of the Ordinance.

- v. The Impugned Order has failed to recognize the duty of the Commission to act dutifully for the protection of the Appellant, an investor, pursuant to the requirements of Section 20(6)(b) of the 1997 Act. The Respondent No.1 has failed to do everything in its power to implement remedial measures for the relief of the Appellant while being aware of the adverse impact of the price manipulation on the assets of the Appellant. Furthermore, the Impugned Order has failed to consider the investigation report pertaining to trading activity in the shares of the Company and the criminal complaint filed by the Commission against the Company.

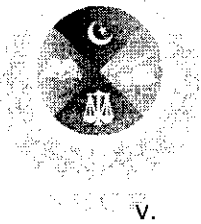
4. The Respondent No.1 rebutted the arguments of the Appellant in the following manner:

- i. Section 59 of the Ordinance is a question for determination by court of competent jurisdiction and, therefore, outside the scope of the Commission. The issue of price manipulation is pending adjudication at the appropriate forum for action against the Respondent No.2. Further, it is stated in the Impugned Order that "As regards the issue of price manipulation, it is a matter of record that the same has been investigated by the relevant department of the Commission and a criminal complaint has already been filed against the Respondent No.2, which is pending adjudication. Without prejudice to the authority of Courts to interpret Prospectus terms, the Appellant is advised to approach relevant forum for resolution of this long outstanding matter in the interest of all stakeholders along with the above referred judgement of this office for careful consideration of its implications, if any, on the implementation/ interpretation of the Prospectus terms."



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- ii. The allegation by the Appellant of alleged misuse of sinking fund for purposes other than redemption of preference shares was investigated by the Respondent No.1. However, it was observed and stated in the Impugned Order that “the decision of the directors of the Company for not redeeming CPS when redemption was applied by the appellant cannot be termed as a violation of Section 196 of the Ordinance. Conversion instead of redemption was one of the expressed options available to them under the terms and conditions of Prospectus. No case for breach of fiduciary duty is hence made.”
- iii. Direction under Section 472 of the Ordinance is issued when there is a breach of any provision of the Ordinance. However, in the instant case no violation of any provision of the Ordinance has been noted. It is a matter of record that the Appellant and the Respondent No.2 differ in their respective interpretations of the terms of the Prospectus related to default date, amount of CPS to be converted as well as the conversion price and the Appellant are praying for direction of the Commission to the Respondent No.2 for conversion of CPS on terms as interpreted by them. In such instances the appropriate forum is a competent court of law which has the authority to interpret and enforce such contracts.
- iv. The allegations of the Appellant regarding misstatement in the Prospectus specifically regarding the disclosures relating to establishment of sinking fund were duly considered and it was clearly stated in the Impugned Order that “None of the allegations of the Complainant bring to light any untrue fact which if had been disclosed in the Prospectus, would have resulted in rejection of the Prospectus by an investor by exercise of ordinary prudence on the date of its issue.” Moreover, it was further observed that sinking fund was required to be created to comply with SBP approval letter dated 21/07/04 only for inclusion of CPS into equity of the Respondent No.2 and any default on part of the Respondent No.2 to redeem CPS other than out of sinking fund would lead only to conversion of CPS into ordinary shares as stated in clause 2.2.3 of the Prospectus. Therefore, the Prospectus did not in any way guarantee redemption of CPS.



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v. The instant case is an outcome of varied interpretations and, therefore, a fit case for arbitration. Moreover, power to enforce a contract such as “the Prospectus” rests with the court. The Commission was, therefore, constrained to provide the relief prayed for.

5. The Respondent No 2. has rebutted the arguments of the Appellants as follows:

i. Preliminary Objections:

It is a settled law that a public authority can only take actions that it is specifically authorized to take by law, as opposed to private individuals who can take such actions, as not prohibited by law from taking. The law does not specifically empower the Commission to take cognizance of an offence under section 474 of the Ordinance, given that none of the provisions of the law being relied upon by the Appellant empower the Commission or the Registrar of Companies to impose any penalty upon the Respondent No.2. Neither the scheme of the Ordinance nor the SECP Act, 1997 empower the Commission to function as an adjudicator sitting in judgment over civil disputes between parties or imposing penalties that fall within the domain of courts of competent jurisdiction empowered to try offences and crimes. The phrase “initiating action against the” in section 20(4)(i) of the SECP Act has been inserted in place of the word “prosecuting” by the Finance Act, 2008. Further, Section 485 of the Ordinance has also been amended by Finance Act 2007, which, without such amendment requires a party aggrieved by an order of the Commission to file an appeal before the High Court.

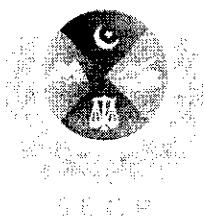
ii. It is well settled that money bills have a limited scope and it was more specifically accepted in the Ashraf Tiwana vs Pakistan cited at 2013 SCMR 115, wherein, it is stated that, “the insertion of section 5(5) in the Act through the Finance Act 2003 was in violation of the Constitution and in particular Article 73 thereof”. Therefore, substitutions within provisions of the SECP Act and the Ordinance made through Finance Acts are null and void and of no legal consequence for falling beyond the scope of a money bill. Reliance is also



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placed in the matter of Sindh High Court Bar Association & another v. Federation of Pakistan cited at PLD 2009 SC 879 and Mir Muhammad Idris and others versus Federation of Pakistan cited at PLD 2011 SC 213. Furthermore, the Appellant has failed to grasp the scope of section 20(6)(b) of the SECP Act. The Commission is restricted by its jurisdiction and powers to take any action beyond that which it has undertaken. Furthermore, the Commission has initiated a complaint regarding price manipulation with the relevant forum and as such has discharged its duty under the SECP Act. The action required pursuant to the investigation report has been initiated. To take further action on the basis of controversial facts would be both inappropriate and against the law. Therefore, the appeal is not maintainable before the Appellate Bench. It is settled law that amendment in substantive provisions of the law are given effect prospectively and amendment in procedural provisions apply retrospectively. Section 6 of the General Clauses Act 1897 has been interpreted to mean that where the law is changed during the pendency of an action, the rights of the parties are decided in accordance with the law as it existed at the time when the action was begun. The principle is, however, of no assistance to the Appellants as this case falls within the exception that the new law shall apply if it is a mere rule of procedure or if it has been applied retrospectively to pending proceedings (reliance is placed on 2005 SCMR 1785 which refers to PLD 1971 SC 252.) The appeal involves issues of civil and interpretational issues which the Commission is not competent to adjudicate. None of the provisions of the Ordinance and the SECP Act, being relied upon by the Appellant, vest any adjudicatory authority in the Registrar or the Commission and thus the prayers made in the appeal cannot be granted by the Commission.

- iii. The Appellant has alleged that Respondent No.2 has breached sections 59 and 60 of the Ordinance, which stand repealed in terms of section 178(1) of the Securities Act 2015 (Securities Act). Even otherwise, the Commission is not authorized to take cognizance of any breach of sections 59 and 60, as adjudication of such matters falls within the domain of courts of competent jurisdiction. Section 178(2)(a) further states that "any notifications, rules,

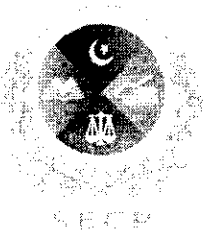


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regulations, bye-laws, orders or exemption issued, made or granted under any such enactment shall have effect as if had been issued, made or granted under the corresponding provisions of this Act. The corresponding provisions for sections 59 and 60 of the Ordinance, sections 92 and 93 of the Securities Act, are provisions the breach of which clearly requires cognizance to be taken by the court in terms of section 163 of the Securities Act. The principle of separation of powers is a salient feature of the Commission and the Commission being a public authority vested with executive powers is barred from determining the civil or criminal rights and liabilities of parties, such functions fall within the domain of the judiciary and not the executive organs of the state.

- iv. The interpretation of terms of the Prospectus and conditions related to conversion of preference shares into ordinary shares is the subject matter of dispute. The Appellants demand of conversion of the entirety of the preference shares is not supported by the provisions of the Prospectus, which only allows for conversion of such number of preference shares as the Company has failed to redeem for consecutive years. A complaint has been filed before the court of competent jurisdiction with regard to allegations of price manipulation, which is pending adjudication. Such frivolous allegations of price manipulation are not and cannot be the subject matter of the present proceedings. It would be erroneous to place reliance on allegations made in the complaint while the matter is sub judice and remains to be determined on its merits. The findings made by the investigation of the Commission cannot be viewed as conclusive as the matter is sub judice and remains subject to adjudication and determination by the court of competent jurisdiction. The preference shares redemption reserve was created as per the directive of the State Bank of Pakistan. The State Bank of Pakistan specifically approved the inclusion of the Preference Shares in the equity of the Company for purposes of Prudential Regulations subject to the following conditions:

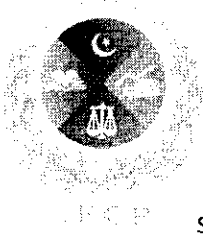
- a. After issue of the Preference Shares, a sinking fund would be built up from un-appropriated profit;



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- b. Such sinking fund/reserve will not be counted towards part of the equity for the purposes of Prudential Regulations for Corporate/ Commercial Banking;
 - c. Payment in respect of any redemption of the Preference Shares would be made from the aforementioned sinking fund/reserve only;
 - d. Any default by the Company in respect of Preference Shares would lead only to the conversion of the Preference Shares into Ordinary Shares.
- v. The findings made by the investigation of the Commission cannot be viewed as conclusive as the matter is sub judice and remains subject to adjudication and determination by the court of competent jurisdiction. The preference shares redemption reserve was created as per the directive of State Bank of Pakistan (SBP). SBP specifically approved the inclusion of the Preference Shares in the equity of the Company for purposes of Prudential Regulations subject to the conditions as mentioned in para iv above.

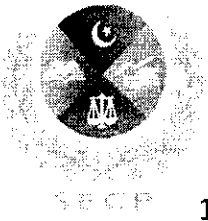
As such, Respondent No.2 had been maintaining Preference Shares Redemption Reserve and has not violated any provisions of SBP letter or commitment disclosed in the Prospectus. The Appellant itself acknowledges the creation of such fund and as such, allegations of misstatements in the Prospectus are self-contradictory. The Impugned Order is a well-reasoned order which addressed individual legal issues raised in the matter. Sections 20 and 22 of the SECP Act vest no power with the Commission to adjudicate upon the subject matter. Moreover, section 59 of the Ordinance stands repealed and replaced, and even otherwise it fell within the domain of courts to determine any breach of section 59 of the Ordinance. None of the other provisions cited vest any authority in the Registrar or the Commission to adjudicate the rights and obligations of parties pursuant to a mutual agreement. The matter of price manipulation is not a fact but a controversy which is before the competent forum for adjudication. As such no discussion regarding a matter which is sub judice can be undertaken as part of these proceedings. The content of preliminary objections with regard to separation of powers is reiterated. The Appellant failed to prove any breach of



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section 196 of the Ordinance, therefore, there can be no question of the Commission availing powers under section 472 of the Ordinance for requiring Respondent No.2 to make good for any alleged loss suffered by the Appellant. Like the rest of the Appeal, this assertion is rooted in misperception regarding the scheme of the Ordinance and powers of the Commission. A prerequisite for exercise of powers vested in the Commission under section 472 is a determination establishing the breach of provisions of the Ordinance. Since there is no such determination, the resort to section 472 of the Ordinance is misplaced. In light of section 63 of the Ordinance, the statement regarding the Sinking Fund is not a misleading statement and a remedy in case of failure to redeem preference shares was expressly provided. This fact, along with the absence of any statement regarding ring-fencing clearly shows that there was no misleading statement made in the Prospectus.

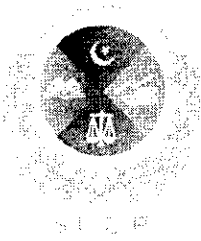
6. We have heard the parties i.e. the Appellant and the Respondents.
7. The Appellant's representative has argued that the Respondent No.1 has failed to take into consideration that the Appellant has suffered losses and criminal proceedings initiated by the Commission do not have a bearing on the outcome of the application made to the Respondent under section 474 of the Ordinance. Further, the Impugned Order has failed to recognize the availability of powers of the Commission pursuant to section 472 of the Ordinance and the Respondent No.1 also has powers under section 59 and 60 of the Ordinance to initiate against Respondent No.2 for alleged misstatement in the Prospectus. The Respondent No.2 is also in breach of its fiduciary duties in terms of section 196 of the Ordinance. The Representatives of Respondent No.1 have argued that direction under 472 of the Ordinance can only take place if there is breach of any provision of the law. Further, it was argued that the Respondent No. 1 does not have the powers under section 474 of the Ordinance to prosecute Respondent No. 2 or compel them to enforce the Prospectus which is a contractual agreement between the parties. Matters pertaining to price of the preference shares and to what extent CPS shares were to be converted whether



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1/3 or all shares as alleged by the Appellant are a matter of dispute which the Respondent No.1 does not have powers to decide. The Counsel of Respondent No.2 has also argued that a public authority can only take actions that it is specifically authorized to take by law and the findings made by the investigation of the Commission cannot be viewed as conclusive as the matter is sub judice and remains subject to adjudication and determination by the court of competent jurisdiction. Further, the maintainability of appeal has also been questioned by Respondent No.2 on the basis of amendments to the SECP Act including insertion of section 5(5) in the SECP Act as well as the Ordinance through various Finance Acts. Respondent No.2 is of the view that as the amendments were invalid, therefore, the appeal could not have been filed in terms of section 33 of the SECP Act. Our observations are as follows:

- (a) The appeal is maintainable in view of section 2 of the Securities and Exchange Commission of Pakistan (Amendment) Act, 2013 (SECP Amendment Act), wherein, section 5 of the SECP Act was amended and the following was substituted namely, "(5) No act, proceeding or decision of the Commission shall be invalid only by reason of the existence of a vacancy or defect in the constitution of the Commission.". Further section 4 of the SECP Amendment Act provides, that "Anything done, actions taken, orders passed, instruments made, notifications issued, agreement made, proceedings initiated, processes or communications issued, powers conferred, assumed or exercised by the Commission as defined in clause (g) of Section 2 of the said Act or its employees as defined in clause (k) of Section 2 thereof in terms of amendments made through this Act, on or after the 19th December, 1997 and before the commencement of this Act, shall be deemed to have been validly done, made, issued, taken, initiated, conferred, assumed and exercised and the provisions of this Act shall have and shall be deemed to have had effect accordingly." Any amendments made through the Finance Acts have now been regularized through the SECP



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Amendment Act. The appeal, therefore, was correctly filed in terms of section 33 of the SECP Act.

- (b) On merits of the instant case, we concur with both Respondent No. 1 and 2 that the Respondent No.1 only has powers to enforce the existing provisions of the law but cannot decide on disputes between the Appellant and Respondent No.2 pertaining to the Prospectus. Further, the Appellant has failed to state any specific provision of the law that has been violated by Respondent No.2 for which action can be initiated by Respondent No.1. Further, we concur with the Counsel of Respondent No.2 that Respondent No.1 does not have the powers to take cognizance of any offence in terms of section 474 of the Ordinance and such power only lies with a court of competent jurisdiction. Furthermore, Section 20(6) of the SECP Act only confers executive powers on the Commission being a public body to maintain the confidence of investors but does not give powers to determine civil and criminal liability.
- (c) The Appellant has been unable to prove that there was a misstatement in the Prospectus. Clause 3(xi) of the Prospectus states "In the event that the Company fails to redeem the Cumulative Preference Shares upon exercise of the Put Option by the holders of the Cumulative Preference Shares in terms of para 5(ii) above, within the stipulated period for any reason whatsoever (including the legal inability to do so on account of the provisions of section 85 of the Companies Ordinance 1984) for any two consecutive years in which such Put Option was exercised by the holders of Cumulative Preference Shares, the holders of the Cumulative Preference Shares shall be entitled by notice in writing to the Company to call upon the Company to convert the Cumulative Preference Shares into Ordinary Shares; or (ii) 75% of the market value (iii) the face value of the Ordinary Shares..." Furthermore, preference shares were to constitute Equity of the Company for purposes of prudential regulations of SBP as stated in clause 2.2.3 of the Prospectus and a sinking fund was established for payment in respect of any redemption. However, clause



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2.2.3(iv) states that, "Any default by the Company in respect of Preference Shares would lead only to the conversion of the Preference Shares into Ordinary shares." Therefore, any dispute pertaining to subsequent conversion of shares can only be settled in a court of competent jurisdiction. The Respondent No.1 cannot go beyond the ambit of its powers and try to enforce the provisions of the Prospectus which are subject to different interpretations by both the Appellant and the Respondent No.2. The Appellant has also been unable to show that there was breach of any fiduciary duty by Respondent No.2 in terms of section 196 of the Ordinance. The Respondent No.1 can only penalize or issue a direction to the Respondent No. 2 if breach of any provision of the law has taken place which the Appellant has failed to substantiate in its appeal. Further, the Appellant has been unable to rebut any of the observations made in the Impugned Order by the Respondent on merit. All of the issues raised in the instant appeal have been properly addressed in the Impugned Order. The Appellant has not been able to satisfy the Bench that the Respondent No.1 has erred in any way in the Impugned Order.

- (d) In view of the foregoing, the Impugned Order is upheld and the appeal is dismissed with no order as to costs.

(Fida Hussain Samoo)
Commissioner (Insurance)

(Zafar Abdullah)
Commissioner (SCD)

Announced on: **02 AUG 2016**