

IN THE HIGH COURT OF SINDH, KARACHI

M. A. No.11 of 2020
*[Muhammad Iqbal (Partner) versus
Appellate Bench No.1 and another]*

Dates of hearing : 30.09.2024 07.10.2024
and 10.10.2024.

Appellant
[Muhammad Iqbal (Partner)] : Through Barrister Syed
Ahsan Ali Shah.

Respondents No.1 and 2.
*[Appellate Bench No.1,
SECP and the Executive
Supervision Department,
Company Law Division-SECP]* : Through M/s. Syed Imran
Hashmi and Syed Ibad,
Advocates.

JUDGMENT

Muhammad Faisal Kamal Alam, J: The Appellant has challenged the impugned Order dated 23.12.2019 passed by the Respondent No.1 [Appellate Bench No.1, Securities and Exchange Commission of Pakistan (“SECP”)], whereby the Order dated 22.05.2018 given by the Respondent No.2 (the Executive Director, Corporate Supervision Department) has been upheld, imposing a Token Penalty of Rs.10,000/- (rupees ten thousand only) on the Appellant.

2. The relevant facts are that the Appellant is the Partner of a Chartered Accountants Firm (Reanda Haroon Zakaria & Company Chartered Accountants). During the period ending on 31.03.2017, the Appellant was on a review engagement of its Client-Al-Abbas Sugar Mills Limited and issued a Report which, upon consideration by SECP, resulted in issuance of a Show Cause Notice dated 29.09.2017, which was responded to by the Appellant.

3. Crux of the matter is that the above Company has reclassified its short term investments from 'fair value through profit or loss' category to 'available for sale' and classified them as long term, which purportedly violates the **IAS-39** (International Accounting Standard), which was construed as a misstatement in the Accounts of the Company for which the Appellant, as the Company's Auditor, was also held responsible.

4. Barrister Syed Ahsan Ali Shah, on behalf of Appellant, has argued that when the International Accounting Standard provides more than one option, the Appellant cannot be penalized. Contends that the penalty in such matters can only be imposed when there is a *mens rea* on the part of the Appellant or there is a willful breach of any of the statutory provisions; relied on the Case Law in support of his arguments. Has also cited the Decision of Respondent No.1 in another case, in which some major irregularities were found in calculating net capital balance of a Company, but a lenient view was taken by giving a warning. Has cited the following Case Law_

1) **2016 CLD 1468**

[Riaz Ahmed, Saqib, Gohar and Co. Chartered Accountants versus Director (Marketing Supervision and Registration Department) Securities and Exchange Commission of Pakistan]-Riaz Ahmed Case.

2) **2023 PTD773** [Sindh High Court]

[Commissioner (Legal Division) versus Pakistan Services Limited]

3) **2018 CLD 177** [Supreme Court of Pakistan]

[State Bank of Pakistan through Chief Manager, Peshawar and another versus Securities and Exchange Commission of Pakistan and others]-SBP Case.

4) **2004 PTD 559** [Karachi High Court]

[Messrs Iram Ghee Mills (Pvt.) Ltd. Lahore, versus Customs, Central Excise and Sales Tax (Appellate) Tribunal, Karachi and another]-Iram Ghee Case.

5. Mr. S. Imran Hashmi, Advocate along with Syed Ibad, Advocate, on behalf of SECP, has defended the impugned Order and argued on the basis of the Objections / Para-wise Comments, *inter alia*, that opinion given by the Appellant has materially changed the financial position of the above Company and it is not a *bona fide* error. States that the present Appeal should be dismissed. Contends that matter of reclassification of the investment was a conspicuous matter which should have been highlighted by the Appellant being auditors in their Review Report, but, failing to do so, has violated provisions of IAS 39, besides, Section 255(3) and 260 of the erstwhile Companies Ordinance, 1984.

6. Arguments heard record perused.

7. Précis of the Case Law cited by the Appellant's Counsel is that imposing of penalty is not a criminal liability carrying any stigma, as against imposition of fine on conviction (which is a criminal liability); for establishing a quasi-criminal offence, the presence of guilty intent / *mens rea* is to be established, "*until and unless there is a case of absolute statutory liability, where no mens rea is required to be proved*", unless there is an evidence of fraud or willful gross negligence in payment of Income Tax, *ipso facto* a penalty cannot be imposed on the Taxpayer. In the **SBP Case**, the Hon'ble Supreme Court, while expounding Sections 412 and 413 of the erstwhile Companies Ordinance, (1984), has ruled, that "*if any penal provision is susceptible to two or more interpretations, then one that does not extend penalty / liability is to be preferred to one that does*". It has discussed the principle of interpretation of statutes, by reiterating that in the event of ambiguity in a penal provision, it would be resolved in favour of the person who is liable to penalty. In the **Case of Riaz Ahmed (supra)**, the learned Appellate Bench of SECP only issued warning to the Chartered Accountants Firm, which verified the accounts

of its Client, wherein major irregularities were highlighted in calculating the net capital balance, while exercising jurisdiction under Section 22 of the Securities and Exchange Ordinance, 1969.

8. The Special Prosecutor of SECP has filed a Statement dated 7th October, 2024 along with documents, including the Order of 22nd February, 2018 passed by SECP against the Directors of the above Client [Al-Abbas Sugar Mills Limited], imposing a penalty of Rs.10,000/- (*rupees ten thousand only*) each and a warning.

9. Whereas, the learned Counsel for the Appellant in compliance with the Court Order has also filed a Statement dated 7th October 2024, together with documents including Reply of another Chartered Accountants Firm, submitted before the SECP to the Show Cause Notice issued by it to the above Client / Company, so also the Order of the Audit Oversight Board [AOB] of Pakistan Stock Exchange Limited.

10. The afore-referred reply of another CA Firm was not accepted by the SECP [discussed in the above Paragraphs], and thus, it does not advance the case of the Appellant. Whereas, the Order of Audit Oversight Board [AOB] of Pakistan Stock Exchange Limited is in respect of the Appellant, is passed in connection with the Show Cause Notice issued to the Appellant for non-provision of updated information about the CA Firm [of the Appellant], because it did not disclose the imposition of the impugned fine of Rs.10,000/- (*rupees ten thousand only*) to AOB, which after considering all the facts and circumstances of the case, arrived at the conclusion that it did fail to comply with the requisite Regulations, but did not take any adverse action, except directing the Appellant Firm to submit a revised Form “A” along with a note of caution. This Order of AOB also does not lend any help to the case of the Appellant.

11. The Appellate learned Bench-Respondent No.1 has not given finding on the crucial fact, such as, that a written third opinion was obtained by QCR (Quality Control Review) compliant Firm, agreeing with the impugned accounting treatment done by the Appellant [*fact stated in Paragraph-3 of the impugned Order*], and whether this opinion would have impacted the Decision given by the Respondent No.2. Similarly, the impugned Appellate Order, though agreed with the legal aspect of the case that the reclassification concerning the investment can be done, yet, maintained the Impugned Original Order and stated that “*usual uneven political and economic trends cannot be considered as rare circumstances*”, for justifying such reclassification, which fact the Appellant explained in his Reply to Show Cause Notice, reproduced by Respondent No.2 in its Order, that the short-term investment done by the Appellant’s Client in shares of different Companies had experienced significant variation in price / valuation due to volatile market conditions, therefore, the Appellant construed that fact as a rare circumstance, as provided in **IAS-39**.

12. The impugned Orders have acknowledged the ‘rare circumstances’ factor only to the extent of the Press release of October 13 2008 issued by IASB [International Accounting Standards Board]. This Press Release [available in the Record of LIS] was about the deterioration of the international financial markets, that occurred during the third quarter of year 2008. If the reclassification is still can be done through IAS 39, then in my considered view, it cannot be confined only to what happened in the past, but, this option [of re-classification] can be invoked in cases where there are legally recognizable *force majeure factors*.

13. From the Order dated 22.05.2018 passed by Respondent No.2 (Executive Director Corporate Supervision Department), it appears that the disputed non-compliance has been done for the first time, regarding

which more than one interpretation is possible. The relevant amendments to **IAS 39** have been placed on record, and the amended Paragraphs-50B and 50C state as follows_

“50B A financial asset to which paragraph 50(c) applies (except a financial asset of the type described in paragraph 50D) may be reclassified out of the fair value through profit or loss category only in rare circumstances.

50C If an entity reclassifies a financial asset out of the fair value through profit or loss category in accordance with paragraph 50B, the financial asset shall be reclassified at its fair value on the date of reclassification. Any gain or loss already recognized in profit or loss shall not be reversed. The fair value of the financial asset on the date of reclassification becomes its new cost or amortised cost, as applicable.”

14. In view of the above, it appears that the impugned act of reclassification attributed to the Appellant was not a result of some *mens rea* or a willful default (as expounded in the Case Law, *supra*), but a result of professional Judgment. Consequently, imposing even a token penalty of Rs.10,000/- (*rupees ten thousand only*) can have adverse consequences. Consequently, the impugned Appellate Order, in which the above Original Order has merged, are modified to the extent that the impugned penalty is set-aside, and this Appeal is disposed of with a note of caution / warning to the Appellant, that he should exercise better standard of due diligence in the assignments, in order to avoid adverse consequences.

JUDGE

Karachi

Dated 19.11.2025

M.Javaid PA