

Securities and Exchange Commission of Pakistan

BEFORE APPELLATE BENCH No. I

In the matter of

Appeal No. 44 of 2017

The Pakistan Credit Rating Agency Limited

Appellant

Versus

1. Public Offering and Regulated Persons Department, SECP, Islamabad.
2. JCR-VIS Credit Rating Company Limited.

Respondents

Dates of hearing:

22/02/19, 13/03/19 & 22/03/19

Present:

For Appellant:

- i. Rahat Kaunain Hassan
- ii. Gulalay Zeb
- iii. Mohammad Adnan Afaq

For Respondent No.1:

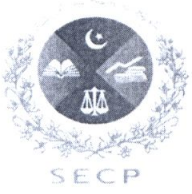
- i. Adil Anwar, Director Adjudication (SMD)
- ii. Nasir Askar, Director (SMD)
- iii. Mehwish Naveed, Management Executive (SMD)

For Respondent No.2:

- i. Ijaz Ahmed
- ii. Sarfraz Ahmed

ORDER

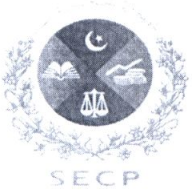
1. This Order is in the matter of Appeal No. 44 of 2017 filed by the Pakistan Credit Rating Agency Limited (the Appellant) against the Order dated 28/04/17 (the Impugned Order) passed by the Executive Director (SMD-PRPD) under Section 22 of the Securities and Exchange Ordinance, 1969 (the Ordinance).
2. The brief facts of the appeal are that the Securities and Exchange Commission of Pakistan (the Commission) received a complaint dated August 28, 2015 from JCR-VIS Credit Rating Company



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Limited (the Respondent No.2) whereby it was alleged that one of its clients namely; Faysal Asset Management Limited (the FAML) had switched over to the Appellant for their fund stability rating without obtaining NOC. The Respondent No.2 further stated that the Appellant accepted the rating assignment in contravention of clause 2.3.3(b) of the Conduct for Credit Rating Agencies (the Code). In view of the alleged violation a show cause notice dated October 6, 2015 issued to the Appellant and subsequently, the Respondent No.1 imposed a penalty of Rs. 600,000/- on the Appellant, vide order dated 19/01/16 (the Original Order).

3. The Appellant has impugned the Original Order through an appeal under Section 33 of the Securities and Exchange Commission of Pakistan Act, 1997 before the Appellate Bench (the Bench). The Bench, vide an order dated 01/09/16 (the Remand Order) had remanded the matter with the direction to make the Respondent No.2 party in the case and examine the conduct of FAML.
4. In view of the Remand Order, the Respondent No.1 heard the Respondent No.2 on 27/10/16. Furthermore, in compliance of the Remand Order, the Respondent No. 1 examined the conduct of FAML and found that there are no conduct requirements for Asset Management Company in respect of acquisition of rating. It is also pertinent to mention here that on Respondent's No.1 query, the relevant department of the Commission apprised that FAML had disclosed both ratings i.e rating assigned by Appellant and Respondent No. 2 in their Fund Manager Report and advertisements. Thereafter, Respondent No.1 concluded the matter vide the Impugned Order and imposed a penalty of Rs. 600,000 on the Appellant, for violation of clause 2.3.3(b) of the Code.
5. The Appellant had challenged the Impugned Order before the Bench and during the hearing, the Appellant's representative argued the case and reiterated the grounds of Appeal. The Appellant had challenged the Impugned Order *inter alia* on the grounds that the Respondent No.1 had not provided opportunity of hearing to the Appellant while deciding the matter, hence, violated the principle of natural justice whereby Appellant may not be deprived to defend a case against it. The Appellant had taken plea that the default under clause 2.3.3(b) of the Code may not be established unless precondition of premature termination of rating contract is met and in this case, the FAML had not terminated the rating contract with the Respondent No.2 during the time Appellant had assigned credit ratings to the FAML. The Appellant had also taken a stance that FAML had obtained credit ratings from the Respondent No.2 and the Appellant, therefore, this is a case of



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multiple ratings, which is not prohibited under the Code. The Appellant contended that Section 22 of the Ordinance maybe invoked if there is any violation or default under the Ordinance or any rules or regulation made thereunder. However, Clause 2.3.3(b) of the Code, is neither part of the Ordinance, rules or regulations, nor do the Credit Rating Companies Rules, 1995 (the CRC Rules) prescribe any penalty for non-compliance of its directives. Lastly, Appellant stated that the Respondent No.1 had also failed to prove willful default of the Appellant, as required under Section 22 of the Ordinance.

6. The representatives of the Respondent No.1 had vehemently denied the assertions of the Appellant and relied upon the facts and findings of the Impugned Order. They prayed to dismiss the Appeal. The representative of the Respondent No.2 appeared and stated that *“the Commission has now issued Credit Rating Companies Regulations, 2016, which adequately address the concerns of the answering respondent, Since the issue raised by the answering respondent stands resolved it is respectfully submitted that the answering respondent does not intend to proceed with or pursue this matter further. Therefore, an appropriate order may be passed by this Hon’ble Appellate Bench for disposal of the instant appeal.”*
7. The Bench has heard the parties and perused the record. Although, proceedings against the Appellant were initiated upon the complaint of the Respondent No.2, however, the Respondent No.1 had independently analyzed the facts and relevant law, to establish the alleged violation of the Code. Resultantly, withdrawal of complaint by the Respondent No.2, at appellate stage is immaterial, therefore, we will conclude this matter on merits of the case.
8. The reason behind the Remand Order was that the Respondent No.2 was not heard during the proceedings of the Original Order. However, upon remand, the Respondent No.1 had heard the Respondent No.2 but the Appellant was not called to join the proceedings. In para 12 of the Impugned Order the Respondent No.1 had interpreted the Remand Order in the following manner:
“In my opinion, the primary reasons for remanding of the instant matter was to make the Respondent no. 2 as party to the proceedings, which has been complied with.”
9. The bare reading of Respondent’s No.1 opinion is a reflection of the fact that judicial mind had not been applied while passing the Impugned Order. Fresh opportunity of hearing was the fundamental



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right of the Appellant whether or not it was mentioned in the Remand Order. We are of the view that the Appellant had been condemned unheard. Appellant should have been given a fair chance to rebut the allegations and arguments of Respondent No.2. The Impugned Order is a glaring violation of the right to a fair trial envisaged and guaranteed under Article 10A of the Constitution of Pakistan. The Bench has observed that in this matter there had been continuous legal omissions on part of the Respondent No.1 and the officer who passed the Original Order. Decision of the case based on proceedings conducted during the Original Order, which had been *set aside* by the Bench is a serious matter. Non provisions of opportunity of hearing is not a matter that could be condoned, rather, on this sole ground Impugned Order is liable to be *set aside* however, as we have decided to conclude this matter on merits therefore, we will not rely on this grave violation.

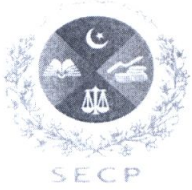
10. The Bench is of the view that for the conclusive determination of the facts and law, it is important to deliberate upon the relevant provision. The clause 2.3.3 (b) of the Code is reproduced below for reference:

“Rating Shopping: CRA shall:

(b) not accept a rating assignment where a client has prematurely terminated a rating contract with its existing CRA, unless such client obtains No Objection Certificate (NOC) from its existing CRA or ensure in writing that it shall continue credit rating with its existing CRA till the period as agreed in the rating agreement. A clause to this effect shall be included by the CRA in each rating agreement;”

Emphasis Added

11. The phrase “*prematurely terminated*” used in clause 2.3.3 (b) of the Code, dominates the entire clause, therefore, prohibition and exceptions of this clause shall be construed accordingly. The Appellant had been penalized under the clause 2.3.3(b) of the Code however, this provision is not applicable in present case. It is admitted fact that Appellant provided ratings on August 20, 2015, however, Respondent No.2 received the FAML’s letter dated August 21, 2015, vide an email dated August 25, 2015 for FSR’s withdrawal. Therefore, it is evident that at the Appellant provided ratings during the existence of the contract between the Respondent No.2 and the FAML. Furthermore, it is also on record that without premature termination of the contract with Respondent No.2, the FAML had obtained credit ratings from the Appellant, therefore, this is a case of multiple ratings, which is not prohibited under the Code. It is also important to note here that the Respondent No.2 had mentioned in the Impugned Order that “*there is no conduct requirement applicable on*



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an Asset Management Company in respect of acquisition of rating". It is also pertinent to mention here that FAML had disclosed both the ratings i.e rating assigned by the Appellant and Respondent No. 2 in their Fund Manager Report and advertisements. This fact is sufficient to prove that neither the FAML nor the Appellant had any malice or intention to drive undue benefits from the questioned transactions.

12. The Bench has perused the CRC Rules, Code and the Ordinance, to determine whether Respondent No.1 was authorized to penalize the Appellant under Section 22 of the Ordinance or there was misapplication of law. As per scheme of subordinate legislation, the CRC Rules were made under the Ordinance and the Code was issued under the CRC Rules therefore, the Respondent No.1 was duly authorized to proceed under the relevant law. The Code was a directive, issued by the Commission, in exercise of the powers conferred by Rule 7 of the CRC Rules. For reference, relevant part of Section 22 of the Ordinance and preamble of the CRC Rules and the Code is reproduced below;

Securities and Exchange Ordinance, 1969

"Section 22. Penalty for certain refusal or failure. -(1) If any person-

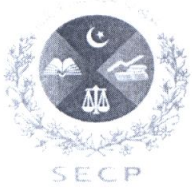
(a); or

(b); or

(c) contravenes or otherwise fails to comply with the provisions of this Ordinance or any rules or regulations made thereunder; the Commission may, if it is satisfied after giving the person an opportunity of being heard that the refusal, failure or contravention was willful, by order direct that" **Emphasis Added**

Credit Rating Companies Rules, 1995

Preamble: *"S.R.O. 759 (I)/95.- In exercise of powers conferred by section 33 of the Securities and Exchange Ordinance, 1969 (XVII of 1969), the Federal Government is pleased to make the following rules to regulate the business of credit rating companies,"* **Emphasis Added**



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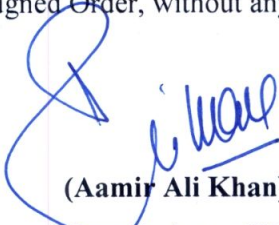
Directive under the Credit Rating Companies Rules, 1995

Preamble: “For establishing a procedural framework for credit rating companies and in the interest of public and the capital market, the Commission, in exercise of the powers conferred by rule 7 of the Credit Rating Companies Rules, 1995 is pleased to direct that the Credit Rating Companies shall follow and comply with the following Code of Conduct for Credit Rating Companies/Agencies with immediate effect.”

Emphasis Added

13. In view of the preceding para, there is no doubt that the Respondent No.1 was authorized to inflict a penalty under Section 22 of the Ordinance if default of the Ordinance, rules or the regulations made thereunder had been established. Appellant’s plea that CRC Rules, do not prescribe any penalty for non-compliance of its directives is apparently true, however, Section 22 of the Ordinance is the relevant penal provision to deal with the violations of the CRC Rules or the Code.
14. The above discussion has made it clear that the respondent No.1 was duly authorized to invoke the Section 22 of the Ordinance for the violations of the CRC Rules or the Code, however, the Respondent No.1 had failed to establish the Appellant’s default under the clause 2.3.3 (b) of the Code therefore, penalty under Section 22 of the Ordinance is not sustainable. In the circumstances, we hereby accept this Appeal and set *aside* the Impugned Order, without any order as to cost.


(Shaukat Hussain)
Commissioner (CLD-CCD)


(Aamir Ali Khan)
Commissioner (SCD-PRDD)

Announced on: **05 APR 2019**