



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN
(Securities Market Division)

Before the Director (Securities Market Division)

In the matter of Show Cause Notice issued to

SAT Securities (Pvt.) Limited

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

Number and Date of Notice	No. MSW/SMD/LSE/1(5)2006/75 dated September 04, 2007
Date of Hearing	September 18, 2007
Present at the Hearing:	Mr. Shah Zeb Khan – General Manager Mr. Asad Ullah Javied (Advocate)
Date of Order	January 10, 2008

ORDER

1. This order shall dispose of the proceedings initiated through Show Cause Notice bearing No. MSW/SMD/LSE/1(5)2006/75 dated September 04, 2007 ("the SCN") issued to SAT Securities (Pvt.) Limited ("the Respondent"), member of the Lahore Stock Exchange (Guarantee) Limited ("LSE") by the Securities and Exchange Commission of Pakistan ("the Commission") under Rule 8 of the Brokers and Agents Registration Rules, 2001 ("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 of the Brokers Rules.
2. The brief facts of the case are that the Respondent is a member of LSE 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 ("the Ordinance") and Ford Rhodes Sidat Hyder & Co. ("the Enquiry Officer") was appointed as the Enquiry Officer under the above mentioned Section for the following:
 - (a) to enquire into the dealings, business or any transaction by the Respondent during the period from April 01, 2006 to June 15, 2006 ("the Review Period").
 - (b) to identify any and all the acts or omissions constituting the violation of the Ordinance and the Rules made thereunder.
 - (c) to identify violations of any other applicable laws, including but not limited to the Brokers Rules, Regulations for Short Selling under Ready Market, 2002 ("Short Selling Regulations"),



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General Rules and Regulations of LSE, Securities and Exchange Rules 1971 ("the 1971 Rules") and directives issued by the Commission from time to time.

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 on May 22, 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 in respect of some instances, the SCN was issued to the Respondent under Rules 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 Securities and Exchange Commission of Pakistan Act, 1997 ("the Act") and the rules, regulations issued by the Commission and the stock exchange from time to time as may be applicable to him".

5. On September 04, 2007, the Respondent was called upon to show cause in writing within seven days and appear before the undersigned on September 13, 2007 for a hearing, to be attended either in person and/or through an authorized representative. However, on Respondent's request hearing was re-fixed for September 18, 2007.

6. The hearing was attended by Mr. Shah Zeb Khan, General Manager of the Respondent and Mr. Asad Ullah Javied, Advocate, who argued the case and also submitted written reply dated September 12, 2007.

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

8. **Preliminary Objections**

8.1 The objections raised by the Respondent on the Enquiry conducted by the Enquiry Officer are given as under:-

- The Enquiry Officer was not appointed in accordance with the provisions of Section 21 of the Ordinance. For the purpose of enquiry under Section 21 of the Ordinance a 'person' has to be appointed as enquiry officer, whereas Ford Rhodes Sidat Hyder & Co. is neither a natural person nor a legal person.



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- In delegation of powers under Section 10 of the Act on July 07, 2006 the Director (SM) did not have powers to order enquiry under Section 21 of the Ordinance. Further under delegation of powers under SRO 1061 (I)/2005 dated 18th October, 2005, the Director (SM) does not have the power to issue a Show Cause Notice, hear or decide under Rule 8 and 12 of the Brokers Rules.
- The requirement of Section 21 of the Ordinance is that an enquiry can only be conducted by an "order in writing" and it cannot be conducted by mere intimation. The Respondent was never informed about the order, which was passed for conducting its enquiry and neither the Respondent was heard before passing such order of enquiry.
- Section 21 (4) of the Ordinance, provides following procedure of enquiry.

"The person holding an enquiry under sub-section (1) shall, for the purpose of such enquiry have the same powers as are vested in a court under the Code of Civil Procedure, 1908 (Act V of 1908), when trying a suit, in respect of the following matters, namely :-

(a) enforcing the attendance of a person and examining him on oath or affirmation;

(b) compelling the production of documents;

(c) issuing commissions for the examination of witnesses;

and any proceedings before such person shall be deemed to be "judicial proceeding" within the meaning of Sections 193 and 228 of the Pakistan Penal Code (Act XLV of 1860)."

The Enquiry Officer did not follow the aforementioned procedure in conducting the enquiry. Moreover, the Respondent was also not provided a proper opportunity to provide evidence and material in support of the contentions raised in the report. The statements of the persons and the documents marked as provided in Civil Procedure Code were not taken under oath. The Respondent asserted that the use of word "shall" in the abovementioned Sub-section makes it mandatory for the Enquiry Officer to exercise these powers and conduct the enquiry accordingly.

- During the hearing the Respondent further asserted that the use of word "and" between the clause 12 and 13 of the Rule 8 of the Brokers Rules connects all the 13 clauses given under the said rule, therefore, action under Rules 8 of the Brokers Rules can only be taken against the Respondent if it has violated all the 13 clauses of the said rule.



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8.2 I have considered the contentions and the preliminary objections raised by the Respondent and the issues raised therein and the same are addressed below:

- The Respondent's assertion that to conduct an enquiry under Section 21 of the Ordinance only a natural or legal person can be appointed as an Enquiry Officer is not correct. In this regard attention of the Respondent was brought to the Section 2(1)(j) of the Ordinance which defines the term "person" as follows:

"person" includes a Hindu undivided family, a firm, an association or body of individuals, whether incorporated or not, a company and every other artificial juridical person;

Since Ford Rhodes Sidhat Hyder & Co. is a firm, therefore, it falls under the definition of "person" and can be appointed as Enquiry Officer under Section 21 of the Ordinance.

- The assertion of the Respondent that Director (SM) does not have the power to order enquiry under Section 21 of the Ordinance, issue a show cause notice, to hear or decide under Rule 8 and 12 of the Brokers Rules is also not correct. The powers under Section 21 of the Ordinance and Rule 8 of the Brokers Rules were delegated to Director (SM) by the Commission under Section 10 of the Act vide S.R.O. 1075(1)2005 dated October 21, 2005.
- The contention of the Respondent that the Enquiry does not stand valid or enforceable as the Enquiry Officer did not conduct the Enquiry in accordance with the procedure laid down in the Section 21(4) of the Ordinance, is not correct. It is not mandatory for the Enquiry Officer to exercise the powers conferred under the Section 21(4) of the Ordinance. It is his discretion to adopt a suitable method for carrying out an enquiry.
- With regard to the Respondent's assertion that action against the Respondent under Rule 8 of the Brokers Rules can only be taken if the Respondent has violated all the 13 clauses of the said Rules is not correct. The use of word "and" between clause 12 and 13 of the Rule 8 of the Brokers Rules does not mean that all the 13 clauses are connected to each other. This is a self serving interpretation and is not the intention and spirit of the law.

9. **Blank Sales ("Issue No. 1")**

9.1 In terms of Regulation 4 of the Short Selling Regulations, Blank Sales are not permissible and in terms of Regulation 5 of the Short Selling Regulations, it is provided 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"



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- 9.2 The findings of the Enquiry Officer revealed 24 instances of Blank Sales during the Review Period.
- 9.3 The Respondent made the following submissions on the issue:
- In its earlier reply dated July 18, 2007 the Respondent stated that sales given in Annexure – A ("the Annexure") of the SCN were not Blank Sales and provided copies of letters from Y.S. Securities (Pvt.) Limited, member LSE, which stated that it authorized the Respondent to sell shares of NBP and BOP on June 01, 2007 and June 08, 2007 respectively on its behalf in Respondent's own account. Whereas, during the hearing the Respondent stated that the said trades were result of error as it made sales over and above its CFS positions.
- 9.4 I have considered the contentions of the Respondent and the issues raised therein and the same are addressed by me below:
- From the Respondent's stance taken during the hearing it is clear that the trades mentioned in the Annexure are Blank Sales. The Respondent during the hearing and in its written reply failed to provide any documentary evidence of the pre-existing interest in the shares before sale. However, in its earlier replies the Respondent provided documents to prove that the Blank Sales mentioned in the Annexure were executed by it on behalf of another member of LSE. However, during the hearing the Respondent changed its stance and stated that these trades were result of errors.
- 9.5 Considering the above facts and the contentions of the Respondent, it is an established fact that on 24 occasions Blank Sales have been made in violation of Regulation 4 of the Short Selling Regulations. In terms of Rule 8 of the Brokers Rules, sub rule (ii) where the Commission is of the opinion that a broker has inter alia failed to comply with any requirements of the Act or the Ordinance or of any rules or directions made or given thereunder, in terms of sub rule (iii) has contravened the rules and regulations of the exchange, in terms of and sub rule (iv) has failed to follow any requirement of the Code of Conduct laid down in the Third Schedule, the Commission may in the public interest, take action under Rule 8(a) or (b) of the Brokers Rules.
- 9.6 In light of the above i.e. the fact the Respondent by making Blank Sales has violated the Short Selling Regulations thereby attracting sub rule (ii) of the 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 the Rule 8 of the Brokers Rule. Accordingly, a penalty of Rs. 10,000 (Rupees Ten Thousand only) is hereby imposed on the Respondent under Rule 8 (b) of the Brokers Rules.
10. **Account Opening Forms ("Issue No. 2")**
- 10.1 In terms of Commission's Directive No. SMD/SE/2(89) 2003 dated July 23, 2003 which requires all the members-brokers to maintain Account Opening Form(s) ("the AOF(s)") in conformity with the

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Standardized Account Opening Form ("the SAOF") prescribed by the Commission and subsequent changes made to the SAOF vide letters No. SMD/SE/2(89) 2003, dated November 19, 2003 and January 20, 2004. Subsequently this SAOF was also made part of LSE General Rules and Regulations as Chapter VIII. The said directives of the Commission require that

- i) All the relevant information / fields of the AOFs should be properly filled in.
- ii) Copies of customers' CNICs should be attached with the AOFs.
- iii) Attested copies of customers' CNICs should be attached with the AOFs.

10.2 Findings of the Enquiry Officer revealed that;

- i) All the relevant information / fields of the AOFs were not properly filled in.
- ii) Copies of customers' CNICs were not attached with the AOFs.
- iii) Attested copies of customers' CNICs were not attached with the AOFs.

10.3 The Respondent made the following submission on these issues:

- The Respondent stated that during the enquiry it was in process of completing its AOF(s), however, currently it has completed all the AOF(s).
- As for the missing and unattested copies of CNICs the Respondent stated that it has taken corrective actions and now attested copies of CNICs of customers are attached with all AOFs.

10.4 I have considered the contentions of the Respondent and the issues raised therein and the same are addressed by me below:

- From the aforementioned assertion of the Respondent it is clear that the Respondent has failed to comply with the requirements of SAOF. The SAOF requires that all the fields of the AOFs should be properly filled in and in case a field is not applicable same should be marked as "N/A" in order to ensure that same is not amended by the broker without the consent of the clients. Further the SAOF also requires that attested copy of CNICs of the client's should also be attached with the AOFs. However, the Respondent failed to comply with the said requirement.

10.5 Considering the above facts and the contentions of the Respondent, it is established that the Respondent has failed to comply with Commission's directives and General Rules and Regulations of the LSE. In terms of Rule 8 of the Brokers Rules, more particularly sub rule (iii), (iv) and sub rule (v) therefore, where the Commission is of the opinion that a broker has inter alia failed to comply with requirements of the any directions of the Commission 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, to take action under Rule B(a) or (b) of the Brokers Rules.



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10.6 In light of the above i.e. the fact the Respondent failed to comply with Commission's directives thereby attracting sub rule (v) of the Rule 8 of the Brokers Rule. However, based on the Respondent's statement that it has already taken corrective actions and assured the Commission that such violations will not occur in future, 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 these instances to the Respondent would suffice and I would further direct the Respondent to ensure that full compliance is made of all rules, regulations and directives of the Commission in the future for avoiding any punitive action under the law.

11. **Order Register ("Issue No. 3")**

11.1 In terms of Rule 4(1) of the 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, the 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."

11.2 The findings of the Enquiry Officer revealed that the register as mentioned above was not maintained by the Respondent during the Review Period.

11.3 The Respondent made the following submission on the aforementioned issue:

- The Respondent in its written reply asserted that electronic ledger as maintained today fulfills the requirement of abovementioned Rule. The Respondent further asserted that the said Rule was introduced when manual trading was prevalent in the stock market.
- During the hearing the Respondent stated that now-a-days due to high volume and speed of trading it is practically impossible to maintain manual order register. However, after the Enquiry the Respondent has started to maintain the Order Register.

11.4 I have considered the contentions of the Respondent and I am of the view that electronic ledgers or the Daily 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. The aforementioned Logs only record those orders that are placed by the Respondent into LOTS and not all the orders which were received from the clients and not entered into LOTS. Further, the said Log only records the time of placement of orders into the system and not the time of receipt of orders.

11.5 The Commission is also cognizant of the practical difficulties associated with the maintenance of such an Order Register manually. However, it is noted with disappointment that the brokerage house and LSE were not able to keep pace with evolution in technology and significant increase in trading activities



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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 Rule 4(1) of the 1971 Rules.

- 11.6 Considering the above motioned fact 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 that 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 laws, regulations and directives of the Commission in future for avoiding any punitive action under the law.
12. **Separate Bank Account for Clients Funds ("Issue No. 4")**
- 12.1 In terms of Commission's directive No. SMD/SE 2(20)/2002 dated March 4, 2005 which states that:
- "The exchanges are to ensure that brokers follow the practice of segregating clients' assets from the broker's assets in order to ensure that clients' assets are not misused.
- For this purpose brokers should have one separate bank account which includes all the cash deposits of their clients along-with records/breakdown of client positions."
- 12.2 The findings of the Enquiry Officer revealed that the Respondent was not maintaining a separate bank account for clients' funds.
- 12.3 The Respondent made the following submission on the aforementioned issue:
- The Respondent during the hearing assured that it will maintain a separate bank account for clients' funds and vide letter dated January 04, 2008 confirmed that it has started to maintain separate account for clients' funds with effect from November 07, 2007.
- 12.4 I have considered the contentions of the Respondent and it is clear to me that the Respondent has failed to comply with the Commission's directive No. SMD/SE 2(20)/2002 dated March 4, 2005. However, the Respondent after the hearing has confirmed that it has taken corrective steps and is now complying with the abovementioned directive of the Commission.
- 12.5 Considering the above mentioned fact 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 that 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 laws, regulations and directives of the Commission in future for avoiding any punitive action under the law.
- 13 As stated above, the Respondent is penalized as follows:
- a) As regards Issue No1, as stated above, a penalty of Rs. 10,000/- (Rupees Ten Thousand only) is imposed.

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- b) No punitive action is taken in relation to Issue No. 2, 3 and 4 and a simple caution will suffice.

13.1 The matter is disposed of in the above manner and the Respondent is directed to deposit the fine with the Commission not later than fifteen (15) days from the receipt of this Order.

Imran Inayat Butt
Director (SM)
Securities Market Division