

# **A Critical Examination of Investor Protection under the Securities and Exchange Commission of Pakistan about Investment Policies in Pakistan**

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**Abstract:** This article's main objective is to critically assessing Pakistan's investment policies and investor protection strategies under SECP. The SECP's incentives for both domestic and foreign investors are included. A special focus is paid to identifying the barriers that prevent investment in Pakistan. Major obstacles include high business expenses, unpredictable politics, corruption, bureaucracy, conflicting government policies, and a lack of law and order. The investor complaints cell and the awareness-raising activities they carry out about their financial market investments are also included in this study. If investors are aware of their dangers and the rules and regulations of the country, they can be appropriately protected. The comparison emphasizes how important it is for investors to be informed about the dangers involved in the investments they are making in the securities market. The paper also lists international best practice solutions, like the IOSCO Principles, designed to encourage foreign investment in the country.

**Keywords:** Investor, Investor Protection, Securities, Securities Market, Regulators

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## **1. Introduction**

Investor protection is the most crucial element of the securities industry. Making sure that investors get as much information as they can before making any investment is the key to safeguarding them. American Bar Association [1] Although the regulator claims that investors are protected, they must make sure that these people are fully informed about their purchases, transactions, and relationships with issuers. Governmental and other authorities' laws must be both sufficient and effective in how they are carried out. American Bar Association [2].

Investment has become a major strategy for promoting and maintaining economic growth on an

international level. Business law is in charge of and governs all of those commercial and industrial processes. The US, UK, and even India staying true to their image as developed countries, have a variety of laws and standards controlling all of their corporate operations as well as the investment process. Commercial law covers both the law of contracts and the law of property. The investment of money and the application of contract law are required to enforce contractual obligations in business transactions. Commercial law is produced via state-recovering legal systems because investment activity is governed by commercial laws. Carvajal Ana and Jennifer [3].

Investor confidence is a key component of the capital market's health. Furthermore, investor trust is promoted by a capable capital market regulator. The finest investment choice should be made by a wealthy investor in the securities market, one for whom the economy will provide adequate revenue. Brummer and James [4]. As a result, the goal of the capital market regulator is to foster greater investor confidence through a range of laws, rules, market awareness campaigns, and educational activities. Bodellini and Marco [5].

It is crucial to protect investors and, in particular, to stop unscrupulous trading strategies to maintain the fairness of the markets. On the other hand, the IOSCO Regulations should work to guarantee that investors have equal access to market infrastructure, all data, and pricing information. In this way, the IOSCO Principles' goals would be successfully achieved. It is important to encourage the market's behavior, which is supported by law and regulation, to employ a standardized methodology for generating prices and processing orders fairly.

All across the globe, securities supervisors and controllers are connected and united by the Worldwide Organization of Securities Commissions (IOSCO), a multinational organization. The IOSCO develops and executes all investment policies for the regulation of securities as well as generally acknowledged standards for investor protection.

Strong domestic markets are becoming more and more integrated into the global securities market today since they are necessary for the growth of investors in both the private sector as a whole and foreign investment as well. The IOSCO principles can be applied to build robust domestic markets. By the IOSCO principles, securities regulators at both the national and international levels ought to be motivated by a steadfast desire to safeguard investors' interests, and in some cases, they are. After concluding that the only way to help the domestic economy is

to control thriving local markets, IOSCO offers the regulator crucial advice. The IOSCO Principles' Part II, Paragraph 6, lists the requirements for a regulator. Karmel [6].

The Securities and Exchange Commission of Pakistan plays a vital role in securities regulation in Pakistan. However, it struggles to fulfill its objectives, highlighting the need for an adequate mechanism based on IOSCO's principles. This paper analyzes deficiencies in Pakistan's law, including silence on intermediary misconduct and lack of penalties for law breaches. Carvajal, Ana, and Jennifer [3].

## **2. Literature Review**

The study explores the legal aspects of regulating securities markets for investor protection under SECP based on a comprehensive literature review of relevant books, research papers, policy summaries, and reports, providing a comprehensive understanding.

Securities laws are essential for functioning markets, guaranteeing firms, and providing a legal framework for capital production. Investor protection is a goal of IOSCO principles, which also promote justice, efficiency, and openness. Additionally crucial is systematic risk, a type of market risk. Since more than 90% of security regulators are IOSCO members, accountability and fairness are guaranteed. To evaluate circumstances that can impact regulators' activities, information on financial markets, especially securities financing markets, should be accessible. In the financial markets, systematic risk is foreseen but unseen. Shabbir [7].

Fairness in the market and the protection of investors go hand in hand. The laws put in place by the Securities and Exchange Commission of Pakistan to protect investors in the securities markets do not achieve their desired outcomes. To keep the financial system safe and sound, improve the regulatory and legal framework, and make the capital markets the greatest place for investors both at home and abroad to put their money, it is essential to follow the IOSCO principles. Shabbir [7].

In addition to discussing the benefits of IOSCO Standards, Cally Jordan provides background on the organization's standard-setting process and states that IOSCO is no longer in control of its agenda for standard-setting. The long-standing regulatory goals of investor protection were superseded by new regulatory goals that were incorporated into international standards. Jordan [8].

According to the organization's rules and regulations, IOSCO's goal is to "cooperate in

establishing, enforcing, and encouraging compliance with internationally acknowledged and constant norms of regulation, monitoring, and execution to defend the rights of investors; continue objective, well-organized, and obvious markets; and further strive to discourse complete concerns about active and unbiased marketing in regulations." By collaborating to eradicate misbehavior, increasing data sharing, and conducting market surveillance with market intermediaries, IOSCO not only improves investor protection but also increases investor trust and integrity in the securities markets. Defond and Hung [9].

Marco Bodellini argues in his paper that those who are permitted to invest in hedge funds are smart, affluent, and powerful individuals who do not require legal protection. Bodellini asserts that it is not usually seen as a high priority to consider whether the current legislative framework is acceptable and, at the very least, sufficient for commentators to debate the difficulties that hedge funds might provide to investors and markets. Therefore, regulators should be motivated by crucially essential legal goals like investor protection and systemic risk mitigation. Bodellini [5].

An outstanding piece of writing by Abraham M. Stanger lays out its plan for enforcing fair investment policies. The responsibility for effectively regulating the market lies with the regulator, who must ensure that investors' protection is not compromised in any way and that investors' protection is given top priority. We should so embrace the International Organization of Securities Commissions (IOSCO). Stranger [10].

### **3. Material and Methods**

The researcher uses doctrinal legal research methodology. This study will include both a descriptive technique and an analytical approach. Systematization will be utilized in this study to evaluate the laws and rules currently in place to control the securities markets for the protection of investors under SECP.

### **4. Results and Discussion**

Pakistan has made significant advancements in both the design and implementation of regulations, according to IOSCO principles. Pakistan adopted the published recommendations from the 2015 Report in the form of new legislation that covers a variety of unique facets of capital market regulation. Daniela and Russo, 2013 only two of the laws that have been

introduced or altered to implement legislative and regulatory reforms under SECP's worldwide leadership are the 2015 Securities Act and the (2016) Futures Market Act. Deterrence and Credible [11].

Some more acts that are referenced include the Companies Act of 2017 and the SECP Amendment Act of 2016. The Pakistan Stock Exchange, the Central Depository Company of Pakistan, the National Clearing Company of Pakistan, non-bank financing businesses, and self-regulatory bodies have all changed. Godwin, Andrew, Kourabas, and Ian-Ramsay 2016 Additionally, the SRO had major control changes, issuers, and investment market mediators received organizational changes, the Pakistan Audit Oversight Board was created, and enhancements were made to investor communication, responsiveness, defense, and support. The rules for investor facilitation and the supervisory architecture also underwent adjustments. Hellwig and Martin [12].

To safeguard investors, uphold unbiased, orderly, transparent markets, and attempt to address systemic risks, the members of IOSCO agreed to cooperate first to enhance, implement, and support adherence to globally acknowledged standards and constant principles and benchmarks of regulation, supervision, and enforcement. Furthermore, they have made the joint decision to collaborate to establish proper oversight, enforcement, and regulatory mechanisms that will enhance and modernize investor protection and foster investor integrity and trust in the securities markets. Thirdly, it's critical to disseminate all information and data on their varied experiences at the local and international levels to create economic institutions, encourage and stimulate market expansion, and pass appropriate legislation. IOSCO Emerging Markets Committee [13].

#### ***4.1 Comparison between IOSCO Principles and Objectives of SECP regarding Investor***

*Protection.*

IOSCO PRINCIPLES	SECP'S ACT
<p><b>Principle 6:</b> The mechanism to monitor, mitigate, and manage systemic risk should be in place or contributed to by the regulator, as it is suitable for its mandate.</p>	<p>Systemic risk cannot be monitored, reduced, or managed because no regulatory framework is in existence to do so. During the research, there were discussions about revising the SECP Act, which could have an impact on the authority and duties of the SECP. The ability of the SECP to identify and address systemic risk issues has been enhanced. So, it is critical to swiftly execute the SECP plan for systemic risk reduction and the amendments to the SECP Act. There have been no changes or additions to the Act; SECP has just established the Risk Management Department.</p>
<p><b>Principle 12:</b> An efficient compliance program and the legitimate application of enforcement, investigation, and inspection powers are essential components of any functional regulatory system.</p>	<p>The SECP's on-site inspection program and risk-based assessment methodology are currently neither rigorous nor organized. Most businesses are only permitted to undergo inspections once every 10 years. However, the main barriers to efficient compliance are the backlog and delays in the courts. The SECP's "International Inspection" strategy should be prioritized and put into action to fully cover brokers. The joint inspection initiative should also continue in 2016–17, and the entire brokerage Community should be made aware of the Joint Examination Regulations program so they can be ready for and anticipate such an inspection.</p>

<p><b>Principle 15:</b> To carry out their duties and exercise their authority, international regulators may require assistance from the regulatory system to conduct investigations.</p>	<p>The SECP became a signatory to the IOSCO MMoU on March 10, 2011. Before publishing financial papers, the Central Bank must provide its approval. As a result of errors in procedures made by the SECP under Section 42C of the SECP Act and the Central Bank, a request for MMoU clearance was turned down. The SECP would be able to access and share bank records without the Central Bank's permission under the SECP Act's proposed Section 42C, which is now being considered in Parliament. The SECP is essential to Pakistan's stock market regulation. Despite this, it falls short of its objectives, highlighting the need for an appropriate system based on IOSCO's principles.</p>
<p><b>Principle 16:</b> All information relevant to an investor's decision-making process, including financial performance, risk, and other relevant data, must be disclosed in a complete, accurate, and timely manner.</p>	<p>Sub-section 1 of Section 88 of the Securities Act of 2015 states that since then, it has been mandatory to publish prospectuses in Urdu. Prospectuses are available in English and Urdu as well. The SECP published a guideline on December 31, 2015, requiring all enterprises to publish the language of the circular and an announcement in both Urdu and English marketing new shares. You can also access prospectuses in Urdu. For the advantage of investors, the websites for SECP and SRO are available in both Urdu and English.</p>
<p><b>Principle 23:</b> The regulatory system should keep an eye on other businesses that provide analytical or evaluative services to investors, and those entities should be regulated according to the market influence or degree of reliance their operations have.</p>	<p>The research analyst regulations, which established the fundamental training, real-world experience, and certification requirements for research analysts, including those for independent research, were passed by Pakistan in 2015. The SECP analyzes these standards often to make sure they are being followed. These research analysts do their own, independent research to create their research reports. The rules for research analysts specifically highlight and encourage morality and honesty, among other things.</p>

<p><b>Principle 24:</b> Eligibility, governance, organization, and operational behavior rules for anyone wishing to market or run a collective investment scheme should be specified by the regulatory framework.</p>	<p>The Securities and Futures Advisors (Licensing and Operations) Regulations of 2017 require mutual fund distributors, who are regarded as securities advisors under the Securities Act of 2015, to apply for a license to the SECP. The provisions of the Act and the Regulations provide substantial jurisdiction to the SECP concerning distributor licensing, regulation, supervision, and monitoring.</p> <p>For anyone looking to provide or oversee a collective investment plan, the SECP's regulatory framework requirements have been considerably tightened in terms of eligibility, governance, organizational design, and operational behavior. Enhancing and ensuring a high degree of investor protection will be made possible by changes that will eventually be required to safeguard investor rights and create an operational rule that will allow a thriving CIS business environment in Pakistani jurisdiction. This could ultimately result in a developed rating. Since these changes are still in the early stages of development, the assessor is unable to predict how they will impact investor protection, particularly about the novice investors who constitute the foundation of Principle 24.</p>
<p><b>Principle 30:</b> There should be initial and ongoing capital and other prudential requirements for market intermediaries that reflect the risks that the intermediaries Undertake.</p>	<p>The SECP is empowered by Section 81(4) of the Securities Act of 2015 to issue directives or impose sanctions, such as suspension, on intermediaries who are unable to meet their Capital or financial resource requirements or Who violates any provisions of the Act and the rules and regulations adopted There under. According to Article 70, SECP may impose any restrictions or conditions it Thinks fit on a licensing subject and may</p>



	<p>Change, revoke, or add additional restrictions or requirements with written notification to the license holder.</p> <p>The Broker Regulations' Regulation 33 outlines the standards for keeping books of accounts and other documents. Securities brokers are required by Regulation 33(1) to maintain accounting and other records that, at all times, accurately reflect their financial situation, enable them to prepare financial statements as required, and establish that they have the resources necessary to carry out their contractual obligations.</p>
<p><b>Principle 32:</b> To limit systemic risk and minimize harm to investors, protocols should be in place for when a market intermediary fails.</p>	<p>The default management system has been significantly improved by the Securities Act of 2015 and the Clearing House (Licensing and Operations) Regulations of 2016. The NCCPL emphasizes the following significant achievements: Novation is legally obligated to settle all trades by Clause 3.16 of Chapter 3 of the NCCPL Regulations, 2015, as the NCCPL ensures its role as central counterparty.</p> <p>At the discretion of the Minister-in-Charge, NCCPL may be able to establish a credit line below the new Companies Act, 2017, Section 244(12) using assets such as the funds from the sale of shares or Modaraba certificates as collateral, in addition to the bank account for unpaid or unclaimed dividends. If this were to happen, NCCPL would be better able to address a systemic threat to the investment industry and resolve broker settlement failures. The Commission can only use the power granted to it by this paragraph if it determines that the reimbursement house does not have enough resources, or is likely to have inadequate resources, to quickly clear transactions conducted at futures and securities exchanges.</p>

The current discussions highlight the significance of strengthening the securities legislation. For securities markets to be successful we need institutions and a regulatory framework designed for capital production. The securities markets must be home to businesses and have a regulatory environment that supports them. Three objectives must be accomplished. The IOSCO principles' primary objectives are investor protection and the development of logical, informed, organized, and transparent markets. A risk that impacts the entire market is referred to as "systematic risk," a term that is usually used to refer to the market as a whole. Newman, Patterson and J. Reed Smith [14].

## **5. Conclusion**

Traders, investors, and hedgers are the three main stakeholders in any futures market. They put aside cash for trading, hedging, or investing, which has an impact on the number of transactions and market activity. Therefore, ensuring the safety of market participants is crucial for the growth, profitability, and expansion of Pakistan's derivatives market.

The stock market and SECP are essential for the regulation of stocks in Pakistan. Despite this, it falls short of its objectives, highlighting the need for an appropriate system based on IOSCO's principles. This article looks at Pakistan's legal problems, including the lack of penalties for breaching the law and the lack of awareness of intermediary misbehavior. The SECP in Pakistan faces a lack of effective regulation of investment and, highlighting the need for a more comprehensive system based on IOSCO's principles.

Securities and investment markets like the stock exchange heavily rely on investing. They make decisions based on the level of market activity. The protection of stakeholders and shareholders is viewed in modern times as an essential and motivating step in the development and growth of businesses and organizations. Investors' safety was prioritized for their protection. If we look at the improvements made by these industrialized countries, we can see that they still put a lot of attention on safeguarding investors; however, in Pakistan, this problem is constantly disregarded by everyone.

On the other hand, the IOSCO principles demonstrate that they succeed in achieving this objective. The process of setting prices is a representation of the thorough and timely transmission of relevant information that distinguishes a successful market. As a result, it is crucial for the effectiveness of the market. To safeguard the legitimacy and integrity of the

financial system, enhance the legal and regulatory environment, and advance capital markets, the IOSCO guidelines must be followed. Only then will both domestic and international investors view market investment as the preferred course of action. They are selling shares to lessen the risk. However, they don't appear to be in equilibrium between supply and demand. The decrease in share values hurts businesses as well as investors as a whole.

Applying IOSCO principles is a crucial strategy for accomplishing these goals. Consequently, they make a big difference in the growth of the economy and the creation of capital. Although there have been several changes to Pakistan's legal and regulatory framework, it is anticipated that the majority of these changes will still be carried out in compliance with the IOSCO Objectives and Principles. The SECP developed and vigorously carried out a comprehensive strategy to meet IOSCO's evaluation criteria to bring Pakistan's securities regulatory system into compliance with international standards.

The study found that fruitful conversations were had on the endorsements that were preferred over significant legal procedures, keeping an eye on developments, and getting market participants on board to accept cutting-edge ideas and procedures. The Securities Act, the SECP Amendment Act, a new regulatory framework for securities brokers, an investor education campaign, modifications to the supervisory architecture, and risk-based supervision and enforcement are just a few of the legislative and regulatory changes that have been implemented. The study concluded that putting the recommended reforms into practice enhanced investor protection, fair and well-organized markets, market efficiency, and a decrease in systemic risk in Pakistan's securities markets.

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