



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
SPECIALIZED COMPANIES DIVISION

Before Commissioner (SCD)

In the matter of Show Cause Notice issued to MCB Arif Habib Savings and Investments Limited under Section 282J (1) read with Section 282M (1) and Section 282D of the Companies Ordinance, 1984

Date of hearing:

April 14, 2016

Present (on behalf of MCB AHSIL):

- i. Mr. Rabel Z. Akhund (Legal Adviser)
- ii. Ms. Sahar Iqbal (Legal Adviser)
- iii. Mr. Muhammad Saqib Saleem (CEO)
- iv. Mr. Shaukat H. Rizvi (Head of QA & HR)
- v. Mr. Syed Sohail Ahmed (Head of Compliance)

Assisting the Commissioner (SCD)

- i. Mr. Imran Inayat Butt (Executive Director)
- ii. Mr. Javed Akhter Malik (Joint Director)

ORDER

This Order shall dispose of the proceeding initiated against MCB Arif Habib Savings and Investments Limited (the "Company" or "MCB AHSIL" or "Respondent") through show cause notice (the "SCN") bearing No. SCD/AD-AMCW/ MCB AHSIL/01/ 03/2016 dated March 24, 2016 under section 282J (1) read with section 282M (1) and Section 282D of the Companies Ordinance, 1984 (the "Ordinance").

2. The brief facts of the case are that Shaikh Zain-ul-Abidin (the "Complainant"), who invested Rs. 7.5 million in MCB Pakistan Asset Allocation Fund ("MCB-PAAF") on December 4, 2015 through Standard Chartered Bank (the "Distributor"), Shakra-e-Quaideen Branch, acting as Distributor of the Company, has lodged a written complaint with the Commission and alleged that:

- i. MCB-PAAF was mis-sold to him by the Distributor.
- ii. An amount of Rs.297,540/- was deducted as Front End Load (FEL) from the Complainant's investments of Rs. 7.5 million in MCB-PAAF without any prior intimation to him.
- iii. Offering document of MCB-PAAF was not given by the Distributor and the same was only given by Ms.Aliya Irfan, Customer Service Head, of the Company on December 29, 2015 pursuant to Complainant approached the Company.



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- iv. The first statement regarding his investment and deduction of FEL was received by him on December 28, 2015 i.e. after lapse of twenty four days.
- v. Customer Service Head of the Company has informed him that he has been guided wrongly as MCB-PAAF is meant for long term period and not suitable for monthly income purposes.
- vi. The Branch Manager of the Distributor has informed the Complainant that investment in MCB-PAAF is suitable for regular monthly income.

3. The Supervision and Enforcement Department of Specialized Companies Division (the "Department") called relevant information and documents from the Company and also had separate meeting with the representatives of the Company and the Distributor. The following facts have been gathered by the Department from the information and documents provided by the Company and the Complainant:

- i. The Complainant opted for monthly payment frequency which is mentioned on his duly filled investment form.
- ii. The Company in its e-mail dated January 14, 2016 has informed that MCB-PAAF does not offer any type of income units.
- iii. The Customer Investment Profile (CIP) Form forwarded by the Distributor to the Company appears to have been filled electronically by the officers of the Distributor.
- iv. CIP mentions that the Complainant is not above the retirement age, whereas, the date of birth of the Complainant is April 20, 1955 which indicates that the Complainant was of 60 years and 7 months old at the date of signing of the form i.e. November 24, 2015.
- v. CIP indicates that the Complainant possess high net worth (i.e. Rs.57 million), and the sources of income as "Business Income". Investment Form also indicates that the Complainant source of funds is business income. However, the supporting document provided by the Company is copy of the employment certificate of the Complainant which indicates that the Complainant is a salaried person.
- vi. CIP highlights ticking on the options pertaining to high risk product features. However, Investment Form mentions investment in a monthly payment frequency which is a low risk. Furthermore the fund i.e. MCB-PAAF sold by the Distributor to the Complainant does not offer monthly payment frequency.
- vii. No action was taken by the Distributor or Company to remove the inconsistencies in the dully filled CIP and Investment Form.
- viii. High risk product has been sold to a person who is more than 60 years old and was in need of monthly payment.



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- ix. Distributor is sole beneficiary of the FEL on mutual funds sold through it.
- x. Units of MCB-PAAF were issued by the Company on December 4, 2015 and account statement to this was e-mailed to the Complainant on December 8, 2015. However, intimation of the deduction of FEL which was required to be sent to the Complainant within 48 hours of realization of funds in terms of Circular 26 of 2015 dated July 15, 2015 has not been conveyed by the Company.
4. It was construed from the facts gathered that the Respondent, *prima facie*, has not made compliance to sub-section (b), (c), (d) of section 66A of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 (the "Regulations"), clause (1), (2) & (3) of Circular 23 of 2013 and sub clause (c) of Circular 26 of 2015.
5. Consequently, the SCN was issued to the Respondent whereby it was called upon to show cause in writing as to why penal action may not be taken against it for the aforesaid contraventions and hearing was fixed for April 7, 2016. In response to the SCN, the chief executive of the Company through letter dated March 31, 2016 requested for extension of seven days in time for submission of reply and hearing. The extension was granted till April 11, 2016 for submission of reply and hearing was rescheduled to April 14, 2016. In response to the SCN, Mr. Rabel Z. Akhund of Akhund Forbes, submitted reply dated April 11, 2016 on behalf of Respondent. With reference to contents of the SCN, a brief of submissions of the Respondent are reproduced below:
- i. The Company and its Distributor deny that it failed to comply sub-section (b), (c), (d) of section 66A of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 (the "Regulations"), clause (1), (2) & (3) of Circular 23 of 2013 and sub clause (c) of Circular 26 of 2015.
- ii. The Company has entered into a written agreement with the Distributor dated December 31, 2013 and its clause 5.1 (e) clearly states the terms and condition for avoidance of fraud and mis-selling by the Distributor as required in sub-section (b) of section 66A of the Regulations.
- iii. The Company has not been afforded a proper opportunity of defending itself, rendering the allegations invalid in the eyes of law, being contrary to the right to a fair trial and due process guaranteed by Constitution of Islamic Republic of Pakistan. Such a fundamental defect is fatal to the SCN as a whole as it taints the SCN with mala fides in law. For this reason alone, SCN is liable to be withdrawn or set aside.



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- iv. Risk profiling of MCB-PAAF was explained in detail to the Complainant, including the applicability of the front end load and frequency of profit payments and was also given a booklet containing information about different types of mutual funds.
- v. The Complainant opted for capital growth preference in the Customer Investment Profile (“CIP”) document dated November 24, 2015 duly signed by him. Furthermore, in the same document i.e. CIP, the Complainant stated that he did not wish to withdraw his investment for liquidity needs and that his sole objective was to protect the value of his investment. The fact that his monthly salary is USD 7,920 is also consistent with his statement regarding low liquidity need and investment preference. It is therefore incorrect to say that there was any mis-selling on the part of the Company or the Distributor. because the Distributor fully and exhaustively apprised the Complainant of the risks and benefits of investing in, and the key features of, MCB-PAAF, in great detail and at great length, during the call back confirmation conversation that took place between the Complainant and the Distributor on November 24, 2015 (“Call”).
- vi. The Complainant made an informed decision of investing in MCB-PAAF, after being thoroughly satisfied of the specific terms and conditions of MCB-PAAF. This is evidenced from the Call where the Distributor’s representative asked the Complainant to confirm whether the CIP correctly and accurately reflects his responses and whether the product assigned to him met his requirements. The Complainant emphatically and wholeheartedly responded in the affirmative.
- vii. The Complainant’s execution of the Account Opening Form (AOF) should be taken to imply his understanding of its terms and conditions, including the frequency of profit payouts and deduction of front end load as it is preposterous to argue that a well-educated man of Complainant experience and standing would have signed the AOF without reading or understanding its contents.
- viii. By signing the Debit Authority Form (“Debit Form”), the Complainant agreed that he has made his own appraisal of the investment opportunity in MCB-PAAF (clause 13 of the Debit Form), has understood and agreed that all decisions to purchase units in MCB-PAAF are his own and based on his independent assessment of the risks associated with investing in the fund and the decision to invest in MCB-PAAF is in no way reliant on any advice received from the Distributor (clause 14 of the Debit Form).



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- ix. CIP is an application which prepares the investor's profile on the basis of his responses to assess his risk appetite along with his investment goals. This document was endorsed by the Complainant through sign off which shows his consent to the individual responses. This confirms that the Distributor carried out the risk profiling of the Complainant after following the due and proper procedure and did not carry out any wrongful or misleading action nor was negligent in any manner.
- x. Regarding incorrect information relating to the Complainant's retirement age in CIP, it is submitted that even if the CIP would have mentioned that the Complainant was over the age of 60, this fact would not have altered the Distributor's recommendation of MCB-PAAF to the Complainant in view of the other relevant risk profile assessment facts of the Complainant. Furthermore, the law has not stipulated retirement age for a common man (i.e. non civil servant) in Pakistan. Specifically, no age limit or age restriction has been imposed on unit holders of collective investment schemes by the law. Hence, the fact that the Complainant was aged 60 years and 7 months at the date of signing the AOF for MCB-PAAF is immaterial and irrelevant.
- xi. The Complainant's source of income is 'Salary' and not 'Business Income'. However, this classification for the purpose of risk profiling of the Complainant is immaterial and does not alter the risk rating or any other parameter facilitating/aiding the sale of MCB-PAAF to the Complainant. The Distributor already knew about his employment from the information provided by the Complainant to the Distributor and selecting 'Business Income' was merely an oversight on the part of the Distributor and the risk profiling was actually done on the basis that the Complainant was a salaried employee.
- xii. The Offering Document and Fund Manager's Report of MCB-PAAF were showed to the Complainant by the Distributor's representative in person and the representative also explained to the Complainant the salient information contained in these documents, including the applicability of the front end load. Had he asked for a hardcopy of the Offering Document, the Distributor would have provided it to him. Furthermore, the Offering Document and the brochure of MCB-PAAF were readily available on the Company's website which the Complainant could easily access. Since the Complainant is a holder of an email address, it is reasonable to assume that he could have accessed the website as well.
- xiii. The Complainant has signed:



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- a. Debit Form which contains a statement (clause 16) that he has received a copy of the Offering Document. Furthermore, when the Distributor's representative asked him during the Call whether he had received, inter alia, the Offering Document, he responded in the affirmative.
- b. Investment Form which contains a declaration in Clause 3(1)(a) that the Complainant has read and understood the constitutive documents of the fund in which he is investing in.
- xiv. Hardcopy of the product brochure/booklet was provided to the Complainant which is also confirmed by the Complainant during the Call. It is, therefore, incorrect and untruthful of him to write in the Complaint that he was not given this booklet.
- xv. The Complainant's complaint regarding deduction of front end load without prior intimation is rebutted by the fact that Clause 7 of the Debit Form, which was executed on November 24, 2015 prior to the execution of the AOF by the Complainant on December 4, 2015 specified the percentage of front end load that would be deducted at the time of subscription in MCB-PAAF. Moreover, clause 3(1) (b) of the Investment Form duly signed by the Complainant, states that the offer price of the fund may include front end load which may be higher than the NAV of the fund.
- xvi. Regarding delay in sending account statement to the Complainant it is submitted that it had commenced the process to update its system to comply with the requirements of the Circular and the new statements of account was generated from December 11, 2015. However, notwithstanding this delay, the Distributor informed the Complainant of the front end load deduction prior to the Complainant investing in MCB-PAAF. Furthermore, this non-compliance was also reported by the Company to the Securities and Exchange Commission of Pakistan ("SECP") through the Company's Compliance Report for the quarter ended September 30, 2015 wherein the Company had informed SECP that because MUFAP was under discussion with SECP for making certain changes in the account statement format, the Company was waiting for final outcome of the discussion, prior to updating its system to comply with the Circular. The Respondent also requested to consider this non-compliance separately.
- xvii. The Respondent admits that it is responsible for the acts and omissions of the Distributor under the Agreement. However, it has asserted that the Distributor did not commit any act or omission contrary to the law for which the Company should be held responsible.



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6. A hearing in the matter was held on April 14, 2016 wherein Mr. Rabel Z. Akhund (Legal Adviser), Ms. Sahar Iqbal (Legal Adviser), Mr. Muhammad Saqib Saleem (CEO), Mr. Shaukat H. Rizvi (Head of QA & HR) and Syed Sohail Ahmed (Head of Compliance) appeared on behalf of the Respondent through video link from SECP office, Karachi and made submissions verbally mainly reiterating the earlier written submissions. The CEO of the Company also admitted their non-compliance to sub clause (c) of Circular 26 of 2015 and requested to take a lenient view considering that the Respondent is one of the most compliant Company.

7. I have analyzed the facts of the case, relevant provisions of the Ordinance, Regulations, Circulars referred and the arguments put forth by the Respondent in writing as well as during the course of hearing. My observations are as under:

- i. The Respondent contended that it has entered into a written agreement with the Distributor dated December 31, 2013 clearly stating the terms and conditions for avoidance of fraud and mis-selling of its collective investment schemes by the Distributor in clause 5.1 (e) of the agreement which is reproduced below:

"The Bank hereby undertakes and agrees with the Management Company that it will not accept any investment on the basis of false or mis-leading statement, by concealing or omitting material information and concealing associated risk factors of the Scheme in relation to the Scheme."

It is very obvious from the above that although, the Company has entered into a written agreement with the Distributor, however, the distribution agreement does not contain any clause with particular reference to avoidance of fraud and mis-selling by the Distributor. Moreover, clause 5.1 (e) quoted by the Respondent in this respect is also not relevant as the same does not specifically state terms and conditions for avoidance of fraud and mis-selling. It is therefore evident that the Respondent has not made compliance to sub regulation (b) of regulation 66A of the Regulations which is reproduced below:

"An Asset Management Company shall enter into a written agreement with the distributors clearly stating the terms and conditions for avoidance of fraud and mis-selling of Collective Investment Scheme."

- ii. The Respondent claimed that proper opportunity of defending itself has not been afforded is not true considering the fact that proper opportunity to defend itself by submitting a



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written reply has been granted through SCN. Additionally opportunity of personal hearing has also been granted to Respondent which has been availed by the Respondent through video link.

- iii. According to Respondent, risk profiling of MCB-PAAF was explained in detail by the Distributor to the Complainant. However, it is to highlight that risks associated with the fund are mentioned in the Offering document of the Fund which was not provided by the Distributor to the Complainant and this fact has been also been admitted by the Respondent. Therefore, statement of Respondent that risk profiling of MCB-PAAF was explained to Complainant is not acceptable.
- iv. Risk profiling of an investor is the basis which determines the type of fund to be sold to a prospective investor. The risk profiling questionnaire is provided by the Company in the AOF which considers investors age, source of income, investment horizon, existing investment of potential investor in equity market, objective of investment and risk tolerance. However, in this case, the Distributor has not used the risk profiling questionnaire given by the Company and used its own risk profiling for accessing the suitability of product to the Complainant. The risk profiling carried out by the Distributor ignores three main factors which Company considers i.e. age, source of income and existing investment of Complainant in equity market which has been admitted by the Respondent in its reply. Additionally, information regarding age, source of income and investment objective was inconsistent in the AOF and CIP. Due to these inconsistencies in the CIP and AOF and use of its own risk profiling criteria, the Distributor was not able to properly ensure the suitability of product for the Complainant. Moreover, due to inconsistency between risk profiling used by the Distributor and Company, the Distributor was not able to consider the all relevant factors which normally Company considers for evaluating the suitability of product when investor approaches the Company directly. Further, neither the Distributor nor the Company has made any efforts to remove the discrepancies in the information provided by the Complainant.
- v. It is also pertinent to highlight that if the Complainant had approached the Company directly, it may not be possible to sell the asset allocation fund based on the risk profiling criteria of the Company and the information given by him i.e. (having age more than 60 years, salaried individual, wants regular income, willing to take moderate risk, investment horizon of more than 5 years) because his aggregate score would have been 12 and a score of 22-28 is required to sell an equity or asset allocation fund. Even if, I assume that the objective of the Complainant was capital growth and not of regular



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income, his score would have been 16 which is still below than the score required (i.e. 22-28) to sell the equity or asset allocation fund. Based on above, it is evident that the Distributor has not taken reasonable care to ensure suitability of the scheme to the Complainant.

- vi. The Distributor has also not used the new AOF despite the fact that the same was implemented and uploaded by the Company in May 2015. Had the Distributor, used the new AOF, the risk profiling would have been correctly done by the Distributor in accordance with the risk profiling criteria given in the form and thus this fund would not have been sold to the Complainant. It was the responsibility of the Respondent to ensure that updated AOF should be used by its Distributors.
- vii. In terms of clause 5.1 (c) of the distribution agreement, it is obligatory on the Distributor to provide latest annual/semi-annual accounts and offering document of the fund to the potential investor which has not been provided by the Distributor in this case. Therefore, the Distributor has violated the aforementioned clause of the distribution agreement. This has also been admitted by the Respondent that had Complainant asked the copy of the offering document, the same would have been provided to him. clause 5.1 (c) of the distribution agreement is reproduced below:

"The Bank hereby undertakes and agrees with the Management Company that it will provide or supply to potential investors in the Scheme (where available) the latest annual or semi-annual reports of the Scheme provided by the Management Company, or make the Offering Document available"

- viii. There were many inconsistencies in the CIP and AOF with respect to age, objective of investment, source of income etc. which are considered mis-leading information and no action has been taken by the Distributor to remove these discrepancies prior to accepting investment. Even the call made to the Complainant has no reference to seek explanation from the investor to remove these discrepancies. Therefore, the Distributor has not made compliance to clause 5.1 (e) of the distribution agreement which is reproduced below:

"The Bank hereby undertakes and agrees with the Management Company that it will not accept any investment on the basis of false or mis-leading statement"

- ix. Based on the observations referred at para iii to viii above, it is implicit that the Distributor has made non-compliances of sub-section (c) (i) (iii) (iv) & (d) of section 66A



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of the Regulations and clause (1), (2) & (3) of Circular 23 of 2013 which are reproduced below:

“c) An Asset Management Company and distributor shall not:

- i. involve either directly or indirectly in the mis-selling of Collective investment schemes;*
- iii. sell units of Collective Investment Scheme directly or indirectly by concealing or omitting material facts of the scheme; and*
- iv. sell units of Collective Investment Scheme directly or indirectly by concealing the risk factors associated with the scheme.*

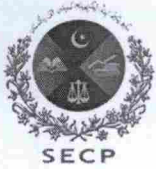
d) An Asset Management Company or distributor shall take reasonable care to ensure suitability of the scheme to the investor.”

- x. The contention of the Company regarding delay in sending account statement to the Complainant, it is stated that no exemption has either sought by the MUFAP or the Company from the Commission. Further no application for deferment of the requirement of sub clause (c) of Circular 26 of 2015 by the MUFAP or the Company was pending with the Commission. Therefore, the Company has made violation of sub clause (c) of Circular 26 of 2015 which is reproduced below:

..... “Issue to the unit holder, within 48 hours of the realization of funds, breakup of the total amount received from the unitholder, sales load charged and net amount invested in the fund on his behalf ”

9. Before proceeding further, it is necessary to advert that the Complainant had also approached Banking Mohtasib Pakistan and complained that he has become victim of mis-selling by the Distributor while marketing the fund to him. The Banking Mohtasib in its Order dated April 14, 2016 has made the following findings and directed the Distributor to make good the loss of the Complainant by refunding him Rs.297,540 which was recovered from his investment upfront as front end load:

“ The basic investment forms are full of flaws and also do not match with the vital document of relationship i.e AOF and cannot be relied upon as a credible document and as such, the entire super structure created thereupon fell collapsed including all subsequent actions in whatever shape i.e. pre-sale advice or call back confirmation (CBC). When centralized control



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office entrusted with the responsibility to verify the information given in a sales proposal/application forwarded by the Sales Staff does not verify the details in terms of parameters defined by SBP, CBC is meaningless as it is not meant to get the things endorsed which are false and misleading.”

10. Before proceeding to decide this case, I consider it necessary to highlight that SECP is deeply thoughtful of protecting the rights of investors and any unjust treatment with the investors cannot be tolerated to maintain investor confidence in the mutual fund industry. For the foregoing reasons and facts cited at para 7 and 8 above, I am of the considered view that Distributor has not made compliance to sub-section (b), (c), (d) of section 66A of the Regulations, clause (1), (2) & (3) of Circular 23 of 2013 and clause 5.1 (c) and (e) of the distribution agreement whereas the Respondent has not made compliance to sub clause (c) of Circular 26 of 2015. As the Respondent is responsible for all the acts of Distributor, I am of the view that the Respondent is found liable for all the aforementioned non-compliances. Therefore, in exercise of powers conferred by Section 282 J read with 282 M of the Ordinance, I hereby impose an aggregate fine of Rs.500,000/- (Rupees five hundred thousand only) on the Respondent. Moreover, in exercise of powers conferred by Section 282 D of the Ordinance, I hereby direct the Respondent to:

- a) refund Rs.297,540/- (Rupees two hundred ninety seven thousand and five hundred forty only) to the complaint within seven days from the receipt of this Order, if the same has not yet been refunded by the Distributor pursuant to Banking Mohtasib Order dated April 14, 2016;
- b) amend the distribution agreements with all its Distributors within one month from the date of this Order by incorporating clear terms and conditions for avoidance of fraud or mis-selling, use of same risk profiling criteria by the Distributor and the Company and procedure to be adopted for ensuring suitability of product to the investors; and
- c) ensure placement and implementation of centralized control function entrusted with the responsibility to verify the information given/application forwarded by the sales staff and Distributor so that reoccurrence of such violations are eliminated in future and that the funds are sold by the Company and its Distributors strictly in accordance with the NBFC Regulatory Framework and in compliance to distribution agreement.

11. The aforesaid fine must be deposited in the designated bank account maintained with MCB Bank Limited in the name of SECP within seven days from the receipt of this Order and




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furnish receipted bank challan to SECP. In case of non-deposit of the penalties, proceedings for recovery of the fines as arrears of land revenue will be initiated.

12. This Order is issued without prejudice to any action, which may be taken or warranted for the above said defaults under any other provision of the law.


(Zafar Abdullah)
Commissioner (SCD)

Announced: May 05, 2016 at Islamabad.