

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

In the matter of Show Cause Notice dated October 22, 2012 issued to M/s. IGI Finex Securities Limited, TREC holder Karachi Stock Exchange Limited

Date of Hearing: November 15, 2012

Present at the Hearing: Authorized Representatives of IGI Finex Securities Limited

1. Mr. Ali Almani (Legal Counsel)
2. Mr. Muhammad Ali Aziz (Legal Counsel)
3. Mr. Raza Hussain Rizvi (CFO)
4. Mr. Junaid Qamar (AVP)
5. Mr. Farrukh Mustafa (Deputy Manager)

Representing (BR&ICW): Mr. Murtaza Abbas (Deputy Director (BR&ICW))

ORDER

This Order shall dispose of the proceedings initiated through a Show Cause Notice No. 4/BRK-19/SE/SMD/2004 dated October 22, 2012 (**“the SCN”**) issued to M/s. IGI Finex Securities Limited (**“the Respondent”**), under section 22 of the Securities and Exchange Ordinance, 1969 (**“the Ordinance”**).

2. Brief facts of the case are that the Respondent is a Trading Right Entitlement Certificate (**“TREC”**) holder of the Karachi Stock Exchange Limited (**“the Exchange”**) and is registered with the Securities & Exchange Commission of Pakistan (**“the Commission”**) as a broker under the Brokers and Agents Registration Rules, 2001 (**“the Rules”**). 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 of the books and records required to be maintained by the Respondent. The report dated March 22, 2012 submitted by the inspection team highlighted major violations of the existing regulatory framework governing the brokerage business. The findings of the report were duly forwarded to the Respondent on April 4, 2012. An opportunity of hearing in terms of rule 7(i) of the Inspection Rules was also provided to the Respondent on November 15, 2012.



3. Given the violations highlighted in the inspection report a Show Cause Notice (“SCN”) dated October 22, 2012 was issued to the Respondent, the contents of which are reproduced below:-

SUBJECT: SHOW CAUSE NOTICE IN THE MATTER OF INSPECTION OF BOOKS AND RECORD OF M/S. IGI FINEX SECURITIES LIMITED – BROKER/ TRE CERTIFICATE HOLDER OF KARACHI STOCK EXCHANGE LIMITED.

WHEREAS, M/s. IGI Finex Securities Limited (“IGI”) is registered as Trading Right Entitlement (“TRE”) Certificate Holder of the Karachi Stock Exchange and registered as a broker with the Securities and Exchange Commission of Pakistan (the “Commission”) under the Brokers and Agents Registration Rules, 2001 (the “Brokers Rules”).

2. *AND WHEREAS, the Commission in exercise of its powers under sub section (1) of section 6 of the Securities and Exchange Ordinance, 1969 (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. SECP/SMD-CW/(91)/2011 dated December 9, 2011 of the books and record required to be maintained by IGI. The inspection team submitted the inspection report to the Commission on March 22, 2012 which was forwarded to IGI in accordance with rule 7 of the Inspection Rules.*

3. *AND WHEREAS, on review of the inspection report it was revealed that IGI has been involved in trading for generating commission income in violation of Clause B 4 (1) of the Code of Conduct of Brokers Rules. The detail of these transactions observed by the inspection team is as under:*

Date	Time	Trans ID	Symbol	BUYER	Seller	Rate	Qty	Value
4-Feb-11	1550039468	CROSS	ENGRO	GOLDMAN SACHS & CO.	IGI FINEX SECURITIES LIMITED	217.51	100,000	21,751,000
4-Feb-11	1550268843	CROSS	ENGRO	GOLDMAN SACHS & CO.	IGI FINEX SECURITIES LIMITED	217.51	100,000	21,751,000
4-Feb-11	1550506500	CROSS	ENGRO	GOLDMAN SACHS & CO.	IGI FINEX SECURITIES LIMITED	217.51	50,000	10,875,500
4-Feb-11	1636445093	CROSS	ENGRO	IGL FINEX SECURITIES LIMITED	GOLDMAN SACHS & CO.	217.51	100,000	21,751,000
4-Feb-11	1636574156	CROSS	ENGRO	IGL FINEX SECURITIES LIMITED	GOLDMAN SACHS & CO.	217.51	100,000	21,751,000
4-Feb-11	1637081343	CROSS	ENGRO	IGL FINEX SECURITIES LIMITED	GOLDMAN SACHS & CO.	217.51	50,000	10,875,500
21-Dec-10	1502424918	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1503070856	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	AS KARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1503109606	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1503157731	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1503365231	CROSS	AIVIMF	IGL FINEX SECURITIES LIMITED	AS KARI BANK LIMITED	8.14	500,000	4,070,000

21-Dec-10	1508041950	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	AS KARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1512320231	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1512398043	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1512560856	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1513035700	CROSS	AMMF	IGI FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1513125231	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1513249450	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1513296012	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1532534137	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1533098512	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1533279918	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1534239606	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1534322106	CROSS	AMMF	IGL FLNEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1536557262	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1537178043	CROSS	AMMF	IGI FINEX SECURITIES LIMITED	AS KARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1538094606	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1538165856	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1539024293	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1540470856	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1540573512	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1541389450	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1541436012	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1541492731	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	15415,49450	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1542017418	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1542226012	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1542348825	CROSS	AMMF	IGI FLNEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1542406325	CROSS	AMMF	IGI FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1542455387	CROSS	AMMF	IGL FLNEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1542501793	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1542549293	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000

21-Dec-10	1543018981	CROSS	AMMF	IGI FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1543065856	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1543113200	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1543157575	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1543326793	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1543390543	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1543470075	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1544074606	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1544138668	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1544206481	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1544261325	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1544531012	CROSS	AMMF	IGI FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1544580856	CROSS	AMMF	IGI FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1545221793	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARI BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1545357106	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	500,000	4,070,000
21-Dec-10	1545568356	CROSS	AMMF	IGL FINEX SECURITIES LIMITED	ASKARJ BANK LIMITED	8.14	400,000	3,256,000

4. **AND WHEREAS**, IGI used "Portfolio" reason code for the purpose of transfer its securities under repo/ reverse repo transactions to lenders, which is a clear violation of Regulation 9.1.1. of the CDC Regulations, as portfolio reason code can only be used in the case of transfer of securities of the same person from his/her one account to another. Further, the team identified number of instances, wherein, IGI transferred shares of various scrips to First Capital Equities Limited with the description "On request", however, same were not reflected in the back office records and trading records. The aforesaid transfers are in contravention with Regulation 9.1.1. of the CDC Regulations, details of which are reproduced hereunder:

Date	Scrip	Transaction ID	Quantity
05/11/2010	DGKC	2010-1250952	1,407,600
25/11/2010	Engro	2010-1272985	314,600
02/12/2010	Engro	2010-1284194	123,000
03/12/2010	Engro	2010-1285594	317,400
13/12/2010	Engro	2010-1299991	108,556
14/12/2010	Engro	2010-1302739	691,444
10/11/2010	FFBL	2010-1256535	400,000
10/11/2010	FFBL	010-1256671	100,000
11/11/2010	FFBL	2010-1259430	440,000

11/11/2010	FFBL	2010-1259435	60,000
25/11/2010	FFBL	2010-1273814	175,052
25/11/2010	FFBL	2010-1272982	324,948
29/11/2010	FFBL	2010-1277532	500,000
22/11/2010	HUBC	2010-1267141	750,000
05/11/2010	I.M. C.L.	2010-1250973	37,000
15/11/2010	IGI Insurance	2010-1264245	40,000
16/11/2010	IGI Insurance	2010-1266117	37,500
22/11/2010	IGI Insurance	2010-1267759	28,222
23/11/2010	IGI Insurance	2010-1268559	48,123
26/11/2010	IGI Insurance	2010-1276072	52,300
02/12/2010	Lucky Cement	2010-1283428	150,000
20/12/2010	Lucky Cement	2010-139548	225,000
24/12/2010	Lucky Cement	2010-1316864	225,000
02/12/2010	UBL	2010-1283424	502,050
30/11/2010	UBL	2010-1279477	152,553
23/11/2010	UBL	2010-1268561	145,639

5. **AND WHEREAS**, in the financial statements of IGI for the year ended June 30, 2011 it has been disclosed that "clients shares" have also been underlined against the repo borrowing and details of these clients were not provided to the inspection team by IGI which implies that these shares were underlined without proper authorization. Further, in the said audited financial statements, IGI has disclosed 859,405 shares of Bank Al-Falah Limited amounting to Rs. 8.13 million as their investment in shares. This investment was compared with the House Account of IGI maintained with CDC, as at June 30, 2011 which reflected 33.907 million shares thereby resulting in huge difference of 33.047 million shares. IGI has also failed to provide to the inspection team details with regard to name of clients whose securities were pledged, details of such securities and written authorization from such clients in respect of pledging of shares. Failure of IGI to provide these details/information/documents implies that these shares were moved and/or pledged with the Banks/others without authorization and appears to be a violation of Section 24, of the CDC Act, 1997.

6. **AND WHEREAS** during the course of inspection, it was also observed that IGI has been charging liquidation damages to its clients, who have debit balances, at the rates ranging from 18% to 24% p.a. and in this regard they have earned Rs. 18.675 million as per audited financial statements of IGI for the year ended June 30, 2011.

7. **AND WHEREAS**, on review of the inspection report it has come to the notice of the Commission that the calculation of Net Capital Balance ("NCB") of IGI as on June 30, 2011 certified by M/s. Yousuf Adil Saleem & Company, Chartered Accountants, has various irregularities and consequently after incorporating the adjustments by our inspection team, the NCB of IGI shows negative balance of Rs. 425.09 million.

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8. **AND WHEREAS**, Prima facie, it appears that the NCB as calculated by IGI is not in accordance with the Third Schedule of the 1971 Rules and that IGI by submission of overstated NCB has prima facie 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 which provides that:

“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.”

9. **AND WHEREAS** in light of the facts mentioned above, it appears that IGI is prima facie in contravention of Clause B 4 (1) of the Code of Conduct of Brokers Rules, Regulation 9.1.1 of CDC Regulations, Section 24 of the CDC Act, 1997 and Third Schedule of the 1971 Rules read with Section 18 of the Ordinance.

10. **AND WHEREAS**, if any person contravenes or otherwise fails to comply with the provisions of the Ordinance or any rules or regulations made thereunder, the Commission may by order direct such person to pay the Commission by way of penalty such sum in accordance with Section 22 of the Ordinance.

11. **AND WHEREAS**, Section 22 of the Ordinance provides that:

(1) “if any person-

(c) contravenes or otherwise fails to comply with the provisions of the Ordinance or any rules or regulations made there under;

the Commission may, if it is satisfied after giving the person an opportunity of being heard that the refusal, failure or contravention was willful, by order direct that such person shall pay to the Commission by way of penalty such sum not exceeding fifty million rupees as may be specified in the order and, in the case of a continuing default, a further sum calculated at the rate of two hundred thousand rupees for every day after the issue of such order during which the refusal, failure or contravention continues.

12. **AND WHEREAS**, Section 28 of the CDC Act, 1997 provides that:

- i. Whoever knowingly and willfully contravenes or attempts to contravene or abets the contravention of any of the provisions of this Act or the regulations made thereunder shall be punishable with a fine which may extend to five hundred thousand rupees and to a further fine not exceeding ten thousand rupees for every day if such contravention continues after the imposition of the fine.



- ii. *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 rupees and to a further fine not exceeding twenty thousand rupees 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.*
- iii. *Where an offence under this Act has been committed by a company, every person who at the time the offence was committed was in charge of, and was responsible to, the company for the conduct of the business of the company shall be deemed to be guilty of the offence and shall be liable to be proceeded against and punished accordingly.*
- iv. *Notwithstanding anything contained in sub-section (3), where an offence under this Act has been committed by a company and it is proved that the offence has been committed with the consent or connivance of, or is attributable to any neglect on the part of any director, manager, secretary or other employee of the company, such director, manager, secretary or other employee shall also be deemed to be guilty of the offence.*

13. ***NOW THEREFORE***, you are hereby called upon to show cause in writing by **October 31, 2012**, as to why action as provided in Section 22 of the Ordinance read with Section 28 of the CDC Act, 1997 may not be initiated against IGI for violations stated above. You are further directed to appear in person or through an authorized representative (with documentary proof of such authorization), on **November 2, 2012 at 11.00 a.m.** at the Commission's Head office at 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/defense of your stance. This notice sufficiently discharges the Commission obligation to afford IGI an opportunity of hearing in terms of Section 22 of the Ordinance and in case of failure to appear on the stated date of hearing it will be deemed that IGI has nothing to say in its defense and the matter will be decided on the basis of available record.

Hasnat Ahmad
Director

4. Thereafter, the hearing fixed for October 31, 2012 was adjourned till November 15, 2012 on the request of the Respondent. Pursuant to the SCN and the said hearing, the Respondent submitted written reply vide its letters dated November 10, 2012 and November 27, 2012 respectively.



a) ***Generation of Commission in violation of Clause B 4(1) of the Code of Conduct for Broker***

In the said observation, the Respondent *prima facie* entered into transactions with Askari Bank Limited (“ASKB”) and Goldman Sach for generating income through commission. The Respondent in its written submission dated November 10, 2012 asserted that certain clients requested the Respondent to act as a counter party in order to facilitate them in revaluing their assets. These clients are large institutions with large quantity orders and cannot be encouraged by a broker to enter into trades against their interest. All the trades mentioned in the SCN were executed on the specific instructions of these clients. In support of its contention the Respondent provided a copy of the Memorandum of Confirmation dated December 21, 2010 from ASKB showing that these were genuine transactions executed on the instructions of ASKB.

b) ***Non-compliance with Regulation 9.1.1 of CDC Regulations***

In reply to this observation, the Respondent submitted that it entered into repo and reverse repo transactions with counter parties against shares. In reverse repo transactions with First Capital Equities Limited (“FCEL”) it had an arrangement that shares will be transferred in the name of the Respondent rather than being pledged in order to secure its position in case the counter party defaults. The same arrangement was in place for repo transactions with other parties. Earlier, reason code “Repo” was available in the Central Depository System (“CDS”) and the same was used for repo transactions. Later on the reason code “Repo” was discontinued by Central Depository Company of Pakistan Limited (“CDC”) and consequently reason code “Portfolio transfer” was used for repo transactions. The Respondent asserted that it has now abandoned the practice of repo borrowings and the only transaction pending for settlement is of a reverse repo with FCEL for which recovery process is underway. In support of the said statement the Respondent submitted its letter dated December 30, 2011 addressed to FCEL for returning the shares of SNGPL, SSGC, NML, LUCK, UNILEVER and MCB. The Respondent also mentioned that its Ex-CEO entered into various transactions on behalf of the Respondent which resulted in heavy losses. The Ex-CEO was later on suspended by the Board of Directors on November 22, 2011 and was terminated with effect from December 20, 2011 for failing to perform his fiduciary duties and breach of trust. In addition, the Respondent also provided copies of Suit No. 686 of 2012 and FIR dated March 24, 2012 through which legal actions were initiated against the Ex-CEO. The Respondent also asserted that as CEO he signed the ‘code of conduct – employee’s declaration’ according to which he was duty bound to comply with the laws, regulations, and statutory provisions in good faith. According to the Respondent, Ex-CEO contravened the terms of the code duly signed by him and defrauded the Respondent in various business transactions. In view of this the Respondent requested that since the violation mentioned herein was due to the misconduct of its Ex-CEO against whom legal action had already been initiated, therefore, no action should be initiated against the Respondent for the wrong doings of its employee. In support of this request, the Respondent provided a copy of order dated March 20, 2012 passed by HOD-MSCID in the matter of SCN issued to JS Global Capital Limited (“JSGCL”), wherein the honorable HOD-MSCID stated that “*after analyzing*

the policies and procedures in the matter, it is likely that JSGCL may not be aware of the activities of the Individual clients in collusion with its employees. This assumption regarding non-involvement of JSGCL is further supported by the fact that it took timely action against the employees found to be non-compliant of the policies and controls.”

Here it is important to note that the Respondent accepts the said violation however puts up the responsibility on its Ex- CEO for all the wrong doings. In this regard, I have perused the offer letter dated April 6, 2009 along with the ‘minutes of Board of Director’s meeting’ held on February 7, 2009 and the General Power of Attorney issued in the name of Ex-CEO by the Respondent. The perusal of these documents reveals that Ex-CEO was fully empowered by the Board of Directors to act on behalf of the Respondent and to take all the business decisions. Ex-CEO after joining the Respondent as CEO also signed the ‘code of conduct – employee’s declaration’ according to which he was duty bound to comply with the laws, regulations, and statutory provisions in good faith. All the documents pertaining to the appointment of Ex-CEO clearly show that he was duly empowered by the Board of Directors to act as CEO of the Respondent. However, at the same time we cannot forget this fact that the intentions of a person can only be gauged by his actions and in this particular case Ex-CEO kept the Board of Directors in complete darkness due to which his misdeeds remained hidden.

c) *Non-Compliance with Section 24 of the CDC Act 1997*

With regard to this violation, the Respondent categorically denied that shares of any client were pledged, used or transferred. Here the Respondent reiterated that the Ex-CEO entered into various arrangements with certain brokerage houses. The shares appearing in the CDC account of the Respondent mainly related to unsettled trades with certain brokerage houses and shares relating to Repo arrangements.

d) *Charging of liquidation damages from the clients*

With regards to this observation, the Respondent stated that it charged liquidation damages to clients under the relevant clause of the account opening form which states that:

“In case the account holder fails to pay any amount due on or before the due date specified herein or otherwise notified to the account holder, the Broker shall have the right to claim liquidation damages @ 1 month KIBOR + 10% p.a. whichever is higher on per day basis for each day of delay in payment by the account holder (as compensation for financial loss but not by way of financing or penalty). The account holder shall be liable to make such payment without prejudice to any other legal or contractual rights of the Broker, including the Broker’s other rights, discretions, remedies and recourses specified in these Special Terms and Conditions.”

Based on the contents of this clause the Respondent asserted that the amount was charged as compensation for financial loss but not by way of financing or penalty. Therefore, it may not be construed as in-house badla financing. The Respondent also mentioned that the new

management is now working with the clients purely on cash basis and no client is entertained who delays payments. Clients now trade through the Respondent either against cash balance available in their accounts or purely on Delivery versus Payment basis. In support of its efforts and commitment to eliminate this practice the Respondent informed that as on June 30, 2011 the liquidation damages were amounting to Rs. 18.67 million, however, due to the continuous efforts of the new management this amount has been substantially reduced to Rs. 0.15 million as of September 30, 2012. The Respondent further assured to remain compliant with the requirements of law in future.

e) Calculation of Net Capital Balance as on June 30, 2011

With regards to this violation, the Respondent asserted that the major item which resulted in difference in calculation of NCB submitted to KSE and the one calculated by the inspection team was the "trade receivables". The amount of Rs. 654.7 million includes Reverse Repo payable by FCEL to the Respondent. The Respondent discussed this issue with its external auditor and then it was concluded that the Third Schedule of the SEC Rules, does not cater to the treatment of these items, therefore there was an element of interpretation involved in determining the treatment of this item. It was further discussed that since the Third Schedule mentions valuation basis only and explicitly for 'Trade Receivables' to be valued at 'Book value less those overdue for more than fourteen days', therefore this valuation basis cannot be applied to these items. However, the Respondent interpreted that since these amounts were recoverable by the Respondent, therefore it was justified to value the same at their face/book value. However, due consideration was given to the fact that such treatment of these items should be duly disclosed in the statement of NCB and that was done accordingly. The Respondent further asserted that this treatment was consistently followed in the earlier statements of NCB and no objection was ever received from the regulator. The amount of Rs. 654.7 million also included unsettled transactions made through Negotiated Deal Markets and due consideration was given to the fact that such treatment of including unsettled trades in 'Trade Receivables' should be duly disclosed in the statement of NCB. The Respondent also stated that Section 18 of the Ordinance incorporates an element of *mens rea* and in this case the Respondent calculated the NCB in accordance with International Accounting Standards and to the best of its knowledge. The Respondent or any of its employees did not knowingly or willfully made wrong or incorrect statement. This fact was substantiated by the fact that the Respondent specifically disclosed in its statement the manner in which the NCB was calculated. Further, Respondent's view that in the past the regulator did not object to any such treatment also carries some weight since regular inspections of the brokerage houses were recently started and flaws in the current business practices started surfacing recently.

5. I have examined the facts, evidences and documents on record, in addition to written and verbal submissions made on behalf of the Respondent and the documents submitted subsequent to the hearing. The perusal of facts and statements presented by the representatives of the Respondent strongly suggests that transactions in which the violations were observed were carried out by the Ex- CEO of Respondent by misusing his powers delegated to him by the Board of

Directors. The present management of the Respondent is putting up serious efforts to keep the business issues back on track. The cases filed against the Ex-CEO of the Respondent, abandoning the practice of repo borrowing and ongoing negotiations with FCEL for the reconciliation of repo transactions, providing memorandum of confirmation from ASKB regarding the genuineness of transactions, abandoning the practice of charging the liquidation damages from the clients, dealing with clients on Delivery versus Payment basis and reducing the liquidation damages from Rs. 18.67 million in June 30, 2011 to Rs. 0.15 million as of September 30, 2012 strongly indicates the positive intent of the present management.

6. However, this office also considers it necessary to record its deep concern over the lack of control by the Board of Directors of the Respondent on the activities of the CEO. Given the above findings, the Respondent is hereby reproached and censured for conduct which does not commensurate with high standards of conduct expected of the Respondent. It is also stressed that the Respondent should ensure proper control over the activities of all of its employees to avoid violations of the regulatory framework in future.
7. Although the violations of the rules and regulations mentioned in the SCN demands for much higher degree of penalty, however, while deciding this matter I have given due weightage to the aforesaid efforts of the Respondent and therefore while taking a lenient view, in exercise of the powers under Section 22 of the Ordinance, through this Order, I hereby impose a penalty of Rs. 50,000/- (Rupees Fifty Thousand Only) on the Respondent. Further, the Respondent is directed to make necessary arrangements for compliance with the regulations mentioned in the SCN and submit a comprehensive report in this regard to this office within sixty days of the date of this order.
8. The matter is disposed of in the above manner and the Respondent is directed to deposit the penalty 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 chalan to the undersigned.
9. This Order is issued without prejudice to any other action that the Commission may initiate against the Respondent in accordance with the law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.


Hasnat Ahmad
Director (MSCID)

Announced on February 15, 2013
Islamabad.