



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
SPECIALIZED COMPANIES DIVISION
POLICY, REGULATION AND DEVELOPMENT DEPARTMENT

Before Commissioner (SCD)

In the matter of Show Cause Notice under Section 282M (1) of the Companies Ordinance, 1984 read with Regulation 41A of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 for Violation of Regulation 41 (d) of the Non-Banking Finance Companies and Notified Entities Regulations, 2008

<i>Date of hearing:</i>	<i>February 14, 2019</i>
<i>Present (on behalf of Central Depository Company of Pakistan Limited)</i>	<i>i. Mr. Atiqur Rehman Head of Trustee & Custodial Services</i>
<i>Assisting the Commissioner (SCD)</i>	<i>i. Ms. Tanzila Nisar Mirza, Additional Director</i> <i>ii. Mr. Murtaza Abbas, Joint Director</i>

ORDER

This Order shall dispose of proceedings initiated against Central Depository Company of Pakistan Limited (“CDC”) through Show Cause Notice (the “SCN”) bearing No. SCD/AMCW/ADJ/CDC/271/2019 dated January 31, 2019 under Section 282M (1) of the Companies Ordinance, 1984 (the “Ordinance”).

2. The brief facts of the case are that upon receipt of a complaint on August 31, 2018 from Mr. Zahid Oosman (the “Complainant”), an enquiry was ordered under Section 282I of the Ordinance vide Order bearing number SCD/S&EDAWT IL/2018/252 dated November 19, 2018.

3. Based on the findings of the enquiry team, a Show Cause Notice (“SCN”) dated January 31, 2019 was issued to CDC to show cause in writing by February 7, 2019 as to why action may not be taken for alleged violations of Regulation 41 (d) of the Non-Banking Finance Companies and Notified Entities Regulations 2008 (“the Regulations”). An opportunity of hearing in the matter was provided on February 14, 2019.

4. CDC vide letter dated February 6, 2019 submitted its written reply which is summarized as follows:

- i. CDC has fulfilled all its obligation as provided under Regulations 39 and 41 of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 (**Regulations**), as well as the provisions of the Trust Deeds and Offering Documents of PIML Islamic Income Fund **PIML IIF**), PIML Income Fund (**PIML**

IF), PIML value Equity Fund (PVEF), PIML Islamic Equity Fund (PIEF) and other funds of which CDC is the Trustee.

- ii. CDC is only the Trustee and the matter falls in the exclusive realm of the Management Company to check fraudulent activities in the accounts of the investors.
- iii. CDC did not receive the copy of Report of the investigation Team and requested for the same.
- iv. CDC clarified that the third party cheques favoring Mr. Asaduliah Khan for Rs5 million dated February 22, 2017 and Rs0.8 million dated July 04, 2017 respectively were issued by CDC in its capacity as the Trustee of PEF and PIEF respectively on the specific instructions of AWTEL (Formerly Primus Investment Management Limited), being the Asset Management Company (AMC) of these funds. Further, clauses 4.6.6 and 4.5.7 of the offering document of PVEF and PIEF respectively state that "..... The signature of any Unit Holder or joint Unit Holder on any document required to be signed by him under or in connection with the application for redemption of Units may be verified by Management Company or the Registrar or otherwise authenticated to their reasonable satisfaction."

Above clause clearly indicates that the AMC is responsible for;

- (i) Signature verification of the unit holders or joint unit holders or the Registrar (RTA) or the Distribution Company who is the agent of AMC, in accordance with the conditions contained in the Offering Documents.
- (ii) Applying "signature verified" stamp on redemption form and third party payment letter since it is the custodian of the signature records of the Unit Holder.

Thus, CDC can only ensure that AMC has applied the signature verification stamp on redemption form/ third party authority letter. It is neither the responsibility of the trustee to verify the signatures nor does it have the means to do so. CDC states that it is an industry wide practice whereby AMCs or its RTA verify the signatures on third party authority letters and send the same to the Trustee (CDC) for execution of the payment.

Similarly, in the instant case, third party authority letter was duly stamped by AMC indicating that the signature had been verified. Moreover, it was for AMC to check whether the authority letters for third party payments were personally signed by Mr. Shahid Arif Oosman or by Mr. Zahid Arif Oosman. CDC has no means to verify the credentials of principal account holders. It is therefore incorrect to say that CDC has contravened Clause 3.6 of the Offering Document of PIML IIF or that CDC has failed to protect the interest of the complainant/investor. CDC has all along acted diligently on the instructions of the Management Company.

- v. CDC also stated that it is a generally accepted practice in our industry that irrespective of what date is written on the application form/ third party authority letter by the unit holder, the AMC or the Trustee allots units on the basis of the date on which the form is received in their office or authorized branches. In the instant

case, the redemption application was dated February 22, 2017 while the time and date stamp affixed on the third party authority letter was July 03, 2017, i.e., the date on which the redemption application was actually received. The transaction was thus executed accordingly.

- vi. CDC submitted that it has neither violated Regulation 41(d), nor clause 3.6 of the offering document of PIML IIF i.e. of the fund in which initial investment was made. CDC has exercised all due diligence and vigilance in carrying out its duties and protecting the interest of the unit holders to every extent possible. By checking the time stamp, signature verified stamp on third party payment authority letter and honoring instructions of the AMC, CDC has complied with all the provisions of the Offering Document and reiterates that it has exercised all due diligence and vigilance in executing the AMC's instructions. CDC has therefore fully complied with the requirements of Regulation 41(d) of the Regulations, Clause 3.6 of the Offering Document of the PIML IIF, Clause 4.6.11 of the Offering Document of PIML IIF and clause 4.7.9 of the Offering Document of PIML IF.

5. The Hearing in the matter was held on February 14, 2019, during which CDC was represented by Mr. Atiq ur Rehman Head of Trustee & Custodial Services who reiterated the points mentioned at Para 4.

6. **Relevant Provisions of Law**

S. No.	Relevant Provision of Law
i.	<i>Regulation # 41 (d) of the Regulations clearly stipulates "A Trustee shall ensure that repurchase, redemption and cancellation of units are carried out in accordance with the provisions of the Constitutive Documents."</i>
ii.	<i>Clause # 3.6 of the Offering document of PIML Islamic Income fund: The Trustee shall exercise all due diligence and vigilance in carrying out its duties and in protecting the interests of the Unit Holder(s).</i>
iii.	<p><i>Clause No. 4.6.11 of the offering document of PIML Islamic Income Fund & Clause No. 4.7.9 of offering document of PIML Income Fund reads as follows:</i></p> <p><i>" The amount payable on redemption shall be paid to the Unit Holder or first named joint Unit Holder by dispatching a cheque/ bank draft/ pay order for the amount to the registered address of the Unit Holder or may be paid to the Unit Holder through Electronic Bank transfer to the Unit Holder's designated bank account as mentioned in the Investor Account Opening Form or Redemption form within six Business Days from the date of presentation of the duly completed Redemption form, electronic or otherwise, at the Authorized Branch or office of the Distributor or the Management Company. The amount can also be paid to the third party upon instruction of the Unit Holder through Electronic Bank transfer to the Unit Holder's designated bank account as mentioned in the Investor Account Opening Form or Redemption form."</i></p>

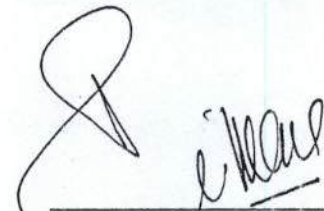
7. I have examined the facts of the case, written responses submitted along with documentary evidences, the arguments put forth by the Respondent during the course of hearing and the relevant regulatory requirements. I am of the considered view that CDC being the Trustee has a critical role in protecting the rights of unit holders and therefore is expected to be more diligent and to have

robust systems in place. In the subject issue, it is clear that CDC was neither able to recognize the sensitivity of the matter nor perceive the risk associated with third party payments.

Although, CDC acts upon the instructions of the AMC, presuming that the AMC has conducted due diligence and necessary verification of unitholders, CDC should have adequate systems/procedures to guard against the possibility of forged requests for redemption being processed. Moreover, despite the fact that the subject complaint has been in the notice of CDC for the past six months, it has neither identified the loopholes present in the process pertaining to third party payments nor has it submitted any proposal for improvement of the process. CDC being the Trustee should not have only acted proactively but rather should also have strengthened its procedures/systems, especially where payments to third parties were involved.

CDC provides trusteeship to almost 95% of the mutual fund industry and earns a sizeable amount of its revenue from trustee fee. Hence being the dominant market leader in this sector, adherence to the highest standards of vigilance and caution is expected. In my view, CDC's obligation to exercise all due diligence and vigilance in carrying out its duties and in protecting the interests of the unit holders has not been to the level expected of it and therefore the onus of lack of exercising its fiduciary responsibility falls on CDC. However, by taking a lenient view in this instance, owing to this being a first incidence of its type in a very long period, the company is hereby warned to ensure compliance of the applicable regulatory framework in future. Keeping in view, money laundering, CFT and other associated risks, CDC is also instructed to strengthen its systems and devise adequate controls in order to mitigate the inherent risk pertaining to third party payments. Non-compliances, if any, shall be dealt with in accordance with the enforcement action(s) as provided in law.

8. This order is issued without prejudice to any other action that the Commission may initiate against the Company in accordance with the law on matter subsequently investigated or otherwise brought to the knowledge of the Commission.



Aamir Khan
(Commissioner SCD)