

Before the Director (Market Supervision & Registration Department)
Securities Market Division
Securities and Exchange Commission of Pakistan

**In the matter of Show Cause Notice dated May 30, 2013 issued to
M/s. Ismail Iqbal Securities (Pvt.) Limited under Section 22 of the
Securities and Exchange Ordinance, 1969 and Section 28 of the Central Depositories Act,
1997**

Date of Hearing: July 17, 2013

Present at the Hearing: Authorized Representative of M/s. Ismail Iqbal Securities
(Pvt.) Limited
Mr. Mehmood Sheikani

Representing (MSRD): Mr. Tahir Mahmood Kiani (Deputy Director – MSRD)

ORDER

This Order shall dispose of the proceedings initiated through a Show Cause Notice No. SMD/KSE/4-BRK-183/2004 dated May 30, 2013 (“**the SCN**”) under Section 22 of the Securities and Exchange Ordinance, 1969 (“**the Ordinance**”) read with Section 28 of the Central Depositories Act, 1997 (“**CD Act**”) issued to M/s. **Ismail Iqbal Securities (Pvt.) Limited (“the Respondent”)**, Trading Right Entitlement Certificate Holder of Karachi Stock Exchange Limited (“**the KSE**”) and a broker registered with the Securities and Exchange Commission of Pakistan (“**the Commission**”) under the Brokers and Agents Registration Rules, 2001.

2. The Commission in exercise of its powers under Sub-Section (1) of Section 6 of the Ordinance read with Rule 3 and Rule 4 of the Stock Exchange Members (Inspection of Books and Record) Rules, 2001 (“**the Inspection Rules**”) ordered an inspection vide order No. SMD-MS&CID-C&IW/10-1/(230)/2012 dated December 31, 2012 of the books and records required to be maintained by the Respondent. On review of the inspection report various *prima facie* violations regarding calculation of Net Capital Balance (“**NCB**”), difference in shareholding of the clients between back office record and their CDC sub-accounts, charging of late payment charges and non-segregation of clients funds were observed and accordingly the subject SCN was issued, the contents of which are reproduced below:-

SUBJECT: SHOW CAUSE NOTICE IN THE MATTER OF INSPECTION OF BOOKS AND RECORD OF M/S. ISMAIL IQBAL SECURITIES (PRIVATE) LIMITED – “TREC” HOLDER OF KARACHI STOCK EXCHANGE LIMITED

WHEREAS, M/s. Ismail Iqbal Securities (Private) Limited (**'IISPL'**) is a Trading Right Entitlement Certificate (TREC) holder of the Karachi Stock Exchange Limited and registered as a broker with the Securities and Exchange Commission of Pakistan (**"Commission"**) under the Brokers and Agents Registration Rules, 2001 (**"Brokers Rules"**).

2. **WHEREAS**, the Commission in exercise of its powers under Sub-Section (1) of Section 6 of the Securities and Exchange Ordinance, 1969 (**"Ordinance"**) read with Rule 3 and Rule 4 of the Stock Exchange Members (Inspection of Books and Record) Rules, 2001 (**"Inspection Rules"**) ordered an inspection vide its Order No. SMD-/MS&CID-C&IW/10-1(230)/2012 dated December 31, 2012 of the books and record required to be maintained by IISPL.

3. **WHEREAS**, on review of the inspection report it has come to the notice of the Commission that Net Capital Balance (**"NCB"**) of Rs. 88.471 million as of June 30, 2012 as calculated by IISPL and certified by M/s. Ibrahim Shaikh & Co. Chartered Accountants, is not in accordance with the Third Schedule of the Securities and Exchange Rules, 1971 (**"1971 Rules"**) and has various irregularities. Consequently, after incorporating the adjustments, the NCB shows negative balance of Rs.310.551 million and is overstated by Rs.399.023 million.

	Adjusted Net Capital Balance, As on June 30, 2012 (Rs.)			
	As submitted by IISPL		Calculated by Inspection Team	
Current Assets				
Cash in hand	23,607		23607	
Cash at Bank	89,732	113,339	99,732	123,339
Trade Receivables				
Book Value	561,820,521		675,522,365	
Less overdue for more than 14 days	(78,019,529)	483,800,992	(627,746,035)	47,776,330
Investment in Listed Securities in the name of Broker				
Securities on the exposure list marked to market	42,687,771		44,623,271	
Less: 15% Discount	(6,403,166)	36,284,605	(6,693,491)	37,929,780
Securities held for clients		102,385,449		207,933,964
TOTAL CURRENT ASSETS (A)		622,584,385		293,763,414
Current Liabilities				
Trade payables	148,286,401		148,965,322	
Less overdue for more than 30 days)	(85,000,000)	63,286,401	(62,920,775)	86,047,037
Other Liabilities		470,826,544		518,267,518
TOTAL CURRENT LIABILITIES (B)		534,112,945		604,314,555
NET CAPITAL BALANCE (A-B)		88,471,440		(310,551,141)

4. **AND WHEREAS**, prima facie, it appears that IISPL by submission of overstated NCB has given information which it had reasonable cause to believe to be false or incorrect in material particular in violation of Section 18 of the Securities and Exchange Ordinance, 1969 (“Ordinance”) which reads as follows:-

“No person shall, in any document, paper, accounts, information or explanation which he is, by or under this Ordinance, required to furnish, or in any application made under this Ordinance, make any statement or give any information which he knows or has reasonable cause to believe to be false or incorrect in any material particular.”

5. **AND WHEREAS**, review of securities balances of the following selected clients has revealed differences between clients shares balances as per back office record and their CDC sub-accounts balance. Pursuant to Rule 8 of the 1971 Rules every member/TREC Holder shall prepare and maintain, as required by Sub-Section (1) of Section 6, the books of accounts and other documents, in a manner that should disclose a true, accurate and up-to-date position of his business. However, the below instances reflect non-compliance of the 1971 Rules and also establish that IISPL has prima facie contravened the requirements of Section 12 (6) and 24 of the Central Depositories Act, 1997 (“CD Act, 1997”). Details of the difference in books of accounts are given below:-

No	Name of Sub-Account holder	Symbol	Balance as per CDC Statement	Balance as per Back Office
1	SOHRAB RUSSIE DINSHAW, (SUB Ale. # 8912)	HUBC	Nil	42,500
		INIL	Nil	76,930
		NCPL	Nil	47,415
2	002004 RASHEED IBRAHIM (BOK) (SUB Ale. # 3384)	BILF	3,000	Nil
3	002007 MEHMOOD SHEIKHANI (SUB Ale. # 8383)	GAMON	5,000	Nil
		HMIM	2,659	Nil
		QUICE	600	Nil
4	005001 MOHAMMED TAUFIQ (SUB Ale. # 646)	ASLPS	500	250
5	015023 ABDUL KADER (2) (SUB Ale. # 4242)	ASLPS	7,500	Nil
		BGL	500	Nil
		EFOODS	9,000	25,000
		EPCL	25,000	Nil
		FFBL	19,000	Nil
		FFC	50	Nil
		JSVFL	10,000	Nil
		KOHC	906	Nil
		MBF	25,000	Nil
		PAKRI	70,000	50,000
		PASL	3,525	Nil
5MBL	111	Nil		

		TRG	600,000	Nil
6	026002 SHAIKH KHURRAM MAZHAR (SUB Ale. # 6825)	AHL	Nil	8400
		FFC	NIL	36000
7	026003 MUHAMMAD AFZAL SHEIKH (SUB Ale. # 6841)	DGKC	Nil	5,000
		NBP	Nil	12,000
		PAKRI	Nil	100,000
		PTC	Nil	20,000
8	026004 IRFAN IQBAL (SUB Ale. # 6858)	GLAXO	40	2,640
		NML	Nil	52,500
		NPL	Nil	54,000
9	026031 RAFAQAT IQBAL (SUB Ale. # 7468)	AICL	200	20,200
		DGKC	150	73,150
		NML	Nil	7,500
10	026040 SHEHZAD ANWAR (SUB Ale. # 2030)	EFOODS	13,000	28,000
		EFUL	4,400	20,400
		LUCK	13,425	13,125
		NBP	65	13,565
		NML	301	78,801
11	026054 FAHAD SHAHZAD (SUB Ale. # 9647)	AICL	Nil	5,000
		NBP	Nil	5,000
		NML	2,985	15,985
12	029004 SAQIB FERAZ (SUB Ale. # 9167)	DGKC	Nil	40,000
		NBP	Nil	35,000
13	029008 ABDUL RAHEEM (SUB Ale. # 9415)	NCPL	NIL	1,200,000

6. **AND WHEREAS**, Section 24 of the CD Act, 1997 provides:-

“(1) A participant shall not handle or authorize or permit any handling of book-entry securities entered in the sub-accounts maintained under his account without authority of the sub-account holder.

(2) A participant shall not, except with the authority of his clients, handle or authorize or permit any handling of book-entry securities beneficially owned by such clients and entered in his account.”

7. **AND WHEREAS**, Section 28 of the CD Act, 1997 provides that:

“Notwithstanding anything contained in Sub-Section (1) whoever knowingly and willfully contravenes or attempts to contravene or abets the contravention of the provisions of Section 24 shall be punishable with a fine which may extend to one million rupee and to

further fine not exceeding twenty thousand rupee for every day after the first contravention during which the contravention continues or with imprisonment for a term which may extend to five years, or with both”

8. **AND WHEREAS**, Regulations 41(1)(a) requires the broker to maintain separate bank account which will include all the fund deposits of its clients along with record/breakdown of clients' balances. Perusal of Books of Accounts has revealed that IISPL has, effective from May 31, 2012, been maintaining a separate Bank Account No. 000515-03-07 in Bank Al-Habib with the title of client account. However, said account is not being used for clients' funds. Only four transactions amounting to Rs. 81,000 have been observed since opening of the account, whereas, clients' funds are being dealt with through other bank accounts such as Bank Al-Falah Limited Account No. 0100-2094 001, Bank Al Habib Account No. 0081-000515-01-5.

9. **WHEREAS**, it has been observed that IISPL has been charging late payment charges to its clients @ 24% p.a. on monthly basis, who do not clear their dues in time, For the year ended June 30, 2012, IISPL has charged an amount of Rs. 54.655 million on account of late payment which is contravention of Section 16 of the Ordinance, which is reproduced below for convenience.

“No member or associate shall, in contravention of any rules under this Ordinance, directly or indirectly,-

- a) Extend or maintain credit, or arrange for extension or maintenance of credit, to or for any person for the purpose of purchasing or carrying any security; or*
- b) Borrow on any security or lend or arrange for the lending of any carried for the account of a customer; or*
- c) Pledge or arrange for the pledging of any security carried for the account of any customer.”*

Term and Condition No.7 (b) of SAOF which is mentioned below:

“In the event of non-receipt of payment from the Account Holder on settlement day against securities bought on account of the Account Holder, the Broker may transfer such securities to his Collateral Account under intimation to the Exchange, after complying with the requirements as mentioned in the General Regulations of the Exchange.”

10. **WHEREAS** it has been observed that shares of Mr. Dewan Mujtaba Faruqi - Sub Account No 9498 have been pledged, directly from his sub account, in favor of Habib Metro Bank Limited in respect of running finance facility provided to IISPL. IISPL failed to provide specific authority of the respective client for the said pledge. Section 12 (6) of the CD Act, 1997 stipulates that a participant shall not create a pledge over any book-entry securities entered in any sub-accounts maintained under his account with the Central Depository Company without authorization of the sub-account holder concerned. In line with that Section 24 of the CD Act, 1997 also prohibits handling of book entry securities entered in the sub accounts without the authority of the sub account holders.

11. **NOW THEREFORE**, you are hereby called upon to show cause in writing by **June 14, 2013** as to why action as provided under Section 22 of the Ordinance and/or Section 28 of the CD Act, 1997 may not be initiated against IISPL for violation as indicated above. You are

further directed to appear in person or through an authorized representative (with documentary proof of such authorization), on **June 19, 2013** at 11:00 a.m. at the SECP Headquarters, 9th Floor, NIC Building, Jinnah Avenue, Blue Area, Islamabad. You are advised to bring all relevant record in original, which you may consider necessary for clarification/or in your defense. This notice sufficiently discharges the Commission's obligation to afford IISPL an opportunity of hearing in terms of Section 22 of the Ordinance and Section 28 of CD Act, 1997 and in case of your failure to appear on the stated date of hearing it will be deemed that IISPL has nothing to say in its defense and the matter will be decided ex-parte on the basis of available record.

12. Please note that this show cause is being issued without prejudice to any action, which may be taken or warranted for the above said or any other default under the above referred or any other provision of law. Kindly acknowledge receipt of this show cause notice through return fax or courier at your earliest

Hasnat Ahmad
"Director (MSRD)"

3. Pursuant to the said SCN, the Respondent submitted its comments on June 27, 2013. However, on the request of the Respondent and its legal counsel, the hearing was adjourned thrice and rescheduled for July 1, 2013, July 2, 2013 and July 17, 2013. Mr. Mehmood Sheikhan, representative of the Respondent appeared for hearing on July 17, 2013. The following arguments were put forward by the Respondent in its written response and during the hearing held on July 17, 2013:-

1. **"Net Capital Balance.**

i. **Trade Receivable;** The team has considered Rs. 627.746 million receivables out of Rs. 675.522 million as overdue i.e. for more than 14 days which is not the case as most of our clients are running and active while those clients who are in-active and their receivables balance is more than 14 days is being already considered as overdue for more than 14 days i.e. Rs. 78.020 million.

ii. **Investment in listed Securities in the name of Broker;** The team has calculated investment value of Rs. 44.62 million and taken 15% margin of Rs. 6.693 million while difference in IISL and team is coming due to non-exclusion of not eligible securities for KSE margin eligible list.

iii. **Current Liabilities;** The Team has excluded an amount of Rs. 75 million which is overdue more than 30 days. The team reported gross trade creditors are of Rs. 148.968 million which IISL reported trade creditors of Rs. 194.79 million i.e Rs. 45.82 million difference which being an amount of provided as fund to invest in market and we handle the each client separately. Therefore, we formed an account for collective investment in the name of Ismail Iqbal Securities (Pvt.) Ltd. which also shows the investment of clients.

Therefore these clients' balances are credits and more than 30 days. After the liquidation of investment securities we distributed their profit but team has reported these clients as loan and classified as other liabilities and adjusted with Net Capital Balance which is not the case. More ever, the team has taken 62.292 million as overdue more than 30 days while excluding an amount of Rs. 75 million which is overdue more than 30 days. Therefore, IISl calculation is correct in this head.

iv. **Other Liabilities;** The Team has included Rs. 47.44 Million of client credits which are overdue more than 30 days and included in other liabilities.

2. **Difference in Books of Account/shares in back office and CDC accounts of clients**

S. No.	Name of Sub-Account holder	Symbol	Balance as per CDC statement	Balance as per office book	Remarks
1	SOHRAB RUSSIE	HUBC	NIL	42,500	The client has not cleared his debit and his shares are lying in house. Also reconciliation has been provided with comments showing house and client Investment
	Dinshaw (sub Ale #8912	INIL	NIL	76930	
		NCPL	NIL	47415	
2	2004				Client shares are lying in another trading account # 1112, copy of back office is attached
	RASHEED IBRAHIM (BOK) (SUB Ale #3384	BILF	3,000	NIL	
3	2007	GAMON	5,000	NIL	Client shares are lying in another trading account # 1228 copy of back office is attached.
	MEHMOOD SHEIKHANI (SUB Ale 8383)	HMIM	2,659	NIL	
		QUICE	6000	NIL	
4	MOHAMMED TAUFIQ (SUB Ale 646)	ASLPS	500	250	
	15023	ASKOS	7,500	NIL	Client shares are lying in another trading account # 15007 which team do not request for print also the client has not cleared his debit and his shares are lying in house account copy of back office is attached.
5	ABDUL KADAR (2) (SUB Ale # 4242)	BGL	500	NIL	Client shares are lying in another trading account # 15007 which team do not request for print also the client has not cleared his debit and his shares are lying in house account copy of back office is attached.
		EFOODS	9000	25000	
		EPCL	25000	NIL	
		FFBL	19000	NIL	
		FFC	50	NIL	
		JSVFL	10000	NIL	
		KOHC	906	NIL	
		MBF	25000	NIL	
		PAKRI	70000	50000	
		PASL	3525	NIL	
		SMBL	111	NIL	
6	26002	AHL	NIL	8400	The client has not cleared his debit and his shares are lying in house. Also reconciliation has been provided with comments showing house and client Investments.
	SHAIKH KHURRAM				
	MAZHAR (SUB Ale # 6825	FFC	NIL	36000	
7	26003	DGKC	NIL	5000	The client has not cleared his debit and his shares are lying in house. Also reconciliation has been provided with comments showing house and client Investments.
	MUHAMMAD AFZAL	NBP	NIL	12000	
	SHEIKH (SUB Ale # 6841)	PAKRI		100000	
		PTC	NIL	20000	
8	26004	GLAXO	40	2640	The client has not cleared his debit and his shares are lying in house. Also reconciliation has been provided with comments showing house and client Investments.
	IRFAN IQBAL (SUB Ale # 6858)	NML	NIL	52500	
		NPL	NIL	54000	
9	26031	AICL	200		The client has not cleared his debit and his

	RAFOAT IQBAL (SUB Ale # 7468)	DGKC NML	150 Nil		shares are lying in house. Also reconciliation has been provided with comments showing house and client Investments.
10	26040 SHEHZAD ANWAR (SUB Ale # 2030)	EFOODS EFUL LUCK NBP NML	13000 4400 13425 65 301	28000 20400 13125 13565 78801	The client has not cleared his debit and his shares are lying in house. Also reconciliation has been provided with comments showing house and client Investments.
11	26054 FAHAD SHAHZAD (SUB Ale # 9647)	AICL NBP NML	NIL NIL 2985	5000 5000 15985	The client has not cleared his debit and his shares are lying in house. Also reconciliation has been provided with comments showing house and client Investments.
12	29004 SAQIB FERAZ (SUB Ale # 9167)	DGKC NBP	NIL NIL	40000 35000	The client has not cleared his debit and his shares are lying in house. Also reconciliation has been provided with comments showing house and client Investments.
13	29008 ABDUL RAHEEM (SUB Ale # 9415)	NCPL	NIL	1200000	The client has not cleared his debit and his shares are lying in house. Also reconciliation has been provided with comments showing house and client Investments.

3. Segregation of Clients Assets by the Broker;

IIAPL maintained the separate bank accounts to deposit the clients' funds for this purpose following bank accounts are opened and we have also given our comments in reply to finding of inspection team

- a. 0100-2204 Bank Al Falah Ltd. with title "Ismial Iqbal Securities (Pvt.) Limited-Client Fund"
- b. 0100-2205 Bank Al Falah Ltd. with title "Ismial Iqbal Securities (Pvt.) Limited-Client Fund"
- c. 60118206147-133891 Habib Metropolitan Bank Ltd. -Client Fund"

Out of above three accounts, two accounts of Bank Al Falah accounts has been closed during the year and a new account opened with Habib Metropolitan Bank Ltd. which is operational and IISPL is maintaining this account for clients fund and also break-up of this account has been provided with comment report.

4. I have examined the facts, evidences and documents on record, in addition to written and verbal submissions made on behalf of the Respondent. The arguments raised by the Respondent are discussed and apprised hereunder in seriatim:-

1. Overstatement of the Net Capital Balance

- i. **Trade Receivables.** With regard to the Respondent's comments regarding overstatement of trade receivables, it has been observed that the Respondent in its Clients Accounts Aging Receivable Statement from June 16, 2012 to June 30, 2012 (provided to the inspection team) explicitly reflected gross receivables of Rs. 675.522 million instead of Rs. 561.820 million reported in the NCB and amount of overdue

for more than 14 days Rs. 565.775 million instead Rs. 78.020 million reported in the NCB. The inspection team calculated Rs. 627.746 million overdue for more than 14 days. The inspection team, for the purpose of NCB, excluded three proprietary investment accounts amounting to Rs. 47.503 million from the trade receivables. The team also determined that an amount of Rs. 39.740 million should have been reported being not overdue for more than 14 days. As per the team's calculation trade receivables were Rs. 47.776 million instead of Rs. 483.801 million. Resulting thereby Rs. 436.025 million was overstated by the Respondent in NCB. Therefore, the Respondent's methodology of aging of trade receivables was not in accordance with the requirement of the 1971 Rules. Further, the said methodology did not consider the overdue balances as determined by the Respondent in its own receivables aging report.

ii. **Securities held for clients.** With regard to the understatement of Rs. 105.549 million in the head of securities held for clients, the Respondent reported Rs. 102.385 million in NCB and the inspection team calculated Rs. 207.934 million. In this regard no written/oral comments were submitted by the Respondent in order to explain the said difference. However, while considering the Respondent's comments provided to the inspection team vide letter dated June 26, 2013, it has been observed that the Respondent purchased the securities for clients and showed separately in the net capital balance. In response, the Respondent did not provide any calculation/evidence in support of its calculation. The team calculated Rs. 207.934 million based on their calculation regarding securities lying in the respective CDC sub-accounts as on June 30, 2012 and considering the securities lying in the Respondent's House Account as per the break up provided by it. Further, The inspection team in its Inspection Report explicitly mentioned that benefit of valuation should be subject to the following two points:

- a. Benefit of valuation should only be passed on to the respective clients, who hold securities in their respective CDC Sub Account or as per back office record
- b. Benefit of valuation should not exceed the value of overdue balance

In view of the above, it is evident that the Respondent did not follow the proper methods/basis/procedures for determining the amount reported as clients' securities in NCB, in accordance with the guidelines as provided in Third Schedule of the 1971 Rules.

iii. **Trade Payables.** With regard to the Respondent's written/oral argument regarding understatement of trade payables by Rs. 45.818 million, the inspection team calculated difference amount to Rs. 45.818 million by excluding the amounts payable to those clients where predetermined pattern of profit payments was witnessed, as business relations inheriting specified profit payments reflected more of a loan nature rather than that of trade creditors of the brokerage house. The Respondent did not

provide its basis/methods to the inspection team, whereby, it calculated the amount of overdue trade creditors. Besides, the amount of overdue trade creditors as reported by the Respondent in its NCB did not match with that of its Clients Aging Statement as provided to the inspection team. As per the said statement, the amount of trade creditors overdue more than 30 days was Rs. 58.862 million, whereas the Respondent reported Rs. 75.00 million in NCB. Further, the Respondent has contended that it operates an account for collective investment in the name of the Respondent which shows the investment of clients. After the liquidation of investment securities, profit is distributed among the clients. As per the certificate of Registration granted to the Respondent under the Brokers and Agents Registration Rules, 2001, the Respondent cannot collect deposits from the clients on profit and loss basis and such activity is a violation of the regulatory framework mentioned above. Further, that the Respondent failed to provide basis/method of its calculation.

- iv. **Other Liabilities.** The Respondent has reported an amount of Rs. 470.827 million as other liabilities; however, the inspection team has calculated the same as Rs. 518.267 million. The Respondent has stated that the team has included the difference of Rs. 47.441 million of client credits in other liabilities which is overdue by more than 30 days. As per requirements of Schedule III of the SEC Rules, all current liabilities, other than those reported under trade creditors, are required to be reported under this head i.e. other liabilities. The inspection team has traced the balances of current liabilities other than trade creditors from the Respondent's trial balance as at June 30, 2012 and determined the nature of other liabilities for calculation of NCB and included in other liabilities. The Respondent failed to give any satisfactory explanation in this regard. Therefore, it stands established that other liabilities of the Respondent were understated by an amount of Rs. 47.441 million.

In view of the preceding paras, it has been established that the Respondent overstated its NCB.

2. Difference in shareholding of the clients between back office record and their CDC sub-accounts;

With regard to the issue of non-availability of client's shares in their respective sub-accounts, the Respondent stated that the reason behind transferring of the shares from clients' sub-accounts to its House Account was due to non-payment by the said clients. Therefore, their shares were lying in the House Account. It is pertinent to mention here that the definition of House Account as provided in the Central Depository Company of Pakistan Limited Regulations means an account maintained on the Central Depository Register ("CDR") by an account holder for recording book-entry securities beneficially owned by the account holder. This definition clearly states that only those securities which are beneficially owned by the accountholder can be placed in the House Account.

In this case, the Respondent failed to provide any evidence that the securities appearing in its House Account were beneficially owned by it. In line with that Section 24 of the CD Act also prohibits handling of book entry securities entered in the sub-accounts without the authority of the sub-account holders. Moreover, pursuant to condition 7(b) of the Standardized Accounting Opening Form (“SAOF”) the Respondent was required to transfer such securities to its collateral account under intimation to the Exchange in case of non-receipt of payment from the clients and as per condition 6 of the SAOF, the broker was required to liquidate client holdings in case of non-payment. In view of the above, act of the Respondent to transfer clients’ shares from their sub-accounts to the House Account was in violation of Section 24 of CD, Act 1997.

3. Non-segregation of clients’ assets

Regarding the issue pertaining to non-maintenance of separate accounts for the clients, the inspection team reported that the Respondent opened bank accounts but the same were not being used for clients’ funds. Four transactions amounting to Rs. 81,000 were observed since opening of one of the account. The Respondent’s non-maintenance of separate account for clients’ funds was violation of Regulations 41(1)(a) of the General Regulations.

4. Charging of late payment charges to the clients;

The Respondent admitted the practice of charging late payment charges/liquidation damages to those clients who do not clear their debit balances in time. This practice is identical to in-house/badla financing, which is prohibited under the law and is a blatant violation of Section 16 of the Ordinance. It is clarified that Section 16 of the Ordinance clearly states that *no member or associate can directly or indirectly extend or maintain credit or arrange for the extension and maintenance of credit to or for any person for the purpose of purchasing or carrying any security;* Further, In the presence of margin trading and financing system which is duly regulated under Securities (Leveraged Markets and Pledging) Rules, 2011, opting for other financing mechanism is a clear cut violation of Section 16 of the Ordinance.

5. After a detailed and thorough perusal of the facts, evidence/ information available on record and contentions and averments made by the Respondent during the course of hearing, it is established that NCB submitted by the Respondent was overstated by a large amount and if calculated in strict compliance with the requirements of the 1971 Rules, the NCB of the Respondent would have been in negative thereby implying that the Respondent intended to attain much higher trading exposures and increasing the systemic risk in the market. Therefore, it stands established that the NCB as calculated by the Respondent is not in accordance with the Third Schedule of the 1971 Rules and the Respondent by submission of overstated NCB has submitted a statement and given information which it had reasonable cause to believe to be false

or incorrect in material particular in violation of Section 18 of the Ordinance and Rule 8 (viii) of the Brokers and Agents Registration Rules, 2001. Furthermore, it has also established that the Respondent was found guilty of mishandling the shares of the clients in violation of Section 24 of the CD Act, 1997, non-segregation of the clients assets in violation of Regulation 41(1)(a) of the General Regulations and charging of the late payment charges in violation of Section 16 of the Ordinance. Therefore, in exercise of the powers under Section 22 of the Ordinance and Section 28 (2) of the CD Act, 1997 through this Order, I hereby impose a penalty of Rs. 500,000/- (Rupees Five hundred thousand only) on the Respondent to be deposited in the account of the Commission being maintained in the designated branches of MCB Bank Limited not later than thirty (30) days from the date of this Order and furnish copy of the deposit challan to the Commission. The Respondent is further directed to:-

- i. Discontinue the practice of keeping clients' securities in its House Account and transfer such securities from the House Account to the respective sub-accounts under the supervision of Central Depository Company of Pakistan Limited;
- ii. Discontinue the practice of charging the late payment charges to the clients.
- iii. Discontinue the practice of managing an investment account on behalf of the clients;
- iv. Properly maintain separate bank account for the clients funds; and
- v. Regularize its NCB in line with the requirements of Third Schedule of the 1971 Rules;

6. Moreover, through this Order the Karachi Stock Exchange Limited is directed to vigilantly monitor the trading positions and exposure of the Respondent and to curtail the capital adequacy/exposure limit of the Respondent, as deemed appropriate, till submission of the revised NCB.

7. 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.




Hasnat Ahmad
Director (MSRD)

Dated December 18, 2013