



Securities and Exchange Commission of Pakistan

Securities Market Division

Through Courier

Before The Director / HOD (MSRD)

In the matter of Show Cause Notice issued to B&B Securities (Private) Limited

Date of Hearing:

November 8, 2013

Present at the Hearing:

Representing B&B Securities (Private) Limited

(i) *Mr. Adnan Mehboob*

Chief Executive Officer

Assisting the Director/HOD (MSRD)

(i) *Ms. Najia Ubaid*

Deputy Director

(ii) *Mr. Mian Muhammad Imran*

Deputy Director

ORDER

1. This Order shall dispose of the proceedings initiated through Show Cause Notice bearing No. 1(9) SMD/MSRD/C&IW/2013 dated October 7, 2013 ("SCN") served to B&B Securities (Private) Limited ("**Respondent**"), Trading Right Entitlement Certificate Holder/Broker of the Karachi Stock Exchange Limited ("**KSE**") by the Securities and Exchange Commission of Pakistan ("**Commission**") under Section 22 of the Securities and Exchange Ordinance, 1969 ("**Ordinance**") read with Rule 8 of the Brokers and Agents Registration Rules, 2001 ("**Brokers Rules**") and Section 28 of the Central Depositories Act, 1997 ("**CDC Act**").

2. Brief facts of the case are that 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 ("**Inspection Rules**") ordered an inspection of the books and records required to be maintained by the Respondent. The

SECURITIES & EXCHANGE
COMMISSION OF PAKISTAN
NIC Building, 63 Jinnah Avenue,
Islamabad, Pakistan





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following officers of the Commission were appointed as inspectors ("**Inspection Team**") for the purpose vide order dated May 8, 2013:

- | | |
|---------------------------|--------------------|
| a) Mr. Muhammad Tanveer | Deputy Director |
| b) Mr. Adnan Ahmed | Deputy Director |
| c) Mr. Moizuddin Siddiqui | Assistant Director |

3. The Inspection Team submitted the report ("**Inspection Report**") on June 25, 2013 which was shared with the Respondent in accordance with Rule 7 of the Inspection Rules on June 27, 2013. The response of the Respondent in the context was received vide letter dated July 29, 2013. The Inspection Report revealed that the Respondent was involved in imposing late payment charges to its clients. Moreover, irregularities in calculation of Net Capital Balance ("**NCB**") as on December 31, 2012 were observed and it appeared that NCB certificate was not in accordance with the Third Schedule of the Securities and Exchange Rules, 1971 ("**Rules 1971**").

4. The Inspection Report further revealed that M/s. BDO Ebrahim & Co. Chartered Accountants ("**Auditor**") qualified the report for the period ended June 30, 2012 and NCB certificated for June 30 and December 31 2012. The qualification of auditor in the context is reproduced below:

"The Company has transferred investments of its clients in its own CDC sub account for purposes of meeting pledge requirements for financial institutions. This is a violation of the directives issued by the Securities and Exchange Commission of Pakistan with respect of transfer of book entry securities, further clarified through circular dated September 22, 2008. As a result of this transfer, we are unable to independently verify the completeness of investments held by the Company as at the balance sheet date as the CDC sub account of the Company includes the Company's own investments as well the investments of its clients which have been pledged with financial institution.

The balance under the head "trade debts" and "trade and other payables" includes balances amounting to Rs. 68.561 million (unsecured - net of provisions) and Rs. 73.901 million, respectively, which have remained unchanged. We understand that the ageing is prepared by applying receipts/payments on a first in first out basis. Consequently, the ageing does not





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reflect an invoice wise position of amounts outstanding. On the basis of the above, we have not been able to obtain sufficient and appropriate audit evidence to support management's assessment of impairment of trade debts outstanding and carrying value of payables outstanding."

5. The Commission in light of the Inspection Report and the comments of the Respondent served a SCN to the Respondent under Section 22 of the Ordinance, Rule 8 of the Brokers Rules and Section 28 of the CDC Act. Hearing in the matter of aforesaid SCN was scheduled for October 22, 2013 at the Commission's head office at Islamabad. The Respondent vide letter dated October 21, 2013 requested that hearing be fixed at Karachi and further requested for extension of 15 days. Acceding to the request of the Respondent, hearing was rescheduled for November 8, 2013 at the Commission's Karachi Office.

6. The Respondent's written response was received in the Commission on November 4, 2013. Mr. Adnan Mehboob, Chief Executive Officer of the Respondent attended the hearing on behalf of the Respondent ("**Representative**"). The following arguments were put forward by the Respondent in its written response to the SCN and by the Representative of the Respondent during the hearing held on November 4, 2013:

a) **Trade Receivables:** The Respondent in its written response stated that:

"The primary difference computed related to impact of custody of clients for whom balances exceeds 14 days period. The gross amount of receivables overdue for more than 14 days is Rs. 165,635,040.62/. This does not take into account impact of custody held in respect of balances overdue for more than 14 days amounting to Rs. 63,971,139 permissible under rule 2d and presented as adjusted against the amount overdue by more than 14 days. The trade debts have not been overstated as we have taken the benefit of securities held by client and adjusted the balance of overdue amount for more than 14 days. Please note that we have discounted the custody by 15% although this is not required under the Regulation. "

The Representative of the Respondent during the hearing asserted the stance taken by the Respondent in its written response. He was enquired about the difference in figure calculated by the Inspection Team and submitted in the written reply of the Respondent, however, no reasonable response in the context was provided.





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- b) **Investment in Listed Securities:** The Respondent with regard to understatement of investment in listed securities stated that:

"The investment is not understated as the company has investments under its own name amounting to Rs. 12.483 million. The total value of securities held by B&B is Rs. 77.878 million. Out of this, Rs. 12.483 million represents investment of B&B Securities and the remainder amount to Rs. 65.395 million represents securities held by clients."

The Representative of the Respondent reiterated the above stance and further added that no complaint has ever been registered with the Commission against the Respondent. He further added that the Respondent does not maintain collateral accounts.

- c) **Securities purchased for clients:** With regard to securities purchased for clients, the Respondent in its written response stated that:

"The securities purchased for clients have not been overstated and misclassified because the company has transferred investment of its clients in its own CDC sub account for the purposes of meeting pledge requirements for financial institutions. As a result of this transfer, the investment held by the company as well as the investments of its clients which have been pledged with the financial institutions are both held in the house account. The custody balance shall be separately presented under a different line as per the format prescribed as opposed to being adjusted against the balance in excess of days. The NCB certificate is also qualified as we were unable to provide independent verification of this to our auditors as securities were transferred to house account. Accordingly, NCB is overstated rather the custody has been classified under trade debts rather than as a separate line."

The Representatives of the Respondent asserted the above position.

- d) **Trade Payables:** The Respondent in the written response communicated that:

"The company now adopts that all cheques are received and paid by customer are kept in client separate account and we also maintain that separated banks are balance with payable to customer as per rules and regulations KSE and also the company has now opened collateral accounts under its participant accounts."

7. I have heard the arguments presented by the Representative of the Respondent at length during the hearing. Additionally, I have perused the available record and the written





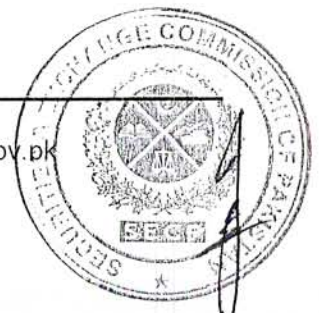
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reply filed by the Respondent. Accordingly, my findings on the arguments and assertions made by the Respondent to the issues raised in the SCN are as follows:

- a) The Respondent while explaining the overstatement of trade receivables, in its response to the SCN, provided a new figure to which no reconciliation was attached; neither Representative of the Respondent was being able to explain it during the course of hearing. Furthermore, the Respondent in its written response added that it applied a haircut of 15% on the receivables' figure which wasn't a requirement of the regulatory framework and doesn't justify the overstatement of receivables and NCB, resulting thereby in allowance of extra exposure.
- b) The qualification of the report by the Auditor of the Respondent supports the fact that the Respondent has failed to maintain proper books of accounts in order to allow the Auditor to verify the payables and receivables figure and prepare correct NCB certificate.
- c) The Respondent in its written response and the Representative of the Respondent during the course of hearing accepted the fact that they have placed clients' securities in the house account of the Respondent to meet the pledge requirements being in violation of the applicable rules and regulations. The Representative of the Respondent further added that no collateral account has been opened by the Respondent.

8. After a detailed and thorough perusal of the facts, evidence/information available on record, contentions and averments made by the Representative of the Respondent during the course of the hearing, it is evident that the Respondent failed to perform its responsibilities by not maintaining proper books of accounts and not preparing the NCB Certificate in accordance with the Rules 1971. In order to maintain the confidence of investors in the securities market, a number of rules, regulations and procedures have been formulated by the Commission which prescribes the minimum set of standards that a broker has to follow. A broker should be perceived as professional that is beyond reproach and it should perform its functions in a fair, proficient and impartial manner.





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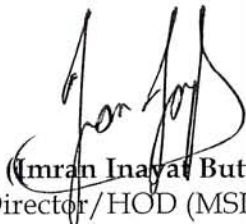
9. The violation of the Rules and Regulations is a serious matter. Taking a lenient view in the matter, in exercises of the powers under Section 22 of the Ordinance, I hereby impose on the Respondent a penalty of Rs. 50,000/- (Rupees Fifty Thousand Only). The Respondent is further directed to submit a compliance report to the Commission within 45 days of the date of this Order containing:

- a) Evidence of the separate bank account from that of the bank account used by the Respondent for operational purposes.
- b) Detail of the securities available in house account, clearly mentioning that the securities available in the house account of the Respondent belong to the Respondent and further stating that clients' securities have been moved to their respective sub-accounts and the Respondent is now in compliance with the applicable rules and regulations.

10. The matter is disposed of in the above manner and the Respondent is directed to deposit the fine 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 a copy of the deposit challan to the undersigned.

11. This Order is issued without prejudice to any other action that the Commission may initiate against the Respondent in accordance with the law on matter subsequently investigated or otherwise brought to the knowledge of the Commission.




(Imran Inayat Butt)
Director/HOD (MSRD)

Announced on November 29, 2013
Islamabad.