



Securities and Exchange Commission of Pakistan
Securities Market Division

Through Courier

Before the Commissioner (SMD)

In the matter of Show Cause Notice issued to AKD Securities Limited

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| Date of Hearing | August 6, 2019 |
| Present at the Hearing | i. Mr. Muhammad Farid Alam Chief Executive |
| <i>Representing AKD Securities Limited</i> | ii. Mr. Naveed Anjum Head of Compliance |
| | iii. Mr. Tanveer Khan Chief Financial Officer |

ORDER

This Order shall dispose of the proceedings initiated through the Show Cause Notice bearing No. 1(164) SMD/ADJ/KHI/2019 dated July 15, 2019 (“SCN”) issued to AKD Securities Limited (“Respondent”) by the Securities and Exchange Commission of Pakistan (“Commission”) 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 (“PSX”) and licensed as a securities broker under the Securities Act, 2015.
- (b) An inspection conducted by the Commission revealed that the Respondent was non-compliant with the Securities and Exchange Commission of Pakistan (Anti Money Laundering and Countering Financing of Terrorism) Regulations, 2018 (“AML Regulations”). Keeping in view that the AML Regulations were new at the time of inspection, Commission ordered to conduct a follow up review (“Review”) to assess the Respondent’s compliance with the AML Regulations.
- (c) The Review, *inter alia*, revealed the following:
 - i. The Anti Money Laundering/Know Your Customer (AML/KYC) policy was not updated so as to meet the requirements of the AML Regulations in contravention of Regulation 4(a) of the AML Regulations which requires





Securities and Exchange Commission of Pakistan

Securities Market Division

that a regulated person shall develop and implement policies, procedures and controls, which are approved by its board of directors, to enable the regulated person to effectively manage and mitigate the risks that are identified in the risk assessment of ML/TF or notified to it by the Commission. The policy is found deficient in the following areas:

- a. Politically exposed persons (PEPs)
 - b. Beneficial ownership of legal arrangements
 - c. Enhance due diligence
- ii. The Respondent had failed to perform Customer Due Diligence of ten (10) clients i.e. information such as source of income, occupation, monthly/yearly income and beneficial ownership, etc. was not obtained at the time of opening of the account in violation of Regulation 6 which requires that a regulated person shall apply Customer Due Diligence measures when establishing business relationship with a customer.
- iii. The Respondent did not have a mechanism for ongoing monitoring of its clients in contravention of Regulation 13 which requires that all business relations with customers shall be monitored on an ongoing basis to ensure that the transactions are consistent with the regulated person's knowledge of the customer.
- iv. The Respondent did not have a system that generated alerts one month before the expiry CNICs of its customers as required under Regulation 6 (Annexure I). Moreover, CNICs of ten (10) of its clients were expired.
- v. The Respondent had not developed an independent audit function in violation of Regulation 4(d).
- vi. The Respondent had not reported five (5) transactions valuing Rs. two million and above in violation of Regulation 14.
- vii. Circular 10 of 2017 requires the Respondent to maintain record of its clients who had traded in excess of Rs. 5 million during a month. However, the Respondent has not maintained record of two (2) of its clients where net traded value during a month was greater than Rs. 5 Million.

3. It appeared from the preceding that the Respondent *prima facie* acted in contravention of the AML Regulations and Section 150 of the Securities Act, 2015. Accordingly, the Commission took cognizance of the aforementioned facts and served the SCN requiring the Respondent to explain its stance in person on August 6, 2019.



Securities and Exchange Commission of Pakistan Securities Market Division

4. The Respondent was accorded an opportunity of personal hearing dated August 6, 2019. Mr. Muhammad Farid Alam, Mr. Naveed Anjum and Mr. Tanveer Khan (the “**Representatives**”) appeared for and on behalf of the Respondent and made following submissions verbally and through written reply.

- a) *In this regard we state that Board of Directors of the AKDSL approved its "Anti Money Laundering/ Countering Financing of Terrorism (AML/CFT) Policies, Procedures and Controls" on 19 December 2018 about which you have highlighted certain observations.*
- i. *We tried to cover all the requirements of the AML Regulations in our AML/CFT Policy and for this purpose we also consulted and reviewed AML/CFT Policies of certain Banks, NBFCs and other securities brokers so as to know how extensive an AML/CFT Policy should be;*
 - ii. *We also consulted the draft AML/CFT Policy circulated by the Pakistan Stockbrokers Association to help their members for drafting their AML/CFT Policies;*
 - iii. *You may appreciate that every requirement of the AML Regulations and Guidelines need not to be part of policy since certain requirements are very clearly stated in the AML Regulations and Guidelines and their reproduction in the Policy will only result into a lengthy draft. In this respect, Regulation 7, 9 and 10 of the AML Regulations and Clause 13 of the AML Guidelines are very clear on the areas pointed out by the SECP inspection team.*
 - iv. *We would like to draw your kind attention as a matter of abundant caution we have included following paragraph in AKDSL's AML/CFT Policy as approved by the Board on 19 December 2018 and the same was provided to the SECP team;*

Quote

In case of any inconsistency in this Policy and prevailing Law, Rules and Regulation, the relevant Law, Rules and Regulations will prevail. Moreover, in case of any requirement is not listed in this policy but mentioned in the applicable Law, Rules and Regulations, same should be treated as part and parcel of this policy. Unquote

- v. *We further state that we have been applying the required procedures in respect of i) Politically exposed persons (PEPs), ii) Beneficial ownership of legal arrangements and iii) Enhance due diligence but same were not included in AKDSL's AML/CFT Policy due to the reasons explained above. However, as pointed out by the SECP team, we have documented the same under separate sections in the version 1.2 of the AKDSL's AML/CFT Policy which was provided to the SECP team through our email dated 22 April 2019 at the time of our comments on Letter of Findings in draft form. Same draft of Version 1.2 was subsequently approved by BOD through their resolution dated 17 May 2019.*

- b) *The Company has a practice to perform CDD at the time of Account opening as required under Regulation 6 but all the trading accounts highlighted by your goodself have been opened before notification of this SECP's AML/CFT Regulations when KYC/CDD Guidelines notified by the Karachi Stock Exchange were applicable where there was no such requirement. Under the PSX Guidelines, EDD was required to implement following controls (i) Approval of high risk customer from the senior management which was done in the form of approval of Account Opening Form by the CEO, AKD Securities; (ii) Identification of sources of wealth and funds which was done by obtaining information about the business of customer and constitutive document in case of corporate customers. With due respect we*





Securities and Exchange Commission of Pakistan Securities Market Division

would like to highlight that Regulation 6 of the AML Regulations does not require us to know/ascertain monthly/yearly income of ten (10) clients highlighted by the inspection team instead all the ten clients comes under Regulation 6(10) of the AML Regulations . A perusal of Annexure 1 of the AML Regulations shows that minimum document required to be collected from the client for opening a trading account do not require any document related to clients' annual/monthly income or networth information. Therefore the clients do not feel any compulsion to provide such details to the broker in relation to their trading accounts. We would like to draw your kind attention towards the ground reality that the clients are very much reluctant to provide their annual income and networth details.

- c) In this regard we have already provided explanation for every client vide our email dated April 22, 2019 in which we explained our procedure of ongoing monitoring along with all relevant information with brief description of their profile, financial soundness along with funding source through which we get assurance that the transactions are consistent with the regulated person's knowledge of the customer. Further we monitor the client regarding any unusual transaction being highlighted in our system like breach of assigned limits or on the basis of assigned risk. Such queries are asked through recorded telephone lines or emails to the respective client. Having said that we would like to comment that as a matter of policy and to remain embraced with relevant laws and regulations we are in continuous consultation with our vendor to make our Back Office System in accordance with the requirement of AML Rules and Regulation and in accordance with our policy.
- d) We have been using back office system provided by one of the approved back officer vendor — M/S Microlinks (Private) Limited by the Pakistan Stock Exchange. The back officer vendor contain "Client CNIC Expiry Alert" in the form of report that can be generated on any given point of time. We expect that this is back office provided by the approved vendor must be complied with the applicable regulations. In case of expired CNICs we do request our clients for provision of renewed CNICs and we have sent total emails to 2,148 clients during the year 2018 out of which we received 401 replies which have been updated in our system. Moreover, we state that most of the clients do not respond our request of renewed CNIC therefore we have no option but to send them reminder periodically since the clients have not any regulatory compulsion to provide us the updated CNIC.
- e) The AML Regulations do require to appoint a "Compliance Officer" and "Independent Audit Function" but do not prescribe any minimum qualification and experience requirements for both the functions. Therefore, appointment of two separate persons (without any minimum qualification and experience) may comply with the AML Regulation but may not produce the results expected by the SECP. We had stated in our comments to Letter of Findings that we would put this matter before the Board to consider and decide on this matter. Accordingly, the Board in light of observation of the SECP's inspection team, have segregated both the functions which will directly report to the Board of Directors.





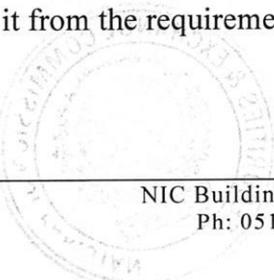
Securities and Exchange Commission of Pakistan Securities Market Division

- f) This is regarding non-reporting of cash receipts valuing Rs. 2,000,000 and above from the clients as "Currency Transaction Report" (CTR) to Financial Monitoring Unit. These cash transactions, however, have been reported to the PSX through the terminal provided for this purpose. This issue was highlighted by the SECP vide their letter no. Ref No. SMD/SSED-C&IW/(916)/2017 dated 18 August 2017 which was duly responded through our letter dated 25th August 2017 explaining that the cash is not received on our premises but it is deposited by our client (usually distant clients) directly into our bank account. This issue was also highlighted during the Review of Compliance Status conducted by the SECP in the last quarter of calendar year 2017 and we provided our same stance in the form of comments. On 07 March 2018, we also obtained advice from our legal counsel on this matter by sending the SECP's letter and our Response and he opined that the stance taken by you is totally in accordance with law. An analysis of five instances of cash deposits highlighted by the inspection team shows that all the deposits were made directly by the respective client himself as the deposit slip contains his own signatures as "depositor". Copies of the deposit slips are enclosed.
- g) The report has been generated from the back office. Month wise reports for the month of November 2018, December 2018 and January 2019 are enclosed. Although we have complied with the requirements of circular 10 but we understand that the threshold were set on lower side perhaps due to the same reasons, the circular has been withdrawn by the SECP vide Circular No. 6/2019 dated April 16, 2019.

5. I have examined the written as well as oral submissions of the Respondent and its Representatives. The Respondent argued that due diligence procedures in respect of politically exposed persons, beneficial ownership of legal arrangements and enhance due diligence were applied. It did not contend the fact that these aspects were missing from its policy, however, the Respondent argued that the same are covered through the following clause of its policy:

"..in case of any requirement is not listed in this policy but mentioned in the applicable Law, Rules and Regulations, same should be treated as part and parcel of this policy."

A 'Policy' is a predetermined course of action, which is established to provide a guide toward accepted business strategies and objectives. In other words, it is a direct link between an organization's 'Vision' and their day-to-day operations. Policies identify the key activities and provide a general strategy to decision-makers on how to handle issues as they arise. This is accomplished by providing the reader (employees) with limits and a choice of alternatives that can be used to 'guide' their decision making process as they attempt to overcome problems. The above clause of the policy quoted by the Respondent does not substitute the importance to have a comprehensive policy. Therefore it cannot be used as a defense of the Respondent or absolve it from the requirement of law.





Securities and Exchange Commission of Pakistan

Securities Market Division

6. In regard to CDD, the Respondent argued that the highlighted ten accounts were opened prior to notification of AML/CFT Regulations and regulation 6 does not require it to ascertain monthly/yearly income. The Respondent, vide email dated August 22, 2019 and September 2, 2019, was required to provide evidence reflecting that it had established level and source of income. However, no response was received. At the outset, it is clarified that the requirement to conduct CDD is not new and it existed even as part of PSX Guidelines of 2012. As a part of CDD, relevant information including identity and source of income of the customer is collected and evaluated for any potential risk for the organization or money laundering/terrorist financing activities. Further, in the absence of vital information such as source of funds and income level of client, ongoing monitoring of client's transaction is not possible. In view thereof, the argument of the Respondent does not hold merit.

7. The Respondent did not contend its failure to develop independent audit function. It was submitted that the board of directors accorded approval in its meeting held on July 22, 2019 to segregate internal audit function from the compliance function to comply with the applicable regulations. Given that the Respondent did not have an independent internal audit function at the time of Review, the violation of AML Regulations is established.

8. The Respondent contended in case of expired CNICs, it requests the client for provision of renewed CNICs. In order to support its claim, it was submitted that a total of 2148 emails have been sent to clients in the year 2018 for this purpose. It provided copies of emails sent to clients that establishes that the Respondent had taken reasonable steps to obtain renewed CNICs. Therefore, the Respondent is not held accountable on this count.

9. In regard to non-filing of CTR, the Respondent contended that it was not required to file CTR because cash was not received at its premises rather it was received in its bank account. The Respondent argued that in such case requirement to file CTR is applicable on the banks. The response of the Respondent is found satisfactory.

10. In regard to noncompliance of Circular 10 of 2017 for two of its clients, the Respondent contended that it had submitted the required information. Given that the said circular stands repealed, the matter is not being pressed further.

11. In view of para 5 to 7 above, contravention of the provisions of AML Regulations have been established. Therefore, in terms of powers conferred under section 40A of the Act, a penalty of **Rs. 250,000/- (Rupees two hundred and fifty thousand)** is hereby imposed on the Respondent. The Respondent is advised to examine client accounts to ensure that the requirements contained in the AML Regulations are met in letter and spirit. A report in this regard shall be submitted to the Commission within sixty (60) days of the date of this order.





Securities and Exchange Commission of Pakistan

Securities Market Division

12. The Respondent 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.
13. 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.




Shauzab Ali
Commissioner (SMD)

Announced on 30-09-2019
Islamabad