



Before the Joint Director (Securities Market Division)

**In the matter of Show Cause Notice dated 15.07.2005
issued to Mr. Nadeem Abdul Ghaffar**

Date of Hearing

25th July 2005

Present at the Hearing:

Representing Mr. Nadeem Abdul Ghaffar:

Mr. Mohammad Hanif s/o Ahmed Ashraf

Assisting the Joint Director (SM):

Mr. Ghulam Mustafa

Mr. Muhammad Atif Hameed

ORDER

1. The present matter arises out of a Show Cause Notice bearing No. SMD/SCN/3/2005 dated 15.07.2005 issued by the Securities and Exchange Commission of Pakistan (“the Commission”) to Mr. Nadeem Abdul Ghaffar (“the Respondent”).
2. Brief facts of this case are that between 8th March 2005 and 31st March, 2005, the Respondent carried out 35 trades involving total 135,000 shares of Oil & Gas Development Company (“OGDC”), Pakistan Oil Field Limited (“POL”), Pakistan State Oil Limited (“PSO”) and Pakistan Telecommunications Company Limited (“PTCL”) through the Karachi Automated Trading System (“KATS”) on behalf of two of his clients.
3. In the course of these trades, the Respondent purchased and sold, on behalf of the same client, 19,100 shares of OGDC, 23,300 shares of POL, 46,300 shares of PSO and 46,500 shares of PTCL. Each of these trades cancelled each other out with the effect that there was no change in the beneficial ownership of the shares.



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4. The trading activity as aforesaid 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 and was to the detriment of the interests of the investors.
5. The Commission obtained the KATS data from the Karachi Stock Exchange (Gtee.) Ltd. for the relevant period, which revealed that during the month of March 2005 the Respondent had executed the following trades which cancelled each other out and did not result in change of beneficial ownership:

DATE	CLIENT CODE	NAME OF SHARE	NUMBER OF SHARES	PERCHASE AND SALE RATE	TIME OF EXECUTION
10/03/2005	370	OGDC-REG	9400	166.3	1139400018
10/03/2005	370	OGDC-REG	600	166.3	1139480030
17/03/2005	370	OGDC-REG	6600	178.75	1023150005
31/03/2005	370	OGDC-REG	2500	118.75	1128190022
09/03/2005	370	POL-REG	1800	357.4	1049410021
11/03/2005	370	POL-REG	5100	347.5	1017360056
11/03/2005	370	POL-REG	100	348	1017360057
18/03/2005	370	POL-REG	1100	326	1104090049
29/03/2005	L01	POL-REG	2000	228.75	1045260009
29/03/2005	370	POL-REG	6000	238	1238590025
30/03/2005	370	POL-REG	200	260.9	1008020033
31/03/2005	370	POL-REG	4100	256.25	1201590006
31/03/2005	370	POL-REG	400	256.25	1202030037
31/03/2005	370	POL-REG	2500	256.25	1202270053
08/03/2005	370	PSO-REG	100	443.7	1004230088
24/03/2005	370	PSO-REG	400	407	1050360002
24/03/2005	370	PSO-REG	5000	404.25	1120050006
24/03/2005	370	PSO-REG	100	404.2	1122520006
28/03/2005	370	PSO-REG	2000	365.5	1147030016
29/03/2005	370	PSO-REG	600	348	959140017
29/03/2005	370	PSO-REG	9400	349.25	1121180006
29/03/2005	370	PSO-REG	500	349.05	1121560006
29/03/2005	370	PSO-REG	4500	349.05	1121580010
31/03/2005	370	PSO-REG	500	439.5	1017370038
31/03/2005	370	PSO-REG	500	439.9	1021010027
31/03/2005	370	PSO-REG	5000	441.25	1207520014
31/03/2005	370	PSO-REG	500	440	1209050002
31/03/2005	370	PSO-REG	4500	440	1209110036
31/03/2005	370	PSO-REG	100	400	1311040015
31/03/2005	370	PSO-REG	500	399.25	1313200015
31/03/2005	370	PSO-REG	10000	399.5	1315330009
31/03/2005	370	PSO-REG	1600	400.15	1316300010
31/03/2005	370	PSO-REG	500	399.1	1317250005
29/03/2005	370	PTC-REG	6500	61.75	1134140019
29/03/2005	370	PTC-REG	40000	61.9	1135130017

6. Accordingly, the Commission issued a Show Cause Notice to the Respondent on 15 July 2005, detailing the aforesaid facts and asking him to show cause as to why action should



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not be initiated against him under section 17 of the Securities and Exchange Ordinance 1969 (“the Ordinance”) and the Brokers and Agents Registration Rules, 2001 (“the Rules”). A copy of the summary of the KATS data was also sent to him in order to allow him an opportunity of answering the same. The Respondent was asked to submit a written reply to the Show Cause Notice and the first hearing was fixed in Islamabad for 25th July 2005.

7. The Respondent submitted a written reply to the Show Cause Notice on 20.07.2005 and also appeared in person through his authorized representative Mr. Mohammad Hanif son of Ahmed Ashraf. The main points raised by the Respondent in his written reply and in the course of hearing were as follows:
 - (a) He admitted to having executed all 35 transactions detailed in the Show Cause Notice and stated that one out of these 35 transactions had been executed on behalf of a client bearing Code no. L01 (“Client L01”) while the remaining 34 transactions were executed on behalf of a client bearing Code no. 370 (“Client 370”).
 - (b) In respect of the trade executed on behalf of Client L01, he stated that it had been erroneously recorded due to the error of the KATS operator. The shares were purchased by Client No. 348 and were sold by Client L01. However the KATS operator erroneously entered the code for Client L01 while recording the bid for Client 348. The error was detected by the back office of the Respondent at the end of the day and was duly rectified. The shares were also transferred to Client 348 from Client L01, and there was therefore a change in their beneficial ownership. He also produced the statements of both Client L01 and Client 348 to substantiate his statements.
 - (c) In respect of the trades executed on behalf of Client 370 he stated that Client 370 was an active “day trader” in both the ready and the futures market. The activity of day trading requires very fast reflexes on the part of investors and KATS operators there are bound to be some human errors. The trades in question may have been a result of error on the part of the KATS operator while punching the bids and offers or the trades may have occurred due to overlapping of limit orders given by the Client 370.



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8. On the basis of the aforesaid the Respondent requested that the Show Cause Notice be withdrawn for the reason that he had not violated any of the provisions of the Ordinance, including section 17 or of the Rules. The trades were not executed to mislead or manipulate the market price of the shares and in any event constitute a very small part of the total trades executed on those dates and therefore were not capable of manipulating the market.
9. I have heard the views and contentions of the Respondent at length after carefully examining the record, I find that the following issues arise out of this matter:
 - (a) Whether the acts of commission and omission as alleged against the Respondent constitute a breach of Rules? If so, up to what extent?
 - (b) What should the order be?

Each of these issues has been examined seriatim:

- (a) Whether the acts of commission and omission as alleged against the Respondent constitutes a breach of Rules? If so, up to what extent?*
10. In the course of its written as well as oral contentions, the Respondent has admitted that he carried out all 35 trades detailed in the Show Cause Notice. In respect of one of these trades, the Respondent has taken the plea of error on the part of the KATS operator which was subsequently corrected by the back office staff and in respect of the remaining 34 trades he has pleaded human error on the part of the KATS operator due to the exigencies of day trading.
11. It is evident from the relevant KATS data obtained from the Karachi Stock Exchange, (which has not been disputed by the Respondent) that all but one of the aforesaid trades had the effect of canceling each other out and did not result in the change in beneficial ownership of these shares. Such trading activity interferes with the fair and smooth functioning of the market due to the fact that it gives the impression of shares being traded in the market when in fact throughout the trades the shares remain in the possession of the same person. The interests of the investor suffer in turn due to the fact that they receive a false impression of trading in the market which influences their decision to invest or trade in the market.



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12. The Respondent has taken the plea of “human error” on the part of the KATS operator to explain the canceling out effect of the aforesaid 35 transactions. During the course of the hearing the Respondent informed us that the relevant KATS operator is the employee of the Respondent. He further informed us that all KATS operators are highly skilled and experienced personnel.
13. The plea of “human error” does not hold weight in view of the fact that the KATS operators are highly skilled personnel whose job it is to record such transactions within a very short time period. Even otherwise the same error cannot be repeated 34 times and that too with the same person who is also the real brother of Mr. Hanif who was representing the Respondent in the hearing before us.
14. The fact that the same error has been repeated by the KATS operator in respect of 34 transactions goes to show that the Respondent, who as the employer of the KATS operator, is responsible for his errors and omissions, has failed to exercise due skill care and diligence in the conduct of his business. Further, there is no evidence that the Respondent has taken any action against the KATS operator for his obvious omissions which in itself is a failure on the part of the Respondent to exercise due care and skill.
15. I do not however find the Respondent liable under the Rules, for the single transaction executed by him on behalf of Client L01, in view of the documentary evidence provided by the Respondent which confirms that the transaction did in fact result in a change in beneficial ownership.
16. In engaging in and allowing trading activity in the market merely for the purpose of creating a false impression of trading activity in particular scrips, is not only contrary to high standards of integrity but is also improper, dishonorable and disgraceful and contrary to law.
17. It is evident from the facts detailed above that the Respondent has failed to follow the requirements of the code of conduct prescribed for brokers in that by executing and permitting to be executed trades which cancelled each other out and did not result in the transfer of beneficial ownership, he has indulged in acts which have interfered with the fair and smooth functioning of the market to the detriment of the interests of investors.
18. In failing to ensure that a proper system was in place to avoid repeated “error” on the part of KATS operators, and in failing to take action against the KATS operator in respect of



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his omission, the Respondent has failed to act with due skill, care and diligence in his omissions, the Respondent has failed 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 all his business and has in fact indulged in dishonorable, disgraceful and improper conduct on the stock exchange, and has therefore acted gross and blatant in violation of Rule 8(iv) read with Rule 12 of the Rules.

(b) *What should the order be?*

19. The Respondent has acted contrary to at least four provisions of the Code of Conduct prescribed for the broker in the Rules in violation of Rule 8(iv) read with Rule 12 of the Rules. The violation of the Rules is a serious matter which entitles the Commission to suspend the Respondent's license, however the Commission has elected not to exercise this power at present. Therefore in exercise of the powers under Rule 8(b) of the Rules, I hereby impose on the Respondent, the penalty of Rs.50,000.00 (Rupees Fifty thousand only). This sum of Rs. 50,000.00 (Rupees Fifty thousand only) should be deposited with the Commission, no later than thirty (30) days from the date of this Order.
20. In addition to the aforesaid, I hereby direct the Respondent to abstain from buying and selling of shares in a manner that these do not result in a change in the beneficial ownership of the shares failing which action will be taken against him in accordance with law.
21. This Order is issued without prejudice to any other action that the Commission may initiate against the Respondent in accordance with law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.

Ikram Ul Haque
Joint Director (SM)

Date of Order: 17th August, 2005