

SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
NIC Building, Jinnah Avenue, Blue Area, Islamabad.

BEFORE THE DIRECTOR (SECURITIES MARKET DIVISION)

**IN THE MATTER OF SHOW CAUSE NOTICE DATED 26/08/2005
ISSUED TO MR. ABA ALI HABIB, MEMBER-KSE**

Date of Hearing

13th September 2005

Present at the Hearing:

Representing Mr. Aba Ali Habib

Mr. Zahid Ali Habib, Chief Executive Officer

ORDER

1. The matter arises out of a Show Cause Notice dated 26/08/2005 (hereinafter referred to as "the Notice") issued by the Securities and Exchange Commission of Pakistan (hereinafter referred to as "the Commission") to Mr. Aba Ali Habib (hereinafter referred to as "the Respondent") Member-broker Karachi Stock Exchange (Guarantee) Limited (hereinafter referred to as "the KSE").
2. Brief facts of this case are that between 1st March 2005 and 22nd March, 2005, the Respondent carried out 23 trades of the shares involving total 76,500 shares of National Bank of Pakistan ("NBP"), Oil & Gas Development Company ("OGDC"), Pakistan Oil Field Limited ("POL"), Pakistan Petroleum Limited ("PPL") and Pakistan State Oil Limited ("PSO") through the Karachi Automated Trading System ("KATS") at KSE on behalf of his five clients.
3. In the course of these trades, the Respondent purchased and sold, on behalf of five clients, 59,100 shares of NBP, 900 shares of OGDC, 4,600 shares of POL, 100 shares of PPL and 11,800 shares of PSO. Each of these trades cancelled each other out with the effect that there was no change in the beneficial ownership of the shares.
4. This practice on the part of the Respondent interfered with the fair and smooth functioning of the market. It creates a false and misleading

appearance of trading activity in the scrips mentioned hereinabove and was, therefore, detrimental to the investors' interests.

5. The Commission obtained the KATS data from the KSE for the relevant period, which showed 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	No. of Shares	Purchase & Sale Rate	Time of Execution
1/03/2005	16	NBP-REG	13,500	139.95	1030270002
1/03/2005	16	NBP-REG	5,000	139.95	1030300035
1/03/2005	16	NBP-REG	1,000	139.95	1030380003
2/03/2005	16	NBP-REG	100	139.95	1018590124
2/03/2005	18	NBP-REG	5,000	139.05	1300370026
2/03/2005	16	NBP-REG	25,000	139.25	1359190036
9/03/2005	16	NBP-REG	4,500	153.20	1133310025
10/03/2005	16	NBP-REG	500	159.95	1038300045
17/03/2005	16	NBP-REG	4,500	153.50	1047060005
16/03/2005	18	OGDC-REG	900	183.30	1338220029
1/03/2005	12	POL-REG	2,500	330.60	1110460021
11/03/2005	372	POL-REG	600	346.85	1136090010
16/03/2005	18	POL-REG	1,500	338.00	1204010023
1/03/2005	S55	PPL-REG	100	252.65	946380111
18/03/2005	18	PSO-REG	500	458.50	1553070015
21/03/2005	18	PSO-REG	1,000	449.00	948570028
21/03/2005	18	PSO-REG	1,800	449.00	1146300015
21/03/2005	16	PSO-REG	1,500	438.50	1258360010
21/03/2005	16	PSO-REG	500	435.00	1347110010
22/03/2005	16	PSO-REG	500	432.00	1040390005
22/03/2005	16	PSO-REG	700	425.00	1111300009
22/03/2005	16	PSO-REG	1,000	425.75	1113480002
22/03/2005	16	PSO-REG	4,300	425.25	1122500015

6. In view of the aforesaid data, the Commission issued the Notice dated 26/08/2005 to the Respondent. In this Notice, the details of the aforesaid facts were provided and the Respondent was asked to show cause as to why action should not be initiated against him under the Brokers and Agents Registration Rules, 2001("the Rules"). A copy of the summary of the KATS data was also sent to the Respondent so that he would have the opportunity of answering the same. The Respondent was asked to submit a written reply to the Notice within seven days from the date of the Notice and hearing in the matter was fixed in Islamabad for 13/09/2005.
7. The Respondent submitted a written reply to the Show Cause Notice on 02/09/2005. On the date of hearing, Mr. Zahid Ali Habib, Chief Executive

Officer appeared on behalf the Respondent in person before me. The main points raised by the Respondent in its written reply and in the course of hearing were as follows:

- (a) The Respondent admitted to have executed all 23 trades detailed in the Notice dated 26/08/2005 and stated that out of the total transactions, 21 trades were executed under the "Traders Code" and not under the client code. The codes mentioned in the Annexure -A of the Notice dated 26/08/2005 are not client codes but these are traders code allocated to different traders at the Respondent's brokerage house. The fact is that these trades belong to different clients, purchased and sold by different traders for their respective clients. The rest of 2 transactions were executed by client codes at the KSE. The Respondent accepted that the above two trades were matched due to entering of the same clients codes (372 and S55) for buyers and sellers by KATS operators and rectified at the day end by the back office staff. The Respondent provided computer generated difference bills in respect of these two trades as proof of change in beneficial ownership of the shares.
- (b) The Respondent informed that the use of traders' codes in their house is temporary and after the trading hours these trades are posted in the back office to the clients' accounts on whose behalf these orders have been executed by the traders.
- (c) The Respondent informed that the Respondent has approximately 400 clients and there are 10 traders / KATS operators who are their employees. The Respondent told that traders / KATS operators are entrusted only with the work of receiving orders from clients and entering orders into KATS. Every trader / KATS operator has allocated clients to deal with. When the Respondent was asked to produce appointment letters of traders / KATS Operators, the Respondent stated that no appointment letter is issued to the employees including traders / KATS operators and they are required only to fill-in a standardized C.V. form of the house. The Respondent stated that humanly it is not possible to memorize the client codes of each client by the traders/KATS operators. Accordingly, the traders/KATS operator put their own codes in KATS to execute orders of their clients. However, in case of few clients they also put clients' codes as well.

- (d) The Respondent emphasized that the buyers and sellers of the trades were not the same; hence these trades cannot be termed as wash trades.
8. On the basis of the aforesaid the Respondent requested that the Notice dated 26/08/2005 be withdrawn. The Respondent stated that he has not violated any of the provisions of the Rules. He pointed out that in all the trades, buyers and sellers were different and beneficial ownership did take place and these cannot be construed to be wash trades.
9. I have heard the views and contentions, written and oral, of the Respondent at length and after carefully examining the facts of the case available on file, 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 the Rules? If so, up to what extent?
- (b) What should the order be?

Each of these issues has been examined seriatim:

10. In the course of written as well as oral contentions, the Respondent has admitted that the Respondent carried out all 23 trades detailed in the Notice dated 26/08/2005. In respect of two of these trades, the Respondent has taken the plea of error on the part of the KATS operator by entering same clients' codes for buyers and sellers in KATS which was subsequently corrected after trading hours by the back office staff. The Respondent during course of the hearing submitted difference bills in respect of all the trades as proof of his contentions that change in beneficial ownership had taken place. These were examined and found to be correct.
11. The Respondent confirmed in his contentions that he is in practice of using traders' codes instead of clients' code for different clients and not the clients' codes for clients while entering orders of his clients for execution in KATS. At the same time, the Respondent admitted that Respondent also uses clients' code for entering orders into the KATS. The admission by the Respondent that he is in practice of using traders code and clients code is not understandable and highly objectionable as he is following two practices at his brokerage house that is inconsistent practice and against the norms of the market as it

would be difficult to find out any trails of these trades. Additionally, by entering traders' code into KATS and at the day end transferring positions to the respective clients accounts, there exists a potential risk that the Respondent may change the trading positions of clients to cover any market abuse by himself or by the client such as blank sale as it is upon the discretion of the broker to allocate trades to whom he desires. Further, the Respondent's practice of entering traders code compromises transparency and the record does not reflect the true positions as trading is being carried out in the name of trader and movement of securities would take place in the name and account of the respective client.

12. The Respondent told during the hearing that there are 70 % active clients of the total 400 clients (approx.) of the Respondent. Having 10 KATS operators, average number for each KATS operator comes out to be 28 which is quite manageable so the Respondent plea for entering traders' codes on the pretext that it is difficult to memorize client codes by the KATS operator for each client does hold any weight as KATS operators are highly skilled personnel and their only job is to operate KATS and they are not entrusted with any other work. It is generally accepted that KATS operators are highly skilled and very well trained for the job as they have to enter orders on a daily basis and always within a very short time period. Therefore, the plea of the Respondent is rejected only on this ground. For the sake of argument and without conceding the viewpoint of the Respondent, if the KATS operators are not well trained that too is a shortcoming on the part of Respondent as under the code of conduct annexed to the Rules, it is required that broker should have adequately trained staff and arrangements to render fair, prompt and competent services to his clients. As an experienced broker and as being employer of the KATS operator it is the duty of the Respondent to ensure that adequate arrangements for proper conduct of his business are in place, to which he has failed.
13. It is the duty of the Respondent to exercise due care and skill while entering information into the KATS. By not entering the correct and required information in the client code field of the KATS, the Respondent has failed to carry out its responsibility to provide accurate information on the KATS.
14. From the preceding facts it is clear that the Respondent has failed to follow the requirements of the code of conduct prescribed in the Rules. Therefore, the Respondent failed to maintain high level of integrity, promptitude and

fairness in the conduct of its business and has in fact indulged in improper conduct on the stock exchange. The Respondent did not comply with the requirements according to the code of conduct of the Rules. Therefore the Respondent acted in violation of Rule 8(iv), read with Rule 12 of the Rules.

15. In view of what has been discussed above, I am of the considered view that the Respondent acted in violation of Rule 8(iv) read with Rule 12 of the Rules and therefore, in exercise of the powers under Rule 8(b) of the Rules, I hereby impose on the Respondent, a penalty of Rs. 25,000.00 (Twenty five thousand only) which should be deposited with the Commission, no later than 30 (thirty) days from the date of this Order.

16. Additionally, I hereby direct the Respondent to refrain from practices such as entering traders' code instead of clients' code as it makes it difficult to find the trails of these trades and other consequences discussed in the paras above. I am of the view that such practices should not be allowed as these create hurdles in the deducting market abuses, proper surveillance and smooth market functioning.

(Imtiaz Haider)
Director (SM)

Date of the Order: 15th September, 2005