



# Securities and Exchange Commission of Pakistan

## BEFORE APPELLATE BENCH NO 1

In the matter of

Appeal No. 46 of 2012

M/S.HH Misbah Securities

..... APPELLANT

Versus

The Director, Market Supervision and Capital Issue  
Department

..... RESPONDENT

Date of Hearing

08/01/15

### ORDER

#### Present:

#### Appellant:

1. Mr. Abdul Wahab, CEO H.H Misbah Securities (Pvt.) Ltd

#### For the Respondent:

- 1, Mr. Adnan Ahmed, Deputy Director, SMD
2. Mr. Amir Saleem, Deputy Director, SMD (through video conferencing)
3. Ms. Tayyaba Nisar, Assistant Director, SMD (through video conferencing)

1. This order is in appeal No. 46 of 2012 filed under section 33 of the Securities and Exchange Commission of Pakistan (the "Commission") Act, 1997 against the order (the "Impugned Order") dated 17/09/12 passed by the Respondent.



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2. M/s Misbah Securities (Pvt) Ltd (“the Appellant”) is registered with the Commission under the Brokers and Agents Registration Rules, 2001 (“the Broker Rules”). On perusal of the trading data of the KSE for the month of April and May 2012, it was noted that the Appellant’s interexchange client namely Azeem Chaudhry (“Client”) having client code “LS114//985 had engaged in selling and squaring up his positions in different scrips.
3. During the month of April 2012, the Client first sold and then squared up positions in the scrips of Arif Habib Corporation (“AHCL”), Askari Bank Ltd (“AKBL”), Azgard Nine Limited (“ANL”), Bank Al-Falah Limited (“BAFL”), Dewan Cement Limited (“DCL”), Engro Polymer & Chemicals Limited (“EPCL”), Fatima Fertilizer Company Limited (“FATIMA”), Fauji Fertilizer Bin Qasim Limited (“FFBL”), JS Bank Limited (“JSBL”) Jahangir Siddiqui Company Limited (“JCSL”), Investment Limited (“JSIL”), Maple Leaf Cement Factory Limited (“MLCF”), National Bank of Pakistan (“NBP”), Nishat Mills Limited (“NML”) and Pak Electron Limited (“PAEL”). During the month of May 2012, the Client first sold and then squared up positions in the scrips of Bankislami Pakistan Limited (“BIPL”), D.G Khan Cement Company Limited (“DGKC”) and Pakistan Telecommunication Limited (“PTC”).
4. The Respondent vide letters dated 09/05/2012 and 05/06/2012 sought clarification regarding the short sales in different scrips executed by the Client through the Appellant. In response the Appellant informed vide letter dated 15/05/2012 that it has asked Equity Master Securities (Pvt.) Limited, member Lahore Stock Exchange Limited (“Member LSE”) to furnish the requisite information as the Client is trading through its account registered for inter-exchange trading. Subsequently, the Appellant informed the Respondent vide letter dated 18/06/2012 that Member LSE has closed



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the trading account of the Client on 08/06/2012. The response of the Appellant was not considered satisfactory as it did not contain any evidence and justification regarding the execution of aforementioned sales by the Client.

5. Show Cause Notice was issued under section 22 of the Ordinance and the Broker Rules with the Appellant found in breach of Clause A (2) and A (5) of the Code of Conduct set forth under the third schedule of Broker Rules. The Respondent in exercise of the powers under section 22 of the Ordinance imposed a penalty of Rs. 100,000 (Rupees One Hundred Thousand only) and additionally strongly advised the Appellant to take immediate measures and put in place proper system and checks to eliminate the occurrence of such instances in future.
6. The Appellant has preferred the appeal against the Impugned Order. The Appellant argued that:
  - a) these transactions took place through Member LSE and the Appellant has no access over the accounts/sub-accounts details of its clients in Central Depository System (CDS). It is, therefore, not possible for the Appellant to monitor such transactions and it was the sole responsibility of Member LSE to monitor its Client's Portfolio positions. Moreover, all transactions in question have been executed through Internet/On-line software and all the deliveries are settled directly by the National Clearing Company of Pakistan Limited ("NCCPL") through IDS, traded by Member LSE or their clients using the Appellant's On-Line Terminal; and



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- b) the Appellant was neither negligent nor had any knowledge in respect of the said account and the trades were merely a result of ignorance without any fraudulent intentions.

7. The department's representative argued that:

- a) the Appellant's assertion that all the transactions of LSE Broker dealing in the securities are separately settled with NCCPL are not relevant in the instant case. The Appellant have not implemented adequate system and controls in his brokerage house due to which it failed to detect the short sale executed through its KATS terminal. The responsibility to monitor all trading activities being carried out through the KATS terminal of the Appellant by its interexchange client rests with the Appellant to track and prevent any transaction being made in violation of any applicable rules and regulations. Inter exchange clients are the responsibility of the Appellant and the said transaction carried out through Member LSE had also been verified by the Appellant; and
- b) the Appellant has failed to exercise due care, skill and diligence in conduct of its business and has also failed to abide by the provisions of the Rules and Regulations issued by the Commission and KSE. The Appellant is, thus, in violation of Clause A(2) and A(5) of the Code of Conduct set forth under the third schedule of the Brokers Rules, which in turn is violation of Rule 12 of the Broker Rules read with Rule 8 of the Broker Rules.

8. We have heard the parties. Rule 8, 12 of the Broker Rules and Extract from the Code of Conduct are reproduced for ease of reference:



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## **Rule 8. Suspension of registration;**

*Where the Commission is of the opinion that a broker-*

*(iv) has failed to follow any requirement of the code of conduct laid down in the Third Schedule, the Commission may, if it considers necessary in the public interest so to do, by order in writing:-*

*(a) suspend the registration of a broker for such period as may be specified in the order; or*

*(b) impose on a broker a fine not exceeding one hundred thousand rupees.*

## **Rule 12. Brokers to abide by the Code of Conduct;**

*A broker holding a certificate of registration under these rules shall abide by the code of conduct specified in the Third schedule.*

*Emphasis added*

## **THE THIRD SCHEDULE (See rules 8 (iv) and 12)**

### **CODE OF CONDUCT**

#### **A. General**

*(1) Integrity.---A broker shall maintain high standards of integrity, promptitude and fairness in the conduct of all his business.*

*(2) Exercise of due skill and care. - A broker shall act with due skill, care and diligence in the conduct of all his business.*

*(3) Manipulation. - ... ..*

*(4) Malpractices.---A broker shall not create false market either singly or in concert with others or indulge in any act detrimental to the investors' interest or which leads to interference with the fair and smooth functioning of the market. A broker shall not involve himself in excessive speculative business in the market beyond reasonable levels not commensurate with his financial soundness.*



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(5) Compliance with statutory requirements.---A broker shall abide by all the provisions of the Act and the rules, regulations issued by the Commission and the stock exchange from time to time as may be applicable to him."

Emphasis Added

- (a) clause 2(a) of the Short Selling under Ready Market, 2002 ("the Regulations") says "Blank Sale" means "a sale by a party that does not own shares or the sale does not constitute a sale with pre-existing interest or is a sale by a party that has not entered into a contractual borrowing arrangement to meet delivery requirements." The sale, therefore, by the Appellant without pre-existing interest in the client's account falls within the ambit of Blank Sale which is prohibited in the Regulations. The Appellant, in the instant case, had verified the transaction carried out through Member LSE and was responsibility to ensure that all transactions conducted through their online terminal were in accordance with the applicable rules and code of conduct. We, therefore, accept the Respondent's argument that it was the responsibility of the Appellant and not Member LSE to monitor all trading activities being carried out through its brokerage house; and
- (b) the 'Code of Conduct', prescribed in the Third Schedule of the Rules read with rule 12 of the Rules prohibit interference with the fair and smooth functioning of the market. The Appellant's argument that the violations were a result of ignorance and not fraud cannot suffice. The Appellant has not been alleged to have benefitted by indulging in the said transactions, however, it is evident from the facts that the Appellant has failed to act with due skill, care and diligence in the conduct of its business and has, therefore, acted in violation of Rule 8(iv) read with Rule 12 of the Rules. The unfair trade practices like 'wash trades' are harmful for the development of market. The Commission is bound to protect the



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interest of investors and in doing so it has been empowered to deal with elements which effect smooth and fair functioning of the stock exchanges.

The Respondent could have suspended the license of the Appellant as a broker; however, the Respondent by taking a lenient view has rightly imposed a penalty of Rs.100,000 (Rupees One Hundred Thousand only) under rule 8(b) of the Rules.

In view of the above, we see no reason to interfere with the Impugned Order. The Appellant is directed to ensure compliance of all the rules, regulations and directives of the Commission in future for avoiding any serious punitive action under the law. The appeal is dismissed with no order as to cost.

**(Fida Hussain)**  
Commissioner (Insurance)

**(Tahir Mahmood)**  
Commissioner (CLD)

Announced on: **20 JAN 2015**