



# Securities and Exchange Commission of Pakistan

## **BEFORE APPELLATE BENCH**

In the matter of

**Appeal No. 17 of 2019**

MRA Securities Limited

Appellant

Versus

The Commissioner, (SMD), SECP, Islamabad.

Respondent

**Date of hearing:**

November 28, 2019

**Present:**

For Appellant:

- i. Mr. Salman Iqbal Bawaney
- ii. Ms. Samina Fazal
- iii. Muhammad Farhan (CEO)
- iv. Mr. Muhammad Zubair (Compliance Officer)

For Respondent:

- i. Ms. Amina Aziz, Director (SMD), SECP
- ii. Ms. Mehwish Naveed, Management Executive (SMD), SECP

## **ORDER**

1. This Order shall dispose of Appeal No. 17 of 2019 filed by M/s. MRA Securities Limited (the Appellant) against the Order dated April 8, 2019 (the Impugned Order) passed by the Commissioner-SMD (the Respondent) under 40A of the Securities and Exchange Commission of Pakistan Act, 1997 (the SECP Act) read with Section 150 the Securities Act, 2015 (the Act).
2. Brief facts of the case are that the Appellant is a Trading Rights Entitlement Certificate (TREC) holder of the Pakistan Stock Exchange Limited (the PSX) and licensed as a securities broker under the



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Securities Act, 2015. The Joint Inspection Team of PSX, Central Depository Company and National Clearing Company of Pakistan Limited conducted an inspection (the Inspection) of the Appellant in September 2018, to assess its compliance with the regulatory requirements contained in the Securities and Exchange Commission of Pakistan (Anti Money Laundering and Countering Financing of Terrorism) Regulations, 2018 (the Regulations). The Inspection, inter alia, revealed the following:

- i. The risk ratings of clients mentioned in the consolidated list of risk ratings were different from the risk ratings assigned to the clients in the know your customer (KYC) and customer due diligence (CDD) forms. However, difference in risk ratings was not documented in a required manner. Furthermore, incorrect risk ratings were assigned to nine clients.
- ii. The Anti Money Laundering and Countering Financing of Terrorism policy of the Appellant was not in consonance with the requirements of the Regulations.
- iii. The Appellant had not established internal audit function.
- iv. In violation of the Securities Brokers (Licensing and Operations) Regulations, 2016 (the Brokers Regulations), the Appellant had opened a trading account of the immediate family member (Mr. Waqas Tanveer) of the chief executive of another brokerage house (Mannoo Capital (Pvt.) Limited). This reflects that the CDD procedures were not applied in letter and spirit.
- v. The Appellant had failed to obtain evidence relating to the source of income of nineteen clients.
- vi. The Appellant had failed to establish beneficial ownership of six clients.
- vii. The Respondent had failed to develop a mechanism to ensure ongoing monitoring of its clients.

3. In view of the above alleged violations, the Respondent issued a Show Cause Notice dated February 7, 2019 (the SCN) to the Appellant. The Appellant submitted a written reply to the SCN on February 28, 2019 and hearing in the matter was held on March 11, 2019. In terms of powers conferred under section 40A of the Act, a penalty of Rs. 250,000/- (Rupees two hundred fifty thousand) under section 40A of the Act was imposed by the Respondent.

4. The Appellant has challenged the Impugned Order *Inter alia* on the grounds that the Impugned Order is *per se* unlawful because in various paragraphs of the Impugned Order it had been alleged that the Appellant had violated the requirements of AML regulatory framework of 2012, introduced through regulation 4.18 of the Karachi Stock Exchange Rule





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Book and KYC and CCD guidelines of 2012, however, the SCN and Inspection observations are related to the violations of the Regulations. The Appellant stated that under the Regulations, it cannot be penalized for the alleged violation of the regulatory framework of 2012. The Appellant further stated that clarity was required in implementation of the Regulations, therefore, the Commission organized awareness sessions for the brokerage house including the Appellant. The Appellant stated that its Inspection was conducted during the time when awareness sessions were being conducted by the Commission, therefore, initiation of Inspection and issuance of the SCN were premature.

5. The Appellant explained that the Appellant's representatives never accepted noncompliance of the Regulations. The Appellant contended that violations of Regulation 16(5) of the Brokers Regulations, cannot be attributed to the Appellant because Appellant's chief executive or his family had not traded through another securities broker rather it was the family member of another securities broker who had traded through the Appellant. The Appellant stated that the requisite KYC/CDD measures were applied in this case and had acted in good faith. Therefore, the same cannot be considered as violation of KYC/CDD procedures.
6. The Appellant stated that risk categorization and risk ratings were assigned as per the regulatory framework of 2012. However, after the promulgation of the Regulations and awareness sessions, risk categorization of clients was updated. The Appellant stated that it has a full internal audit control system and audit function, therefore, requirements of the Regulations had never been compromised. The Appellant stated that it has an appropriate ongoing monitoring mechanism for its clients and this information was shared on several occasions, that is, during the Inspection, in the response to the Inspection report as well as in the reply to the SCN, however, such facts were not considered by the Respondent while passing the Impugned Order.
7. The Respondent has rebutted the grounds of Appeal and stated that the Appellant had not been penalized under the regulatory framework of 2012, rather penalty had been imposed due to violation of the Regulations. The Respondent clarified that in the Impugned Order it had been mentioned that the Regulations are new, however, requirements contained therein are not different and were introduced in 2012. The Respondent contended that the Appellant's





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representatives accepted the Appellant's failure to comply with the requirements of the Regulations.

8. The Respondent stated that there was difference in risk categorization of the Appellant's clients. The Respondent stated that risk categorization may change from time to time, however, the Appellant's documentary record does not reflect that any change was adequately documented along with reasoning, therefore, either the list maintained by the Appellant contained incorrect ratings or the revised ratings were not documented. The Respondent further stated that the Appellant had categorized two non-resident clients as low risk despite the fact that the 2012 regulatory framework required non-residents' customers to be categorized as high-risk. This contradicts the Appellant's plea that it had categorized the clients as per the 2012 regulatory framework. The Respondent contended that establishment of an independent audit department, devising a mechanism for ongoing monitoring of clients and updating AML/CFT policy post the Inspection does not undo the Appellant's default. The Respondent stated that the Appellant had acquired information with regard to sources of funds from clients after the Inspection, therefore, at the time of the Inspection it was non-compliant. The Respondent stated that the Appellant failed to identify beneficial ownership of its clients at the time of opening of account. Moreover, the Respondent stated that even if the beneficial owner is a relative of the account holder, it does not discharge the Appellant from its responsibility of performing CDD to this effect.
9. The Respondent indicated that opening of account of a close relative of the chief executive of another brokerage house was violation of the Brokers Regulations. The Appellant, during the hearing, was asked whether any inquiry was made at the time of opening of account to which the Representative responded in the negative. The Appellant failed to conduct CDD in letter and spirit while opening accounts of new clients, therefore, was non-compliant with the Regulations.
10. The Bench has heard the parties and perused the record. The Appellant's representative reiterated the grounds of Appeal and contended that the inspection/review was carried out before the issuance of AML guidelines 2018, therefore, sufficient time was not provided to understand and comply with the requirements of the Regulations. The Respondent's representative rebutted such grounds and argued that the violated requirements of the Regulations were also part of the 2012 regulatory framework,





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therefore, the Respondent cannot take the plea that requirements of the Regulations were new and sufficient time was not provided for compliance.

11. The Bench has examined the Appellant's reply to the Respondent's para-wise comments, wherein, objection has been raised on the evidentiary value and authenticity of the Inspection report. As per our examination, the relevant part of the Inspection report was shared with the Appellant through the covering letter dated October 8, 2018. The Appellant had annexed the covering letter and relevant part of the Inspection report as annexure "B" and "B1" of the memorandum of Appeal (Page 45 to 69). Furthermore, the Appellant also annexed the reply of the Inspection report as annexure "C" of the memorandum of Appeal (Page 71 to 101) wherein, without objecting on the evidentiary value or authenticity of the Inspection report, the reply was submitted. We are of the view that the Appellant's objection is not plausible because the Inspection report had reasonably communicated the violations of the Regulations and thereafter, duly SCN was issued and Impugned Order was passed.
12. The Bench has carefully gone through the contents of the Impugned Order and other relevant record, which revealed that the Appellant had violated the requirements of Regulation 3, 4, 6, 7 and 13 of the Regulations though the Respondent had not specifically mentioned the aforesaid provisions in the Impugned Order. The Bench is of the view that the violated provisions should have been mentioned in the Impugned Order. However, not mentioning specific provisions do not vitiate the proceedings when, otherwise violations were duly mentioned and established.
13. The Bench has examined the memorandum of Appeal and found that the Appellant had denied the alleged admission of violations mentioned in the Impugned Order. However, in ground "B" of memorandum of the Appeal, the Appellant has stated that pursuant to the awareness sessions on the Regulations, KYC/CDD documents were re-examined and all necessary documents/information were obtained and Risk Categorization was updated as per Regulations 3(1)(a) and 3(2)(a) of the Regulations. We are of the view that the above narrated ground of appeal is the Appellant's implied admission that it failed to comply with the requirements of the Regulations after their promulgation on June 13, 2018. Furthermore, the Appellant's plea contained in ground "D" of the memorandum of Appeal that the Regulations were not clear and their implementation was not applicable until completion of awareness sessions, is neither tenable nor supported by any legal provision.





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14. The Bench has no doubt that the requirements of the Regulations were not new, rather similar provisions existed in the regulatory framework of 2012 of the Karachi Stock Exchange (presently PSX), issued with the approval of the Commission, through regulation 4.18 of the Rule Book (current Regulation 4.17). These requirements were made mandatory for the securities brokers to formulate and implement an effective KYC and CDD policy in accordance with the KYC and CDD guidelines issued by the Karachi Stock Exchange in 2012. The Bench has compared the requirements of the regulatory framework of 2012 with the Regulations and SECP's AML guidelines 2018, and observes that they do not reflect any material difference in terms of requirements, for instance, customer identification, risk assessment of customer, CDD and on-going monitoring. Therefore, the Bench has no doubt to hold that the Regulations had not introduced significantly different regulatory requirements, rather the prior regulatory requirements had been streamlined. The Bench has observed that even prior to the promulgation of the Regulations, the Appellant was required to have AML/CFT Policy, customer identification, risk assessment of customer, CDD, on-going monitoring, beneficial ownership, evidence of sources of fund and internal audit department under the previous regulatory legal framework, however, the Appellant had failed to comply with the applicable requirements.
15. The Bench is of the view that Respondent's assertion with regard to non-establishment of Appellant's internal audit function is not tenable because the Appellant had an internal audit department under the Brokers Regulations. We are of the view that the Respondent had failed to differentiate between non-establishment of internal audit function and failure to update audit function for ongoing monitoring of clients. Furthermore, violations of the Regulation 16(5) of the Brokers Regulations, cannot be attributed to the Appellant because this provision is applicable on the CEO (and family) of brokerage house, who traded through other brokerage house. In this the Appellant's chief executive or his family had not traded through another securities broker rather it was the family member of other securities broker who traded through the Appellant. Moreover, violation of the Brokers Regulations cannot be dealt under the Regulations.
16. The Bench is of the view that the memorandum of Appeal, reply of the SCN and Inspection observations are sufficient to establish that the Appellant had failed to comply with the mandatory regulatory requirements of the Regulations in a timely manner. The Respondent had already considered the Appellant's efforts to undo its defaults, however, subsequent compliance or desire to comply with the requirements does not exonerate the Appellant from penal consequences. Updating AML/CFY policy and information with regard to source of funds and beneficial ownership were



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provided after the Inspection, therefore, the Appellant's claim that it had not violated the requirements of the Regulation is not reasonable.

17. The Bench believes that there were circumstances, wherein, the Respondent should have imposed a higher penalty, however, the Respondent had taken a lenient view and instead of imposing maximum penalty of ten million rupees, had imposed a penalty of Rupees 250,000 on the Appellant.
18. In the circumstances, we refrain ourselves, to interfere with the merits and imposed penalty of the Impugned Order, therefore, we hereby dismiss this Appeal, without any order as to cost.

(Farrukh Hamid Sabzwari)

Commissioner (AML)

(Shaukat Hussain)

Commissioner (Insurance)

Announced on: **01 JAN 2020**