



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

Securities Market Division

Surveillance, Supervision and Enforcement Department

F. No. SMD-/SSED-C&IW-(633)/2016

Dated: September 08, 2016

The Managing Director

Pakistan Stock Exchange Limited
Stock Exchange Building
Stock Exchange Road
Karachi

The President

The Institute of Chartered Accountants
of Pakistan
Chartered Accountants Avenue
Clifton, Karachi

The President

The Institute of Cost and Management Accountants
of Pakistan
ICMAP Building St-18/C, ICMAP Avenue
Block 6, Gulshan-e-Iqbal
Karachi.

SUBJECT: CLARIFICATION(S) ON CALCULATION AND REPORTING OF NET CAPITAL BALANCE

Dear Sir(s)

Net Capital Balance (NCB) as prescribed in Third Schedule read with Rule 2(d) of the Securities and Exchange (SEC) Rules, 1971 is a measure of financial soundness of a broker and determines the capacity of brokers to take exposure in capital markets; hence holds a great significance in the capital market industry. Therefore, it is imperative that consistent methods and treatment for computation of NCB are followed while computing and auditing the NCB Certificate.

The Securities and Exchange Commission of Pakistan (the Commission) has issued various clarifications to stakeholders including auditors / brokerage houses from time to time for proper computation of NCB in accordance with the requirements of Third Schedule read with Rule 2(d) of the SEC Rules, 1971. However, pursuant to promulgation of Securities Brokers (Licensing and Operations) Regulations, 2016, the brokers shall submit an audited statement of NCB on half yearly basis till the time a notification is issued by the Commission after which the requirement of submission of Liquid Capital shall be applicable.

For this purpose, the Commission has considered it appropriate to compile and issue a Guidebook in respect of various clarifications previously issued either individually, collectively or through feedback of stakeholders and has also included certain new clarifications to facilitate users to obtain necessary guidance and clarity in matters relevant to NCB. Any clarifications issued in the future will also be made part of the book.



SECURITIES & EXCHANGE COMMISSION OF PAKISTAN

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In view of the above, all brokerage houses of the Stock Exchange and their auditors appointed for audit of NCB are hereby directed to ensure compliance of the Clarifications in letter and spirit. Any violation or circumvention in calculation of NCB shall be dealt with under the provisions of the applicable laws.

The Stock Exchange, ICAP and ICMAP are requested to disseminate this letter under intimation to the Commission to all their members for compliance and record and the same shall also be placed on their respective website.

Further, SECP has developed below mentioned email ID to submit query if any, in respect of subject matter and/or query pertaining to newly promulgated Securities Brokers (Licensing and Operations) Regulations, 2016.

The email ID: auditors.queries@secp.gov.pk

Yours truly

Muhammad Tanveer Alam

Additional Director

Surveillance, Supervision and Enforcement Department

C.C:

1. The Chief Regulatory Officer, Pakistan Stock Exchange Limited
2. The Chief Executive Officer, National Clearing Company of Pakistan Limited
3. The Chief Executive Officer, Central Depository Company of Pakistan Limited

Enclosed: Guidebook on calculation and reporting of Net Capital Balance

Securities and Exchange Commission of Pakistan



SECURITIES MARKET DIVISION

SURVEILLANCE, SUPERVISION AND ENFORCEMENT DEPARTMENT (SSED)

GUIDEBOOK

IN RESPECT OF VARIOUS CLARIFICATIONS ISSUED BY THE COMMISSION FOR COMPUTATION
AND REPORTING OF NET CAPITAL BALANCE UNDER APPLICABLE LAWS

Dated: September 8, 2016



Securities & Exchange Commission of Pakistan
Securities Market Division
SSED (Compliance & Inspection Wing)

This Guidebook is a compilation of various clarifications or replies issued by the Securities and Exchange Commission of Pakistan in response to various queries raised by the stakeholders from time to time in calculating and reporting Net Capital Balance (NCB) of the brokerage house of Pakistan Stock Exchange (PSX) under applicable laws. All brokerage houses of the Stock Exchange and their auditors appointed for certification of NCB are hereby directed to ensure compliance of the Clarifications in letter and spirit.

The objective of these Clarifications is to facilitate respective stake holders in calculating and reporting the NCB. These guidelines do not override the primary requirements of the applicable law. In case of any inconsistency the requirements of applicable law shall prevail.



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CLARIFICATIONS

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<u>I.</u>	<u>CASH IN HAND AND BANK BALANCES</u>				
<u>A.</u>	<u>RESPONSES / CLARIFICATIONS ISSUED TO BROKERAGE HOUSES / AUDITORS ON ISSUES RAISED</u>				
1.1A	Cash deposited as Basic Deposits with Stock Exchanges and National Clearing Company of Pakistan Limited (NCCPL).	Whether cash deposited with Karachi Stock Exchange (KSE) and NCCPL may be incorporated as Cash and Cash Equivalent in Net Capital Balance (NCB) as these deposits are made by the Brokerage House out of their own funds.	Basic Deposits with Stock Exchanges and NCCPL are mandatorily required to be maintained for existence in a particular market and therefore, these are unrealizable, inconsumable and are not convertible into Cash or Cash Equivalent in normal course of business and are not withdrawn unless the Broker abandons Brokerage Business or a particular market. Hence, these items may not be included in NCB.	Clause 1.2 of Clarifications / Guidelines dated July 3, 2013 and December 20, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	July 15, 2013.
1.2A	Cash deposited as Margins with Stock Exchanges and NCCPL.	Whether deposits / margins collected by the Clearing House of the Exchange from Brokers as detailed below be included in NCB: Ready Market: <ul style="list-style-type: none"> • Deposit against exposure and losses; Futures DFC: <ul style="list-style-type: none"> • Deposit against exposure in DFC; • Deposit against losses in DFC; • Ready Profit DFC; • Deposit against exposure in SIFC; • Deposit against losses in 	Cash deposited with the Stock Exchange against exposures and Mark to Market (MTM) losses in Ready Market, Deliverable Futures Contract (DFC) Market, Cash-Settled Futures (CSF) Market, Stock Index Futures Contracts (SIFC) Market and Futures Trading in Provisionally Listed Companies Market represent Short Term outflows of funds from Broker to the Stock Exchange, therefore, may be classified under "Cash in hand and Bank Balances" for the purpose of calculation of NCB. However, profits retained by the	Clause 1.1 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	September 2, 2013.



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		SIFC; <ul style="list-style-type: none"> • Deposit against exposure in CSF; • Deposit against losses in CSF. <p><u>Futures Trading in Provisionally Listed Companies:</u></p> <ul style="list-style-type: none"> • Deposit against exposure; • Deposit against losses. 	Stock Exchange on Deliverable Futures Contract may not be classified under "Cash in hand and Bank Balances" for the purpose of calculation of NCB.		
1.3A	Clients' Bank Account Balance.	The Brokers are required to maintain exact client-wise bank balance and that the corresponding liability in respect of each such client has been reported in trade payables as on that reporting date of NCB. Therefore, no Broker should hold lesser amount in the client-wise bank balance report, however, seems that the wording rather also restricts that the client-wise bank balance report should not exceed the actual amount. This requirement seems excessive and beyond the spirit of the Rules.	If a Brokerage House in their NCB incorporates clients' bank balances in excess of trade creditors balance, it may indicate situations including the following: <p><u>Situation I:</u></p> <ul style="list-style-type: none"> • Corresponding trade creditors have not been recorded in their books of accounts; and / or <p><u>Situation II:</u></p> <ul style="list-style-type: none"> • Brokerage House has mingled its own cash funds with that of clients. Under Situation I, as stated above, where corresponding liability is not appearing as trade creditors in the books of accounts of a Broker, the NCB of that Broker may become overstated by that amount. Moreover, Situation II indicates contravention of requirements relating to segregation of clients' assets as prescribed in General Regulations of the Exchange.	Clause 1.5 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	September 5, 2013.



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1.4A	Clients' Bank Account Balance.	Whether there is a requirement to maintain bank account-wise break-up of clients funds as required for trade creditors.	<p>Rule Book of KSE requires Brokers to ensure that the assets belonging to their clients are kept separated from the assets of the Broker. For this purpose, the Broker is required to maintain separate bank account(s), with word "Clients" in the title, which will include all funds of their clients along with record / breakdown of clients' balances.</p> <p>The spirit of Guidelines and Rule Book of KSE is to safeguard clients' funds and avoid its misuse. In view of the above, it is clarified that the balance of bank account or the balances of bank account(s) maintained for the said purpose should match and / or reconcile with the trade payables maintained in back office record (client level and overall basis) on the reporting date.</p>	<ul style="list-style-type: none"> • Clause 1.5 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971. • Regulation 4.18.1(a) of the Rule Book of PSX. 	September 18, 2015.
1.5A	Clients' Bank Account Balance.	The client's bank account balance was in excess against trade payables balance. Resultantly, the Company has deducted the said excess amount from client's bank account and added back the same in the Company's bank balances for the purpose of NCB. However, the Guidelines are silent on considering the excess cash as part of the Company's bank balance.	<p>Balances of all bank accounts being maintained by the Brokerage House including bank account for clients' funds would be included for the purpose of NCB. Furthermore, the Brokerage Houses are also required to ensure that corresponding liability in respect of each such client has been reported in trade payables as on that reporting date for NCB.</p> <p>In order to ensure compliance of Regulatory Requirement, the</p>	Clause 1.5 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	October 28, 2015.



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			<p>balances are required to be reviewed / monitored regularly so that any required rectification in the books of accounts could be made on timely basis.</p> <p>In addition to other audit procedures that are applied on funds of the Brokerage House, the auditor must ascertain the following:</p> <ul style="list-style-type: none"> • Legal ownership of the funds; • Proper classification and disclosure of each fund in the statement of NCB; • Valuation and completeness of trade payables <p>With regard to your query pertaining to excess client's bank account balance, that as per your findings pertain to Brokerage House and has been transferred to clients' related bank account, it is clarified that the same may not be classified under "Client related Bank Account" for NCB purpose. If the auditor is satisfied that the funds are legally owned by the Brokerage House then they must be classified accordingly and included in NCB calculation.</p>		
1.6A	Clients' Bank Account Balance.	Client's bank balance should not exceed the corresponding trade payable client-wise and / or overall basis.	The spirit of the Law is to ensure protection of clients' assets and for that purpose the assets of the clients are required to be kept separated. The Brokers should not commingle those customers'	<ul style="list-style-type: none"> • Clause 1.5 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of 	December 11, 2015.



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			<p>assets with its own assets.</p> <p>PSX Rule Book requires Brokers to ensure that the assets belonging to their clients are kept separated from the assets of the Broker. For this purpose, the Broker shall maintain separate Bank Account(s), with word "Clients" in the title, which will include all funds of their Clients alongwith record / breakdown of clients' balances. It is, therefore, clarified that funds from clients, whether bearing receivables or payables, should directly be deposited into clients' bank account.</p> <p>In order to ensure compliance of Regulatory Requirement, the balances are required to be reviewed or monitored regularly so that any required rectification in the books of accounts could be made on timely basis. In case, aforesaid deposit results in excess balance in client bank account, a proper justification of the same alongwith reconciliation and documentary evidence should be made available for audit / verification / inspection purpose.</p> <p>If the funds are legally owned by the Brokerage House, then they may be classified and included accordingly in NCB calculation provided necessary corresponding adjustments, if required, is made in the balance of trade receivables and</p>	<p>Securities and Exchange Rules, 1971.</p> <ul style="list-style-type: none">• Regulation 4.18.1(a) of the Rule Book of PSX.• Section 78(1)(c) of Securities Act, 2015	



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			<p>completeness of trade payables are ensured and related documentary evidences are made available for audit / verification / inspection purpose.</p> <p>It is clarified that any shortage / excess in client bank balance, against unsettled trades, will not result in non-compliances of the Guidelines, since the said amount is receivable from / payable to NCCPL, thereby making an overall impact on NCB. However, proper reconciliation alongwith related documentary evidence of the same should be made available for audit / verification / inspection purpose.</p>		
<u>B. RESPONSES ISSUED TO PSX ON COMMENTS / RECOMMENDATIONS ISSUED BY THEIR BOARD</u>					
1.7B	Cash Deposited as Basic Deposits with Stock Exchanges and NCCPL.	Agreed with Broker's view to include basic deposits with Stock Exchanges and NCCPL in NCB calculations.	As per Rule 2(d) of SECP Rules "Net Capital" means excess of current assets over the liabilities determined in accordance with the Third Schedule to these Rules. The basic deposits with stock exchanges and NCCPL are mandatorily required to be maintained for existence in a particular market and therefore, these are unrealizable, inconsumable and are not convertible into cash or cash equivalent in normal course of business and are not withdrawn unless the broker abandons brokerage business or a particular market. The allowable current assets as provided under Third Schedule does not include	Clause 1.2 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	December 20, 2013.



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			<p>deposits and advances; hence subject matter may not be allowable.</p> <p>In view of above facts, basic deposits with KSE and NCCPL is not permissible for NCB purpose, however, it may be noted that impact of basic deposit on NCB is not material. For ready reference, information and details relating to basic deposits is illustrated below:</p> <ul style="list-style-type: none"> • Deposit with NCCPL for broker clearing member Rs 200,000; • Deposit with NCCPL for broker clearing member for BTB / MF facility Rs 100,000; • Security Deposit with NCCPL from Broker CFS Financier CM Rs 200,000; • Basic Deposit for Index Options Market Rs 25,000; • Basic Deposit for Futures Trading in Provisionally Listed Companies Market Rs 100,000; • Basic Deposit for Market Makers Rs 25,000; • Basic Deposit for Ready Market Rs 200,000. 		
1.8B	Term Deposit / Other Deposit Receipts with Banks.	A Commercial Bank enjoys favor of lien created over TDR. Hence, investment in such TDR on which third	The Third Schedule does not deal with long term assets; hence, investment classified in books of accounts as long term may not be	Clause 1.4 of Clarifications / Guidelines dated July 3, 2013 in respect of	December 20, 2013.



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		party lien has been created, may not be classified under "Cash in hand and bank balances."	included. TDR / other Deposit Receipts (DRs) having maturity of more than one year and / or having third party interest or lien may not be included. However, TDR / DRs reported under current assets and are pledged with bank for arranging Bank Guarantees for the Exchange or NCCPL may be allowed to be included as Cash and Cash Equivalents provided the said TDR / DRs are free from further lien or third party interest.	Third Schedule of Securities and Exchange Rules, 1971.	
2.	<u>TRADE RECEIVABLES</u>				
A.	<u>RESPONSES / CLARIFICATIONS ISSUED TO BROKERAGE HOUSES / AUDITORS ON ISSUES RAISED</u>				
2.1A	Other Assets (Commission Receivable).	Commission Receivable should not be excluded from NCB as Financial Institutions usually pay Commission once in a month.	Commission Receivable on account of activities related to Brokerage Business may be included in NCB. Accordingly, Commission Receivable not related to Brokerage Business may not be included in NCB.	Clause 2.8 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	July 15, 2013.
2.2A	Other Assets (Advance against investment or IPO)	Treatment of advance against investment or IPO outstanding as on June 30, 2014 for the purpose of calculation of NCB.	Advances fall under category of other assets. Under the Guidelines, it has been clarified that current asset items not prescribed in Third Schedule of SEC Rules should not be included for the purpose of calculation of NCB. Therefore, advance against investment or IPO appearing as on reporting date of NCB may not be allowable for calculation of NCB.	Clause 2.8 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	August 29, 2014.
2.3A	Other Assets (Advance	Treatment of advance	Advances falls under category of	Clause 2.8 of	



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	against investment or IPO)	against investment or IPO (inclusion of PPL subscription amount in NCB) outstanding as on June 30, 2014 for the purpose of calculation of NCB.	other assets and may not be classified as cash in hand and bank balances or Investment in listed securities in the name Brokerage House. Under the Guidelines, it has been clarified that current assets item not prescribed in Third Schedule of SEC Rules should not be included for the purpose of calculation of NCB. In view of the above, advance against investment or IPO appearing as on reporting date of NCB may not be allowable for calculation of NCB.	Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	September 19, 2014.
2.4A	Forex and money market commission	Section 2.7 of the SECP Clarification / Guidelines on NCB dated July 03, 2013 has disallowed to include the amount receivable other than brokerage business (such as consultancy income receivable) in the NCB calculation. Section 2.8 of the said guidelines further prescribes that "the current assets item not prescribed in the Third Schedule should not be included in NCB calculation including " commission Receivable". However, KSE notification bearing reference KSE/N-5049 dated September 23, 2013 has allowed including commission receivable in NCB calculation which	Brokerage commission related to activities carried out on PSX is only allowed for brokerage commission as stated against Sr. 2.1A above.	Clause 2.8 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971	September 08, 2016



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		was earlier disallowed under the point 2.8(4) of above mentioned guidelines.			
<u>B. RESPONSES ISSUED TO PSX ON COMMENTS / RECOMMENDATIONS ISSUED BY THEIR BOARD</u>					
2.5B	Receivable pertaining to Pakistan Mercantile Exchange Limited (PMEX).	Receivable pertaining to PMEX should be allowed for inclusion in NCB calculations because common Brokers are required to submit their NCBs with all Exchanges and PMEX, therefore, any verification in NCB calculations may attract undue additional cost.	<p>Calculation of NCB for PMEX purpose does not fall under Third Schedule, therefore, receivables pertaining to PMEX may not be included for calculating NCB under Third Schedule.</p> <p>In this regard it may further be noted that as per Para 6.1 of the Guidelines, all the liabilities relating to PMEX may be excluded if the current assets items such as trade receivables, deposit and bank balances pertaining to PMEX have been excluded. In view of the above, receivables from PMEX is required to be excluded for NCB as provided in para 2.4 of the Guidelines.</p> <p>However, if receivables balance from PMEX pertaining to clients' trading is included in NCB, the corresponding liabilities of PMEX's clients will be required to be classified in other liabilities to nullify the impact of said receivables from NCB.</p>	Clause 2.4 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	December 20, 2013.
<u>3. INVESTMENT IN LISTED SECURITIES IN THE NAME OF BROKERAGE HOUSE</u>					
<u>A. RESPONSES / CLARIFICATIONS ISSUED TO BROKERAGE HOUSES / AUDITORS ON ISSUES RAISED</u>					
3.1A	Investment classified in books of account as Long	Long term investment in listed securities in the name	The Third Schedule does not deal with non-current assets; hence	Clause 3.2 of Clarifications /	July 15, 2013.



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	Term.	of Brokerage House be included as disallowance seems to discourage long term investments.	investment classified in books accounts as long term may not be included.	Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	
3.2A	Details regarding Securities on exposure list.	Investment in cash funds of the mutual funds.	Investments made in units of cash funds as specified and declared by the stock exchange for margin eligible securities in respect of a specified period may be classified under "Investment in listed securities in the name of a Broker" for the purpose of calculation of NCB relating to said specified period after applying 15 percent discount as mentioned in the said Schedule.	Clause 3.1 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	September 2, 2013.
3.3A	Explanation of Terms, "Exposure list, tradable and listed securities	Types of securities that are allowed as investment in the name of broker	All listed and tradable securities are allowed under the head Investment in the name of broker. However, for the mutual fund, relevant clarifications will be followed.	Clause 3.1 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	September 08, 2016
3.4A	Investment classified in books of account as Long Term.	Investments in listed securities held for over the period of one year but not classified as long term.	The Third Schedule does not deal with non-current assets; hence investment classified in books of accounts as long term may not be included. However, investment in listed securities held for more than one year and classified as short term investments may be included in calculation of NCB if the said classification has not been made in contradiction with Generally Acceptable Accounting Principles and / or relevant Regulatory / Statutory	Clause 3.2 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	September 5, 2013.



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			requirement as applicable from time to time. However, any improper classification of long term investment into short term may not be allowed.		
3.5A	Details regarding Securities on exposure list.	Treatment of investment in mutual funds.	Under Third Schedule of SEC Rules, Investments in Listed Securities on the exposure list are allowable. Moreover, investments in securities that do not fall under the ambit of market tradable securities and / or have not been declared / specified by the Stock Exchange as margin eligible securities may not be allowed for the purpose of calculation of NCB. However, investments made in units of cash funds / open-end funds as specified and declared by the Stock Exchange for margin eligible securities in respect of a specified period may be classified under "Investment in Listed Securities in the name of a Broker" for the purpose of calculation of NCB relating to said specified period after applying 15 percent discount as mentioned in the Schedule.	Clause 3.1 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	September 5, 2013.
3.6A	Details regarding Securities on exposure list.	Investment in open-end mutual funds which are / are not reflected in CDC statement of the house account.	Investments in listed securities on the exposure list are allowable. Moreover, investments in securities that do not fall under the ambit of market tradable securities and / or have not been declared / specified by the Stock	Clause 3.1 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	March 14, 2014.



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			<p>Exchange as margin eligible securities may not be allowed for the purpose of calculation of NCB. However, Investments made in units of cash funds / open-end funds as specified and declared by the Stock Exchange for margin eligible securities in respect of a specified period may be classified under "Investment in Listed Securities in the name of a Broker" for the purpose of calculation of NCB relating to said specified period after applying 15 percent discount as mentioned in the said Schedule. In this regard reference may be made to KSE Notice dated July 12, 2013 regarding list of margin eligible securities whereby it has specified that electronic units of CDC eligible open-ended funds are accepted by the Exchange as collateral for all market.</p>		
3.7A	Details regarding Securities on exposure list.	Whether Shares appearing in House Account in pledge position in favor of Karachi Stock Exchange be included in calculation of NCB.	<p>It is clarified that:</p> <ul style="list-style-type: none"> • Shares are pledged with KSE as a part of normal business requirement and without any liability towards KSE; • Outstanding unsettled position with NCCPL and / or KSE is NIL and no claim / compliant whatsoever is pending against it as on relevant date; • Shares are owned by the Brokerage House and it can get these shares released from KSE at any time as the said shares are unused and free 	Clause 3.1 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	March 21, 2014.



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			<p>from any outstanding exposure demand as on relevant date.</p> <p>Based on facts and details stated above, the shares may be taken in calculation of NCB after applying 15 percent discount as mentioned in the said Schedule.</p>		
<u>B. RESPONSES ISSUED TO PSX ON COMMENTS / RECOMMENDATIONS ISSUED BY THEIR BOARD</u>					
3.8B	Investment classified in books of account as Long Term.	Considering the fact that in case of need this can be liquidated by the Broker, Board on RAC's recommendation agreed that same should be treated as liquid / current asset for this Regulatory purpose only.	The Third Schedule does not deal with non-current assets; hence investment classified in books of accounts as long term may not be included. However, investment in listed securities, which is classified as short term investments, and is held for more than one year may be included in calculation of NCB under Third Schedule of SECP Rules if the said classification has not been made in contradiction with Generally Acceptable Accounting Principles and / or relevant regulatory / statutory requirement as applicable from time to time. However, any improper classification of long term investment into short term may not be allowed.	Clause 3.2 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	December 20, 2013.
<u>C. ISSUES HIGHLIGHTED BY / SUGGESTIONS FROM AUDITORS</u>					
3.9C	Inclusion of mutual fund units for NCB purpose.	Mutual Fund Units (both open and closed end) be allowed for inclusion in NCB. Currently only closed end funds which are allowed by the exchange through margin eligible securities are	As per 3rd Schedule of SEC Rules 1971, listed securities declared as Margin Eligible Securities are permitted for inclusion in Net Capital Balance (NCB). Mutual Funds fulfilling the requirements of eligibility	Third Schedule of Securities and Exchange Rules, 1971.	September 08, 2016.



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		considered for NCB.	criteria (approved by the Commission) are included in NCB. For example: As per PSX Notice PSX/N-327 dated January 20, 2016, list of Securities include closed-end fund and open-end funds.		
4.	<u>VALUATION OF TRADE PAYABLES</u>				
A.	<u>RESPONSES ISSUED TO PSX ON COMMENTS / RECOMMENDATIONS ISSUED BY THEIR BOARD</u>				
4.1A	Overdue trade payables.	The Board was of the view that there has been a practice to treat trade payables over 30 days as effectively a part of equity and any immediate and non-transitional change will not be practically possible, therefore the Board considered that a mechanism be introduced where any amount held to be subordinated to other liabilities will remain outside the calculation for this purpose.	The Third Schedule deals with current assets and current liabilities therefore; question of subordinated loan does not arise. Moreover, the current practice with regard to trade payables over 30 days does not resemble with the treatment of trade receivables. The overdue trade receivables more than 14 days are excluded but securities against such overdue balance are allowable. Similarly, with regard to other liabilities the Third Schedule prescribe to include those items which are classified under Generally Accepted Accounting Principles. Therefore, trade payables more than 30 days are required to be included in other liabilities for calculating NCB.	Clause 6.1 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	December 20, 2013.
4.2A	Loan Account.	The Board was of the view that if trade payable overdue more than 30 days is addressed as recommended above then clients' deposits may not be the issue for	During onsite inspection of Brokerage Houses, the Commission has observed certain accounts in which only receipts and payments were recorded and no transaction relating to	Clause 6.3 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and	December 20, 2013.



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		treating them as other liability.	products traded on the Exchange were recorded. In most of the cases, the concerned Brokers accepted Commission's stance that such accounts are of loan nature and have given assurance to the Commission that in future such accounts will be classified as loan and not as trade creditors / debtors as the case may be.	Exchange Rules, 1971.	
5.	<u>VALUATION OF OTHER PAYABLES</u>				
A.	<u>RESPONSES / CLARIFICATIONS ISSUED TO BROKERAGE HOUSES / AUDITORS ON ISSUES RAISED</u>				
5.1A	Loan from Director(s).	Directors' Loan extended to Brokerage Houses are normally of long term nature, therefore, such loans fall under the category of "Sub-Ordinated Loan", hence, it should be classified and treated as long term liability under NCB statement.	<p>It is clarified that:</p> <ul style="list-style-type: none"> For the purpose of calculating NCB, Loan from Director to their Brokerage House, would be considered as long term loan if loan agreement executed on stamp paper, clearly reflects repayment after twelve months of the reporting period; Director's Loan or part of such Loan due to be payable within twelve months from the reporting period shall be classified as short term loan irrespective of its classification / disclosure in the books of accounts of the Brokerage House; In case of early repayment of long term loan from Director, the Brokerage House shall immediately report the transaction to the Stock Exchange for adjustment of 	Clarifications / Guidelines dated July 3, 2015 in respect of Third Schedule of Securities and Exchange Rules, 1971.	June 24, 2015.



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			<p>its trading exposure to that extent;</p> <ul style="list-style-type: none">• The Brokerage House, within 15 days of such repayment of Director's long term loan shall provide to the Stock Exchange, a fresh NCB certificate duly certified by the auditor.		
5.2A	Advance against share or conversion of short term payables in to advance against shares	It is observed that advance against shares is shown in the books of accounts as long term liability. However, the analysis of the same shows that there are no underlying documentary evidences / regulatory approvals to substantiate classification of current liability into non-current liability.	<p>It is clarified that classification or treatment of advance against shares as long term or non-current may be allowed subject to verifications only if;</p> <ol style="list-style-type: none">The existing authorized capital allows the proposed enhanced capital and advance against thereof.Board of directors has approved such enhancement of paid up capital.Relevant regulatory approvals/compliance has been ensured by the broker.Advance is not unnecessarily prolonged and/or all regulatory requirements for increase in capital have been completed at the time of audit.Auditor/broker is satisfied that such advance is against the increase of capital.	Third Schedule of Securities and Exchange Rules, 1971.	September 08, 2016



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<u>B.</u> <u>RESPONSES ISSUED TO PSX ON COMMENTS / RECOMMENDATIONS ISSUED BY THEIR BOARD</u>					
5.3B	Loan from Director(s).	The Board on RAC's recommendation agreed that Loan from Directors classified as long term loan in the books of Broker should be allowed provided Broker must report to the Exchange if the same is repaid any time before next NCB review. The Exchange will be required to reduce the paid liability form the NCB of the Broker immediately in the event of repayment.	The Commission during onsite inspection noted instances that frequent receipts / payments transactions were recorded in Directors' Loan account during current period as well as in subsequent period but such account was classified as long term and thus excluded from NCB. The purpose of the Guidelines issued by the Commission was to prevent misuse, malpractices and wrong interpretation. Moreover, in this connection reference may also be made to Para 72 of IAS-1 which prescribes as follows: <i>"72 An entity classifies its financial liabilities as current when they are due to be settled within twelve months after the reporting period, even if:</i> <i>(a) The original term was for a period longer than twelve months, and</i> <i>(b) An agreement to refinance, or to reschedule payments, on a long-term basis is completed after the reporting period and before the financial statements are authorised for issue".</i>	Clause 7.1 of Clarifications / Guidelines dated July 3, 2013 in respect of Third Schedule of Securities and Exchange Rules, 1971.	December 20, 2013.
<u>6.</u> <u>FORMAT OF CERTIFICATION</u>					
<u>A.</u> <u>ISSUES HIGHLIGHTED BY / SUGGESTIONS FROM AUDITORS</u>					
6.1A	Verified / audited NCB	PSX circular Notice No.	Pursuant to promulgation of	Regulation 6(4)	



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	certificate.	KSE/N-4163 of PSX dated August 29, 2002 / Rule book needs to be revisited which requires verified / audited NCB certificate. As per auditors, this is not an audit assignment.	Securities Brokers (Licensing and Operations) Regulations, 2016, securities brokers are required under Regulation 6(4) to submit an audited statement of net capital balance (NCB) on half yearly basis. Accordingly, audited NCB will be submitted in future.	Securities Brokers (Licensing and Operations) Regulations, 2016.	September 08, 2016
<u>7.</u>	<u>OTHERS</u>				
7.1	Adjusting entries amongst close family members etc.	Various adjustments made in one account to other account of the clients of a brokerage house. In this regard the brokerage house responded that these accounts pertain to close family members.	It is clarified that adjustment is only allowed if beneficiary is same person having different trading accounts. In this regard, written request of client will be maintained by the Broker.	-	September 08, 2016.