



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN
(Securities Market Division)

Before The Director (Securities Market Division)

In the matter of Show Cause Notice issued to

United Capital Securities (Pvt.) Limited

Date of Hearing:

January 13, 2010

Present at the Hearing:

Representing the United Capital Securities (Pvt.) Limited

(i) Mr. Kamran Abbas

Chief Executive Officer

(ii) Mr. Haroon Younus

Head of Operations

Assisting the Director (SMD)

(i) Mr. Waqar Ahmed Siddiqui


Joint Director

(ii) Mr. Farhan Yacoob

Assistant Director

ORDER

1. This order shall dispose of the proceedings initiated through Show Cause Notice bearing No. 1(07) BS/KSE/MSW/SMD/2009/64 dated December 07, 2009 ("the SCN") issued to United Capital Securities (Pvt.) Limited ("the Respondent"), Member of the Karachi Stock Exchange (Guarantee) Limited ("KSE") by the Securities and Exchange Commission of Pakistan ("the Commission") under Section 22 of the Securities and Exchange Ordinance, 1969 ("the Ordinance") and Rule 8 of the Brokers and Agents Registration Rules, 2001 ("the Brokers Rules").
2. The brief facts of the case are that the Respondent is a member of KSE and is registered with the Commission under the Brokers Rules. On perusal of the trading data of Karachi Automated Trading System ("KATS") of the KSE for the month of July 2009, it was observed that the clients of the Respondent namely Muhammad Ashraf ("MA"), Sohail Mustafa ("SM") and Syed Jamsheed Zaidi ("SJZ") had been engaged in selling and then squaring up their positions in different scrips. During the month of July 2009, MA & SM first sold and then

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squared up their positions in the scrips of Oil & Gas Development Company Limited ("OGDC") & WorldCall Telecom Limited ("WTL") to the tune of 20,000 shares and 40,000 shares respectively. Further, SJZ first sold and then squared up his position in the scrips of D.G. Khan Cement Company Limited ("DGKC") to the tune of 50,000 shares, Arif Habib Securities Limited ("AHSL") to the tune of 30,000 shares, Azgard Nine Limited ("ANL") to the tune of 20,000 shares and OGDC to the tune of 70,000 shares.

3. The Commission vide its letters dated August 31, 2009 and October 02, 2009 sought clarifications regarding the Blank Sales by the Respondent on behalf of its clients. The Respondent in its replies vide letters dated September 04, 2009, October 06, 2009, October 13, 2009 and October 16, 2009 admitted that its two clients MA & SM have mistakenly executed the sale transactions without having pre-existing interest and squared the positions on same day. Further, the Respondent submitted a Contractual Agreement between its client SJZ with Asim Saghir & Saeed Akhtar in support of the pre-existing interest in the shares.
4. On perusal of the trading data of the KSE for the month of August 2009, it was noted that the clients of the Respondent namely Mashood Ameer ("MHA"), Arif Khalid ("AK") and SJZ had been engaged in selling and then squaring up their positions in different scrips. During the month, MHA first sold and then squared up his position in the scrips of OGDC to the tune of 198,000 shares, Pakistan Petroleum Limited ("PPL") to the tune of 30,000 shares and MCB Bank Limited ("MCB") to the tune of 207,785 shares. Further, AK & SJZ first sold and then squared up their position in the scrips of OGDC & DGKC to the tune of 20,000 shares & 100,000 shares respectively.
5. The Commission vide its letters dated October 06, 2009 and October 13, 2009 sought clarifications regarding the Blank Sales by the Respondent on behalf of its clients. The Respondent in its replies vide letters dated October 10, 2009 and October 15, 2009, admitted that its client MHA has mistakenly executed the sale transactions without having pre-existing interest and subsequently squared the position on same day. Further, the Respondent produced a Contractual Agreements between its client AK with Saeed Akhtar and SJZ with Asim Saghir in support of the pre-existing interest in the shares.
6. On further perusal of the trading data of the KSE for the month of September 2009, it was observed that the clients of the Respondent namely Syed Mansoor Abbas Kazmi ("MAK"), AK and SJZ had been engaged in selling and then squaring up their positions in different scrips.



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During the month, MAK first sold and then squared up his position in the scrip of NIB Bank Limited ("NIB") to the tune of 100,000 shares. Further, AK first sold and then squared up his position in the scrip of Nishat Mills Limited ("NML") to the tune of 20,000 shares, and SJZ first sold and then squared up his position in the scrip of AHSL to the tune of 70,000 shares.

7. The Commission vide its letter dated November 16, 2009 sought clarification regarding the Blank Sales by the Respondent on behalf of its clients. The Respondent in its reply vide letter dated November 20, 2009 informed the Commission that MAK and SJZ had furnished the Agreements with different persons in support of the pre-existing interest in the shares whereas in the matter of AK the Respondent requested ten days time to investigate the matter.
8. The above mentioned replies of the Respondent were not considered satisfactory and it clearly showed that Respondent has executed the said trades without having pre-existing interest. Consequently, SCN was issued to the Respondent under Section 22 of the Ordinance and the Brokers Rules stating that the Respondent has prima facie contravened Clause A (2) and A (5) of the Code of Conduct set forth under the third schedule of the Brokers Rules. The Respondent was required to appear in person or through an authorized representative before the undersigned at Commission's Islamabad Office on December 29, 2009. for hearing. However, the date of hearing was changed on the Respondent's request and the hearing was held at Commission's Karachi Office on January 13, 2010.
9. The Respondent submitted its written reply to the SCN vide its letter dated December 23, 2009. Some of the contentions raised by the Respondent in its reply are as follows:
 - a. *"UCS admitted that Mr. MA and SM (as told by the clients) unconsciously got into such situation. This is evident from the fact that both persons trading position resulted in net loss to them. Moreover, the position was squared up within second in one transaction whereas in the second transaction the time is also very short. Therefore, squaring up of selling order within fraction of second and the resultant loss clearly leads to believe that it was unintentional and by accident".*
 - b. *"UCS vide its letter 15/10/2009 & October 10, 2009 informed the SECP that the concept of short selling is misunderstood by the client and hence the trading by him was all unintentional and without any intention to manipulate in the*



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market. His net loss for the trading transactions mentioned clearly depicts that he suffered huge loss. MHA did commit the mistake but it was all unintentional based on misunderstanding of short selling concept".

- c. "Again SECP vide its letter dated 16/11/2009 conveyed to UCS the alleged blank sales positions of its clients during the month of September-09, namely Syed Mansoor Abbas Kazmi ("MAK"), AK & SJZ. UCS through its letter dated 20/11/2009 submitted that MAK and SJZ had furnished the agreements with different persons to support the pre-existing interest in the shares mentioned by SECP whereas in regard to Mr. AK, UCS requested for ten days time to investigate the matter. However, for regulatory requirement, we hereby admit under the circumstances that AK has committed a default but it is pertinent to mention that AK incurred loss by virtue of trading transactions".
- d. "The regulation 5 of Regulation for Short Selling under Ready Market, 2002 attaches certain strings for short sell and we admit that all these pre-requisites were not met by UCS, although more than 90 percent of clients and brokers doing short selling do not comply with the regulation 05 of the short selling Regulations".
- e. "Hence, there was no gain from such activity that clearly illustrates one thing very evident all such trading transactions were inadvertent and without any design or artifice or scheme for any kind of manipulation rather the concept of short selling has been misunderstood. Therefore, if you analyze it from month-wise or client-wise, the net result is loss that concludes that these squaring up of the position were unintentional and the concept of short sells being misunderstood by the clients and even the KATS operator".
- f. "The UCS submitted agreements for contractual arrangement to show pre-existing interest of the clients namely SJZ, AK, and MK those clearly show that all these clients had pre-existing arrangements and were fully entitled for selling the securities (except compliance to regulation 5 of the Short Selling Regulations). If these are taken into consideration by SECP then there remain few transactions/clients which committed non-compliance to Short-selling



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regulations. In order to provide proof that the lenders were holding securities, UCS furnished to SECP the individual clients sub-accounts sheets, CDC house account and securities available in house account. There could be a probable objection that securities lying in the pledge account/margin account cannot be taken as available, in this regard we have to submit that all such securities can be made available and held by lender as these can be taken out/unpledged within minutes for settlement purpose with the condition that the brokerage house has to substitute the securities in the pledge/margin account".

- g. *"Having all the aforementioned in view and our admission that non-compliance has been committed by our clients whereas UCS also overlooked such non-compliances, we request you to take lenient view and these trading instances and non-compliances may be ignored. This is for the first times that UCS has been show caused for such non compliance otherwise UCS has a neat and clean record. At present, there is not a single complaint outstanding against our brokerage house and UCS has never been involved into such instances previously. We assure you that best efforts would be made for non-occurrence of such events in future and process and procedures would be improved and we would be more vigilant to refrain from such mistakes in future. It is once again requested that lenient view may be taken keeping in view all the above submissions and no action be taken against UCS having been assured by UCS that strict adherence to all rules and regulations to be observed in future".*

10. On the hearing date the authorized representative of the Respondent Mr. Kamran Abbas, Chief Executive Office ("CEO") and Mr. Haroon Younus, ("Head of Operations") appeared before me and made the following submissions:

- a) The CEO informed that the Regulations for Short Selling were not properly followed due to misunderstanding of the short selling concept and the transactions have been executed without having pre-existing interest in respective scrips and most of the clients had incurred losses with respect to excess selling and then squaring up in the scrip.
- b) The CEO stated that the Respondent is actively promoting internet trading services for retail customers for trading purposes, which will hopefully enable them to



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reduce the chance of such violations which unfortunately being made at their end. He also added that Respondent's intentions with regard to business objectives are fair and it transparent and always try to maintain good relationship with investors.

c) The CEO stated that it has always complied with all the directives issued by the Commission and Stock Exchange from time to time and never provided any opportunity of complaint. The CEO further stated that short sale transactions are not allowed to any of its clients but due to heavy work load on KATS system few transactions of short sale were executed erroneously and same were corrected immediately. He also added that the Respondent has conveyed to all the KATS Operators and trading staff to strictly follow the Rules and Regulations of KSE and the Commission but in the above cases, KATS operators executed short sale orders erroneously without using Short Sale Order Window.

d) The CEO emphasized that the transactions in question were not executed with the intention to manipulate the share price of the scrip and no material benefit was gained through these transactions. The CEO requested that the Commission may take a lenient view in this matter and drop the proceedings together with the show cause notice because the said trades were merely results of ignorance and unawareness, without having fraudulent intentions.

11. Considering the contentions made in written reply of the Respondent and arguments made by CEO during the course of hearing, it is established that Respondent's clients sold shares without having pre-existing interest. The assertion of the CEO that the Respondent was not properly following the Regulations due to misunderstanding of short selling concept and its clients incurred losses with respect to excess selling may not hold true because the Respondent was responsible for each and every order placed or trade executed through its trading terminal. Further, merely acknowledging and regretting a mistake and sustains loss due to excess selling does not absolve the Respondent from its responsibilities and the adverse consequences of the subject violation. It was the responsibility of the Respondent to monitor all trading activities being carried out through its brokerage house in order to track and prevent any transaction being made in violation of any applicable rules and regulations. Moreover, in case of the error made by its KATS Operators, the Respondent should have immediately informed the KSE.



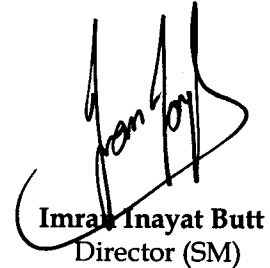
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12. The Respondent through its written replies provided the Agreements by SJZ, AK and MAK allowing them to borrow shares from lenders. While reviewing the contents of the Agreements it transpired that details of the contractual arrangements have not been specified in these Agreements. It is a known fact that if the terms of the Agreement are uncertain or ambiguous, the agreement is void and unenforceable. Moreover, for the sake of arguments, if it is assumed that the Agreements allow SJZ, AK and MAK to meet delivery requirements by using the securities of the lender, the sale transactions cannot be classified as a short sale till the sale transaction is formally declared as short sale transaction at the time of placing the order on the KATS trading system and fulfill the Short Sale Prerequisites as defined in Clause 5 of the Regulations for Short Selling under Ready Market, 2002.
13. After a detailed and thorough perusal of the facts, evidence/information available on record, contentions and averments made by the CEO during the course of the hearing, it is established that the Respondent has placed the sale orders in its client's accounts without having pre-existing interest. Further, placement of the sale orders without having pre-existing interest interfered with the fair and smooth functioning of the market and created misleading impression for the other investors. Thus the Respondent by executing sales in the client's account without pre-existing interest has violated the Regulations which in turn is violation of Code of Conduct set fourth under the third schedule of the Brokers Rules that makes it mandatory on the Respondent to execute its business with due care and skill. Therefore, keeping in view the aforementioned, it is evident to me that the Respondent has violated Clause A2 and A5 of the Code of Conduct of the Brokers Rules which in turn is a violation of Brokers Rules.
14. The violation of the Rules and Regulations is a serious matter which entitles the Commission to suspend the Respondent's membership but I have elected not to exercise this power at present. However, in exercise of the powers under Section 22 of the Ordinance, I hereby impose on the Respondent a penalty of Rs. 200,000 (Rupees Two Hundred Thousand only). I strongly advice the Respondent to take immediate measures and put in place proper checks and procedures to eliminate the occurrence of such instances in future. I again direct the Respondent to ensure that full compliance be made of all rules, regulations and directives of the Commission in the future for avoiding any punitive action under the law.



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15. The matter is disposed of in the above manner and the Respondent is directed to deposit the fine in the account of the Commission being maintained in the designated branches of MCB Bank Limited not later than thirty (30) days from the date of this Order and furnish the copy of the deposit challan to the undersigned.
16. This Order is issued without prejudice to any other action that the Commission may initiate against the Respondent in accordance with law on matters subsequently investigated or otherwise brought to the knowledge of the Commission.



Imrat Inayat Butt
Director (SM)

Announced on March 31, 2010
Islamabad.