



Securities and Exchange Commission of Pakistan

BEFORE THE APPELLATE BENCH

In the matter of

Appeal No. 63 of 2023

Mr. Adnan Afridi

...Appellant

versus

Director/ Head of Department, Adjudication-I, SECP, Islamabad.

...Respondent

Date of hearing:

February 6, 2025

Present:

For the Appellant:

1. Mr. Muhammad Masood Khan, Advocate Supreme Court
2. Mr. Saad M. Hashmi, Advocate Supreme Court
3. Mr. Muhammad Zeeshan Khan, Advocate
4. Mr. Adnan Afridi
5. Mr. Najam Ali

For the Respondents:

1. Mr. Sohail Qadri, Director, Adjudication-I, SECP
2. Mr. Mehboob Ahmed, Additional Director, Adjudication-I, SECP
3. Mr. Muhammad Akram Farooka, Assistant Director, Adjudication-I, SECP

ORDER

1. This Order shall dispose of Appeal No. 63 of 2023 filed by Mr. Adnan Afridi (the "Appellant") under Section 33 of the Securities and Exchange Commission of Pakistan Act, 1997 (the "SECP Act") against



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the Order dated April 11, 2023 (the “Impugned Order”) passed by the Director/HOD, Adjudication-I, Adjudication Division, SECP (the “Respondent”) under Section 106(2)(a) of the Securities Act, 2015 (the “Act”).

2. Brief facts of the case are that Next Capital Limited (the “Company”) is a company listed on the Pakistan Stock Exchange Limited (the “PSX”). That the Appellant was a shareholder and an active trader in the shares of the Company since 2016. It had been revealed from the record maintained at the Securities and Exchange Commission of Pakistan (the “Commission”) that the Appellant, by virtue of acquiring 10.96% shares, became a substantial shareholder of the Company on April 12, 2018 and within a period of less than six months i.e. from May 16, 2018 to June 20, 2018 (the “Period”), executed the following sale and purchase transactions in shares of the Company:

Date	Shares Purchased	Shares Sold	Rate
May 16, 2018	744,500	-	9.56
May 16, 2018	500	-	9.99
May 16, 2018	3,000	-	10.00
May 18, 2018	1000	-	10.00
May 20, 2018	-	425,000	10.99

3. As a result of the aforesaid transactions, a tenderable gain amounting to Rs. 607,750/- accrued to the Appellant. The Appellant did not report the gain that had been made during the Period to the Commission that was required to be reported via Form-7, within seven (07) days of the accrual of the gain i.e. latest by June 27, 2018, as required under Section 105 of the Act. Also, the Appellant did not tender the gain made during the Period, within six months of the accrual of gain i.e. by December 19, 2018, to the Commission for onward credit to the Federal Consolidated Fund.
4. That *Prima-facie* the actions/omissions of the Appellant were in contravention of Section 104 and 105 of the Act. A Show-Cause Notice dated October 05, 2020 (the “SCN”) was issued to the Appellant. The Appellant submitted a written reply to the SCN vide letter dated October 26, 2020. First hearing in the matter was held on March 05, 2021. The Appellant’s counsel furnished additional submissions vide letter dated March 15, 2021 and also requested for re-hearing of the case for further clarification,



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which was held on February 8, 2023. Based on the submissions and facts on record, the Respondent concluded the SCN proceedings by directing the Appellant to report and tender the gain amounting to Rs. 607,750/- with the Commission and imposed a penalty of Rs. 500,000/- on the Appellant.

5. The Appellant has preferred this appeal on the grounds that the Impugned Order is 'harsh' and has been passed without considering the facts of the matter. The Appellant has contended that he has not made any gain for the purpose of Sections 104 and 105 of the Act or Reporting and Disclosure (of Shareholding by Directors, Executive Officers and Substantial Shareholders in Listed Companies) Regulations, 2015 (the "Regulations"). The Appellant's arguments in support of his contention are summarized below:

- a. Computation of gain for the purpose of Sections 104 and 105 of the Act requires two important determinations.
 - i. Inventory accounting method.
 - ii. Holding period.
- b. As the securities of the same class and company are fungible, there is a need to follow some inventory accounting method to determine the gain. FIRST IN FIRST OUT (FIFO) method of inventory accounting should be used.
- c. The holding period for computation of gain should begin from the date of purchase of the oldest security in the portfolio.
- d. This view is supported by the following arguments:
 - i. For computing capital gains tax on securities, the Federal Board of Revenue (FBR) has prescribed "First In and First Out (FIFO)" method which is a sequential inventory accounting method to determine the capital gain on trading of securities. This method is also recognized/ prescribed in the regulations of National Clearing Company of Pakistan Limited (NCCPL).
 - ii. The Appellant Bench has, in an earlier order in Appeal No. 47 of 2011, decided that "gain is to be calculated by matching the purchase and sale transactions in a sequential manner rather than by applying lowest in highest out manner". The same principle should be followed in the instant case as well.
- e. The Appellant had initially purchased a significant quantity of shares in this company during the year 2016 and later purchased more shares to eventually become a substantial shareholder



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in April 2018. Afterwards, he purchased another 749,000 shares and sold 425,000 shares during the period from May 16, 2018 to June 20, 2018. If FIRST IN FIRST OUT (FIFO) method is applied to compute the gain on sale of these shares, and it is assumed that the oldest 425,000 shares in the Appellant's inventory were sold on June 20, 2018, the holding period for these shares works out to be more than six months and Sections 104 and 105 of the Act do not apply.

- f. The Respondent has erred by computing the gain by looking at the purchases and sales of shares during the period from May 16, 2018 to June 20, 2018 and computing the gain on sale of 425,000 shares by applying an average purchase price of Rs 9.56 per share and average sale price of Rs 10.99 per share resulting in a gain of Rs 1.43 per share and Rs 607,750 in total.
- g. The Appellant has relied on a judgement rendered in the matter of SECP versus First Capital Securities Corporation rendered by the Hon'ble Supreme Court of Pakistan reported as PLD 2011 Supreme Court 778. That in terms of the said judgement the gain will remain under all circumstances the property of the Company and SECP or the State has no inherent power to confiscate asset or property, and ownership will always vest in the Company in similar circumstances.
- h. The Appellant had acted in good faith based on his understanding that gain on sale of securities was to be computed according to FIRST IN FIRST OUT method of inventory accounting and his holding period was much longer than six months.
- i. If the Appellant had known that gain on trading of securities would be computed by looking only at the purchases and sales during a six-month period, he would have waited longer before selling the shares purchased by him during May 2018.

6. The Respondent contended as follows:

- a. The Impugned Order accurately computes the tenderable gain based on the sale and purchase transactions executed by the Appellant within a period of less than six (06) months.
- b. Sections 104 and 105 of the Act are applicable in the instant case as the Appellant is a substantial shareholder of the Company who has made a gain through purchase and sale of shares during a six-month period.



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- c. Sections 104 and 105 have a specific context and purpose. These sections aim to discourage substantial shareholders of a company from making gains through short-term trading in the shares of that company.
- d. Regulation 4(2)(a) and (b) of the Regulations categorically requires matching of purchase and sales of securities by substantial shareholders during any six-month period in a chronological order.
- e. Application of FIFO method on entire inventory of shares belonging to a substantial shareholder, without regard to a particular six-month period makes these sections and the regulations largely irrelevant. If this is allowed, substantial shareholders can continue to purchase and sell shares within six-month periods and claim that the shares sold during a particular six-month period are the ones purchased before that six-month period and that the shares purchased during that six-month period have not yet been sold. It will thus defeat/compromise the very purpose of these provisions of law.
- f. The appropriate way to compute trading gains made by a substantial shareholder for the purpose of these sections is to see whether both trading legs (purchase and sale of shares) exist during any six-month period and compute the gain by matching the shares bought or sold in a chronological order during that particular six-month period.
- g. The aforementioned treatment has exactly been followed in this case. The tenderable gain has been calculated by matching the purchases and sales in a chronological order during the period from May to June 2018.
- h. The Appellant became a substantial shareholder of the Company on April 12, 2018. After becoming a substantial shareholder, the Appellant purchased and sold additional shares and made a gain of Rs 607,750 by June 20, 2018.
- i. The reliance placed by the Appellant on a judgment passed by the Honorable Supreme Court of Pakistan in PLD 2011 SC 778 is not relevant to the facts of the case.
- j. Similarly, the reliance placed on FBR's approach towards computation of gains for taxation purposes is not relevant to the computation of gains under Sections 104 and 105 of the Act because the context and purpose of computation of gains is very different in the two situations.



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7. The Appellate Bench (the "Bench") has heard the parties and perused the record and relevant provisions of the law, the Act and the Regulations. Before proceeding to decide the Appeal, the Bench deems it useful to summarize and review the relevant legal provisions:

- a. Section 104 of the Act mandates reporting of any gain accrued from the sale and purchase of securities by certain persons within six months, while Section 105 of the Act requires the tendering of such gain to the SECP for onward deposit in the Federal Consolidated Fund.
- b. Regulation 4(2)(b) of the Regulations lays down the mechanism for computation of gain for this purpose, which is reproduced as under:

"Computation of Gain under Section 104 of the Act: (1) Any gain made from the purchase and sale, or sale and purchase, of any beneficially owned listed equity securities within a period of less than six months shall be reported to the Commission in Form 7 within seven days of accrual and shall be tendered to the Commission for onward credit to the Federal Consolidated Fund.

(2) The gain referred to under sub-regulation (1) shall be computed in the following manner

(a) by matching the transaction in chronological order and the recoverable amount shall be calculated with respect to every individual transaction by reference to the difference between the sale price and the purchase price, made within the period of less than six months;

Explanation: For the purpose of this clause, the term "gain" includes profit made by purchase and sale or sale and purchase of same class of securities within the period of six months. (b) the purchases and sales shall be matched as aforesaid so long as the securities involved in the purchase and sale are of the same class and of the same listed company and for this purpose the shares shall be deemed as fungibles "

8. The Bench's observations, opinions and conclusions are as under:

- a. It is important to understand the context and purpose of Sections 104 and 105 of the Act, and the Regulation 4(2)(a) of the Regulations. These legal provisions aim to deter and discourage substantial shareholders of listed companies from making gains through short-term trading in the securities of those companies.
- b. Section 104 mentions gains through PURCHASE AND SALE as well as through SALE AND PURCHASE of securities. This implies that the purchase may not necessarily precede the sale



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of securities; it may as well be the other way around. A substantial shareholder may even sell the securities initially (either out of his existing inventory or through a short sale) and later on purchase the securities to make a gain which falls under the ambit of Sections 104 and 105 of the Act.

- c. In order to serve the purpose of these legal provisions, the gains must be computed over a particular six-month period in which both trading legs, i.e. purchase and sale of shares, exist.
 - d. The gains need to be computed in a chronological order by matching the purchases and sales or sales and purchases made within a six-month period, in a sequential order. Both FIRST IN FIRST OUT (FIFO) and LAST IN FIRST OUT (LIFO) follow a particular chronological order. However, as the intended purpose is to deter and discourage the substantial shareholders from making short-term trading gains in the shares of the company they have substantial shareholding in, the Bench considers it appropriate to compute the gains by using both the methods and using the figure which is higher. In the instant case, the Respondent has computed the gain using FIFO method which has resulted in a slightly higher gain than the LIFO method. The Bench endorses the amount of trading gain as computed by the Respondent.
 - e. Computation of capital gains for the purpose of taxation has a different context and use of a particular inventory accounting method or holding period by the Federal Board of Revenue is not relevant to the computation of gain, inventory accounting method and holding period for the purpose of sections 104 and 105 of the Act.
 - f. The Respondent has correctly computed the tenderable gain in this case. The contentions and arguments of the Appellant are not tenable.
 - g. As the Appellant has stated that he acted in good faith, it is appropriate to give him an opportunity to deposit the tenderable gain in the Federal Consolidated Fund. Penalty should be applicable only if the Appellant fails to deposit the tenderable gain within a reasonable time.
9. Accordingly, the Bench directs the Appellant to deposit the tenderable gain amounting to Rs. 607,750/- with the Commission within 30 days from the date of issuance of this order. Failure to comply with this direction shall render the Appellant liable to also pay the penalty amounting to Rs. 500,000/-.



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10. In view of the above, the instant Appeal is disposed of on above terms without any order as to costs.

(Abdul Rehman Warraich)

Commissioner

(Zeeshan Rehman Khattak)

Commissioner

Announced on:

05 JUN 2025