

SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
Securities Market Division

Before the Joint Director (Securities Market Division)

**In the matter of Show Cause Notice dated 28.07.2005
issued to D.J.M. Securities (Pvt.) Ltd.**

Date of Hearing

13. 08. 2005

Present at the Hearing:

Representing DJM Securities (Pvt.) Ltd.

Mr. Dawood Jan Muhammad C.E.O. DJM Securities (Pvt.) Ltd.

Mr. Mahfooz Abbasi, Manager Islamabad office, DJM Securities (Pvt.) Ltd.

ORDER

1. The case arises out of a Show Cause Notice No. SMD/SE/2(126)/2005 issued on 28.07.2005 by the Securities and Exchange Commission of Pakistan (the "Commission") to DJM Securities (Pvt.) Ltd. (the "Respondent").
2. Brief facts of this case are that between 1/03/2005 and 21/03/2005, the Respondent carried out 12 trades involving 169,400 shares, in the aggregate, of Pakistan State Oil Limited ("PSO"), Oil & Gas Development Company ("OGDC"), Pakistan Oil Field Limited ("POL") Pakistan Telecommunications Company Limited ("PTCL") and Pakistan Petroleum Limited (PPL), through the Karachi Automated Trading System ("KATS") on behalf of three of his clients.

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3. In the course of these trades, the Respondent purchased and sold 100,000 shares of PSO, 52,900 shares of OGDC, 11,000 shares of POL, 5000 shares of PTCL, and 500 shares of PPL. Consequently, the trades cancelled each other out and there was no change in the beneficial ownership of the shares.
4. The trading activity carried out by the Respondent interfered with the fair and smooth functioning of the market by creating a false and misleading appearance of trading activity in the scrips mentioned hereinabove which worked to the detriment of the interests of the investors.
5. The Commission obtained the following KATS data from the Karachi Stock Exchange regarding the 12 transactions executed by the Respondent in the month of March alone, which revealed as follows:

DATE	CLIENT CODE	SCRIP	NO. OF SHARES	PURCHASE AND SALE PRICE	TIME OF TRADE
15/03/2005	6	PTC-REG	500	87.9	1347570009
1/03/2005	12	PTC-REG	1000	68.75	1412390068
2/03/2005	12	PPL-REG	500	257.5	1337010011
10/03/2005	12	POL-REG	10000	350	1414280034
11/03/2005	12	PTC-REG	1000	88	1434530019
14/03/2005	12	PTC-REG	2500	88.1	1403480027
15/03/2005	12	POL-REG	1000	346	1221140037
16/03/2005	12	OGDC-REG	13100	195.5	1028460033
21/03/2005	12	OGDC-REG	39800	161	945040015
1/03/2005	101	PSO-REG	5500	436	1119110050
1/03/2005	101	PSO-REG	44500	436	1119080004
1/03/2005	101	PSO-REG	50000	436	1119050048

6. After examining the aforesaid data, the Commission issued a Show Cause Notice to the Respondent on 28/07/2005, detailing the aforesaid trade information and asking the Respondent to show cause as to why action should not be initiated against the Respondent under section 17 of the Securities and Exchange Ordinance 1969 (the

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“Ordinance”) and the Brokers and Agents Registration Rules, 2001 (the “Rules”). The Commission also provided a copy of the summary of KATS data so that the Respondent would have adequate opportunity to explain the same. The Respondent was asked to submit a written reply to the Show Cause Notice and the hearing was fixed in Islamabad for 11/08/2005 which was subsequently postponed to 13/08/2005, at the telephonic request of the Respondent. The Respondent was unable to appear before the Commission at the fixed time; he was late by about two and a half hours and did not provide the Commission with any prior notice of delay.

7. The Respondent submitted a written reply to the Show Cause Notice dated 02.08.2005. The Commission requested the Respondent for additional information. He provided the same by his letter dated 08.03.2005. The Respondent also appeared before the Commission in person on 13.08.2005, before the Commission. The points raised by the Respondent in his written reply dated 02.08.2005 were:

- (i) “500 shares PTCL regular (trade date 15-03-2005)
One of the brokers of DJM Securities (Pvt.) Ltd. by mistake placed the order of buy instead of sale and afterwards he cancelled out the trade by buying the equivalent number of shares at the same rate. Manipulation of stock is not base on 500 shares.”
- (ii) “Shares traded on account no. 12 by the name of Col. Rt. Muhammad Ahmed Nadeem
Mr. Col. Rt. Muhammad Ahmed Nadeem is a member of Islamabad Stock Exchange he trades on behalf of his clients through D.J.M. Securities (Pvt.) Ltd. and he requires that all the trades be executed through KATS even if it is a buy and sale order in the same scrip at the same time and same rate. So that

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he may be able to satisfy his clients that all the trades are done through KATS in case they ask for the KATS confirmation.”

(iii) “Shares traded on account no. 101 by the name of Mr. Akhtar
Mr. Akhtar placed two orders of PSO 50,000 shares each on the 1st March, 2005 which he tried to cancel afterwards but due to heavy volumes traded in the market and some technical problems in our trading system we were unable to cancel the order as per clients instruction and decided to cancel the order by making a contra entry through KATS to keep unchanged the beneficial ownership of the securities involved.”

(iv) “We would state thus that none of the transactions mentioned in your letter were executed with unfair or fraudulent intent on our or our clients behalf. Moreover keeping in view the volumes and volatility witnessed in the month of March, it is hard to see how the changes levied against DJM Securities (Pvt) Limited should be termed as justified.”

8. In the hearing held on 13/08/2005, the Respondent stated that he is dealing in a large volume of securities and has some high net worth clients who place huge volumes of orders during the day and that their positions may match un-intentionally. Further the total numbers of shares in which transactions have been made, as stated in the Show Cause Notice, is just 169,400. This is only a small proportion of the total trades made in the said period of time, and therefore these trades cannot manipulate the market.
9. The Respondent requested that the Show Cause Notice be withdrawn for the reason that the Respondent had neither violated any provision of the Ordinance, including section 17, nor any of the Rules. The trades were not executed to mislead or

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manipulate the market price of the shares and even other wise constitute such a small part of the total trades executed on the dates in question that these trades could not have manipulated the market.

10. I have read and heard the arguments of the Respondent at length and after carefully examining the record, I find that the Commission must address the following questions :
- (a) Did the acts or omissions as alleged against the Respondent breach the Rules and do such acts or omissions warrant action against the Respondent?
 - (b) If the Respondent is found in breach of the Rules, what should be the penalty imposed on the Respondent ?
11. I have examined all the relevant issues pertaining to this case in depth as follows:
12. In the course of the Respondent's written as well as oral response to the Show Cause Notice, the Respondent has admitted that he carried out all 12 trades detailed in the Show Cause Notice. Even if the Respondent's claim with regard to the 500 shares of PTCL that his KATS operators made a mistake while processing the transaction is accepted; it does not mitigate the responsibility of the Respondent. The Respondent should have had adequate procedures in place to ensure KATS operators work properly. The current practice shows that KATS operators are insufficiently trained and are inexperienced for their job. I am not aware whether or not any action was taken against the KATS operators who had made the said mistake. The Respondent, by ignoring the negligent and erroneous practices of the KATS operator, who is an employee of the Respondent has in fact encouraged his employee to conduct his business in a manner contrary to the Rules and has failed to exercise due skill, care and diligence in the conduct of business.

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13. Further the Respondent asserts that the alleged trades took place inadvertently due to the high volume of businesses managed by his brokerage. This is clearly tantamount to negligence on part of the Respondent. It is also a violation of the brokers' code of conduct under which a broker is required to have in place adequate arrangement for proper conduct of his business, irrespective of the volume of such business. According to the broker's code of conduct laid down in the Third Schedule of the Rules, the Respondent is obliged to have adequately trained staff and arrangements to render fair, prompt and competent services to his clients. Engaging in and allowing trading activity in the market merely for the purpose of canceling an order previously entered in KATS created a false impression of trading activity in that particular scrip, and is not only contrary to high standards of integrity but is also improper, dishonorable, disgraceful and against the law.
14. Col. (R) Muhammad Nadeem being a member of Islamabad Stock Exchange, operated account no. 12 with the Respondent. Col. Nadeem's representative argued during his oral submission before the Commission that the trades were conducted on behalf of various clients as follows:

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DATE	SCRIP	BUYER'S NAME	PURCHASED QUANTITY	SELLER'S NAME	SOLD QUANTITY	MATCHED QUANTITY	STRIKE PRICE (Rs.)
01/03/2005	PTCL	Shahid Pervaiz	1000	Syed Ilyas Rizvi	25,000	1,000	68.75
02/03/2005	PPL	Mumtaz Ali Malik Ghulam Pervaiz	1000 1000	Muhammad Qasim Janjua	500	500	257.50
10/03/2005	POL	Mumtaz Ali Malik Saif Ur Rehman	15,700 200	Saif Ur Rehman Saqib Malik Rizwan Ahmed	500 5,000 5,000	10,000	350.00
11/03/2005	PTCL	Saqib Malik Rizwan Ahmed Malik Rashid	16,000 25,000 1000	Malik Rashid Irfan	1,000	1,000	88.00
14/03/2005	PTCL	Syed Ilyas Rizvi	100,000	Mumtaz Ali Malik	25,000	2,500	88.10
15/03/2005	POL	Syed Qaiser Zameer Shah	1,000	Sikander Hayat Bakth	6,000	1,000	346.00
16/03/2005	OGDC	Saqib Malik	13,100	Mumtaz Ali Malik	200,000	13,100	195.50
21/03/2005	OGDC	Abid Malik	50,000	Irfan Khurram Qureshi Farasat Ali Ch. Ashiq Ali	1,000 1,500 50,000	39,800	161.00

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15. The practice of brokers operating through other brokers whether of the same exchange or of other exchange(s) is an unhealthy practice detrimental to the interest of investors. I am not aware whether the investors investing through Col. Nadeem are aware of the fact that their securities are being traded through the Respondent. The investors who have invested through Col. Nadeem do not have any contract with the Respondent and in case any dispute arises, they stand at a weak legal position, as their transactions are being carried out and recorded in Col. Nadeem's name. This practice of broker appointing a sub-broker not only hampers the functioning of stock exchange and the Commission while undertaking monitoring and surveillance of trading activity but also compromises on transparency of the market. The aforesaid practice is also contrary to international best practices undertaken by brokerage houses. The Respondent has thus acted against the interest of the investors and has failed to act with due skill, care and diligence in conduct of his business by allowing his client, Col. Muhammad Ahmad Nadeem, to act on behalf of other clients under one account.
16. The relevant KATS data independently obtained by the Commission from the Karachi Stock Exchange, (which was made available to the Respondent and has not been disputed by it) establishes that the aforesaid trades had the effect of canceling each other out and did not result in any change in the beneficial ownership of these shares. Such trading activity interferes with the fair and smooth functioning of the market and undermines market integrity by creating an impression of shares being traded in the market when in fact the trades have been cancelled out by the same person. The interests of the investor are compromised due to the fact that they receive a false impression of trading in the market which is more than likely to influence the decision of any reasonable investor to invest or trade in the market.

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17. For the three transactions dealing in shares of PSO, made through account No. 101, the Respondent placed a new order, at the same price as the previous order that resulted in reversing the previous order. The practice of entering a reversal order in KATS instead of canceling the wrong order is an undesirable practice that creates the appearance of false trading and is therefore illegal. By failing to take any corrective measures the Respondent has allowed such activities to continue unabated.

18. The Respondent could not justify or explain the technical problems cited in his reply as the reason for entering a contra entry. In failing to ensure that the order was cancelled in a timely manner and instead revising the previous order entered in KATS by the KATS operators, the Respondent has acted improperly and negligently in breach of his duty to act with due skill, care and diligence in the conduct of his business. Consequently, the Respondent has failed in his duty to maintain high standards of integrity, promptitude and fairness in the conduct of his business.

19. It is clear from the facts detailed above that the Respondent has failed to follow the requirements of the Code of Conduct prescribed for brokers. By executing and permitting the execution of trades which cancelled each other out and did not result in the transfer of beneficial ownership the Respondent has indulged in acts which have interfered with the fair and smooth functioning of the market to the detriment of the interests of investors. The Respondent has failed to maintain high standards of integrity, due skill and care in the conduct of his business. He has indulged in manipulative, fraudulent and deceptive practices, has engaged in malpractices and has not complied with statutory requirements, and has therefore acted in violation of Rule 8(iv) of the Rules.

(b) *What should the order be?*

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20. The violation of the Rules is a serious matter. In exercise of the powers under Rule 8(b) of the Rules, conferred by S.R.O.847(I)/2005 dated 19/08/2005, I hereby impose on the Respondent, a penalty of Rs. 25,000/- (Rupees Twenty Five Thousand only), which should be deposited with the Commission no later than thirty (30) days from the date of this Order.

21. In addition to the aforesaid, I hereby direct the Respondent to abstain from buying and selling of shares in a manner that does not result in a change in the beneficial ownership of the shares, failing which action will be taken against him in accordance with law.

22. This Order is issued without prejudice to any other action that the Commission may initiate against the Respondent in accordance with the law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.

Aly Osman
Joint Director (SM)

Date of the Order: 23/08/2005.