



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 Invest & Finance Securities Limited
under Section 22 of the Securities and Exchange Ordinance, 1969

Date of Hearing:

October 28, 2014

Present at the Hearing:

Representing Invest & Finance Securities Limited

(i) Mr. Muhammad Awais

Company Secretary

(ii) Mr. Ahmad Zakir Hafeez

Chief Financial Officer

Assisting the Director/HOD (MSRD)

(i) Mr. Muhammad Tanveer Alam

Joint Director

(ii) Ms. Najia Ubaid

Deputy Director

ORDER

1. This Order shall dispose of the proceedings initiated through Show Cause Notice bearing No. 1(34) SMD/MSRD/C&IW/2014 dated September 4, 2014 ("SCN") served to Invest & Finance Securities 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**").

2. Brief facts of the case are that the Commission in exercise of 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 record required to be maintained by the Respondent. The following officers of the Commission were appointed as inspectors ("**Inspection Team**") for the purpose vide order dated March 31, 2014:

a) Mr. Mian Muhammad Imran

Deputy Director

b) Mr. Adnan Ahmad

Deputy Director

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





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division
(Market Supervision & Registration Department)

Continuation Sheet - 1 -

3. The Inspection Team submitted the report ("Inspection Report") on June 17, 2014 which was shared with the Respondent in accordance with Rule 7 of the Inspection Rules. The response of the Respondent in the context was received vide letter dated July 2, 2014. The Inspection Report highlighted that the Respondent failed to maintain proper books of accounts; segregation of clients' assets and Standardized Account Opening Forms ("SAOFs"); did not have collateral account and was imposing late payment charges to its clients.

4. In light of the Inspection Report and the comments received from the Respondent, the Commission served a SCN to the Respondent. Hearing in the matter of aforesaid SCN was scheduled for September 18, 2014 at the Commission's Head Office in Islamabad. However, the Respondent vide letter dated September 8, 2014 requested for change in venue to the Commission's Karachi Office. Acceding to the Respondent's request, hearing was rescheduled to October 28, 2014.

5. The arguments put forward by the Respondent in its written response to the SCN submitted vide letter dated September 12, 2014 are reproduced below:

a) **Improper Books of Accounts:**

"We again submit that Rule 8 of Securities and Exchange Rules, 1971 is not relevant/applicable in this specific scenario as this is only clubbing and classification/representation of accounts. The Company maintains five proprietary accounts for own control purposes as explained to the inspection team in detail. These accounts are clubbed for reconciliation; therefore no entries are required/made in this respect. Further, please note that the said entries are not originating entries and do not fall under Section 8(a) of the Securities and Exchange Rules, 1971 as referred in Inspection Report. The difference highlighted in the Inspection Report between the ledger balances and the trial balance was due to the nature of amounts requiring adjustments only for the purpose of presentation of interim financial statements; thus showing a true and fair view. Please appreciate that this is done only for interim period as the figures are reversed immediately on the very next day. While for the annual accounts the books are properly adjusted to reflect the figures for carrying forward to the subsequent year as opening balances. This should be considered as a matter of practice developed based on the nature of figures as detailed above. Further, you will appreciate the fact that adjustments of trial balance are properly explainable which further fortifies the good intention regarding maintenance of proper books of accounts and correct presentation of balances in the financial statements."





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division
(Market Supervision & Registration Department)

Continuation Sheet - 2 -

b) **Late Payment Charges:**

"We are of the view that Regulation does not make it mandatory to immediately transfer the securities to the collateral account. It is also important to mention that immediate transfer of securities from clients' accounts shall affect relations with clients thus resulting in reduction in Company's revenues/business. We have to create a balance to retain the clients that is a very difficult task in current competitive environment. Please note that keeping in view volatile nature of stock market, economic and law & order situation of the country; investors' participation is required to be encouraged by providing some easy executable avenues and strict actions should be avoided. Company highly discourage the practice of imposition of service charges and does not follow the practice as policy. The Company had already taken appropriate steps to discontinue this practice and issued notices to its clients in this respect in September 2013 (enclosed as Annexure 1) about eight months prior to the issuance of Inspection Order and subsequently has restricted/stopped this practice. We could not immediately stop the practice due to excellent business relations with prestigious clients. We are not charging any such charges to clients still having debit balance. We would like to clarify that the Company used its own resources and there was no risk to 'client assets.'"

c) **Collateral Account:**

"The utilization of collateral account due to time schedule issues is practically very difficult/in-efficient. The Company has already opened the collateral account in compliance with the requirement of relevant statute. Letter issued by CDC in respect of opening of collateral account is enclosed as Annexure 2."

d) **Segregation of Clients' Assets:**

"The Company normally uses one account for receipts and payments. However, credit balances of clients are transferred to specified account on recurring basis. The Company take care that balance shall not be less than the credit balances of clients. You will agree that available balance in the specified account is not less than the credit balances of clients.

The Company maintains NCSS settling bank account and clients' receipts/payments account(s) other than Client Account (CA) due to some practical implications, technical problems and time constraint issues. It is Company's responsibility to timely pay its obligations/liabilities to NCSS/clients whether clients' funds are available or not and for this purpose uses its running finance facility account for smooth and timely payments and fulfill its obligations. Due to some unavoidable reasons/nature of transactions beyond our control, as detailed below, force us to follow this practice:

- *Sometimes Company has to pay huge clearing amounts to NCSS in respect of settlements of its clients' purchases whether they are in credits or not or whose cheques are in clearing/transit or their commitment for payment.*





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division
(Market Supervision & Registration Department)

Continuation Sheet - 3 -

- The Company has to pay to its clients against their sale proceeds whether NCSS clearings are settled or not or delay due to non-availability of funds in NCSS bank account or due to late credit in our account from bank side.
- Some clients give cheques from other banks which take two to three days for credit in our account or much more days for outstation cheques. We strive to get credit through online transfer in our relevant bank accounts to facilitate our clients and also mitigate our risk/exposure as well.
- To manage exact amount of credits of clients in bank account by extracting receivables and payables from clearing on daily basis is a difficult/lengthy practice and will require extra resources to drive the same result which we are in practice.
- Sometimes clients request to issue/pay cheques from those banks in which they have accounts for getting immediate credit through online transfer facility.

Therefore, we follow/adopt the practice to credit clients' funds in clients' bank account on recurring basis to avoid difficulties/inconveniences such as uncertainty, delay in payments and dishonoring of cheques that may result in loss/shake of confidence/trust."

e) **Irregularities in SAOFs:**

"As submitted in reply to Inspection Report; we try our best to satisfy the inspection team in maximum observations if issues mentioned in Inspection Report would have been discussed with us during inspection. We have made certain submissions/explanations in the said reply and trust that you are satisfied with our submissions/explanations except to the extent of certain evidences. In this respect we submit:

- Occupation section for client K252 has been filled and copy of relevant page of Account Opening Form is attached herewith as Annexure 3. He is an ex-employee as also identified by the Inspection Team and all relevant information (visiting card/employee's undertaking etc.) is available with the Form. Further, said particulars were filled on the CDC Sub-Account Opening Form and copy of the relevant page of the same is also enclosed as Annexure 3A.
- Forms have been updated as per format of General Regulations for clients K347 and K352 and copies of Addendums are attached as Annexure 4 & 4A. New Form has been obtained from client K94 and copy of the same is attached as Annexure 4B.
- In respect of proof of delivery of copy of account opening forms, please note that forms are provided to respective clients. Please see clause 20 of the Company's account opening form that states:

'I/we, the Account Holder(s) acknowledge receipt of this Account Opening Form (signed here by me/us in duplicate) along with the copies of all the annexure and I/we, the Account Holder(s) also undertake that I/we have understood all the above terms and conditions of this agreement which are acceptable to me/us.'

Please note that all annexure are provided to client as required.





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division
(Market Supervision & Registration Department)

Continuation Sheet - 4 -

Expired CNICs for clients FA128 (one director), K298, K252 along with his nominee, K347 and K399 have been updated (enclosed as Annexure 5)."

6. Mr. Muhammad Awais, Company Secretary of the Respondent and Mr. Ahmad Zakir Hafeez, Chief Financial Officer of the Respondent ("**Representatives**") attended the hearing on behalf of the Respondent on October 28, 2014 at the Commission's Karachi office. The arguments put forth by the Representatives of the Respondent during the course of hearing are summarized below:

- a) The Representatives, with regard to maintenance of proper books of accounts, stated that the Respondent had no malintent. They further explained that the differences identified in values of the Net Capital Balance Certificate and that of appearing in the trial balance in the books of accounts was because of adjustment entries which are generally accounted for in the books of accounts at year end, however, the Respondent did provide the reconciliation of the figures to the inspection team which is available in the Commission's record and is also part of annexures of the inspection report.
- b) With regard to the opening of collateral account, the Representatives reiterated the stance taken by the Respondent in its written response and communicated that the evidence of opening of collateral account has been provided to the Commission.
- c) The Representatives, regarding imposition of late payment charges, apprised that the Respondent has stopped imposing late payment charges as a practice, however, in few instances where the Respondent had no other option for recovery it imposes very little amount on this account. The Representative, however, assured that imposition of late payments charges to the clients having debit balances has been stopped and that the Respondent in future shall be compliant with the regulatory requirements.
- d) Regarding segregation of clients' funds the Representatives stated that they have bank accounts with almost every bank, which have been opened to facilitate the Respondents' clients. The Representatives asserted that the Respondent is not involved in use of clients' funds and that the clients' funds are transferred to the bank account at the end of each day. The Representatives further added that sometimes if a payment from National Clearing Company of Pakistan Limited is to be received during the day and the clients' demand immediate payment earlier in the morning, then the Respondent is left with no choice but to issue cheque in favour of the client from





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division
(Market Supervision & Registration Department)

Continuation Sheet - 5 -

the Respondent's own bank account. The Representatives stated that they always try to ensure compliance with the regulatory requirements regarding segregation of clients' assets. The Representatives agreed to provide reconciliation of the funds available in clients' bank account as of September 30, 2014 with that of the trade payables of the same date.

- e) With reference to updating the SAOFs, the Representatives stated that had the issue been discussed with the Respondent during the course of inspection, the same could have been resolved. However, the Representatives communicated that they have made the required amendments and evidence of the same has been provided to the Commission.

7. I have heard the arguments presented by the Representatives of the Respondent at length during the hearing. Additionally, I have perused the available record and the written 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) In the matter of improper books of accounts, the Representatives during the course of hearing agreed that the Respondent shall make adjustments on half yearly basis in future if the same has to be adopted as a practice to ensure compliance. Moreover, the Representatives also confirmed that the adjustments referred to by the inspection team have already been made in the books of accounts while preparing annual accounts, which is in compliance with the International Accounting Standards.
- b) With regard to segregation of clients' assets, the Respondent in its written response and Representatives during the course of hearing stated that funds are transferred to clients' account at the end of day and also assured that the Respondent never used clients' funds for any other purpose. The Representatives as agreed provided reconciliation of funds in clients' bank account with that of trade payables position as of September 30, 2014 vide letter dated October 30, 2014. As per the information provided trade payables position as of September 30, 2014 also included trade payables from the sponsors in the capacity of Respondent's clients. However, bank position of the same date revealed that other than payables to the sponsors, the Respondent had sufficient funds in clients' bank account as per the existing





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division
(Market Supervision & Registration Department)

Continuation Sheet - 6 -

regulatory requirements, the Respondent is expected to ensure proper segregation of clients' assets and should at all times have an amount equivalent to its trade payables/creditors in the bank account tagged as clients' account, irrespective of the status of the clients i.e. sponsors or other creditors.

- c) In reference to late payment charges, the Representatives during the course of hearing communicated that this amount is charged to recover balances from the Respondents' clients, the Respondent in no manner is involved in extension and/or maintenance of credit. The Representatives during the hearing stated that the amount of late payment charges have gradually decreased over time and the Respondent is also educating its clients in this context. The Representatives further assured that the imposition of late payment charges has now been stopped.

8. After a detailed and thorough perusal of the facts, evidence/information available on record, contentions and averments made by the Representatives of the Respondent during the course of the hearing, it is evident that the Respondent during the inspection period failed to fulfill its regulatory obligations by imposing late payment charges and by not properly maintaining segregation of clients' assets.

9. The violation of the rules and regulations is a serious matter. However, the Representatives of the Respondent during the course of hearing and the Respondent in its written response communicated that it has stopped charging late payment charges to its clients and is now maintaining segregation of clients' assets in letter and spirit. Moreover, the Respondent rectified the identified irregularities highlighted in the inspection report and gave firm commitment to comply with the applicable regulatory framework in future.

10. Therefore, taking a lenient view, in exercise of the powers conferred upon under Section 22 of the Ordinance, I hereby impose a penalty of Rs. 25,000/- (Rupees Twenty Five Thousand Only) on the Respondent. Moreover, the Respondent is directed to:

- i) comply with the Rules 1971 and the guidelines issued in letter and spirit;
- ii) maintain separate bank account for the clients' funds and ensure proper segregation of clients' assets; and
- iii) stop imposing late payment charges.





SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division
(Market Supervision & Registration Department)

Continuation Sheet - 7 -

11. 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.

12. 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.

Announced on November 21, 2014
Islamabad.




(Imran Inayat Butt)
Director / HOD (MSRD)