

Securities and Exchange Commission of Pakistan

NIC Building, Jinnah Avenue, Islamabad
(Securities Market Division)

BEFORE THE COMMISSIONER (SECURITIES MARKET)

Present:

1. Mr. Muhammad Ashraf Hussain Adhi, Member, Lahore Stock Exchange
2. Mr. Aamir Zareef, Legal Advisor, Lahore Stock Exchange
3. Mr. Rehmat Ali Hasnie, Chief Operating Officer, Lahore Stock Exchange

To Assist the Commissioner (SM)

1. Syed Aamir Masood, Director (S-III)
2. Mr. Ikram-ul-Haq, Joint Director (Law)
3. Mr. Imtiaz Haider, Joint Director (SM)
4. Ms. Mahreen Raseed, Junior Executive (SM)

Date of Hearing:- 05-07-2002

ORDER

1. Mr. Muhammad Ashraf Hussain Adhi, Member Lahore Stock Exchange (LSE), hereinafter referred to as the "Member" sent a letter dated 07-06-2002 to the Securities and Exchange Commission of Pakistan (the "Commission") revealing that the Member was trading in securities for more than five months without being registered as a broker with the Commission under the Brokers and Agents Registration Rules, 2001 (the "Rules").

2. The Rules which were promulgated in the year 2001, made registration of brokers with the Commission mandatory and a pre requisite to conduct business in securities. A copy of the Rules was forwarded to the LSE by the Commission vide letter No.2(65)SE/2000 dated 13-06-2001 for compliance. The LSE was further directed vide the Commission's letter No. 2(33)/SE/2001 dated 12-12-2001 that any member who is not registered under the Rules by 31-12-2001 would not be allowed to deal in securities. The LSE was also directed to notify the same to all its members.

3. On receipt of the application for registration of the Member by the Commission on 10-06-2002 from the LSE, the Member was registered as a broker under the Rules on

14-06-2002. However, it came to the knowledge of the Commission that the Member was dealing in securities from 01-01-2002 to 13-06-2002 without being registered as a broker with the Commission under the Rules, which is a flagrant violation of Rule 3(1) of the Rules and Section 5A of the Securities and Exchange Ordinance, 1969 (the "Ordinance").

Rule 3(1) of the Rules reads:

" A member desirous of acting as a broker shall make an application to the Commission in Form A as set out in the First Schedule, for grant of certificate of registration through the stock exchange of which he is a member."

Section 5A of the Ordinance reads:

"No person shall act as broker or agent to deal in the business of effecting transactions in securities unless he is registered with the Commission in such manner, on payment of such fees and charges and on such conditions as may be prescribed."

4. The LSE negligently failed to take any notice of the violations of the Rules and the Ordinance for five months and 6 days consecutively.

5. Soon after, the Commission took cognizance of the matter and issued the following Show Cause Notice to the Member on 22-06-2002:

"Whereas in exercise of the powers conferred by clause (b) of section 43 of the Securities and Exchange Commission of Pakistan Act 1997 read with section 5A of the Securities and Exchange Ordinance, 1969, the Securities and Exchange Commission of Pakistan with the approval of the Federal Government of Pakistan made the Brokers and Agents Registration Rules 2001 ("the Rules") and notified the same vide S.R.O. 299(I)/2001 dated May 10th, 2001. A copy of the said rules was forwarded to Lahore Stock Exchange vide our letter No. 2(65)SE/2000 dated June 13, 2001.

2. *And whereas, sub-rule (2) of Rules 1 provides that these rules shall come into force at once.*

3. *And whereas sub-rule (1) of Rule 3 of the said Rules provides that a member desirous of acting as a broker shall submit an application to the Commission for grant of certificate of registration through the stock exchange of which he is a member.*

4. *And whereas Section 5A of the Securities and Exchange Ordinance 1969 provides that no person shall act as broker or agent to deal in the business of effecting transactions in securities unless he is registered with the Commission.*

5. *And whereas your exchange was directed vide letter No. 2(33)SE/2001 dated December 12, 2001 (notified to all the members by the exchange) that that any member who is not registered with the Commission by December 31, 2001 is not allowed to deal in securities.*

6. *And whereas it has been found that you were dealing in securities at Lahore Stock Exchange without being registered as broker with the Commission till June 14, 2002 the date on which certificate of registration was granted to you.*

7. *And whereas non-compliance to the applicable clauses of the Ordinance and the said Rules warrant action against you under Sections 7 & 22 of the Ordinance.*

NOW THEREFORE, you are hereby advised to show cause, in writing, within seven days (7) days of the date of this notice as to why not action be taken against you under Section 7 & 22 of the Securities and Exchange Ordinance 1969.

You are also advised to appear before the undersigned at the office of Securities and Exchange Commission of Pakistan, NIC building, 12th floor, Jinnah Avenue, Islamabad at 11:00 am on July 5, 2002 for hearing of this matter.”

6. Simultaneously, on 22-06-2002 the Commission issued the following Show Cause Notice to the LSE:

“Whereas in exercise of the powers conferred by clause (b) of section 43 of the Securities and Exchange Commission of Pakistan Act 1997 read with section 5A of the Securities and Exchange Ordinance, 1969, the Securities and Exchange Commission of Pakistan with the approval of the Federal Government of Pakistan made the Brokers and Agents Registration Rules 2001 (“the Rules”) and notified the same vide S.R.O. 299(I)/2001 dated May 10th, 2001. A copy of the said rules was forwarded to Lahore Stock Exchange vide our letter No. 2(65)SE/2000 dated June 13, 2001.

2. *And whereas, sub-rule (2) of Rule 1 provides that these rules shall come into force at once.*

3. *And whereas sub-rule (1) of Rule 3 of the said Rules provides that a member desirous of acting as a broker shall submit an application to the Commission for grant of certificate of registration through the stock exchange of which he is a member.*

4. *And whereas Section 5A of the Securities and Exchange Ordinance 1969 provides that no person shall act as broker or agent to deal in the business of effecting transactions in securities unless he is registered with the Commission.*

5. *And whereas your exchange was directed vide letter No. 2(33)SE/2001 dated December 12, 2001 that any member who is not registered with the Commission by December 31, 2001 is not allowed to deal in securities.*

6. *And whereas it has been found that a member of your exchange namely Mr. Muhammad Ahsraf Hussain Adhi was dealing in securities at Lahore Stock Exchange without being registered as a broker with the Commission till June 14, 2002 the date on which certificate of registration was granted to him.*

7. *And whereas non-compliance to the applicable clauses of the Ordinance and the said Rules warrant action against you under Sections 7 & 22 of the Ordinance.*

NOW THEREFORE, you are hereby advised to show cause, in writing, within seven days (7) days of the date of this notice as to why not action be taken against you under Sections 7 & 22 of the Securities and Exchange Ordinance 1969.

You are also hereby advised to appear before the undersigned at the office of Securities and Exchange Commission of Pakistan, NIC building, 12th floor, Jinnah Avenue, Islamabad at 11:00 am on July 5, 2002 for hearing of this matter."

7. In his written reply dated 25-06-2002 to the Show Cause Notice, the Member stated that submission of the documents for his registration with the Commission at a belated stage was not intentional. That the registration fee was deposited by him on 07-07-2001, which showed his intention to register his brokerage house in time but the registration could not be done due to the fact that his employee who was assigned the task to complete and process the paper work for registration resigned in the meantime. That he was under the wrong impression that papers for registration had been submitted to the LSE in time. That it was a genuine mistake without any intention to violate any provisions of the Rules.

He requested not to take any action against his brokerage house and assured to abide by all the directions of the Commission.

8. In the written reply dated 27-06-2002, the Managing Director LSE stated that when default of the Member came to the knowledge of the LSE, they immediately suspended his trading rights. However, the member approached the LSE and satisfied them that he was fully interested to comply with all the legal statutory requirements of the Rules by registering his brokerage house as required by the Commission. The written reply further states that the Member had prepared the requisite documents for registration but due to some unavoidable “circumstances/ misunderstanding” he failed to deposit the same. It was further stated that the LSE being a front line regulator restored the trading rights of the Member by directing him to immediately send the documents for registration, which was accordingly done by the member.

9. I heard the parties on 05-07-2002.

10. During the course of the hearing, the Member requested the Commission not to take any action against him as he had every intention to get himself registered as a broker under the Rules. He said that he had even prepared all the relevant documents and submitted the registration fee in July 2001 and his employee who was assigned the task to complete and process the paper work for registration resigned without submitting the documents to the LSE.

11. The arguments presented by the Member are not justifiable. Being a Member of the Stock Exchange he is responsible for managing the affairs of his business. It is his responsibility to ensure that the employees hired by him are responsible and are discharging the duties assigned to them in a proper manner. The Member at this stage cannot exonerate himself merely by shifting his responsibility on his ex-employee. The Member himself is accountable for not fulfilling the requisite formalities of registration. I am of strong opinion that brokers who deal with public at large are expected to be more responsible and meticulous in the conduct of their business so as to ensure that all stakeholders have confidence in them. They are responsible for ensuring that they are running their business as per the rules and regulations of their respective stock exchanges.

12. It is also worth mentioning that how the Member was able to trade for more than five months without receiving the certificate of registration from the Commission. According to the Member he was under the impression that all the requisite formalities had been completed and the documents were submitted. If the Member thought so then how

come he did not approach the Commission or the LSE after sometime inquiring about non-receipt of the registration certificate? The Member has been extremely negligent and careless.

13. At the very outset Mr. Amer Zareef, the legal advisor of LSE and Mr. Rehmat Ali Hasnie, the chief operating officer of LSE, admitted negligence on the part of the LSE and requested for the withdrawal of the Show Cause Notice on the grounds that violation of the Rules was not intentional. They reiterated that the LSE would not repeat the same mistake in future. Mr. Zareef time and again said that an inadvertent mistake was committed by LSE.

14. Mr. Zareef during the arguments contended that the Show Cause Notices were issued to the LSE and the Member at a belated stage. He invited our attention towards Rule 4(1)(k) of the Rules which says:

“A person shall be eligible for registration as a broker under the rules if he has not defaulted in compliance with the provisions of the Ordinance the Act and the rules and regulations made thereunder.”

15. He argued that if the Commission believed that the Member and the LSE have violated any Rules, it should have refused registration to the Member. The Show Cause Notices should have been issued and the opportunity of being heard should have been provided to the parties before granting registration to the Member. As the Commission has granted registration to the Member despite the fact that he had not fulfilled the requirements of the Rules earlier, it shows that the Commission has condoned the violation committed by the Member and the LSE.

16. Mr. Zareef also referred to Section 22 (1) of the Ordinance, which reads as:

“ If any person (a) refuses or fails to furnish any document, paper or information which he is required to furnish by or under this Ordinance; or (b) refuses or fails to comply with any order or direction of the Commission made or issued under this Ordinance; or (c) contravenes or otherwise fails to comply with the provisions of this Ordinance; the Commission may, if it is satisfied after giving the person an opportunity of being heard that the refusal, failure or contravention was willful, by order direct that such person shall pay to the Commission by way of penalty such sum not exceeding one hundred thousand rupees as may be specified in the order and, in the case of continuing default, a further sum calculated at the rate of two thousand rupees for every day after the issue of such order during which the refusal, failure or contravention continues.”

17. He contended that the Commission could not penalize the LSE under Section 22 of the Ordinance as the contravention of the Rules by the LSE was not wilful and Section 22 in fact speaks of taking action for any refusal, failure or contravention that was willful.

18. The arguments of Mr. Zareef are totally forceless and misconceived. Despite carelessness on the part of the LSE and the Member, the Commission registered the Member as broker on the basis of the application forwarded by the LSE. Further the Managing Director of LSE informed that the said Member had huge stake in the market and suspension of Member's trading could lead to systemic risk for the market. The Managing Director LSE also informed that the lapse on part of the LSE and the Member was due to oversight and assured that in future foolproof steps would be taken to avoid such lapses. The Managing Director LSE insisted upon the registration of the Member as broker on the plea that it would be in the interest of the LSE to have the Member as a broker. It was under these circumstances that the Commission had registered the Member as a broker and allowed the Member for trading in securities. Had the Commission not registered the Member, complications could have cropped up for the LSE and the investors and they could have suffered irreparable loss.

19. The registration of the Member by the Commission does not in any way condone the negligence, omissions and violations of the laws by the Member and the LSE and also the unlawful inaction on the part of the LSE. The matter came into the notice of the Commission on 07-06-2002. The Commission took cognizance of the matter promptly and sent Show Cause Notices to the LSE and the Member on 22-06-2002.

20. The contention that the omission on the part of the LSE is not willful is baseless. The LSE negligently failed to take proper action against the Member who has been trading for more than five months and the LSE has been in active knowledge of the facts throughout. The negligence by the LSE cannot therefore be unintentional.

21. It would not be out of place to note here that the LSE suspended the trading rights of the Member on June 08, 2002. Since they were aware of the fact that the Member was not registered with the Commission under the Rules, but the LSE later on restored the same before registration was granted to him. Despite the fact that he had not till then got himself registered with the Commission.

22. I am of the opinion that as a front line regulator the LSE is responsible for regulating the conduct of its members to ensure that all its members are trading in securities in

compliance with all the relevant rules and regulations and directives of the Commission. It is the responsibility of the Exchange and its management to be vigilant in discharging its duties and initiating timely and appropriate action against any Member, who acts in violation of the concerned rules and regulations.

23. LSE allowed the Member to trade in securities without being registered as a broker with the Commission under the Rules for more than five months. The Commission cannot neglect this gross negligence on the part of the LSE due to the reasons mentioned above.

24. In view of the foregoing, the arguments of the Member and the LSE are misconceived. I therefore hold that the Member in violation of Rule 3(1) the Rules and Section 5A of the Ordinance carried on trading in securities from 01-01-2002 to 13-06-2002 (excluding days during which his trading rights were suspended by the LSE). I further hold that the LSE allowed the Member to carry on trading during the said period in violation of express directions of the Commission which bar such trading. Both the LSE and the Member are liable to be penalized under Section 22 of the Ordinance.

25. Therefore, in exercise of powers conferred under Section 22 of the Ordinance, I hereby award the penalty of Rs. 100,000/- each both on the LSE and the Member with a direction to deposit the said amount in the collection account of the Commission maintained with the specified branches of Habib Bank Limited, within 14-days of the date of this Order.

Islamabad
24-07-2002

(SHAHID GHAFAR)
Commissioner (SM)