

# Securities and Exchange Commission of Pakistan

## BEFORE APPELLATE BENCH NO. 1

In the matter of

Appeal No. 46 of 2015

United Bank Limited

...Appellant

Versus

Mr. Imran Inayat Butt

Director/HOD (MSRD)

Securities Market Division

Securities and Exchange Commission

of Pakistan

...Respondent

Dates of Hearing: 01/02/16, 29/12/16

### Present:

#### For the Appellant:

(i) Mr. Rashid Sadiq, CEO, RS Corporate Advisory (Pvt.) Ltd

(ii) Mr. Adnan Afzal, AVP, UBL

#### For the Respondent:

(i) Mr. Nasir Askar, Director (SMD)

(ii) Mr. Muhammad Farooq Bhatti, Additional Director (SMD)

### ORDER

1. This order is passed in the matter of appeal No. 46 of 2015 filed under section 33 of the Securities and Exchange Commission of Pakistan (Commission) Act, 1997 (SECP Act) against the order dated 25/09/14 (Impugned Order) passed by the Respondent.



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2. The brief facts of the case are that Fauji Cement Company Limited (Issuer Company) is a public listed company and United Bank Limited (Appellant) is a beneficial owner of more than ten percent ordinary shares of the Issuer Company. The Appellant has made the following sale and purchase transactions in ordinary shares of the Issuer Company, within a period of less than six months:-

Sr. No.	Date	Nature	No. of shares	Rate per share (Rs.)
1.	9/4/2009	Sale	1,405,500	6.97
2.	9/4/2009	Sale	600,000	7.01
3.	16/04/2009	Sale	155,000	6.87
4.	21/05/2009	Purchase	1,000,000	6.49
5.	2/6/2009	Purchase	90,000	6.47
6.	3/6/2009	Purchase	300,000	6.47
7.	3/6/2009	Purchase	200,000	6.45
8.	10/6/2009	Purchase	155,500	6.6
9.	11/6/2009	Purchase	12,500	6.6
10.	17/06/2009	Purchase	157,000	6.74
11.	18/06/2009	Purchase	239,000	6.75
12.	18/06/2009	Purchase	4,000	6.74
13.	18/06/2009	Purchase	239,000	6.75
14.	9/7/2009	Sale	1,972,500	7.49
15.	10/7/2009	Sale	16,500	7.47
16.	13/07/2009	Sale	2,950,000	7.54
17.	15/07/2009	Sale	3,000,000	7.96
18.	16/07/2009	Sale	500,000	7.97
19.	23/07/2009	Sale	400,000	8.29
20.	24/07/2009	Sale	860,000	8.36
21.	31/07/2009	Sale	775,000	8.47
22.	3/8/2009	Sale	500,000	8.57
23.	3/8/2009	Sale	100,000	8.67
24.	7/8/2009	Sale	177,433	8.47
25.	10/8/2009	Sale	100,000	8.59

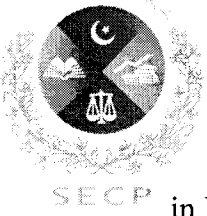
3. On account of the aforesaid, the Appellant in terms of section 224(1) of the Ordinance read with Rule 16 of the Companies (General Provisions and Forms) Rules, 1985 (Rules) apparently made gain of Rs.4,198,308.00. Section 224 of the Ordinance provides that where inter alia a more than ten percent beneficial owner of listed equity securities makes



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any gain by purchase and sale, or the sale and purchase, of any such security within a period of less than six months, such person is required to make a report and tender the amount of such gain to the company and simultaneously send an intimation to that effect to the Registrar of Companies and the Commission. The said section further provides that where such person fails or neglects to tender or the company fails to recover, any such gain within a period of six months after its accrual, or within sixty days of a demand thereof, whichever is later, such gain shall vest in the Commission and unless such gain is deposited in the prescribed account, the Commission may direct recovery of the same as an arrear of land revenue. In the instant case, the Respondent noted that neither the accrual of the aforesaid gain as reported in Part-D of the prescribed returns of beneficial ownership were filed with the Commission on Form 32, nor was the same tendered to Issuer Company by the Appellant. Similarly, the Issuer Company did not raise demand for recovery of the aforesaid gain, within the stipulated time. The Respondent was, therefore, asked vide letter dated 24/01/13 to furnish inter alia documentary evidence, if the legal obligation under section 224 of the Ordinance has already been discharged. Similarly, the Issuer Company did not raise demand for recovery of the aforesaid gain, within the stipulated time limit. The Company Secretary submitted its response vide letter dated 04/02/13. Hearing in the matter was held on 03/05/13 and Mr. Rashid Sadiq (Authorised representative) appeared on behalf of the Appellant and stated that the Appellant neither violated the provisions of section 224 of the Ordinance nor made gains in terms of the provisions of section 224(1) of the Ordinance. The Authorized representative requested to withdraw the Notice without any adverse action.

4. The Respondent, dissatisfied with the response of the Appellant, held that it was evident that the Appellant had made gain on account of the aforesaid sale and purchase transactions. Furthermore, it was held by the Respondent that the amount of gain must be re-calculated keeping in view the Order of the Appellate Bench in the matter of *Mrs. Nasreen Humayun Sheikh in Appeal No. 49 of 2011*, wherein, the Appellate Bench calculated the amount of gain by matching the purchase and sale transactions in sequential manner rather than by applying the lowest purchases with the highest sales as prescribed



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in Rule 16 of the Rules. Therefore, the amount of tenderable gain was re-calculated by the Respondent and the amount of tenderable gain was reduced from Rs.4,198,308/- to Rs.939,945/-. The Appellant was required to discharge its said obligation and transfer the amount of Rs.939,945/- to the Issuer Company within 30 days of the issue of the Order. Furthermore, in exercise of the powers conferred under section 224(4) of the Ordinance, a fine of Rs.30,000 was imposed on the Appellant by the Respondent.

5. The Appellant has preferred the instant appeal against the Impugned Order on the following grounds:

- a) The gain calculated by the Respondent is notional and not an actual gain. Section 224(1) of the Ordinance refers to “*make any gain by the purchase and sale, or sale and purchase*”, which requires that an actual gain should be made. The Appellant has in fact suffered a loss on sale of shares. The Respondent has not adverted to the fact that the Appellant has suffered overall loss of Rs.1.0 billion during the year ended 31/12/09 on said shares. It would, therefore, be unfair to direct the Appellant to tender notional gain calculated by the Respondent against loss suffered by the Appellant on Issuer Company shares during the relevant year. It is also pertinent to note that during the relevant year the stock market was closed by the stock exchanges by imposition of a ‘Floor’ on the prices and consequently the prices of equities including that of the Issuer Company shares held by the Appellant pursuant to underwriting commitment went down sharply for no fault of the Appellant. At that point in time, all efforts were directed to bring in fresh liquidity and every institution was approached to support the market. This vital fact has been ignored by the Respondent with reference to purchases made by the Appellant. Rule 16 of the Rules is not an appropriate method of calculation of tenderable gain. Furthermore, the Order of the Appellate Bench of the Commission in the matter of *Mrs. Nasreen Humayun Sheikh vs. Executive Director (Securities Department) (SECP), Islamabad (Appeal No. 49 of 2011)* maintained that, “...Rule 16 of the Rules is inconsistent with the statute (Ordinance) and contradicts the express provisions of the statute from which it derives authority...” The aforementioned judgment related to purchase and sale of securities between the period of 16/06/09 to 06/07/09, wherein, it



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was held, *“The Appellant cannot be burdened to submit gain, which never accrued to her in the first place.”* In light of the above, the Appellant cannot be burdened to submit notional gain against actual loss suffered by it during the relevant year. The transactions for investment was done in the ordinary course of business of the Appellant and nothing in the transactions suggest that the Appellant had entered into unjust or inequitable transactions or has acted in a manner which is in violation of duties and obligation of the Appellant to the Issuer Company. Reliance is also placed on the judgment of the Appellate Bench in the matter of *Ruhail Muhammad vs. Executive Director (SMD) (Appeal No. 46 of 2011)*, wherein, it was held that no monetary gain was made by the Appellant, and, therefore, the Impugned order was set aside in the particular case. In the instant case, the acquisition of shares was by default and not by choice. Furthermore, the sale of shares pursuant to the underwriting agreement was made to comply with the State Bank of Pakistan’s Regulations and subsequently specific instructions to the Appellant. The purchases were made from 21/05/09 to 18/06/09 as a regular market operation and the Appellant did not make any monetary gains from investment and its disposal.

- b) Section 224 of the Ordinance does not have a mechanical application. In the judgment of *The Securities and Exchange Commission of Pakistan through Commissioner versus First Capital Securities Corporation Limited and another in Civil Appeal No. 946/2005* cited at *PLD 2011 Supreme Court 778*, the Supreme Court of Pakistan, has enunciated and made explicit nexus between section 224 for disgorgement of gains made by the persons enunciated therein, and inside information. The Supreme Court in its analysis observed that while no rationale for the enactment of section 224 has been provided in the section, it can be inferred that the section is meant to penalize the enumerated persons therein from trading on the basis of inside information. The Supreme Court states as follows:

*“...There is a presumption, which is tacit, to the effect that the person has done something which is unjust or inequitable, or in violation of his duties and obligations to the company as a person falling within any one of the prohibited categories, and thus should be compelled to surrender his gains to the company...”* In paragraph 17 of the aforementioned Supreme Court judgment, the Supreme Court refers to the philosophical



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underpinnings and rationale behind the enactment of section 224 of the Ordinance, and articulates that the enumerated persons who carry out the trade by acting in an illegal or inequitable manner by relying on inside information could be directed to tender gain. Conclusively, the Respondent was bound by the aforementioned judgment of the Supreme Court and must administer section 224 in accordance with the principles laid down in the said case. In view of the above, only wrongful gain was to be tendered and the Respondent was required to determine if the alleged gain was wrongful. The Appellant had no way to get any inside information as it has no representative on the board of the Issuer Company. It was only due to underwriting commitment that the Appellant subscribed the shares of the Issuer Company and sustained heavy losses out of this transaction. The Respondent failed to prove that the alleged notional gain is “wrongful gain”. The gain would be unlawful or wrongful only when the same is actual and made on the basis of inside information as per binding interpretation of the Honourable Supreme Court. The Appellant has not acted in an inequitable or illegal manner while making transactions in the shares of Issuer Company. The Impugned Order, therefore, should be set aside on this ground alone being contrary to the interpretation of section 224 of the Ordinance by the Supreme Court.

- c) The Respondent failed to appreciate that section 224(4) of the Ordinance specifically provides that whoever fails to comply with or contravenes the provisions of inter alia section 224(1) of the Ordinance will be liable to be fined if the action has been committed “knowingly and willfully”. Therefore, the imposition of fine under section 224 of the Ordinance is subject to the determination that the default was made “willfully” and “knowingly”. It was held by the Appellate Bench of the Commission in Appeal No. 44 of 2014 in the matter of *Fauji Cement Company Limited vs. Director (MSRD)* that, “...Moreover, penalty can only be imposed under section 224(4) of the Ordinance if the failure to comply was willful which has not been established on the facts of the instant case....” The words “knowingly and willfully” require proof of knowledge, intention and willful action and reliance is placed on the judgment of *Bankat Lal Baduka v. State*, cited at *AIR 1965 Hyd. 49*. The Respondent failed to advert to the settled judicial interpretations of “knowingly and willfully”. Further, the Appellate Bench in the matter



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of Appeal No. 26 of 2015, *Next Capital Limited vs. Director/HOD Market Surveillance and Special Initiative Department*, held that the word “willful” can be used interchangeably with the word “intentional”. The above judgments of the Appellate Bench of the Commission are also applicable in the instant case and the Impugned Order is liable to be set aside on this ground. Reliance is also placed on the Lahore High Court judgment of *Pakistan Indus Promoters Limited vs. Monopoly Control Authority (1990)* cited at *CLC 1008*, wherein, it was held that, the word willful means, “...an act done intentionally, knowingly, or purposefully as distinct from the one done carelessly, thoughtlessly or inadvertently...” The penal provision i.e. section 224(4) of the Ordinance invoked by the Respondent in the SCN and Impugned Order has also recently been interpreted in the aforementioned judgment of the Supreme Court, wherein, it was clarified that since the penal provision is stringent in nature, in applying such a provision, the Commission should always bear in mind the importance of determining not merely a technical contravention but a substantial finding of guilt in relation to the person on whom the fine or penalty is being levied. Therefore, it is not sufficient on the basis of technical contravention to arbitrarily impose a fine of either in full amount or any other arbitrary chosen figure. In view of the above interpretation of the Supreme Court, determination of wrongful gain and substantial finding of guilt is necessary before ordering tendering of gain and imposition of any penalty. Furthermore, no fine has ever been imposed on the alleged defaulter for the contravention of section 224 of the Ordinance. The Impugned Order, therefore, is demonstrating inconsistency by imposing a fine of Rs.30,000 on the Appellant which is in violation of the Commission’s obligation “to achieve uniformity in how to perform those functions and exercise those powers” under section 20(6)(c) of the SECP Act. Furthermore, in the matter of *Crescent Bolts & Nuts Manufacturing Company vs. Registrar, Joint Stock Companies*, cited at *1959 PLD Karachi 32*, it was held that power which is vested in the Registrar for commencing a prosecution is not meant to be abused and inordinate delay in commencing prosecution was held to be a factor which could be helpful to the applicants for obtaining relief. The Respondent should have kept in view the fact that the Appellant is a well-reputed bank and is listed on the Stock Exchange. The Appellant has also won Bank of the Year 2012

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Award for promoting industry wide excellence in the global banking community. The Appellant firmly believes in conducting its affairs in accordance with the legal and ethical standards, therefore, its directors and management cannot think of violating the provisions of the Ordinance or any other law.

6. The Respondent rebutted the arguments of the Appellant as follows:-

a) Tenderable gain was re-calculated by the Respondent in light of the decision of the Appellate Bench of the Commission in the matter of *Mrs. Nasreen Humayun Sheikh vs. Executive Director (Securities Department) (SECP), Islamabad* (Appeal No. 49 of 2011), wherein, it was held that, "...Rule 16 of the Rules has not been framed within four corners of the provisions of section 224 of the Ordinance..." and gain was re-calculated by the Bench in the said judgment by adjusting loss incurred by the Appellant within the period of six months. In the instant case, tenderable gain was re-calculated in the manner developed by the Appellate Bench, as under:

Buy Date	Buy Quantity	Sale Date	Sale Quantity	Buy Quantity to be Matched	Sale Quantity to be Matched	Quantity Matched	Buy Rate	Sale Rate	Gain Per Share (Rs.)	Total Gain (Rs.)
							(Rs.)	(Rs.)		
21/5/2009	1,000,000	9/4/2009	1,405,500	1,000,000	1,405,500	1,000,000	6.49	6.97	0.48	480,000
2/6/2009	90,000	9/4/2009	1,405,500	90,000	405,500	90,000	6.47	6.97	0.5	45,000
3/6/2009	300,000	9/4/2009	1,405,500	300,000	315,500	300,000	6.47	6.97	0.5	150,000
3/6/2009	200,000	9/4/2009	1,405,500	200,000	15,500	15,500	6.45	6.97	0.52	8,060
3/6/2009	200,000	9/4/2009	600,000	184,500	600,000	184,500	6.45	7.01	0.56	103,320
10/6/2009	155,500	9/4/2009	600,000	155,500	415,500	155,500	6.6	7.01	0.41	63,755
11/6/2009	12,500	9/4/2009	600,000	12,500	260,000	12,500	6.6	7.01	0.41	5,125
17/6/2009	157,000	9/4/2009	600,000	157,000	247,500	157,000	6.74	7.01	0.27	42,390
18/6/2009	2,500	9/4/2009	600,000	2,500	90,500	2,500	6.7	7.01	0.31	775
18/6/2009	4,000	9/4/2009	600,000	4,000	88,000	4,000	6.74	7.01	0.27	1,080
18/6/2009	239,000	9/4/2009	600,000	239,000	84,000	84,000	6.75	7.01	0.26	21,840
18/6/2009	239,000	16/4/2009	155,000	155,000	155,000	155,000	6.75	6.87	0.12	18,600
Total Gain										939,945

On account of the aforesaid transactions, the Appellant in terms of Section 224(1) of the Ordinance read with Rule 16 of the Rules apparently made a gain of Rs.4,198,308.00/. The benefit of the revised manner approved by the Commission was passed on to the Appellant.



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The amount of tenderable gain, therefore, was reduced from Rs. 4,198,308/- to Rs. 939,945/. The tenderable gain accrued on transactions made for investment in ordinary course of business is not exempted from the recovery in the manner provided in section 224(2) of the Ordinance.

- b) In Paragraph 15 of the aforementioned judgment of the Supreme Court, the Honourable Apex Court has stated that; “...*there is a presumption, which is tacit, to the effect that the person has done something which is unjust or inequitable, or in violation of his duties and obligations to the company as a person falling within anyone of the prohibited categories, and thus should be compelled to surrender his gains to the company. Obviously, it would have been better if this presumption had been made explicit and not tacit but, accepting that the presumed legislative intent was the above, we can proceed further with our analysis...*” As per the observation made by the Supreme Court of Pakistan, section 224 of the Ordinance is based on the presumption that persons mentioned in the said section are privy to inside information, therefore, the gain accrued on purchase and sale or sale and purchase, within the period of six months is required to be tendered to the company and the Commission does not have entitlement thereto. Therefore, it is not required to be proved that the person has acted on the basis of inside information and the said section will mechanically apply. As in the instant case, if relevant purchase and sale or sale and purchase occur within the period of six months and yield gain, the beneficial owner/insider must tender the gain to the company even in the absence of any wrongdoing. In the instant case, gain was made by the Appellant on the sale and purchase of transactions even if the shares which were subscribed as a result of underwriting agreement are separated from the calculation of tenderable gain. Furthermore, in accordance with the aforementioned Supreme Court judgment, the Appellant was directed by the Respondent to tender the gain to the Issuer Company instead of the Commission.

- c) The Appellant was aware of its obligation of tendering of gain and it was deliberate negligence on their part. Reliance in this regard is placed on case titled *City Equitable Fire Insurance Co. Ltd Re, 1925 Ch 407* (also referred by the Appellate Bench of the



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Commission in Appeal No. 19/2009) cited at 2005 CLD 333, wherein, it was held, “...*That a default, in case of breach of duty, will be considered willful, even it arises out of being recklessly careless even though there may not be knowledge or intent...*” Furthermore, fine can be imposed on the Appellant in terms of section 224(4) of the Ordinance. There was no inordinate delay on part of the Respondent to initiate proceedings. The Appellant in response to letter dated 14/04/2011, filed the returns of beneficial ownership on 20/04/11 inter alia for the under reference changes in beneficial ownership. The reported sale and purchase transactions were examined in the light of provisions of Section 224(1) of the Ordinance. Therefore, in order to meet the ends of justice, the Respondent before initiation of recovery proceedings, decided to review the gain recovery procedure in the light of guidelines given by the Supreme Court in the aforesaid judgment.

7. We have heard the parties i.e. the Appellant and the Respondent. Reliance is placed on the Supreme Court of Pakistan judgment in the matter of *The Securities and Exchange Commission of Pakistan through Commissioner versus First Capital Securities Corporation Limited and another in Civil Appeal No. 946/2005* cited at *PLD 2011 Supreme Court 778*, wherein, it was held that in the event the gains were not tendered to the Company within a period of six months or the fact of gain was not brought in the notice of the Company and the Commission, the gains at all times shall remain the property of the Issuer Company. It was held that, “...the entitlement of SECP to recover the amount in question from the company would be treated as being in the nature of an enforcement mechanism to ensure that the wrongful gains do not remain with the person who has violated the section but are transferred to or for the benefit of the Company...”

In view of the above, it is pertinent to note that the Commission has ample powers under section 224 of the Ordinance to take adverse action against any person found in contravention of section 224 of the Ordinance. The Appellant has argued that no gain was made and the Appellant actually suffered a notional loss and section 224 of the Ordinance requires proof of malafide based on inside information before the relevant provisions of section 224 will apply



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to the facts of the instant case and any contravention was not willful; therefore, fine should not have been imposed. Furthermore, the Appellant argued that if the beneficial owner acted bonafide then in such a scenario the beneficial owner can retain the gains instead of surrendering them to the Company. The Respondent has rebutted the arguments by stating that section 224 of the Ordinance is applied on a presumption that the person was privy to inside information, therefore, malafide is not required to be proved and the said section will automatically apply if the gains are not tendered to the Company within six months. Furthermore, the Respondent argued that the gain was re-calculated in accordance with the judgment of the Appellate Bench of the Commission in the matter of *Mrs. Nasreen Humayun Sheikh vs. Executive Director (Securities Department) (SECP), Islamabad* (Appeal No. 49 of 2011) and the amount of tenderable gain was reduced from Rs.4,198,308/- to Rs.939,945/-.

8. We have perused Paragraph 15 of the aforementioned Supreme Court judgment which states that, *“Although no direct answer can reasonably be inferred, it is clear that this section proceeds on the tacit assumption that the person in question was privy to inside information and, taking advantage of the same, obtained a gain to which accordingly he was morally not entitled and thus was required it to surrender it to the company. In other words, there is a presumption, which is tacit, to the effect that the person has done something which is just or inequitable, or in violation of his duties and obligations to the company as a person falling within any of the prohibited categories, and thus should be compelled to surrender his gains to the company...”*. We concur with the Respondent that as per the observation made by the Supreme Court, section 224 of the Ordinance proceeds on the tacit presumption that the person making the gains is privy to inside information as it is difficult to establish whether the transactions are bona fide or not and that such gains must be tendered to the company. The aforementioned judgment of the Supreme Court has spelled out the purpose of section 224 of the Ordinance which states that that the gains made shall at all times remain the property of the company and the Commission has no entitlement thereto. In the instant case, the transactions were done in the ordinary course of business, however, tenderable gains were made on the sale and purchase transactions in the ordinary shares of the Issuer Company within the period of



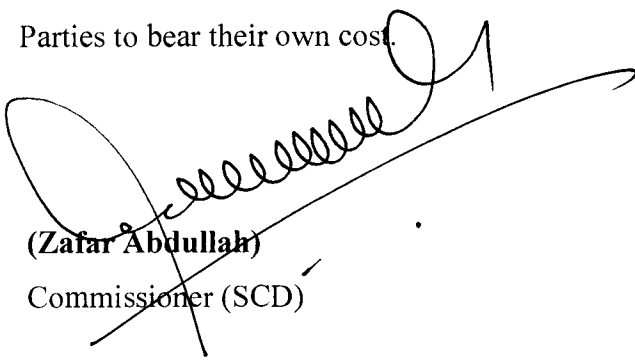
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less than six months, therefore, any gains made by the Appellant shall vest in the Issuer Company.

9. Section 224(4) of the Ordinance provides that, “*Whoever knowingly and willfully contravenes or otherwise fails to comply with any provision of section 222, 223 and or section 224 shall be liable to a fine which may extend to thirty thousand rupees...*” We place our reliance once again on the aforementioned judgment of the Supreme Court, wherein, it was clarified that since the penal provision is stringent in nature, in applying such a provision, there has to be a substantial finding of guilt in relation to the person on whom the fine or penalty is being levied. In the instant case, the Appellant is a well-reputed bank and has normally ensured compliance with the provisions of the Ordinance and the law. The contravention of section 224 of the Ordinance, therefore, cannot be considered to be a willful or negligent act on part of the Appellant.

10. In view of the foregoing, the Impugned Order is set aside to the extent of fine. The amount of tenderable gain of Rs.939,945/-, however, must be tendered to the Issuer Company.

11. Parties to bear their own cost.

  
(Zafar Abdullah)  
Commissioner (SCD)

  
(Tahir Mahmood)  
Commissioner (CLD)

Announced on: **24 FEB 2017**