



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

Adjudication Department-I
Adjudication Division

Through Courier

Before the Executive Director

In the matter of Show Cause Notice issued to M/s. 128 Securities (Pvt.) Limited

Date of Hearing	July 01, 2020
Present at the Hearing	i. Mr. Muhammad Shahzad Haider Zaidi (Director)
Representing M/s.128 Securities (Pvt.) Limited	ii. Mr. Ali Ahmed Khan (Compliance Officer)
	iii. Mr. Shafqat Ali (Consultant)

ORDER

This Order shall dispose of the proceedings initiated against the 128 Securities (Pvt.) Limited (the “Respondent”) and its Compliance Officer through Show Cause Notice No. 1(168)/SMD/Adj/LHR/2019, dated April 27, 2020 (the “SCN”) under Section 40A of the Securities and Exchange Commission of Pakistan Act 1997 (the “Act”).

2. Brief facts of the case are as follows:

- (a) The Respondent is a Trading Rights Entitlement Certificate (TREC) holder of the Pakistan Stock Exchange Limited (the “PSX”) and licensed as a securities broker under the Securities Act, 2015.
- (b) The limited scope thematic review (the “Review”) of the Respondent was conducted by the Commission to ascertain compliance with requirements contained in Securities and Exchange Commission of Pakistan (Anti Money Laundering and Countering Financing of Terrorism) Regulations, 2018 (the “AML Regulations”).

3. The Inspection revealed non-compliances with the AML Regulations; detailed as under:

Regulation 4 (a) of the AML Regulations requires a securities broker to develop and implement policies, procedures and controls, which are approved by its board of directors, to enable the securities broker to effectively manage and mitigate the risks that are identified in the risk assessment of ML/TF or notified to it by the Commission. Review of the AML/ CFT Policy of the Respondent revealed that the following deficiencies in violation of the said regulation:





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(a) The Respondent did not include the following requirements of the AML Regulations in its AML/CFT policy in violation of Regulation 4(a) of the AML Regulations.

- i. Categorizing the overall entity level risk as high, medium or low based on the result of risk assessment as required under Regulation 3(2)(d) of the AML Regulations.
- ii. New Products, Practices and Technologies as required under Regulation 5 of AML Regulations.
- iii. Beneficial Ownership of Legal Persons and Legal Agreements as required under Regulation 7 of the AML Regulations.
- iv. Politically Exposed Persons as required under Regulation 10 of the AML Regulations.
- v. Record keeping as required under Regulation 15 of the AML Regulations.

(b) The Respondent did not update the following requirements of the AML Regulations in its AML/KYC policy in violation of Regulation 4(a) of the AML/CFT Regulation.

- i. Maintenance of list of accounts/customers where business relationship was refused or needed to be closed on account of negative verification as required under Regulation 6(9) of the AML Regulations.
- ii. Enhance Due Diligence measures as required under Regulation 9 of the AML Regulations.
- iii. Simplified Due Diligence measures as required under Regulation 11 of the AML Regulations.
- iv. Ongoing Monitoring as required under Regulation 13 of the AML Regulations
- v. Reporting of Transactions (STRs /CTRs) as required under Regulation 14 of the AML Regulations.
- vi. Reporting line of Compliance Officer as required under Regulation 18 of the AML Regulations.



(c) Regulation 18(c)(iii) requires the Compliance Officer of the Respondent shall primarily be responsible for the areas including, but not limited to monitoring, reviewing and updating its AML/CFT policies and procedures. Since, the areas highlighted in para (a) and (b) above were not incorporated in the Respondent's AML/CFT policy at the time of Review, therefore, Respondent and its Compliance Officer has contravened the requirements of the Regulation 18(c)(iii) of the AML Regulations.

4. It appeared from the preceding that the Respondent *prima facie* acted in contravention of the AML Regulations. Accordingly, the Commission took cognizance of the aforementioned facts and served the SCN requiring the Respondent to submit its reply within 14 days of the date of this notice.



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The Respondent vide its letter dated June 29, 2020 submitted reply to the SCN, which is reproduced below:

“

1. PRELIMINARY SUBMISSIONS OF 128SPL:

1.1. In pursuance of Anti-Money Laundering Act, 2010 ('the AML Act'), the SECP was pleased to promulgate the AML Regulations on June 13, 2018 and brought about wholesale and wide reaching changes in the way the brokers did their businesses and conducted Customer Due Diligence.

1.2. You would appreciate that even though it was the SECP that drafted and promulgated the AML/CFT Regulations in June 2018, who took about 3 months to understand, streamline, and issue guidelines on September 11, 2018 ('the SECP Guidelines') on how to comply with the AML/CFT Regulations. We may take this opportunity to point out that 128SPL, along with all the affected entities, were already in the process of consultation with each other to devise policies and strategies to comply with the AML/CFT Regulations. It is worth pointing out that the SECP Guidelines themselves are extensive and require the implementation of a suitable training program, for the management and employees alike, for full compliance with the AML/CFT Regulations.

1.3. In this regard, we hired the services of competent legal and technical person to devise the appropriate strategies and policies for us and to train our staff in this regard. It bears pointing out that such process required some time and needed to evolve and couldn't be implemented when the law and guidelines pursuant to it were also vague.

1.4. Only after five (5) months, SECP issued its Guidelines, on February 28, 2019 the Commission advised 128SPL to provide certain information and details to assess the compliances status in respect of regulatory requirements relating to AML/CFT Regulations and directive pertain to aforesaid Regulations. We believe that checking compliances through correspondences by the Regulators may be less effective than the inspection of record through physical visit of the Regulators. Therefore, few instances of non-compliances observed through correspondence with 128SPL would be addressed more appropriately by 128SPL if the Commission had visited the office physically and discussed its requirement face to face.

2. OUR REPLIES ON OBSERVATIONS ALLEGED IN THE SCN:

The following are our para-wise comments on the contraventions of various provisions of the AML/CFT Regulations as alleged in the SCN:

2.1. As per point 3(a) of SCN, it was alleged that the Respondent did not include the following requirements of the AML/CFT Regulations in its AML/CFT Policy in violation of Regulation 4(a) of the AML/CFT Regulations and the response of each of the observation is given against each of the allegation:





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i. Categorizing the overall entity level risk as high, medium or low based on the results of risk assessment as required under regulation 3(2)(d) of the AML/CFT Regulations:

Response: Please note that 128SPL is a small scale brokerage house having very limited number of clients working before promulgation of SECP AML/CFT Regulations, therefore, 128SPL is categorized as Low Risk Brokerage House as result of Risk Assessment. Please note that clause 14 of the AML/CFT Policies and Procedures, the process of risk management at 128SPL has been very well defined. In line with said clause, 128SPL has categorized itself as Low Risk entity.

ii. New products, Practices and Technologies as required under Regulation 5 of the AML/CFT Regulations:

Response:

Please note that there are following two products and services offered by 128SPL to its clients who are only available at the Exchange platform:

- a. Ready Market (Cash Market); and
- b. Deliverable Futures Contracts.

128SPL is only offering two products and services to tier clients, which are categorized as Low to medium Risk categories. As defined in clause 12.10 of the AML/CFT Policies, 128SPL has categorized itself as low risk entity in view the risks envisaged on offered products.

In terms of risk assessment of practices and technologies being used by 128SPL, we are a very conservative brokerage house adopting market practices and technologies being used by the small scale and other conservative brokerage houses of the Exchange. Therefore, as per clause 12.10 of the Policy, we have categorized 128SPL as Low Risk entity in compliance with regulation 4(a), 5 and 14(6) of the SECP AML/CFT Regulations.

iii. Beneficial Ownership of Legal Person and Legal Arrangement as required under Regulation 7 of the AML/CFT Regulations:

Response:

Considering 128SPL as small scale brokerage house of the Exchange, we were lacking in compliance of regulation 7(1) of the AML/CFT Regulations relating to maintaining details of Beneficial Ownerships of the Legal Persons. Even though, we have a small number of corporate local clients categorized as legal persons. Now we have been establishing details of beneficial ownerships of all such clients in our database. Therefore, we request your good-self to pardon off this inadvertent negligence.

Now requirement of regulation 7 relating to Beneficial Ownership of Legal Person and Legal Arrangement is covered in point 15.2 of the AML/CFT Policy submitted with SECP on January 23, 2020.

iv. Politically Exposed Persons as required under Regulation 10 of the AML/CFT Regulations:

Response:

Yes, the Respondent agrees that procedure for dealing with PEP's Accounts was not covered





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in the AML/CFT Policy submitted to SECP against its review started in February 28, 2019 shortly after promulgation of AML/CFT Regulations in June 2018 and AML/CFT Guidelines in September 2018.

Now, the Respondent has covered the procedure for dealing with PEPs as required under Regulation 10 of the AML/CFT Regulation in point 18 of the revised AML/CFT Policy of the Responded submitted to SECP on January 23, 2020.

v. Record Keeping as required under Regulation 15 of the AML/CFT Regulations:

Response:

Although, it was the Respondent's obligation under Securities Brokers (Licensing and Operations) Regulations, 2016, to keep and maintain transaction record of all dealing with the customers for minimum period of ten (10) years. The Respondent has been following the regulatory requirement for record keeping in compliance of the Regulation 15 of the AML/CFT Regulations, however, process was not articulate in the its initial AML/CFT Policy submitted to SECP on March 08, 2019.

Now, the Respondent included above requirement n point 20 on page 21 of revised AML/CFT Policy submitted to SECP vide a letter dated January 23, 2020.

Please note, it was acknowledged by the Commission in paragraph 3(a) of SCN that AML/CFT Policies do not include the appropriate procedures for the implementation of its policy and alleged that policy was deficient on only five (5) accounts. Therefore, the observation relating to updation of AML/KYC policy may be pardoned off.

2.2. As point 3(b) of the SCN, it was alleged that the Respondent did not update the following requirements of the AML/CFT Regulations in its AML/CFT Policy in violation of Regulation 4(a) of the AML/CFT Regulations and the response of each of the observation is given against each of the allegation:

i. Maintenance of list of accounts /customers where business relationship was refused or needed to be closed on account of negative verification as required under Regulation 6(9) of the AML/CFT Regulations:

Response:

As explained in our preliminary submission, the 128SPL in very short span of five (5) months from the issuance of SECP Guidelines its initial AML/CFT Policy and did its good efforts to cover each and every aspects of the AML/CFT Regulations. However, policy making is continuously evolving process which needs improvement based on working experience.

Despite of above submission, a policy relating to dealing with the customers who refuses to provide information for their risk assessment was including in para-3 on 2nd Page of the AML/CFT Policy submitted to SECP on March 08, 2019. Now, the same has further been updated in our new policy submitted to SECP along with our reply on January 23, 2020.

ii. Enhanced Due Diligence measures as required under Regulation 9 of the AML/CFT





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Regulations:

Response:

Similarly, 128SPL tried to cover its Enhanced Due Diligence measures in its AML/CFT Policy submitted to SECP on March 08, 2019 in para-4 & 5 on 3rd page of the AML/CFT Policy. Now the same has been further elaborated in our new Policy as per its point 16, submitted to SECP vide its letter dated January 23, 2020.

iii. Simplified Due Diligence measures as required under Regulation 11 of the AML/CFT Regulations:

Response:

Although Simplified Due Diligence measures were not specifically covered in our initial AML/CFT Policy submitted to SECP on March 08, 2019 but generally these measures were covered in the documents. For reference, you may observe para covering Customer Identification and verification on 1st page and process for verifying information explained on 2nd page of the AML/CFT Policy. Now the Simplified Due Diligence measure of very well articulate in point 17 of the AML/CFT Policy of the Respondent submitted to SECP vide its letter dated January 23, 2020.

iv. Ongoing Monitoring as required under Regulation 13 of the AML/CFT Regulations:

Response:

It is humbly submitted that ongoing monitoring of the accounts procedures were initial drafted in para-4 on 3rd page of the AML/CFT Policy initially submitted to SECP vide our letter dated March 08, 2019. The same was subsequently further elaborated in the revised AML/CFT Policy submitted to SECP on January 23, 2020.

v. Reporting of Transactions (STRs and CTRs) as required under Regulation 14 of the AML/CFT Regulations:

Response:

In the initial AML/CFT Policy of the Respondent based on which SCN was issued, suspicious reporting procedures were covered under the heading Confidential Reporting of AML Non-compliances in last paragraph on page 5th of the AML/CFT Policy submitted initial on March 08, 2019. Now, the same process has been covered in point 19 of the AML/CFT Policy submitted to SECP vide our letter dated January 23, 2020.

vi. Reporting Line of Compliance Officer as required under Regulation 18 of the AML/CFT Regulations:

Response:

Please note that the Compliance Officer was reporting to the Board of Director as was communicated to SECP as an answer to question relating to Compliance Function submitted through Google Form on March 08, 2019 against SECP letter dated February 28, 2019.

2.3. As per point 3(c) of the SCN, since the areas highlighted in point 3(a) and 3(b) of the SCN were not incorporated in the Respondent's AML/CFT Policy at the time of Review, therefore, Respondent and its Compliance Officer had contravene the requirements of the Regulation 18(c)(iii) of the AML/CFT Regulations.





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Response:

It is humbly submitted that in compliance with regulation 18(c)(iii) of the AML/CFT Regulations, the Compliance Officer is responsible to update/modify the AML/CFT Policy in line with the changes/amendments in AML/CFT Regulations and receipt of directive/notifications from the Commission time to time. In compliance with said regulatory requirements, the Compliance Officer drafted 1st draft of AML/CFT Policy in February 2019 after promulgation of AML/CFT Regulations and SECP Guidelines during 2nd half of the year 2018. 1st AML/CFT Policy was approved by the Senior Management on March 01, 2019.

Further, the Compliance Officer updated the AML/CFT Policy of the Respondent on in July 2019 and got it approved from the Board of Directors on July 10, 2019.

The Compliance Officer has continuously reviewing the regulatory amendments in regulatory framework governing AML/CFT regime and updated in the Respondent's Policy in line with such amendments/updates. Now, the Compliance Officer in the process of updation AML/CFT Policy of the Respondent in line with NRA-2019.

In view of above, the Commission's allegation that the Compliance Officer was in violation of Regulation 18(c)(iii) of the AML/CFT Regulations is not justified.

*As highlighted in our preliminary submissions vide our letter dated January 23, 2020, despite of short time available to 128SPL, we had developed and implemented policies, procedures and controls with the approval by one of the Executive Director on March 01, 2019 to enable it to effectively manage and mitigate the risks that are identified in the Risk Assessments of ML/TF. A copy of said AML Policies and Procedures were provided to SECP on its requirements vide its letter dated March 08, 2019 as **Annexure-A**.*

*The Respondent also submitted its AML/CFT Policy duly updated on July 10, 2019 on January 23, 2020, copy of same is attached as **Annexure-B** for your reference.*

It is respectfully submitted that under the new Broker Regime developed by the Commission, it was realized by the Commission that the small brokerage houses lack the resources and capacity to meet the compliance burden. Through letters to the SECP, brokers have highlighted their small scale of operations and inability to dedicate sufficient resources to meet financial reporting requirements, develop a sound compliance system and meet FATF standards.

Therefore, we request your good-self to please accept our responses sympathetically and take lenient views on taking enforcement actions against the Respondent."

5. The Respondent was accorded an opportunity of personal hearing dated July 01, 2020. The hearing was attended by Mr. Muhammad Shahzad Haider Zaidi (Director), Mr. Ali Ahmed Khan (Compliance Officer) and Mr. Shafqat Ali (Consultant) as Authorized Representatives. During the hearing proceedings, the Authorized Representatives reiterated the argument as submitted in response to the SCN.





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6. I have examined the written as well as oral submissions of the Respondent and its Authorized Representatives. In this regard, I observe that:

- i. The primary justification extended by the Respondent for not having an updated AML policy was that the AML Regulations were new (promulgated in 2018) and reasonable time was not available to understand the compliance required. The explanation of the Respondent does not hold merit. While the AML Regulations were issued in 2018 but the requirements contained therein are not new. Rather the requirements were introduced in 2012 when Karachi Stock Exchange (presently PSX) with the approval of the Commission, through Regulation 4.18 of the Rule Book made it mandatory for the securities brokers to formulate and implement an effective KYC and CDD policy in accordance with the Know Your Customer and Customer Due Diligence Guidelines issued by the Exchange. A comparison of the regulatory framework of 2012 with AML Regulations does not reflect any material difference in terms of requirements. Further, the Review was initiated in month of February, 2019 i.e. eight months after the promulgation of AML Regulations. Therefore, the AML Regulations cannot be termed as new set of requirements and the argument of the Respondent that sufficient time was not available for compliance is untenable.
- ii. With regard the violation of Regulation 4(a) of the AML Regulations, the response of Respondent on letter of finding vide its dated January 23, 2020 that *these points were apologetically overlooked to incorporate in AML/CFT policy* shows that policy was deficient at the time of Review. During the hearing, the Authorized Representatives also admitted the default on part of Respondent.
- iii. The Authorized Representatives admitted the violation of Regulation 18 c(iii) and submitted that subsequent to the Review, Respondent updated its AML policy in accordance with the regulatory requirements.

7. In view of the foregoing and admission made by the Representatives, contraventions of the provisions of AML Regulations 4(a) and 18 c (iii) have been established, however in reference to Regulation 18 c (iii) Compliance officer is warned to be careful in future. For rest of the violations, in terms of powers conferred under section 40A of the Act, a penalty of **Rs. 175,000/- (Rupees One hundred seventy five thousand)** is hereby imposed on the 128 Securities (Pvt.) Limited. The 128 Securities (Pvt.) Limited is advised to examine its AML/CFT policy & procedures to ensure that the requirements contained in the AML Regulations are met in letter and spirit.

8. The 128 Securities (Pvt.) Limited is directed to deposit the aforesaid penalty in the account of the Commission being maintained in the designated branches of MCB Bank Limited within 30 days of the date of this Order and furnish Original Deposit Challan to this office.





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9. This Order is issued without prejudice to any other action that the Commission may initiate against the 128 Securities (Pvt.) Limited in accordance with the law on matter subsequently investigated or otherwise brought to the knowledge of the Commission.



(Ali Azeem Ikram)

Executive Director (Adjudication Department-1)

Announced on July 9 , 2020
Islamabad