



BEFORE APPELLATE BENCH NO. I

In the matter of

Appeal No. 42 of 2005

DJM Securities (Pvt) Limited
Suit No. 203, 2nd Floor
Business & Finance Centre
I.I Chundrigar Road,
KarachiAppellant

Versus

Joint Director (Securities Market Division) SEC.....Respondent

Date of Impugned Order 23 August 2005

Date of Hearing 6 April 2006

Present:

Mr. Dawood Jan Muhammad for the Appellant

Mr. Aly Osman, Joint Director (SM) for the Respondent



ORDER

1. This order will dispose of appeal No. 42 of 2005 filed under section 33 of the Securities and Exchange Commission of Pakistan Act, 1997 by DJM Securities (Pvt) Limited, against the order dated 23-08-2005 ('Impugned Order') passed by Joint Director (Securities Market Division).

2. The brief facts of the case as stated in the Impugned Order are that between 01-03-2005 and 21-03-2005, DJM Securities (Pvt) Limited ("Appellant") carried out 12 trades involving purchase and sale of 169,400 shares of different companies through Karachi Automated Trading System (KATS) on behalf of 3 of its clients. The said purchase and sale trades cancelled each other out with the effect that there was no change in the beneficial ownership of the shares.

3. Consequently a show cause notice dated 28-07-2005 was issued to the Appellant by the Commission asking why action may not be taken against it under section 17 of the Securities & Exchange Ordinance, 1969 ("Ordinance") and the Brokers & Agents Registration Rules, 2001 ("Rules"). The Appellant submitted a written reply and also appeared before the Joint Director (SM) to plead a defence. However, the Joint Director rejected the arguments presented on behalf of the Appellant and found that the Appellant has acted contrary to the provisions of the Code of Conduct prescribed in the Rules in violation of Rule 8(iv). The Joint Director therefore imposed a penalty of Rs.25,000/- and directed the Appellant to abstain from buying and selling of shares in manner that does not result in change in beneficial ownership of shares.

4. Not being satisfied with the Impugned Order, the Appellant filed this appeal before us which was heard on 6-04-2006. The Appellant's chief executive officer Mr.



Dawood Jan Muhammad gave details of the trades executed on behalf of the three clients. He stated that one transaction of 500 shares was an internal transfer within one client account, i.e. from the sub-account of his mother to the Appellant's sub-account. Due to an earlier clerical error, such transfer had to be made to balance out the books. He stated that this particular trade was only 1 out of 5086 trades made on the same day from the Appellant's brokerage house.

5. He further informed us that the next 8 trades were made for a client who is a registered broker of the Islamabad Stock Exchange, namely Col. Retd Muhammad Ahmed Nadeem ("ISE Broker"). The ISE Broker had several clients of his own and he was dealing through his one client account with the Appellant for all his clients. So, although all the activity was showing in one client account, there were however several different clients buying and selling shares from that account. He stated that since Karachi Automated Trading System (KATS) is programmed to first match the buy and sell orders emanating from the same brokerage house, a false impression is created that the same person has bought back its own sell order. However, as stated aforesaid there are different persons dealing through one account and so there is a definite change of beneficial ownership.

6. Explaining the next set of 3 trades done for its client having code 101, Mr. Dawood Jan Muhammad informed us that the said client had placed several sell orders of PSO shares at various prices. He stated that the PSO share soon became a prized possession and the client instructed the Appellant to cancel one sell order of 100,000 shares of PSO. However, despite its best efforts, the Appellant was unable to cancel the order due to a malfunction in the KATS system caused by high number of traders operating through it. The Appellant therefore did not have choice but to place a buy order of the same number of PSO shares which met with the sell order placed earlier, and therefore these cancelled each other out. He argued that the malfunction was



beyond the Appellant's control and therefore it was not at fault. He contended that the Appellant was required under the law, as well as same Code of Conduct to diligently execute the orders placed by its clients. Additionally, the Appellant never intended to manipulate the market, nor could it have done so with such small volume of trades. He further contended that section 17 of the Ordinance deals with fraud, deceit and manipulation and none of the trades executed by the Appellant amounted to any of the above. He stated that the Joint Director had wrongly concluded in Para 19 of the Impugned Order that the Appellant had "*indulged in manipulative, fraudulent and deceptive practices*". He prayed that the appeal may be accepted and the Impugned Order be set aside.

7. Mr. Aly Osman appearing for himself contended that the Appellant has not been penalized for violation of section 17 of the Ordinance but for failure to maintain high standard of integrity, due skill and care in the conduct of its business, which is required under the Code of Conduct. He stated that a violation of law could not be condoned because it was done on a small scale. He argued that brokers are required to know their clients under the law and the Appellant's admittance that ISE Broker was further dealing on behalf of its clients through his account with the Appellant is a violation of that requirement. He insisted that the Appellant should have asked the ISE Broker to open further accounts for its clients. He stated that allowing the ISE Broker to deal on behalf of different clients through one account, meant that there would not be proper audit trail and any dispute between the clients and the broker would be nearly impossible to resolve. He stated that proper documentation, as required under different rules and regulations was in the interest of the investors and the brokers. He pointed out that at least in the case of the Appellant's client code 101, the Appellant has accepted that instead of canceling the sell order, it entered a new buy order which canceled the earlier order thus resulting in no change in beneficial ownership of shares. He prayed that the appeal be rejected and the Impugned Order be upheld.



8. We have heard both the parties. Mr. Dawood Jan Muhammad has been quite forthcoming in explaining the facts surrounding the trades in question. The Department has contended that the Appellant has been penalized for failure to maintain high standard of integrity, due skill and care in the conduct of its business. However, based on the facts stated above there is no reason to believe that there was a lack of integrity on part of the Appellant while executing the trades, or that it acted in bad faith. Besides, the volume of trades in question is so insignificant that any intended manipulation could not have materialized. In any case, the Appellant has not been penalized for market manipulation. However, the finding given by the Joint Director that the Appellant has indulged in manipulative, fraudulent and deceptive practices is contrary to the conclusion arrived at in the Impugned Order. If the Appellant had indeed indulged in manipulative, fraudulent and deceptive practices then it should have been proceeded against under section 17 of the Ordinance rather than for violation of the Code of Conduct.

9. We do agree that the Appellant has not acted skillfully while trading on behalf of its client. However, as stated above the surrounding circumstances show that there was no lack of integrity on part of the Appellant. Also since the volume of these trades is not significant we are inclined to take a lenient view. Consequently, the fine of Rs.25,000/- imposed upon the Appellant is set aside. The Appellant is however directed to be cautious in future and take necessary measures to abide by the standards set forth for responsible trading.

(SALMAN ALI SHAIKH)
Commissioner

(RASHID I. MALIK)
Commissioner

Announced in Islamabad on 30 June 2006