



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department

**Before the Director/HOD (MSRD)**

In the matter of recovery of gain made in terms of Section 224(1) of the Companies Ordinance, 1984 by Amir Fine (Exports) Limited, a beneficial owner of more than ten percent equity securities of Fazal Cloth Mills Limited

Date of Hearing:

June 13, 2013

Present at Hearing:

- |       |   |  |
|-------|---|--|
| (i)   | Representing the Fazal Cloth Mills Limited        | Mr. M.D. Kanwar,<br>Company Secretary<br>Fazal Cloth Mills Limited |
| (ii)  | Representing the Amir Fine Exports (Pvt.) Limited | Mr. M.D. Kanwar,<br>Company Secretary<br>Fazal Cloth Mills Limited |
| (iii) | Assisting the Director/HOD (MSRD):                | Mr. Muhammad Farooq,<br>Joint Director,<br>SECP                    |

**Order**

This Order will dispose of the proceedings initiated through the following two Show Cause Notices (**Notices**):-

- No. S.M. (B.O)222/4(593)2001-228 dated 16/04/2013, issued under Section 224(2) and Section 224(4) of the Companies Ordinance, 1984 (**Ordinance**) to Fazal Cloth Mills Limited (**Respondent-I**) a issuer company in the matter of Amir Fine Exports (Pvt.) Limited (**Respondent-II**).
- No. S.M. (B.O)222/4(593)2001-229 dated 16/04/2013, issued under Section 224(1) and Section 224(4) of the Ordinance to Respondent-II, a beneficial owner of more than ten percent ordinary shares of the Respondent-I.





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

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2. The facts of the matter leading up to aforesaid Notices are that the Respondent-I is a public listed company. While, the Respondent-II is a beneficial owner of more than ten percent ordinary shares of the Respondent-I. The Respondent-II has made the following purchase and sale transactions in ordinary shares of the Respondent-I, within the period of less than six months:-

Sr. No.	Date	No. of Shares	Description	Rate (Rs.)
1	February 12, 2010	648,867	Purchase	35.04
2	March 31, 2010	100,000	Purchase	35.04
3	May 24, 2010	374,433	Sale	36.00
4	July 13, 2010	346	Purchase	46.00
5	September 7, 2010	617	Purchase	45.00
6	October 12, 2010	140,663	Purchase	65.00
7	October 13, 2010	140,663	Sale	65.00
8	November 3, 2010	3,050	Purchase	51.53
9	November 4, 2010	139,100	Purchase	54.00
10	November 8, 2010	1,500	Purchase	54.25
11	December 3, 2010	691	Purchase	48.72
12	December 6, 2010	700	Purchase	51.25
13	December 7, 2010	609	Purchase	58.90
14	December 8, 2010	900	Purchase	56.59
15	December 9, 2010	900	Purchase	59.51
16	December 10, 2010	600	Purchase	62.48
17	December 13, 2010	1,100	Purchase	65.50
18	February 8, 2011	1,069	Purchase	58.96

3. On account of the aforesaid transactions, the Respondent-II in terms of Section 224(1) of the Ordinance read with Rule 16 of the Companies (General Provisions and Forms) Rules, 1985 (**Rules**) has apparently made gain of Rs. 1,928,177/- (Rupees one million nine hundred twenty eight thousand one hundred seventy-seven only).

4. Section 224 of the Ordinance provides that where *inter alia* a more than ten percent beneficial owner of listed equity securities makes 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



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SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

\*\*\*

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.

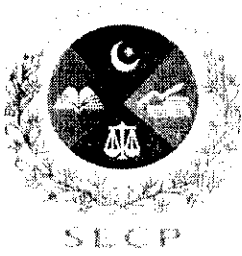
5. In the instant case, as per record of this office, neither the accrual of the aforesaid gain was reported in Part-D of the prescribed returns of beneficial ownership filed with this Commission on Form 32, nor the same was tendered to Respondent-I by the Respondent-II. Similarly, the Respondent-I did not raise demand for recovery of the aforesaid gain, within the stipulated time limit. The Respondent-I and Respondent-II were, therefore, asked (separately) vide letters dated 07/01/2013 to furnish *inter alia* documentary evidences, if the legal obligations arose under Section 224 of the Ordinance has already been discharged. In response, the Company Secretary of the Respondent-II vide letter dated 23/01/2013 stated that no gain was made as shares were sold out of previous shareholding. While, the Company Secretary of the Respondent-I vide letter dated 23/01/2013 instead of offering his comments regarding the matter submitted a copy of the aforesaid letter of the Respondent-II, addressed to the Commission.

6. The aforesaid replies received from the Respondent-I and Respondent-II were examined in the light of provisions of Section 224 of the Ordinance and Rule 16 of the Rules and were not found convincing. Thus, the above mentioned Notices were served under Section 224 of the Ordinance, wherein:-

- a) The Respondent-I was called upon to show cause in writing along with documentary evidence, if any, as to why action may not be taken against it under Section 224(4) of the Ordinance for committing of violation of Section 224(2) of the Ordinance, as it failed to raise demand for recovery of the aforesaid gain, within the stipulated time limit.
- b) The Respondent-II was called upon to show cause in writing along with documentary evidence, if any, as to why:-
  - (i) Action may not be taken against it under Section 224(4) of the Ordinance for non-reporting and non-tendering of gain within the stipulated time period, in violation of Section 224(1) of the Ordinance.
  - (ii) The amount of aforementioned gain may not now be recovered from it in the manner provided in Section 224(2) of the Ordinance.

7. Furthermore, in order to provide an opportunity of being heard in person, hearing in the matter was fixed for 02/05/2013 at the Commission's Head Office, Islamabad, which on the request of the Respondent-II was adjourned and rescheduled for 13/06/2013. On the said date, Mr. M.D. Kanwar ("**Authorized Representative**") appeared on behalf of the Respondent-I as well as for Respondent-II. He also filed two separate written responses to the aforesaid Notices,





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)  
\*\*\*

but both responses were signed by Mr. Rehman Naseem, a director of the Respondent-I as well as the Respondent-II. The submissions made by the Respondents in writing as well verbally by the Authorized Representative during the course of hearing be summarized as under:-

**(i) Submissions made on behalf of Respondent-II:-**

- a) *the issue has been framed on an inadvertent understanding of the facts of company's case as the instances of sales identified in the Notice were effected by the company out of stock of shares held by the company for over six months period i.e. aggregate 2,967,943 shares of the Respondent-I held by the company from March 20, 2006.*
- b) *The core business activity of the company is to trade in shares and for recording transactions in shares company has employed a recognized accounting method of 'first-in-first out'.*
- c) *Accordingly, the intended action of enforcing provisions of section 224(2) as well as 224(4) of the Ordinance is not warranted, it is therefore requested that the notice may be filed without drawing any adverse inference.*

**(ii) Submissions made on behalf of Respondent-I:-**

- a) *We have enquired the matter from the officials of Respondent-II about the issue raised by Commission, as to the violation of provisions of section 224(1) of the Ordinance in respect of alleged gain.*
- b) *We have been informed by the Respondent-II that the issue has been raised on certain inadvertent understanding of the case and that in this connection, the Respondent-II has furnished a reply to Show Cause Notice on this matter to the Commission.*
- c) *We request that such response explaining the position that no violation of provisions of section 224(1) of the Ordinance were committed by the Respondent-II that may lead to invocation of provisions of section 224(2) & 224(4) of the Ordinance, is also considered in the present matter. Copy of Respondent-II's letter dated June 12, 2013 is enclosed herewith for records and perusal.*

8. I have thoroughly reviewed the submissions submitted on behalf of the Respondent-I as well as Respondent-II and in order to address the issue, the following questions have been framed:-





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

\*\*\*

- (i) Has the Respondent-II made any gain by purchase and sale transactions mentioned in the Notices as well as para 2 of this Order?
- (ii) Has the Respondent-II failed to discharge obligations arising under Section 224(1) of the Ordinance?
- (iii) Has the Respondent-I failed to discharge obligation arising under Section 224(2) of the Ordinance?

9. I have examined the above formulated issues/questions in the light of prevailing law and rules on the subject matter and my findings in this regard are as under:-

- (a) **The issue of accrual of gain:-** Concerning the issue of accrual of the tenderable gain, the main plea is that *the Respondent-II by adopting FIFO basis sold (out of its previous holding) 374,433 and 140,663 shares respectively on 24/04/2010 and 13/10/2010 and claimed that "the under discussion purchase and sale transactions do not attract the provisions of Section 224 of the Ordinance because the purchased and sold shares were not same".*

The aforesaid assertion has been considered and observed that the Respondent-II has divided its shareholding of same class of equity/shares into two groups (i.e. previously held and newly purchased shares) and is of the view that Section 224(1) of the Ordinance would only be attracted as and when particulars shares of the same class are purchased and sold or sold and purchased. To ascertain the legitimacy of the contention, I have consulted the prevailing law and rules on the subject matter. In my opinion this aspect of the issue has visibly been narrated in Section 224(1) of the Ordinance and Rule 16 of the Rules. In order to elucidate the position, it is useful to reproduce Section 224(1) of the Ordinance here:

*"Where any director, chief executive, managing agent, chief accountant, secretary or auditor of a listed company or any person who is directly or indirectly the beneficial owner of more than ten per cent of its listed **equity securities** makes any gain by the purchase and sale, or the sale and purchase, of **any such security** within a period of less than six months, such director, chief executive, managing agent, chief accountant, secretary or auditor or person who is beneficial owner shall make a report and tender the amount of such gain to the company and simultaneously send an intimation to this effect to the registrar and the Commission"*

I am of the view that the phrases "equity securities" and "any such security" appear in the Section have very much significance here. The words "equity securities" signifies





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

\*\*\*

that a beneficial owner may own simultaneously more than one class of shares, while the word "such security" symbolizes here security of same class. Furthermore, noticeably the word "any" appears before the words "such security". Thus, it is emphasized here that the law uses word "any" instead of the word "particular". Hence, the tenderable gain will arise through purchase and sale or sale and purchase of "any security of same class" instead of "particular security of same class, by a beneficial owner of a listed company. This suggests that securities of same class of a same listed company are interchangeable/ fungible. And this concept has explicitly been expressed in Rule 16(1)(b) of the Rules, which states that;-

*"-----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.*

It is further pointed out that the concept "shares of same class are fungible in nature" is not a new concept, as it is prevailing since the promulgation of Securities and Exchange Ordinance, 1969 ("SE Ordinance"), when the subject matter of trading by officers and principal shareholders of listed companies was monitored under SE Ordinance. The issue was elaborated in Circular No. 2 of 1971 dated 26/06/1971 of the then Securities and Exchange Authority of Pakistan. The said Circular inter alia states:-

*"A view has been expressed that for the purpose of matching sales and purchases, the securities sold should be same as were purchased during the period. This view is not correct. Securities are fungible and it would, therefore, not be necessary ever to show that the particular security which is sold is the one which was purchased. Purchases and sales would be match-able so long as the securities involved in the purchase and sale are of the same class."*

The aforementioned discussion clearly states that shares of same class are identical and substitutable. Thus, the Respondent-II has misconceived and misinterpreted the words "purchase and sale or sale and purchase" appear in Section 224 of the Ordinance, by arguing that purchased and sold shares were not same.

It is worth mentioning that the under reference transactions have admittedly been made by the Respondent-II in same class of shares i.e. ordinary shares of the Respondent-I as well as were made within the period of less than six months. Thus, the case meets all the prerequisites, laid down in in Section 224(1) of the Ordinance.

In view of the foregoing, I am of the considered opinion that the contentions presented on behalf of the Respondent-II regarding non-accrual of the gain do not have any merit and substance. Tenderable gain has been accrued out of the aforesaid





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

\*\*\*

purchase and sale transactions. Amount of gain in the aforesaid Notices was calculated in the manner prescribed in Rule 16 of the Rules. Since, neither the Respondent-II tendered the gain to the Respondent-I nor the Respondent-I raised demand for its recovery, within the stipulated time limit, therefore, the gain has vested to the Commission, for the purposes of enforcement mechanism.

- (b) **The issue of violation committed by the Respondent-I:** The Authorized Representative argued that since Respondent-II did not make any gain on account of under discussion transactions, therefore, there was no legal obligation required to be discharged on the part of Respondent-I, resultantly, no violation has been committed by the Respondent-I. I have considered the arguments and in this regard attention is invited to Section 224(2) of the Ordinance provides that:-

*Where a director, chief executive, managing agent, chief accountant, secretary, auditor or person who is beneficial owner as aforesaid fails or neglects to tender, or the company fails to recover, any such gain as is mentioned in sub-section (1) within a period of six months after its accrual, or within sixty days of a demand therefor, 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.*

As aforesaid, gain was accrued to the Respondent-II, but it failed to tender the gain to the Respondent-I, within the prescribed time limit, therefore, the Respondent-I pursuant to Section 224(2) of the Ordinance was required to raise demand for recovery of the said gain, under intimation to the Commission, within the stipulated time limited. The correspondence exchanged with the Respondent-I reveals that it did not raise demand for recovery of the gain, until the issue was pointed out by the Commission Thus, I am of the view that the Respondent-I has failed to discharge its obligation arose under Section 224(2) of the Ordinance. The said contravention prima facie attracts penal provisions contain in Section 224(4) of the Ordinance.

- (c) **The issue of violation committed by Respondent-II:-** The Authorized Representative stated that since no gain was accrued to the Respondent-II, therefore, no violation of Section 224 of the Ordinance has been committed. I have considered the plea, but did not find it substantiated, because, it is evident from the foregoing discussion that the Respondent-II has made gain on account of purchase and sale of same class of shares of the Respondent-I, within the period of less than six months. The Respondent-II was, therefore, required pursuant to Section 224(1) of the Ordinance to report accrual of the said gain and tender the same to the Respondent-I, under intimation to the Commission, within the stipulated period. But, it has neither reported accrual of the aforesaid gain nor has tendered it to the Respondent-I. Thus; I





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

\*\*\*

am of the view that the Respondent-II has failed to discharge its obligation arising under Section 224(1) of the Ordinance. The said contravention *prima facie* attracts penal provisions contained in Section 224(4) of the Ordinance, which provides as under:-

*“Whoever knowingly and wilfully contravenes or otherwise fails to comply with any provision of section 222, section 223 or section 224 shall be liable to a fine which may extend to thirty thousand rupees and in the case of a continuing contravention, non-compliance or default to a further fine which may extend to one thousand rupees for every day after the first during which such contravention, non-compliance or default continues”.*

- (d) It is pertinent to mention here that while interpreting the word “vest” appears in Section 224 of the Ordinance, the Supreme Court of Pakistan in Civil Appeal No. 946/2005 held that the gain will remain under all circumstances property of the company. Furthermore, the entitlement of SECP to recover the amount in question from the company would be treated as being in nature of an enforcement mechanism to ensure that the wrongful gains do not remain with person who has violated the Section but are transferred to for the benefit of the company. In addition to above, it is pointed out that the Respondent-II was required to make payment of tenderable gain to the Respondent-I, which in terms of abovementioned judgment of the Supreme Court of Pakistan was supposed to be utilized for the benefit of the shareholders of the Respondent-I. Section 224(2) of the Ordinance supposes that a listed issuer/company will play a proactive role in monitoring the trading activities of its beneficial owners/officers/directors, which will enable it to raise demand for recovery of gain, within the stipulated time limit. The correspondence exchanged with Respondent-I reveals that the Respondent-I has failed to perform proactive role in monitoring the trading activities of the Respondent-II, because it did not take up the issue with the Respondent-II, until the matter was pointed out by the Commission.
- (e) It has been noticed that written replies to both aforesaid Notices have been submitted by Mr. Rehman Naseem (who is simultaneously on the Board of Directors of the Respondent-I and Respondent-II) Furthermore, Mr. M.D. Khawar was authorized by both Respondents to attend the personal hearing on their behalf. These instances may signify rising of conflict of interest, as in the instant matter interest of the both entities was divergent to each other. The issue of conflict of interest was also taken up with the Authorized Representative who stated that the Respondent-II is a group company of the Respondent-I and being an employee his portfolio is looking after the corporate affairs of the group companies, therefore, he has been authorized to represent both Respondents in personal hearing. In this regard, I am of the view that in case of accrual of tenderable gain, the interest of the beneficial owner and the issuer company







SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

\*\*\*

are opposite to each other, therefore, it would be better to make such arrangements by listed companies that trading activities of the directors/officers/directors of the company may be monitored effectively, independently in the best interest of issuer company and its shareholders specifically small shareholders.

10. Prior to conclude the findings, it seems necessitated to mention the following:-
- (a) before announcing decision in the instant matter, the Appellate Bench of the Commission decided Appeal No. 49/2011 (filed by Mrs. Nasreen Humayun Shaikh, a beneficial owner of Azgard Nine Limited) vide Order dated 19/06/2013 stated that *“rule 16 of Rules has not been framed within the four corners of section 224 of the Ordinance. We are aided by the judgment in the matter of Messrs Honda Atlas Car (Pakistan), Ltd., Lahore versus C.I.T, Legal Division, R. T. Lahore”*. The Bench further held that *“the rule 16 of the Rules is inconsistent with the statute and contradicts the express provisions of the statute from which it derives authority. The Appellant cannot be burdened to submit a gain, which never accrued to her in first place”*. Besides, the Appellant Bench in the said Appeal calculated the amount of gain by matching the purchase and sale transactions in sequential manner rather than by applying lowest in highest out manner prescribed in Rule 16 of the Rules.
- (b) subsequent to the said judgment of the Appellate Bench, decision in the instant case was held because the amount of tenderable gain in the instant matter (at the time of issuance of Notices) was calculated pursuant to the manner provided in Rule 16(2) of the Rules, which has been declared *“inconsistent with the statute”* by Appellate Bench of the Commission. After seeking views of the Legislation, Litigation and General Counsel Department of the Commission, the issue of deviation of the manner of calculation of gain used by the Appellate Bench with the method of calculation prescribed in Rule 16 of the Rule was placed before Commission. The Commission considered the matter and *inter alia* decided in its seventh meeting held on 25/05/2014 that the cases of recovery of gain be disposed of in the light of judgment made by the Appellate Bench of the Commission as well as Supreme Court of Pakistan.

11. Pursuant to the aforementioned decision of the Commission, the amount of tenderable gain in the instant matter has been recalculated as under, in the light of manner approved by the Commission:-



9



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

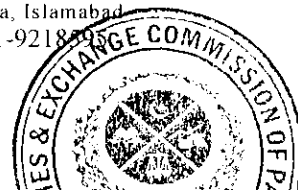
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Buy Date	Buy Quantity	Sale Date	Sale Quantity	buy Quantity to be Matched	Sale Quantity to be Matched	Quantity Matched	Buy Rate (Rs.)	Sale Rate (Rs.)	Gain Per Share (Rs.)	Total Gain (Rs.)	
12-Feb-10	648,867	24-May-10	374,433	648,867	374,433	374,433	35.04	36	0.96	359,456	
13-Jul-10	346	13-Oct-10	140,663	346	140663	346	46	65	19	6,574	
7-Sep-10	617	13-Oct-10	140,663	617	140317	617	45	65	20	12,340	
12-Oct-10	140,663	13-Oct-10	140,663	140663	139700	139700	65	65	0	0	
Total tenderable gain											378,370/-

12. In pursuance of the decision of the Commission, the benefit of the manner approved by the Commission has been passed on in the instant matter, resultantly, the amount of tenderable has been reduced from Rs. 1,928,177/- to Rs 378,370/-.

13. It is evident from the foregoing discussion that the Respondent-II has made gain on account of the aforesaid purchase and sale transactions and the arguments presented by the Respondent-I and Respondent-II do not have any merit and substance, therefore, the request to withdraw the Notices is rejected and matter is disposed of as under:-

- a) The amount of gain is still with Respondent-II, therefore, as provided in Section 222(2) of the Ordinance the gain has vested to the Commission. Since Supreme Court of Pakistan in aforementioned judgment held that "the gain will remain under all circumstances property of the company". While, the entitlement of SECP to recover the amount in question from the company would be treated as being in nature of an enforcement mechanism to ensure that the wrongful gains do not remain with person who has violated the section, but are transferred for the benefit of the company. Since ultimately, the amount of gain is required to be transferred to the Respondent-I, therefore, in order to make the process of recovery of gain simple, the Respondent-II is hereby directed to tender Rs 378,370/- to Respondent-I, within 30 days of the Issue of this Order and provide a copy of its bank account statement of the respective date highlighting therein debit entry of aforementioned amount, for the record of this office, within seven days of the tendering of the gain.
- b) Respondent-I is hereby directed to provide a copy of its bank account statement of the respective date highlighting therein credit entry of aforementioned amount, for the record of this office, within seven days of the receipt of the gain.
- c) It is evident from the foregoing discussion that the Respondent-II has contravened the provisions of Section 224(1) of the Ordinance. In the light of said discussion, I am of the view that the Respondent-II has committed the violation. However, taking a lenient view





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN  
Securities Market Division  
Market Supervision and Registration Department (MSRD)

\*\*\*

of the default, in exercise of powers conferred under Section 224 (4) of the Ordinance, I hereby impose a fine of Rs. 30,000/- (thirty thousand rupees only) on the Respondent-II.

d) It is also evident from the foregoing discussion that the Respondent-I has contravened the provisions of Section 224(2) of the Ordinance. In the light of said discussion, I am of the view that the Respondent-I has committed the violation. However, taking a lenient view of the default, in exercise of powers conferred under Section 224 (4) of the Ordinance, I hereby impose a fine of Rs. 30,000/- (thirty thousand rupees only) on the Respondent-I.

14. The Respondent-I and the Respondent-II are directed to deposit the fine in the account of the Commission being maintained in the designated branches of MCB Bank Limited within 30 days of the date of this Order and furnish Original Deposit Challan to this office.

15. This order is issued without prejudice to any other action that the Commission/Registrar may initiate against the Respondent-I and Respondent-II in accordance with the law on matter subsequently investigated or brought to the Notice of the Commission.



(Imran Hayat Butt)  
Director/HOD (MSRD)

Islamabad.  
Announced on September 04, 2014