Securities and Exchange Commission of Pakistan

BEFORE THE APPELLATE BENCH

In the matter of

Appeal No. 142 of 2020

M/s. HG Markets (Private) Limited

...Appellant

versus

Commissioner-SMD, SECP and another

...Respondents

Date of hearing:

May 18, 2023

Present:

For the Appellant:

1. Mr. Feisal Hussain Naqvi, ASC
2. Mr. Ahmad Abdul Rehman, Advocate
3. Mr. Hussain Gulraze Mir, Chief Executive
4. Mr. Rashid Ali
5. Mr. Mobeen Gilani

For the Respondents:

1. Mr. Hammad Javed, Additional Director, Adjudication-I, SECP
2. Mr. Muhammad Faisal, Assistant Director, Adjudication-I, SECP
3. Syed Asif Ali, Additional Joint Director, Prosecution and Civil Litigation Department, SECP

ORDER

1. This Order shall dispose of Appeal No. 142 of 2020 filed by M/s. HG Markets (Private) Limited (the "Appellant") under section 33 of the Securities and Exchange Commission of Pakistan Act, 1997.

2. The brief facts of the case are that the Appellant is a futures broker of the Pakistan Mercantile Exchange (PMEX) in terms of regulation 3 of the Futures Brokers (Licensing & Operations) Regulations, 2018 read with sub-section (8) and (10) of section 123 of the Futures Act, 2016 (the "Act"). The Securities

and Exchange Commission of Pakistan (the "Commission") received seven complaints (hereinafter individually referred to as 'Complainant No.1', 'Complainant No.2', 'Complainant No.3', 'Complainant No.4', 'Complainant No.5', 'Complainant No.6', and 'Complainant No.7'; and jointly as the 'Complainants') against the Appellant. The Complainants alleged that they had given discretionary authority to the employees of the Appellant to trade in their accounts and the employees of the Appellant indulged in excessive trading with the sole objective of generating commissions, resultantly, they lost all or a significant part of their investments in the form of losses suffered on commissions paid. The Commission took cognizance and initiated an investigation against the Appellant through order dated June 15, 2017. The investigation concluded that the Appellant undertook excessive trades in the accounts of complainants for the purpose of generating brokerage or commission. 3515 trades amounting to US$ 81million or Rs 8.5billion were executed in the accounts of the Complainants and the Appellant earned brokerage commissions of Rs 4.3million on these transactions and the Complainants suffered a loss of Rs 2.4million. Furthermore, the report indicated that the Appellant had also not obtained the Complainant information about their circumstances and investment objectives, hence, the Appellant was non-complaint of clause 1(a), 1(b) and 2(d) of the Schedule to the Commodity Exchange and Futures Contracts Rules, 2005 (the "Rules") read with rule 20 of the Rules and clauses (a) to (f) of section 57 of the Act. A Show Cause Notice (SCN) was issued to the Appellant on January 22, 2019 and upon conclusion of the SCN proceedings, the Respondent in exercise of powers conferred under section 94 of the Act imposed a penalty of Rs. 5,000,000/- on the Appellant vide order date November 10, 2020 (the "Impugned Order").

3. At the outset, Counsel for the Appellant stated that he does not want to press legal objections and intends to argue the instant Appeal on merits. Moreover, upon enquiring that whether the Appellant has any objection with respect to the constitution of the Appellate Bench, as one of the members was Commissioner-Securities Market Division at the time investigation against the Appellant was initiated; the Counsel for the Appellant submitted that he has no objection in this regard.

4. On merits, the Appellant's Counsel argued that section 57(d) of the Act does not say that broker has to seek information 'in writing' rather only requires that broker has to seek information about the circumstances and investment objectives from the customers; and similarly only clause 2(d) of the

Schedule to the Rules is relevant in the instant matter which deals with excessive trading and thus *inter alia* for these reasons the Respondent erred in interpreting the said provisions while passing the Impugned Order as penal provisions are to be construed strictly. The Appellant further submitted that the penalty imposed upon the Appellant vide the Impugned Order is merely based on the statements of the Complainants, having no evidentiary value as the said Complainants were not subjected to cross-examination. The Counsel for the Appellant argued that the Respondent while passing the Impugned Order did not take into account the statements of the employees of the Appellant, which are sufficient to prove the stance of the Appellant, who were trading on behalf of the Complainants and thus the Impugned Order suffers from material irregularity. Moreover, it was submitted by the Appellant that the Respondent vide Impugned Order concluded that the Appellant was unable to produce documentary proof of 'Know Your Customer (KYC)' activity and that the Complainant has invariably followed the brokers recommendations, however, the Impugned Order does not contain any evidence to this effect nor there is any material in any of the statements which would justify such a conclusion. The Counsel for the Appellant while summing up his arguments agreed with the contention of the Respondent that the term 'excessive' is a subjective determination as mentioned in the Impugned Order, however, argued that if the same is subjective or contextual then most important factor is opinion of the customer which in the instant case shows that none of the Complainants alleged 'excessive trading' by the Appellant rather the complaints simply state that trading resulted in loss, and thus no case of churning/excessive trading can be made out without finding of 'intent' which forms the basis of attracting clause 2(d) of the Schedule to the Rules and thus the Appellant can only be penalised if allegation and proof fall within strict ambit of clause 2(d) of the Schedule to the Rules and not otherwise. In support of the above submissions, the Appellant has relied upon various judgments of the superior courts as well as judgments from foreign jurisdictions.

5. Controverting the arguments of the Appellant, the Respondent in support of the Impugned Order reiterated the reasonings given therein and thus contended that the Impugned Order has been passed strictly in accordance with law.

6. The Appellate Bench (the "Bench") has heard the parties and perused the record. At the outset, it is imperative to first have a look at the nature of relationship between the Complainants and the Appellants as per account opening forms.

Complainant #	Name	Discretionary Trading Authority (DTA)	Mode of Instructions	Duration of Account
1	Mushtaq Ahmed Vohra	No (ID & Password provided to the Appellant)	Verbal	Oct'16-Mar'17
2	Sheikh Minhaj Ahmed	Yes	Written	Sep'16-Dec'16
3	Dawood Ahmed	Yes	Verbal	Nov'16-Dec'17
4	Hafiz Asim Akram	Yes	Verbal	Jul'16-Nov'17
5	Hafeez Ahmed	Yes	Verbal	Aug'16-Aug'16
6	Farman Ahmed Jafari	Yes	Verbal	Nov'16-Dec'16
7	Bashirullah	No (ID & Password provided to the Appellant)	Written	Aug'17-Jan'18

7. The above matrix shows that out of all the Complainants, five accorded DTA to the Appellant for trading in their accounts whereas two did not give DTA to the Appellant, however, the same did share their login IDs and passwords with the Appellant. It is also worthwhile to mention, that in general all the Complainants have alleged loss caused to them by the trading carried out by the traders/employees of the Appellant, however, there is no documentary evidence on record showing that the Complainants categorically instructed the Appellant regarding stoppage of trading/revocation of DTA/change of login ID and password, or any other written instruction to the effect which can be deemed as a clear instruction from the Complainants to the Appellant. On the contrary, there is also nothing produced by the Appellant in support of its defense which can suggest that why the Appellant (through its traders/employees) kept trading and kept incurring losses without seeking express instructions from the Complainants. Now the question arises that did the Appellant fulfill its duties diligently as a broker towards its customers. In order to decipher upon the said proposition, there are complaints and statements of the Complainants on the one hand and on the other there are statements of the

traders/employees of the Appellant who were given DTAs/login IDs and passwords by the Complainants. The contention of the Appellant that the statements of the Complainants (which in the case of Complainant No.5 went unrebutted) have no evidentiary value merely because of the reason that the same were not subjected to cross-examination is not tenable and misconstrued as cross-examination of witnesses is not mandatory in show-cause notice proceedings. Moreover, the said contention of the Appellant appears to be self-contradictory in the context of the statements of the traders/employees of the Appellant who were also not subject to cross-examination and yet mere statements of the same are termed by the Appellant as ones carrying evidentiary value to support the stance of the Appellant.

8. Moreover, it is apparent from the record that in case of the Complainants who did not give DTA to the Appellant, the latter kept trading without obtaining the DTA, or to say the least, written instructions thereof, *inter alia* resulting in losses suffered by the said Complainant Nos. 1 and 7, which comprises of approximately two-thirds of the total loss suffered by all the Complainants and commissions of the Appellant. Even in the case of the Complainants who gave the DTA to the Appellant, the Appellant failed to establish as to what mechanism was adopted to obtain their verbal instructions, as it has been alleged by the Complainants that despite repeated attempts, they were unable to establish contact with the traders/employees of the Appellant and, hence, incurred huge losses. Obtaining a DTA places a higher fiduciary responsibility on a broker, and sending emails and text message notifications pertaining to trading activity does not absolve the broker from his duties, particularly where nothing is available on record to show any effort/action by the Appellant, despite losses incurred by the Complainants. Furthermore, it is also imperative to note that the Commission, in exercise of powers conferred under the Rules, issued directions (along with approved template of a DTA both in English and Urdu languages, to be executed on a non-judicial stamp paper) dated January 23, 2017 and April 28, 2017 *inter alia* to all the brokers of PMEX, with respect to DTAs wherein *inter alia* it was mentioned that a loss threshold of 25% of the investment amount shall trigger revocation of the DTA and the discretionary mandate shall continue only upon obtaining a fresh DTA. However, as aforementioned directions is not the subject matter of the SCN or the Impugned Order, nor the same have been discussed during the hearing in the instant Appeal, therefore, no findings in that respect are rendered vide instant Order.

9. The contention of the Appellant that section 57(d) of the Act does not require the Appellant to seek instructions from the customer in writing, is not tenable as the said provision also does not specify any other mode, and thus must be read in the context of overall scheme of law and the functions entrusted to the Commission where investor protection is of primary importance. Needless to mention here that the penalty imposed on the Appellant vide Impugned Order is *inter alia* on account of contravention of clauses (a), (b), (c), (f) and (i) of section 57 of the Act and not under clause (d*)* of the *ibid* provision, however, it can be argued that excessive trading has a subjective connotation but the said argument could have carried weight had there been recording of circumstances and investment objectives of the customer by the Appellant as envisaged under section 57(d) of the Act.

10. The Appellant's contention that clauses 1(a) and (b) of the Schedule to the Rules are not attracted is misconstrued as both the said provisions are part of the code of conduct for brokers under the Rules and the same are attracted in the instant case where the subject matter involves determination of fairness, due skill and care employed by the Appellant towards the Complainants as they were customers of the Appellant, in light of the underlying contracts i.e. the account opening forms, and not customers of PMEX, where trading is carried out and funds are kept to ensure investor protection. As far as clause 2(d) of the Schedule to the Rules is concerned, this Bench has observed that though account opening forms, DTAs and other documents containing risk disclosures are obtained by the Appellant, however, to ascertain the investment objective and risk tolerance, which varies from person to person, no evidence has been placed on record by the Appellant (especially when it is being acknowledged that it is a high-risk market) to show investment objectives of the Complainants in support of its contention that no case of excessive trading is made out.

11. In the instant case, the Appellant, failed to organize and control internal affairs in a responsible manner, employ fairness, due skill and care towards its customers i.e. the Complainants. There can be no justification for obtaining the login IDs and passwords of the clients i.e. Complainant Nos. 1 and 7, in absence of DTAs as the Appellant was required to comply with the relevant provisions of the standards of conduct as envisaged under section 57 of the Act read with Schedule to the Rules. Moreover, obtaining of DTAs from the customers does not absolve a regulated person i.e. the Appellant from

fulfilling the statutory requirements and maintaining the conduct at all times, as prescribed under the law. On the other hand, the primary document determining the nature of relationship between the Appellant and the Complainants i.e. account opening forms, includes disclosures in Urdu language as well and the same have also been signed by all the Complainants. The DTAs given by the Complainants except the two, have not been disputed by the Complainants during the SCN proceedings and apart from their statements alleging losses, no other documentary proof regarding any instruction, for instance correspondence with the Appellant, has been provided by the Complainants in support of their claims against the Appellant.

12. In view of the above, the Impugned Order is hereby modified to the extent that the penalty imposed on the Appellant vide Impugned Order is hereby reduced to Rs. 3,500,000/-, and the instant Appeal is **disposed of** on above terms with no order as to costs.

(Akif Saeed)
Chairman/Commissioner

(Abdul Rehman Warraich)
Commissioner

Announced on: 05 SEP 2023