



# SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

(Securities Market Division)

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**Before the Joint Director (Securities Market Division)**

**In the matter of Show Cause Notice dated 23.08.2005**

**Issued to Mr. Muhammad Munir Muhammad Ahmed Khanani**

**Date of Hearing**

**5<sup>th</sup> September 2005**

**Present at the Hearing:**

Mr. Muhammad Munir Muhammad Ahmed Khanani:

**ORDER**

1. The present matter arises out of a Show Cause Notice bearing No. SMD/SCN/16/2005 dated 23.08.2005 issued to Mr. Muhammad Munir Muhammad Ahmed Khanani, Member of the Karachi Stock Exchange (G) Ltd. (the ‘Respondent’).
2. Brief facts of this case are that between 04.03.2005 and 29.03.2005, the Respondent carried out 11 trades involving total 172,200 shares of National Bank of Pakistan (NBP), Oil & Gas Development Company (OGDC), Pakistan State Oil Limited (PSO) and Pakistan Telecommunication Company Limited (PTC) through the Karachi Automated Trading System (“KATS”) on behalf of five of its clients.
3. In the course of these trades, the Respondent purchased and sold, on behalf of the said five clients, 114,300 shares of NBP, 36,400 shares of OGDC, 500 shares of PSO, and 21,000 shares of PTC. 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 Securities and Exchange Commission of Pakistan (the “Commission”) obtained the KATS data from the Karachi Stock Exchange (G) Ltd. (“KSE”) 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	PURCHASE AND SALE RATE	TIME OF EXECUTION
04/03/2005	801	NBP-REG	45000	143.45	936490095
04/03/2005	801	NBP-REG	50000	143.5	936490098
07/03/2005	801	NBP-REG	19300	144.9	1141030009
07/03/2005	791	OGDC-REG	1200	139.5	1204240004
08/03/2005	801	OGDC-REG	25700	148.85	1402230002
14/03/2005	801	OGDC-REG	9500	168.85	1125560002
29/03/2005	475	PSO-REG	500	344.45	1034210011
04/03/2005	475	PTC-REG	10000	76.55	1557070050
07/03/2005	A82	PTC-REG	500	79.7	1344560042
18/03/2005	475	PTC-REG	500	87	1126490047
28/03/2005	223	PTC-REG	10000	65	1007050020

5. In view of the preceding a Show Cause Notice was issued to the Respondent on 23.08.2005, detailing the aforesaid facts and asking him as to why action should not be initiated against him under Brokers and Agents Registration Rules, 2001 (the “Rules”). A copy of the KATS data was also sent to the Respondent in order to allow him an opportunity to answer the same. The Respondent was asked to submit a written reply within 7 days from the date of the Show Cause Notice and the hearing was fixed for 05.09.2005.
6. The Respondent submitted a written reply to the Show Cause Notice on 30.08.2005 and also appeared in person to defend his position. The main points raised by the Respondent in his written reply and in the course of hearing were as follows:
- a) The Respondent asserted that he is maintaining sub-accounts of more than 3000 clients at his Brokerage House at KSE. His clients also include Members of Islamabad Stock Exchange (G) Ltd. (“ISE”) and Lahore Stock Exchange (G) Ltd. (“LSE”), who on behalf of their clients place orders for sale/purchase of securities at the KSE through the Respondent. He further stated that as a matter of professional



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responsibility he executed all such orders placed by clients strictly in line with the rules and regulations of KSE and the Commission, hence any violation noticed by the Commission is only due to the human error factor.

- b) The Respondent further stated that the trades in question were executed by him on behalf of five clients, out of which two clients bearing Code No 475 and 223 are the members of ISE and the LSE respectively. The aforesaid member clients had placed orders for sale or purchase of securities on behalf of their respective clients. It is probable that in some cases the orders placed by a member client may be squared up with another order placed by a different client of the same member client. In the afore-mentioned scenario, the member client deals on behalf of its various clients, so change of ownership is actually taking place at the end of the member client.
- c) Further, the Respondent pleaded during the hearing, that the market cannot be manipulated with such a low trade volume, particularly in the case of shares in question as these shares were already being traded heavily during the month of March, 2005.
- d) On the basis of the aforesaid the Respondent requested that the Show Cause Notice be withdrawn as it had not violated any rules and regulations of KSE and the Commission.

7. I have heard the Respondent at length after carefully examining the record and 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:

*(a) Whether the acts of commission and omission as alleged against the Respondent constitutes a breach of the Rules? If so, up to what extent?*



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8. In the course of written as well as oral arguments, the Respondent has acknowledged the fact of carrying out all 11 trades detailed in the Show Cause Notice. However the Respondent has pleaded that he has not violated any rules and regulations of the Commission. This assertion of the Respondent does not hold ground on the basis of the fact that the Securities and Exchange Ordinance 1969 (the “Ordinance”) clearly prohibits the execution of such orders where buyer and seller is the same person and such orders do not result in change in beneficial ownership of the shares. It is proved from the data provided by the Respondent and the data annexed to the Show Cause Notice that a change in beneficial ownership did not take place in the trades in question executed on behalf of three clients bearing code 801, 791 and A82. Therefore, in violating the Ordinance, the Respondent has also acted in contravention of clause 5 of the Code of Conduct set forth under the Rules which requires that a broker should abide by all the provision of the Ordinance, rules and regulation set forth by the Commission and the Exchange.
9. The Respondent has also pleaded that the trades in question are result of the human error. This is a clear confession by the Respondent that he failed to exercise due skill and care at all time in conduct of his business. Clause 2 of the Code of Conduct set forth under the Rules requires that a broker should act with due skill and care in the conduct of his business. Therefore the execution of the trades in question clearly shows that the Respondent failed to exercise due skill and care at the time of carrying out these trades. Further it is the responsibility of the Respondent to inform his clients about their unexecuted orders before placing their new order in the system, particularly when the new order is at the same price, so that the possibility of canceling out the previous outstanding orders could be avoided. It is also pertinent to clarify here that KATS also provides the option of withdrawal of unexecuted orders at any time. So instead of placing a new order on the KATS, the Respondent should have first used the option of withdrawal of unexecuted order. Therefore, in the presence of the withdrawal option in KATS the occurrence of trades in question clearly shows that the Respondent did not at all times carry out its business with due skill, fairness, promptitude and diligence.
10. Moreover, the Respondent has also asserted that in the matter of execution of transactions on behalf of its member clients of LSE and ISE (“Member Client”) the beneficial ownership of the shares did take place at the Member Client end. However neither during the course of



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hearing nor vide his written reply the Respondent submitted any documentary evidence in support of his abovementioned claim. Further Section 8 (1) of Ordinance states that “No person shall transact any business in securities on any Stock Exchange unless he is a member thereof”. However the aforesaid assertion of the Respondent clearly proves that Members of ISE and LSE are transacting their business on KSE through the Respondent by placing their clients’ orders with the Respondent and the same is also in the knowledge of the Respondent. Therefore the business conducted by the Member clients on behalf of their clients through the Respondent is illegal and gross violation of the law.

11. Further the assertion by the Respondent that the trades given in the Show Cause Notice constitute a nominal percentage of the total traded volume of a particular day and therefore cannot in any way affect the market price of shares is not accepted. Although the minimal percentage of trades in question might not have affected the price of a share in the instant matter however the fact cannot be ignored that these trades did become the part of over all trading volume and such trades gave a false impression of active trading in these scrips at the time of execution. Moreover, by executing and permitting to execute trades which cancelled each other out and did not result in the transfer of beneficial ownership of the shares, the Respondent has indulged in acts which interfered with the fair and smooth functioning of the market to the detriment of investors and has failed to follow the Code of Conduct prescribed for brokers in the Rules.
12. In failing to ensure that a proper system was in place to avoid repeated occurrence of these trades where buy and sell orders by the same client cancel each other out, 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 in gross and blatant violation of Rule 8(iv) read with Rule 12 of the Rules.

*(b) What should the order be?*

13. From the aforesaid it is clear that the Respondent has failed to maintain high standards of integrity, exercise due skill and care in conduct of business, comply with the statutory requirements and has engaged in transactions which distorted the market equilibrium. This



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conduct of the Respondent is a violation of General provisions 1, 2, 4 and 5 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, I have 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.- (Rupees Fifty Thousand only). This sum of Rs. 50,000.- should be deposited in the account of the Commission being maintained in the designated branches of Habib Bank Ltd., no later than thirty (30) days from the date of this Order. A copy of the Challan form evidencing the deposit of penalty amount must be sent to the Commission.

14. 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 the law.
15. This Order is issued without prejudice to any other action that the Commission may initiate against the Respondent in accordance with the law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.

**Ikram Ul Haque**

Joint Director (SM)

Date of Order: 15.09.2005