



SECP

**Through Courier**

**Before The Director / HOD (Market Surveillance and Special Initiative Department)**

**In the matter of Show Cause Notice no. issued to Al – Meezan Investment Management Limited under Section 15 E of the Securities and Exchange Ordinance, 1969**

**Date of Hearing:**

July 18, 2014

**Present at the Hearing:**

Representing Al Meezan Investment Management Limited

- (i) Mr. Muhammad Asad Chief Investment Officer,  
Al – Meezan Investment Management Limited
- (ii) Mr. Muhammad Rashid Zafar Head of Internal Audit and Compliance,  
Al – Meezan Investment Management Limited

Assisting the Director (SMD)

- (i) Ms. Tayyaba Nisar Assistant Director

**Date of Hearing:**

September 23, 2014

**Present at the Hearing:**

Representing Al-Meezan Investment Management Limited

- (i) Mr. Muhammad Shoaib Chief Executive Officer,  
Al – Meezan Investment Management Limited
- (ii) Mr. Muhammad Asad Chief Investment Officer,  
Al – Meezan Investment Management Limited

Assisting the Director (SMD)

- (i) Mr. Amir Saleem Deputy Director
- (ii) Ms. Tayyaba Nisar Assistant Director

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**SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN**  
**Securities Market Division**  
**(Market Surveillance and Special Initiative Department)**

**ORDER**

- 1 This order shall dispose of the proceedings initiated through Show Cause Notice bearing No. SMD/MSW/Al-Meezan/66/2014-550 dated June 18, 2014 (“**the SCN**”) issued by the Securities and Exchange Commission of Pakistan (“**the Commission**”) under Section 15E of the Securities and Exchange Ordinance, 1969 (“**the Ordinance**”) to Al Meezan Investment Management Limited (“**the Respondent**”).
- 2 The Respondent is registered as a Non - Banking Finance Company under the Non - Banking Finance Companies (Establishment and Regulation) Rules, 2003 and NBFC Entities Regulations 2007 with the Commission to do the business of asset management and investment advisory. The Respondent is also licensed as a Pension Fund Manager under Voluntary Pension System Rules, 2005.
- 3 Karachi Stock Exchange Limited (“**KSE**”) published its notice announcing re-composition of KSE – Meezan 30 Index (“**KMI - 30**”) on May 27, 2014 at 05:40 pm, vide which the list of Incoming and Outgoing Companies of KMI – 30 were announced as follows:

Sr. #	Incoming Companies	Outgoing Companies
1	ICI Pakistan	Lafarge Pakistan Limited
2	Kot Addu Power Company	Lotte Chemical Limited
3	Pioneer Company Limited	Pakgen Power Limited

- 4 The perusal of data of Karachi Automated Trading System (“**KATS**”) for May 27, 2014 showed that two funds of the Respondent namely Meezan Islamic Fund (“**MIF**”) and Meezan Tahaffuz Pension Fund (“**MTPF**”), herein after referred as **the Funds**, traded in the scrip of ICI Pakistan Limited (“**ICI**”) and Pioneer Cement Limited (“**PIOC**”) in both Ready and Off – Market. Summary of the trading is given below:

Meezan Islamic Fund					
Date	Market Segment	Symbol	Member Name	Bot_Qty	Sold_Qty
2014-05-27	Ready	ICI	Taurus Securities Limited	0	440,000
2014-05-27	Ready	PIOC	Shajar Capital Pakistan (Pvt.) Ltd	150,000	0
2014-05-27	Off - Market	PIOC	Shajar Capital Pakistan (Pvt.) Ltd	1,046,000	
				<b>1,196,000</b>	<b>440,000</b>
Meezan Tahaffuz Pension Fund					
Ord_Date	Market Segment	Symbol	Member Name	Bot_Qty	Sold_Qty
2014-05-27	Ready	ICI	Arif Habib Ltd.	80,000	0
2014-05-27	Off - Market	PIOC	Shajar Capital Pakistan (Pvt.) Ltd	142,000	
				<b>222,000</b>	<b>0</b>

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5 Further, details of trading data of ICI for May 27, 2014 and May 28, 2014 revealed that MIF sold – off its position of ICI to Al Meezan Mutual Fund and MTFP and subsequently purchased majority of the shares from both Funds on May 28, 2014. It is pertinent to mention that the said transactions by MIF, MTPF and Al Meezan Mutual Fund have contributed to majority volume in the scrip. The details of the transaction is summarized as below:

Trade Date	Name	Counter Party Name	Bought Qty	Sold Qty
2014-05-27	Meezan Islamic Fund	Al Meezan Mutual Fund		360,000
		Meezan Tahaffuz Pension Fund		80,000
	<b>TOTAL</b>			<b>440,000</b>
2014-05-28	Meezan Islamic Fund	Al Meezan Mutual Fund	345,400	
		Meezan Tahaffuz Pension Fund	77,800	
	<b>TOTAL</b>		<b>423,200</b>	

6 The information pertaining to minutes of meeting of Member of Islamic Index Policy Committee (“Committee”) dated May 26, 2014 were obtained from KSE, which provided the copy of circular for approval of KMI – 30 re-composition by the Committee. The circular was signed by Mr. Muhammad Shoab, Chief Executive Officer (“MS”) and Mr. Ali Hassan Khan, Head of Product Development of the Respondent on behalf of the Respondent.

7 The review of Fund Monthly Report of the Respondent for the month of May 2014 depicts that MS is member of Investment Committee (“IC”) of the Respondent and is responsible for investment decision making of the Funds of the Respondent.

8 Keeping in view of the above, prima facie, it appeared that MS (CEO and member of IC of the Respondent) being member of Committee which is responsible for KMI – 30 re-composition, had prior information pertaining to incoming and outgoing companies of the KMI - 30. The information, regarding the re-composition of KMI – 30, on the face of it constitutes inside information as same was not available publically before its dissemination on May 27, 2014. Therefore, explanation was sought from the Respondent to provide the rationale of the transaction in question vide letter dated June 18, 2014. The Respondent, vide letter dated June 24, 2014 submitted its response. Relevant segment of the response is reproduced hereunder:

- Out of the three incoming companies in the KMI – Index 30, MIF only increased exposure in the scrip of PIOC through Ready and Off – Market due to availability of large block of shares. MIF had started increasing the exposure in the scrip of PIOC nn May 22, 2014 which far prior to the meeting of KMI Re-composition Committee.

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- On the other hand MIF has reduced its exposure in ICI by selling 440,000 shares. Further, in case of ICI, if it had to take benefit of information of Index re-composition, it had not sold ICI, rather purchased it.
- Investment of MTPF is different than rest of the Funds of the Respondent and exposure in ICI and PIOC was increased only due to realization of major inflows which was deployed accordingly.
- The Responded also holds exposure in the scrip of Pakgen Power Limited, which is an outgoing company on the KMI – Index as per announcement of May 27, 2014. Had the Respondent have an intention to trade on the basis of preferential information it would have sold off its position exposure in Pakgen Power Limited.
- The rebalancing of Index was previously done on December 16, 2013 and none of the Funds of the Respondent had been involved in the trading of any incoming or outgoing companies in the KMI – 30 Index in the history.

9 However, the explanation submitted by the Respondent was not found satisfactory. Therefore, SCN dated July 03, 2014 was issued to the Respondent as to why action should not be taken against it under section 15E of the Ordinance for trading on the basis of material non-public information made disclosed to the Funds. The Respondent was required to submit its written reply to the SCN within ten days of the SCN and appear before the undersigned on July 18, 2014 for hearing in the matter.

10 The written response by Respondent was submitted vide letter dated July 10, 2014.

11 On the date of hearing Mr. Muhammad Asad, Chief Investment Officer and Mr. Muhammad Rashid Zafar, Head of Internal Audit and Compliance appeared to represent the Respondent. The assertions made by the Respondent in its written reply and during the course of hearing by the Representatives of the Respondent are summarized below:

- (a) *The Respondent started increasing its exposure in PIOC on May 22, 2014 which was well before the actual notice of re-balancing of the KMI – 30 or even before the date of meeting of the Committee for re-composition of KMI – 30. Further, decision for investment in the scrip of PIOC was done on May 19, 2014.*



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- (b) *PIOC is relatively illiquid scrip and due to availability of large block of shares from an interested seller, the purchase was made in the scrip on May 27, 2014 through Negotiated Deal Market ("NDM").*
- (c) *Purchase of 150,000 shares of PIOC by MIF in the Ready market was done on Rs. 46.13 and the purchase of 1.046 Million shares of PIOC in NDM was executed at Rs. 47.00, wherein both the transactions were near or above the closing rate of May 27, 2014 which was Rs. 46.56.*
- (d) *Investment in the scrip of PIOC is not for trading purposes but it is due to the fact that it is fundamentally attractive as per the Respondent's analysis.*
- (e) *Further, trading in the scrip of ICI indicates that MIF actually sold off 440,000 shares of ICI despite the fact that it was included in the KMI – 30. Had the Respondent intended to trade on the basis of information pertaining to re-composition of KMI – 30, it should have increased the exposure instead of selling the stock.*
- (f) *Moreover, the investments policies and limits of MTPF are different than rest of the funds of the Respondent. The exposure of PIOC and ICI was increased in MTPF – Equity which was due to realization of major inflows that were deployed accordingly.*
- (g) *No funds of the Respondent other than the Funds took positions in the scrips highlighted in KMI – 30 re-composition. Activity in the scrips of PIOC and ICI was done on the basis of the fundamental decisions, rather than by the Respondent's intention to benefit from the insider trading.*
- (h) *It also contented that there is no such history of the Respondent for information based trading. And the instances in questions were purely coincidental and without any malafide intention.*
- (i) *During the course of hearing, the Representatives of the Respondent highlighted the procedure of KMI – 30 re-composition. There are two segments of KMI – 30 re-composition, and the Respondent is only concerned with the Shariah compliance of the companies, which are short listed by KSE. The decision for inclusion or exclusion of a*

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*company in KMI - 30 lies with KSE, whereby the Respondent performs Shariah Screening of the said companies.*

- (j) *The final list of Incoming and outgoing companies is finalized through circular, not through a meeting. The KSE on May 26, 2014 emailed the KMI – 30 Memo to the Respondent to obtain the signatures of the participants of the Respondent in order to confirm the list of incoming and outgoing companies. The notice for the same was circulated on May 27, 2014.*
- (k) *Further, IC of the Respondent decides for investment in the shares and pricing is done by the Fund Managers. Investment in PIOC was done on the basis of positive news and was long term investment not for purpose of benefitting due to information available to the Respondent.*
- (l) *The Representatives of the Respondents contended during the hearing that the selling of ICI by MIF to Al Meezan Mutual Fund and MTPF on May 27, 2014 and subsequent purchase on May 28, 2014 from the same entities is for the purpose of gain realization. The transaction was not executed in NDM due to objection by its auditors in the past. The Fund Managers of MIF, MTFP and Al Meezan Mutual Fund are different.*
- (m) *However, currently there is no mechanism in place to avoid such conflict of interest. The Representatives of the Respondent assured that such scenario will be taken care of in future to avoid the situation.*
- 12 After the hearing Mr. Ali Hassan Khan submitted a copy of the email dated May 26, 2014 which was forwarded by KSE to the Respondent.
- 13 Subsequently, the Commission received a letter from the Respondent dated August 08, 2014 seeking another opportunity of hearing. The Commission vide letter dated September 15, 2014 acceded to the request and hearing was fixed on September 23, 2014.
- 14 On the date of hearing Mr. Muhammad Shoaib, Chief Executive Officer and Mr. Muhammad Asad, Chief Investment Officer appeared to represent the Respondent. The assertions made by



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the Respondent in its written reply and during the course of hearing by the Representatives of the Respondent are summarized below:

(a) *The circumstantial chronology of events as alleged in the SCN suggests that the Funds of the Respondent indulged in insider trading on the basis of inside information. Further, on the face of it, any changes in the composition of a widely followed and tracked index can be construed as "insider information". Internationally there are multibillion dollars funds which track the index in their investment strategies. Whereas, KMI – 30 index is a very smaller index with approximate worth of less than Rs. 1 billion and currently is tracked by only one fund namely KMI Index Fund.*

(b) *A comparative of weightage of the incoming companies in the KMI – 30 Index is presented as follows:*

- KAPCO – 4.08%
- ICI – 0.76%
- PIOC – 0.48%

*Based on Index tracking fund size worth Rs. 1 billion, an investment of Rs. 40.80 million will flow into KAPCO, Rs. 7.60 million in ICI and Rs. 4.80 million in PIOC during the period when index tracker funds will do the relocation of their funds to align it with the index. Based on the price of the scrip on May 27, 2014 a natural demand of 680,680 shares, 19,498 shares and 103,093 shares of KAPCO, ICI and PIOC, respectively would be generated.*

(c) *This background information and statistics lead to the conclusion that small changes in the index which is not widely tracked, are not likely to have significant market impact on the price of the security.*

(d) *Further, keeping in view the Commission's contention that the re-composition of the index was an inside information, the Respondent should have opted for investment in the scrip of KAPCO out of the three incoming companies, however, it invested in PIOC which possessed the least weightage.*

(e) *Rationale of investment in PIOC was purely based on fundamental analysis and was recommended by the research team in the meeting of Investment Committee of the Respondent held on May 19, 2014. The minutes of the said meeting and presentation by the research team recommending the "BUY" stance for PIOC were also presented.*

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- (f) *There were three incoming and three outgoing companies in the KMI – 30 Index and wherein, the funds of the Respondent only invested in scrip of PIOC and sold ICI. Further, total trading executed by the Funds of the Respondent in PIOC on May 27, 2014 constitutes less than 6% of the total volume of the the scrip that day.*
- (g) *The Representatives accepted the circumstantial events indicate that the MS was an insider being a member of the Committee and member of the IC of the Funds at the same time and the information pertaining to the re-composition of the KMI – 30 is an inside information. But they also contended that there was no malafide intention of the Respondent in the execution of the said transactions. Further, the Respondent has also committed to develop a Chinese wall to avoid such conflict of interest in future.*
- (h) *The Respondent submitted that it is already working in collaboration with KSE to avoid any such situation occurring in the future and also sought advice of the Commission to adopt a careful approach in future.*
- 15 I have thoroughly analyzed and examined the facts, evidence and documents on record, in addition to the written replies to SCN and assertions made by the Representatives of the Respondent during the hearings and my findings on the issues are as follows:
- (a) The approval of re-composition of KMI – 30 was done on May 26, 2014 through circular by the members of Islamic Index Policy Committee. The members of the Committee included Mr. Nadeem Naqvi, Mr. Haroon Askari and Mr. Mohammad Hussain from KSE, Mr. Imran Usmani and Mr. Farhan Usmani from Meezan Bank Limited and Mr. Muhammad Shoaib and Mr. Muhammad Aasd from the Respondent. While the notice was circulated on May 27, 2014 at 05:40 pm.
- (b) During the course of hearing the Representatives of the Respondent contented that investment and divestment in the shares of PIOC and ICI are fundamental based not informational based. In this regard, the Respondent also provided minutes of meeting held on May 19, 2014, which was far earlier than meeting of the Index re-composition committee. It is also evident that on the bases of the recommendation of research team of the Respondent, MIF started purchase in PIOC on May 22, 2014 by buying 105,000 shares of the scrip.

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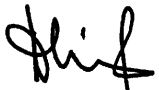
- (c) The review of trading by MIF in the scrip of ICI revealed that MIF sold its holding to Al Meezan Mutual Fund and MTPF on May 27, 2014 and subsequently reversed the same on May 28, 2014. This shows a contradictory stance of the Representatives of the Respondent. In addition majority of the volume in the scrip of these two days were generated due to these transactions of the Funds.
- (d) The stance of the Representatives that said transaction in the scrip of ICI were executed for realization of gain and were not normal trades is not acceptable. Such transaction should have executed through NDM at a given target price to avoid generation of artificial volume.
- 16 On review of the arguments made both in written and verbal form, it is noted that the Representatives of the Respondent have admitted a number of points which were raised in the SCN according to which by definition, MS was an insider being a member of the Committee and member of the IC of the Funds at the same time and the information pertaining to the re-composition of the KMI – 30 also falls under the ambit of inside information. In this connection as stated in the SCN the MS falls under the definition of Insider as defined under Section 15C (1a) of the Ordinance at the time trading of aforementioned shares by the Funds.
- 17 From the facts of the case mentioned above, it is established that MS being the member of the Committee, at the time of trading of shares by the Funds, was an insider and had prior information regarding incoming and outgoing companies of KMI - 30. Further the pattern and timing of trading also leads to the suspicion that trading by the Funds might be based on inside information provided by MS but in absence of any clear and convincing evidence and any benefit made thereafter, the preponderance of evidence is in favor of the Respondent. The Commission is convinced of the fact that although by definition and on the basis of the chronology of the events, the Respondent has indulged in the insider trading, but the supporting documents and clarifications made by the Representatives of the Respondent establishes that there was no malafide intent behind the execution of such transaction, but it was merely result of negligence on part of the Respondent which resulted in conflict of interest.
- 18 The Respondent is a renowned institution and holds a reliable reputation in the market; therefore it attracts a significant responsibility to refrain from the actions which raise conflict of interest. It



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is noted with deep concern that the Respondent being entrusted with a responsibility to carry out the activities which are strictly abided by the law. It is imperative to mention that there has been no set of procedures/ controls in place to monitor conflict of interest. It can be judged that trades in question are result of negligence on part of Respondent and its corporate responsibility was not exercised with reasonable care, skill and diligence.

- 19 In view of the forgoing, the Respondent is hereby warned with directions to develop and implement in-house controls to ensure that no trading is done in a manner which is not in contravention of section 15 A of the Ordinance. Moreover it should also be ensured that appropriate controls are in place to check that inside information is not disclosed in violation of section 15 E of the Ordinance. Further, it is also directed that the investment policies of the Funds should be reviewed especially with regards to investments in the shares of such companies which are under review for inclusion in / exclusion from in KMI – 30.
- 20 This Order is issued without prejudice to any other action that the Commission may initiate against the Respondent in accordance with law on matters subsequently investigated or otherwise brought to the knowledge of the Commission or on the same facts for violation of any other provision of the Ordinance.

  
(Abid Hussain)  
Director/HOD (MSSID)

Announced on 3.10.2014  
Islamabad.