



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN
SECURITIES MARKET DIVISION

Before the Executive Director (Securities Market Division)

In the matter of Show Cause Notice issued to

FDM Capital Securities (Private) Limited

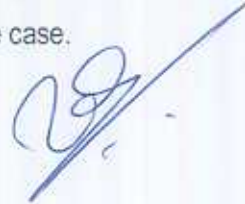
Under Rule 8 read with Rule 12 of The Brokers and Agents Registration Rules, 2001 ("The Brokers Rules")

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| Number and date of Notices | SMD-SOUTH/SCN/110/07 dated August 03, 2007 |
| Date of hearing | August 16, 2007 |
| Present | Mr. Tufail Ahmad-Chief Operating Officer and Mr. M. Ayub-Head of Equity Sales |
| Date of Order | October 30, 2007 |

ORDER

1. This order shall dispose of the proceedings initiated through Show Cause Notice SMD-SOUTH/SCN/110/07 dated August 03, 2007 issued to FDM Capital Securities (Pvt.) Ltd. (the "**Respondent**") by the Securities and Exchange Commission of Pakistan (the "**Commission**") under Rule 8 of the Brokers Rules for violation of Rule 12 of the Brokers Rules and Clause A5 of the code of conduct contained in the Third Schedule to the Brokers Rules.
2. Brief facts of the case are that the Respondent is a member of the Karachi Stock Exchange (Guarantee) Limited ("**Exchange/KSE**") and is registered with the Commission under the Brokers Rules. An enquiry was initiated by the Commission in exercise of its powers under Section 21 of the Securities and Exchange Ordinance, 1969 and Ford Rhodes Sidat Hyder & Co. ("**the Enquiry Officer**") was appointed as the Enquiry Officer under the above mentioned section inter alia:
 - a) to enquire into the dealings, business or any transaction by the Broker during the period from April 1, 2006 to June 15, 2006 ("**the Review Period**").

- b) to identify any and all the acts or omissions constituting the violation of the Securities and Exchange Ordinance, 1969 ("**1969 Ordinance**") and the Rules made thereunder.
- c) to identify violations of any other applicable laws, including but not limited to the Brokers Rules and Regulations for Short Selling under Ready Market, 2002 ("**2002 Regulations**").
3. The findings of the Enquiry Officer revealed several instances of potential non compliances with applicable laws and regulations. A copy of the Enquiry Officer's report was sent to the Respondent under cover of a letter dated May 15, 2007 which required the Respondent to provide explanations on the observations of the Enquiry Officer together with supporting documents.
4. After perusal of the Respondent's replies to the above mentioned letter, which did not adequately explain the position, a Show Cause Notice was issued to the Respondent under Rule 8 of the Brokers Rules stating that the Respondent has prima facie contravened Rule 12 of the Brokers Rules read with Clause A5 of the code of conduct contained in the Third Schedule to the Brokers Rules which are reproduced as under:
- Rule 12-** " A broker holding a certificate of registration under these rules shall abide by the code of conduct specified in the Third Schedule".
- Clause A5 of the code of conduct-**"A broker shall abide by all the provisions of the Act and the rules, regulations issued by the Commission and the stock exchange from time to time as may be applicable to them".
5. The Respondent was called upon to show cause in writing within seven days and appear before the Executive Director (SMD-South) on August 16, 2007 for a hearing, to be attended either in person and/or through an authorized representative.
6. The hearing was held on August 16, 2007 which was attended by Mr. Tufail Ahmad, Chief Operating Officer and Mr. M. Ayub, Head of Equity Sales, the Representative of the Respondent, who submitted a written reply and argued the case.



7. A summary of the contentions that were raised by the Respondent in the written submissions and during the hearing and findings and conclusion of the Commission on the same is as follows:

8. **Blank Sales**

8.1 In terms of Regulation 4 of the 2002 Regulations, blank sales are not permissible. The findings of the Enquiry Officer revealed 18 instances of blank sales during the Review Period.

8.2 The Respondent made the following submission on this Issue ("**Issue No. 1**"):

- The Respondent contended that the above mentioned instances were not blank sales and the respective clients had contractual borrowing arrangements to meet delivery requirements. The Respondent submitted copies of contractual borrowing arrangements in support of its claim

8.3 I have considered the contentions of the Respondent. Since the clients making the sale had entered into contractual borrowing arrangements to meet delivery requirements, the instances identified by the Enquiry Officer are not blank sales but **short sales** as defined under the 2002 Regulations. These short sales were made without identifying the trade as a short sale at the time of placement of order which is a violation of Regulation 5 of the 2002 Regulations which provides that:

"No Member shall make a Short Sale unless:

- a. Prior contractual borrowing arrangement has been made.
- b. The sale is made at an uptick, and
- c. The trade is identified as a Short Sale at the time of placement of order"

8.4 In terms of Rule 8 of the Brokers Rules, more particularly sub rule (ii), sub rule (iii) and sub rule (iv) thereof, where the Commission is of the opinion that a broker has inter alia failed to comply with any requirements of the Securities & Exchange Commission of Pakistan Act, 1997 or the 1969 Ordinance or of any rules or direction made or given thereunder and/ or has contravened the rules and regulations of the Exchange and/or has failed to follow any requirement of the code of conduct laid down in the Third Schedule, it may in the public interest, take action under Rule 8(a) or (b) of the Brokers Rules.



8.5 Since by making short sales without identifying the trade as a short sale at the time of placement of orders, the Respondent has violated the 2002 Regulations, thereby attracting sub rule (iii) of Rule 8 of the Brokers Rule and has also failed to comply with Clause A5 of the code of conduct contained in the Third Schedule to the Brokers Rules, thereby attracting sub rule (iv) of Rule 8 of the Brokers Rule, I am of the view that a penalty of Rs.10,000 (Rupees Ten Thousand only) be imposed on the Respondent under Rule 8 (b) of the Brokers Rules

9. Order Register

9.1 In terms of Rule 4(1) of the Securities and Exchange Rules 1971 ("**1971 Rules**"), it is provided that:

"All orders to buy or sell securities which a member may receive shall be entered, in the chronological order, in a register to be maintained by him in a form which shows the name and address of the person who placed the order, name and number of the securities to be bought or sold, the nature of transaction and the limitation, if any, as to the price of the securities or the period for which the order is to be valid."

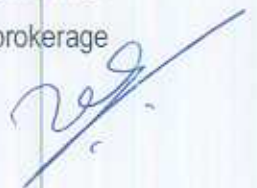
9.2 Findings of the Enquiry Officer revealed that the register as mentioned above was not maintained by the Respondent during the Review Period.

9.3 The Respondent made the following submissions on this Issue ("**Issue No. 2**"):

- The Respondent contended that the register as provided above was not possible to maintain due to practical difficulties and a computerized Activity Log is maintained as a solution.

9.4 I have considered the contentions of the Respondent and am of the view that the computerized Activity Log as mentioned by the Respondent is not a substitute for the Order Register as required under the Rule 4(1) of the 1971 Rules, since the computerized Activity Log as maintained by the Respondent only records those orders that are placed by the brokerage house into KATS and not the orders received from the clients.

9.5 The Commission is also cognizant of the practical difficulties associated with the maintenance of such an Order Register manually and in order to facilitate the brokerage houses in meeting the requirements of the said rule, the KSE is developing a system which will be provided in due course. However, it is noted with disappointment that the brokerage



houses and exchanges were not able to keep pace with evolution in technology and significant increase in trading activities whereby a system should have been developed to enable simultaneous recording of orders received from clients and their incorporation in a database to generate the Order Register as required under the requirements of the Rule 4(1) of the 1971 Rules.

- 9.6 Considering the above mentioned facts I am inclined, on this occasion, to take a lenient view in the matter and will not take any punitive action under Rule 8 of the Brokers Rules. As such, I believe a 'caution' in this instance to the Respondent would suffice and I would further direct the Respondent to ensure that full compliance is made of all the Regulations in future for avoiding any punitive action under the law.
10. In view of what has been discussed above, I am of the considered view that no punitive action is necessary in relation to Issue No. 2 and a simple caution will suffice. As regards Issue No. 1, as stated above, a penalty of Rs. 10,000 (Rupees Ten Thousand) is imposed, which should be deposited with the Commission not later than fifteen (15) days from the date of receipt of this Order



Zafar Abdullah
Executive Director
Securities Market Division