



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division

Before the Commissioner (SMD)

In the matter of Appeal dated July 29, 2015
filed by

DJM Securities (Private) Limited
against

Order dated July 09, 2015
of the Disciplinary Tribunal of CDC
under Regulation 14.7.2 of CDC Regulations

Date of Hearing:

September 03, 2015

Present at Hearing:

Representing DJM Securities (Private) Limited
("the Appellant")

Mr. Dawood Jan Muhammad,
Chief Executive Officer

Representing the Central Depository Company
of Pakistan ("the Respondent")

Mr. Badiuddin Akber,
Head of Compliance

Assisting the Commissioner (SMD)

- i) Mr. Nasir Askar, Director /HOD (LCID)
- ii) Mr. Muhammad Farooq, Joint Director
- iii) Mr. Tahir Mahmood Kiani, Deputy Director

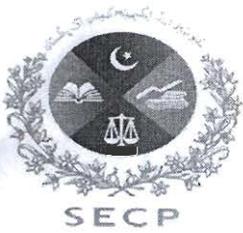
ORDER

This Order will dispose of Appeal dated July 29, 2015, filed by DJM Securities (Private) Limited (**the Appellant**) against Order dated July 09, 2015 (**Impugned Order**) of the Disciplinary Tribunal of Central Depository Company of Pakistan Limited (**CDC Tribunal**) under Regulation 14.7.2 of CDC Regulations (**CDC Regulations**).

2. Brief facts of the case:-

- a) The Appellant is a Trading Right Entitlement Certificate Holder of Karachi Stock Exchange Limited ("KSE") and registered as a broker with the Securities and Exchange Commission of Pakistan ("**Commission**") under the Brokers and Agents Registration Rules, 2001. The Appellant has Participant Account (id:04895) with the CDC.





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- b) The CDC conducted an inspection of records maintained by the Appellant for the period from June 01, 2012 to May 31, 2013. As per the Inspection Report, the Appellant was found failure to:-
- i. Obtain written authorization in 23 instances, from a sub-account holder, for pledging of securities with financial Institutions, in contravention of provision of Regulation 6.7.2 of the CDC Regulations.
 - ii. Provide documentary evidence in 3 instances for sending of Holding Balance Statements to sub-accounts holders, in contravention of 6.2 A-1 of the CDC Regulations.
- c) The Chief Executive Officer of CDC, in exercise of power vested under Regulation 14.3.1 (b) of the CDC Regulations, on account of aforesaid non-compliances/violations of CDC Regulations, imposed penalty of Rs. 260,000 on the Appellant vide notice dated July 24, 2013.
- d) The Appellant challenged the aforesaid notice before CDC Tribunal, which, after providing hearing opportunity to both parties upheld the decision of the CEO of CDC and directed to the Appellant to pay the penalty of Rs. 260,000/- for regularizing of the non-compliances, within 15 days of the receipt of Impugned Order.
3. The Appellant, has preferred to file the instant Appeal against the Impugned Order, under Regulation 14.7.2 of CDC Regulations on the following grounds:-
- a. That the order of the CDC Tribunal is bad in law and wrong on fact of the case.
 - b. That the learned CDC Tribunal has erred in law , on facts of the case an wrongly inferred that the Appellant failed to provide any written authorization from the sub-account holder for executing pledged transaction with financial institution as well as evidence of sending account balance statements.
 - c. That the learned CDC Tribunal was not justified in dismissing the documentary evidence produced before it and ignoring the explanations offered by the Appellant during the course of hearing.
 - d. That the learned CDC Tribunal was not justified in upholding the alleged violations of regulations 6.7.2 and 6.2A 1 of the CDC Regulations.
 - e. That the CDC learned Tribunal was not justified in upholding the arbitrary, very harsh and highly unjustified penalty of Rs. 260,000/.





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4. The Commission sought parawise comments from the Central Depository Company of Pakistan Limited (**Respondent**). The matter was scheduled for hearing for September 03, 2015, at the Commission's Regional Office, Karachi. Accordingly, Mr. Dawood Jan Muhammad Chief Executive Officer of Appellant and Mr. Badiuddin Akbar, Head of Compliance of the Respondent appeared before me. The arguments put forth by the Authorized Representative of Appellant be summarized as under:-

- i. *The documentary evidence submitted by them was not considered by the CDC Tribunal. He added that as per his understanding/ interpretation of regulation only single general authorization was required to be taken from the relevant sub-Account Holder for pledging of shares. He added that all the pledge transactions pointed out by CDC team from-where the securities were pledged belongs to one of his own family member. She is wife of his brother. We perceived that authorization form is necessary for ordinary sub-account holder. He further stated that she was abroad; therefore, it was not possible to obtain such authorization for 23 times. There was no unauthorized movement except this account. He assured that no such non-compliances will be repeated in future.*
- ii. *With regard to 3 instances of contravention of 6.2 A-1 of the CDC Regulations, the Authorized Representative of the Appellant argued that account balance statement were not sent to only those sub-account holders who were having nil security balance. He stated that as per our understanding there was no such major risk involved with it as all such accounts were non-active account. However, we have now started practice of sending account balance statements to all the sub account holders. The Respondent rebutted the clarifications given by the Appellant and reiterated its stance mentioned in the aforesaid para 3(d).*
- iii. *Imposition of penalty of Rs, 260,000 is not justified, because shares were pledged only from one account. Furthermore, the impugned order of CDC Tribunal is not self explanatory, because it failed to set out the bifurcation of imposed penalty.*

5. In response, the Authorized Representative of the Respondent rebutted the arguments advanced by the Appellant and stated that:-

- i. *The documents submitted by the Appellant were duly considered. In fact, the Appellant has misconceived the provision of the CDC Regulations. He added that the Appellant admitted that written authorization had not been obtained for each transaction, and his assertion was that a general authorization was sufficient to meet the requirement of law. While, according to Regulation 6.7.2 of the CDC Regulations, the Participant requires a specific prior written authorization*





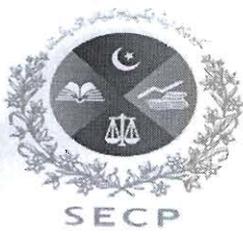
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from the relevant Sub-Account Holders in favor of the participants for each transaction." [Emphasis added].

Therefore, a prior single authorization is insufficient, as the Appellant had made various security pledges without obtaining the written authorization for each of the transaction. The fact that the Sub-Account Holder was 'abroad' or 'a household member' or was not an 'ordinary client' is irrelevant as the CDC Regulations apply to all without making any distinction as to such status of the Sub-Account Holder.

- ii. With regard to the violation of Regulation 6.2A.1 of the CDC Regulations the Respondent stated that *pursuant to the said regulation, every Participant is required to send within 10 days of end of each quarter to all Sub-Account Holders maintaining Sub-Accounts under the control of such Participant Holding Balance Statements..." [Emphasis added]. The words used are such that Holding Balance statements must be sent to the every sub-Account Holder. Therefore, the Appellant's contention that such statements were not sent to only those Sub-Account Holders having 'zero account balance, has no rational and has misconceived the requirement of the regulation. Since the the relevant Regulation does not differentiate between Sub-Account Holders having zero account balance or otherwise, therefore, the regulation 6.2A.1 of the CDC Regulations is applicable to all Sub-Account Holders.*
- iii. Concerning imposition of penalty of Rs. 260,000/- the Respondent stated that *Regulation 14.3.2 (a), provides that the CEO "shall not direct a CDS Element to pay sums exceeding a total of Rs. 10,000 for a single contravention..." [Emphasis added]. Thus, in light of Annexure A and B of the final Report dated 23.7.13, it was clear that the Appellant had contravened Regulation 6.7.2 and 6.2A.1 under the CDC Regulations and in total there were 26 contraventions; 3 contraventions under Regulation 6.2A.1 and 23 contraventions under Regulation 6.7.2, therefore a fine of Rs. 260,000 was imposed. So, imposition of such penalty in the given facts and circumstances of the case is by no means arbitrary or unreasonable. The CEO acted well within the scope of his powers conferred upon him under the CDC Regulations (Regulation 14.3.1(b)). Therefore, the imposition of the said fine is in accordance with the law. In fact the fine was initially imposed by the CEO and further upheld by the CDC Tribunal, which has an independent status, supports the objectivity and reasonableness of the Order.*





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6. I have heard the arguments presented by the Appellant and the Respondent at length during the hearing. Additionally, I have also perused the available record, appeal and written reply filed by the Respondent. It has been observed that the Appellant's pledged heavy quantity of shares (5,950,000/- in total) of different scrips (*Bank Alfalah Limited, PICIC Growth Fund, Askari Bank, ICI, Fauji Cement etc.*) from the sub-account 23 times against the single authorization and argued that it was only due to his misunderstanding of CDC regulations. It is worth mentioning here that the said practice continued for the whole year, which exposed the investor to undue risk. I have read the CDC regulation 6.7.2 and it explicitly states that prior written authorization from the sub-account holder will be required in "***each occasion***". Violation of a CDC regulation for twenty three times cannot be ignored on the pretext of lack of understanding of regulations. The Text of regulation 6.7.2 of the CDC Regulation is reproduced as under for ease of reference:-

*"Handling of Book-entry Securities by a Participant that are entered in the Sub-Accounts of his Sub-Account Holders for any purpose other than those specifically set out in the Authorization shall require the specific prior written authorization of the relevant Sub-Account Holders in favour of the Participant **on each occasion.**"*

7. I am also convinced that the above mentioned regulation doesn't differentiate between an ordinary sub-account holder or sub-account of member of broker family. The Appellant is a broker of KSE for the last thirteen years since July 5, 2002. Therefore, being an experienced broker he was supposed to ensure compliance of regulations. *The legal maxim is that "ignorance of the law is no excuse."* I am convinced that the Appellant has failed to comply the regulation 6.7.2 of the CDC regulations in letter and spirit.

8. With regard to failure to send account balance statement to all sub-account holders, it is very much clear from the language of the regulation 6.2A.1 that every Participant is required to send a statement of account within 10 days of end of each quarter to all Sub-Account Holders maintaining Sub-Account under the control of such Participant Holding Balance Statement. The Appellant's stance that such statements were not sent to those Sub-Account Holders which were having zero account balance is not justified. The Appellant has misconceived the requirement of the regulations.

The said regulation does not differentiate between sub-account holder with zero account balance and sub-account holder with balance of securities. The said regulation is applicable to all account holders.

The CDC regulations are very specific and clear and there is no ambiguity at all. The Text of the regulation 6.2 A-1 of the CDC regulations is reproduced as under for ease of reference:-





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“Regulations 6.2 A-1

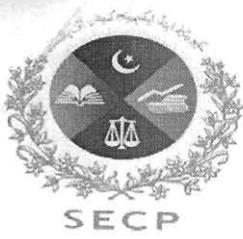
Every Participant shall send within 10 days of end of each quarter to all Sub-Account Holders maintaining Sub-Accounts under the control of such Participant Holding Balance statements showing the number of every Book-entry Security entered in every such Sub-Account as of the end of the preceding quarter. Such Holding Balance statements shall be generated from the CDS and shall be sent to the Sub-Account Holders in the manner set out in Regulation 2.6.4 including to the email addresses of the Sub-Account Holders notified to the Participants by them”.

9. In my opinion, the primary objective of the Regulation 6.7.2 and regulation 6.2 A-1 of the CDC Regulations is to protect the interest and assets of the clients. The client must be aware as and when his/her securities are used by a brokerage house for pledging purpose. Similarly, the submission of account balance statement to every sub-account holder seems to be necessitated, because, there is possibility that “zero” balance in any sub-account might be result of any misappropriation of the clients assets by the brokerage house. It may be recalled that in consequence of stock market crisis 2008, number of brokers were defaulted and investigation of brokers’ record disclosed that most of shares of investors were moved from their respective CDC-sub-accounts by the brokers without intimation/prior permission. In some cases investors shares were transferred to house account of broker for pledging with banks for heavy financing and in some cases transferred to benami accounts for misappropriation. Therefore, keeping in view the misuse of the investors’ shares which may lead to the default of brokers/systematic risks of the market, the regulators inserted specific regulations 6.7.2 and 6.2A.1 in CDC Regulations on August 05, 2009 and made its compliance mandatory.

10. Besides, I have also reviewed the track record of the Appellant. The record of this office has revealed that the Commission has already been taken a lenient view while passing an order dated March 31, 2014 against the Appellant. Through the said order a penalty of Rs. 100,000/- was imposed by the Commission to it upon failure to prepare the NCB in accordance with the Securities and Exchange Rules, 1971 and directed to ensure proper segregation of clients assets, use collateral account in case of non-payment by clients, stop imposing late payment charges, maintain proper books of accounts in case of non-payment by the clients and maintain proper books of accounts. The Appellant has deposited penalty to the Commission accordingly.

11. In view of the foregoing, I do not find any reason to interfere in the Impugned Order or to take a lenient view of the matter. Thus, the Appeal is dismissed with no order as to cost.

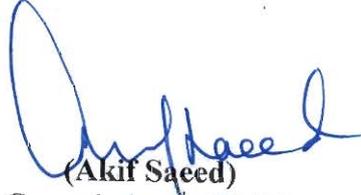




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12. This Order is being issued without prejudice to any other action that the Commission may initiate against the Respondent in accordance with the law on matter subsequently investigated or brought to the Notice of the Commission.




(Akif Saeed)
Commissioner (SMD)

Islamabad.
Announced on November 4, 2015