



# SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

## Adjudication Department- I

### Adjudication Division

*Before*

**Shahzad Afzal Khan, Director/Head of Department (Adjudication-I)**

*In the matter of*

### **Sarhad Rural Support Programme**

Show Cause Notice No. & Issue Date:	SECP/SCD/Adj-I/38/2021/154 March 20, 2024
Date of Hearing:	May 06, 2024
Present at the Hearing Representing the Respondent	Mr. Zafar Naeem, Manager (Compliance Manager) (Authorized Representative)

### **ORDER**

#### **UNDER SECTION 282J (1) OF THE COMPANIES ORDINANCE, 1984 FOR CONTRAVENTION OF REGULATION 28(C) OF THE NON-BANKING FINANCE COMPANIES AND NOTIFIED ENTITIES REGULATIONS, 2008 AND RULE 9 OF THE NBFC RULES, 2003**

This Order shall dispose of the proceedings initiated by the Securities and Exchange Commission of Pakistan (the **Commission**) through the Show Cause Notice dated March 20, 2024 (the **SCN**) against Sarhad Rural Support Program (the **Company**) issued under Section 282.J (1) of the Companies Ordinance, 1984 for contravention of Regulation 28(c) of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 (the **Regulations**) and Rule 9 of the NBFC Rules, 2003 (the **Rules**).

2. The Company was incorporated on November 27, 1989 under section 42 of the repealed Companies Ordinance, 1984 (now repealed by the Companies Act, 2017). In 2017 the Company obtained a Non-Banking Finance Company license to provide investment finance services restricted to micro-financing only under Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003. Its license was renewed for a period of three years with effect from January 10, 2023.

3. Brief facts of the case are that a review of monthly returns filed by the Company through Specialized Companies Return System (SCRS), was carried out by the Commission for the month of December 2023 and it was observed that the investments in microfinancing, excluding deposits with financial institutions and investments in government securities as compared to total assets was 37% as of December 31, 2023 which is less than the required percentage of 50% as per regulation 28(c) of the Regulations. Further, the Company had not obtained sufficient insurance coverage from an insurance company rated minimum "A" by credit rating agency registered with the Commission against any losses that may be incurred as a result of employee's fraud or gross negligence and make a disclosure about the insurance coverage in its financial statements in contravention of Rule 9 of the Rules.

4. The Company had already been granted a relaxation till September 30, 2023 vide Commission letter dated September 22, 2022 to increase percentage of investments in microfinancing, excluding deposits with financial institutions and investments in government securities as compared to total assets. However, the required percentage was not achieved until December, 2023 as provided above.



# SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Adjudication Department-I  
Adjudication Division

Continuation Sheet - I -

Further, the Company in year 2020 informed the Commission that the matter of insurance coverage was under consideration. However, it was observed that the Company continuously failed to comply with the requirement of the Law.

6. The Company, *prima facie*, were, therefore, non-compliant with the provisions of the Regulation 28(c) of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 and Rule 9 of the NBFC Rules, 2003 which attracts the penal provisions provided under Section 282 J(1) of the Ordinance. Therefore, SCN was issued to the Company, calling upon to show cause in writing as to why the penalty as provided under Section 282 J (1) of the Ordinance, may not be imposed on it for the aforementioned contraventions of the law. The Company vide its letter dated March 29, 2024 provided response to the SCN, the relevant extract of which is provided as under:

"3. Initially, SRSP was granted an exemption vide S.R.O 530(I)/2016 dated 8th June 2016 (Annex A). The exemption has allowed a non-banking microfinance company activity to have microfinance assets less than or equal to 30% of its total assets. However, this exemption was subsequently revoked under Regulation 28(C) of the Non-Banking Finance Companies and Notified Entities Regulations, 2008, which stipulated that the microfinance portfolio must account for 50% of its total assets.

4. SRSP with microfinance investment less than 50% of its assets has approached SECP for relaxation in time, which was subsequently approved by SECP vide letter No.SC/NBFC-I-159/SRSP/2022-20 dated September 22, 2022 (Annex...) till September 30, 2023

5. SRSP's microfinance portfolio percentage stands at 37% as on September 2023. SRSP was able to increase its microfinance portfolio to PKR-225 million (Annex ...). However, the desired percentage cannot be achieved due to increase in the other assets, like receivables from PKR-38 million to PKR-108 million (Annex ...) and fixed assets from PKR- 742 million to PKR-792 million (Annex ...) because of SRSP's new engagements/contracts with several donors.

6. In view of the above, approval is requested to relaxation in section 28 (C) till June 2025 under section 67A of the Non-Banking Finance Companies and Notified Entities Regulations, 2008, enabling us to revised our plan to comply with the regulatory requirements.

7. With reference to the rule 9 of the NBMFC Rules, 2003 to obtain sufficient insurance coverage from an insurance company rated minimum "A" by credit rating agency registered with the Commission against any losses that may be incurred as a result of employee's fraud or gross negligence and make a disclosure about the insurance coverage in its financial statements. The SRSP already initiated this process and will be completed till June, 2024. (Annex ...)

8. It is requested that our above-mentioned submission may please be accepted and penalty be waived off and a warning letter be issued against the Show Cause Notice. Sarhad Rural Support Program extend its full commitment towards fulfilment of all regulatory requirement."





# SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Adjudication Department-I  
Adjudication Division

Continuation Sheet - 2

7. In order to provide an opportunity for personal representation, hearing in the matter was fixed for May 06, 2024, wherein an authorized representative Mr. Zafar Naeem, Manager (Compliance) appeared on behalf of the Company. The Representative was advised to explain the reasons for the alleged non-compliances as narrated in the SCN. The Representative took the same stance as taken in their reply submitted that the desired percentage cannot be achieved due to increase in other assets, like receivables from PKR 38 million to PKR 108 million and fixed assets from PKR 742 million to PKR 792 million because of Company's new engagements and contracts with several donors. Further, in the matter of insurance against employee's fraud or gross negligence, the Representative submitted that the issue has been resolved. The Representative during the hearing proceedings assured that they will make serious efforts to comply with the regulatory requirements as highlighted in the SCN.

8. Subsequent to the hearing proceedings, the Company vide email dated May 10, 2024 submitted its plan for achieving 50% investment in microfinancing as compared to total assets which provides that the desired percentage will be realized in December, 2024. Further, the Company submitted evidence of agreement with insurance company for its insurance coverage against Employee's fraud which was availed in April, 2024 i.e. subsequent to the initiation of adjudication proceedings.

9. I have gone through the facts of the case and considered the verbal submissions of the Company and its Representatives in light of the applicable provisions mentioned in the preceding paras and the available record and I have the following question posed before me to take a decision in the matter:

- i. Why is it important for NBFC to maintain 50% of its assets in microfinancing, excluding cash deposits with financial institutions and investments in government securities?

Regulation 28(c) of the regulation clearly requires that Non-Bank Micro Finance Company shall invest at least 50% of its assets in micro financing, provided that cash, deposits with financial institutions and investments in government securities shall be excluded to calculate the above limit. In the instant matter, it was observed that the Company's percentage investment in microfinancing was at 37% in December, 2023 whereas, it was also observed that this percentage has dropped from 41% in January, 2023 to 37% in December, 2023 thereby, showing a downward trend. In its defense, the Representative argued that the Company is a Not for Profit Organization (NGO) and due to increase in other assets, like receivables from PKR 38 million in January, 2023 to PKR 225 million in December, 2023, and increase in fixed assets from PKR 742 million in January, 2023 to PKR 792 million in December, 2023, the desired percentage could not be achieved even though its microfinance portfolio has increased from 208 million in January, 2023 to PKR 225 million.

However, these arguments lack sufficient merit in the context of regulatory compliance. The essence of Regulation 28(c) is to ensure that NBMFCs focus their resources on microfinancing activities, which are crucial for their mission of financial inclusion and poverty alleviation. The significant increase in other assets, such as receivables and fixed assets, does not absolve the Company from its obligation to meet the 50% threshold. These





# SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Adjudication Department-I  
Adjudication Division

Continuation Sheet - 3 -

assets, while potentially valuable, do not contribute directly to microfinancing and therefore should not impact the calculation of compliance with the regulation.

Furthermore, the argument that the increase in the microfinance portfolio justifies the shortfall in percentage investment is fundamentally flawed. The regulation is designed to ensure that a substantial portion of the Company's total assets is consistently devoted to microfinancing. The relative growth in other assets suggests a strategic shift away from the core mission of microfinancing, which the regulation aims to prevent. This downward trend in the percentage of assets allocated to microfinancing is concerning and indicative of a potential misalignment with regulatory requirements and the Company's stated objectives.

In conclusion, while the Company's growth in absolute microfinance figures is acknowledged, it does not compensate for the failure to meet the mandated investment threshold. Compliance with Regulation 28(c) is non-negotiable and essential for maintaining the integrity and focus of NBMFCs. The Company's defense, highlighting the increase in other assets, does not sufficiently justify the non-compliance and underscores the need for a strategic reassessment to realign with regulatory obligations and core mission objectives.

ii. **What is the significance of obtaining insurance coverage against losses incurred from the Employees Fraud or gross negligence and non-compliance made by the Company?**

Rule 9 of the Rules explicitly requires every NBFC to obtain sufficient insurance coverage from an insurance company rated "A" minimum by credit rating agency registered with the Commission against any losses that may be incurred as a result of employee's fraud or gross negligence and make a disclosure about the insurance coverage in financial instruments. In the year 2020, the Company informed that the matter was under consideration however, no compliance was made until the initiation of adjudication proceedings against the Company in March, 2024. In this regard, the Company subsequent to the hearing proceedings submitted evidence of obtaining insurance coverage against employees' fraud in April, 2024 i.e. with a significant delay.

In the instant matter, the company's delay in obtaining the required insurance coverage until after the initiation of adjudication proceedings in March 2024 highlights a significant lapse in compliance and risk management. Despite informing about the consideration of this matter in 2020, the failure to act promptly exposed the company to unnecessary risk for an extended period. The subsequent compliance in April 2024, albeit delayed, underscores the importance of adhering to regulatory requirements in a timely manner to avoid potential financial, operational, and reputational repercussions.

In summary, the importance of Rule 9 lies in its role in safeguarding the financial health and integrity of NBFCs, ensuring regulatory compliance, enhancing stakeholder confidence, and promoting transparency and effective risk management. The significant delay in compliance by the company underscores the critical need for timely adherence to such regulations to protect against potential losses and maintain trust and stability in the financial system.

10. In view of the above-stated facts, circumstances, and submissions made by the Respondent, I am of the considered view that the provisions of regulation 28(c) of the NBFC Regulations and Rule



# SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Adjudication Department-I  
Adjudication Division

Continuation Sheet - 4 -

9 of NBFC Rules have been breached by the Company. I, therefore, in terms of the power conferred under Section 282 J (1) of the Ordinance, conclude the proceedings initiated against the Company by imposing a penalty of **Rs. 250,000 (Rupees Two Hundred and Fifty Thousand Only)** on the Company and warn the Company to remain careful to ensure meticulous compliance with all applicable laws in true letter and spirit, henceforth.

11. The aforementioned penalty must be deposited in the designated bank account maintained with MCB Bank Limited or United Bank Limited in the name of the Securities and Exchange Commission of Pakistan within thirty (30) days from the receipt of this Order, and duly deposited bank challan shall be furnished to the Commission. In case of non-deposit of the penalties, proceedings for recovery under Section 485 of the Act as arrears of land revenue will be initiated.

12. This Order is issued without prejudice to any other action that the Commission may initiate against the Company and/or its CEO in accordance with the law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.

(Shahzad Afzal Khan)  
Director/ HOD  
Adjudication Department-I

**Announced:**  
Dated: May 17, 2024  
Islamabad