

SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

Islamabad, the 3rd of June, 2010

NOTIFICATION

S.R.O(I) /2010. The following draft Securities (Margin Financing, Lending, Borrowing and Pledging) Rules, 2010, proposed to be made by the Federal Government in exercise of the powers conferred by section 33 of the Securities and Exchange Ordinance, 1969 (XVII of 1969), read with section 16 thereof, and clause (b) of section 43 of the Securities and Exchange Commission of Pakistan Act, 1997 (XLII of 1997), are hereby published for the information of all persons likely to be affected thereby, and notice is hereby given that the draft will be taken into consideration after thirty days of its publication in the Official Gazette.

CHAPTER,- I – PRELIMINARY

1. Short title and commencement.- (1) These rules shall be called the Securities (Margin Financing, Lending, Borrowing and Pledging) Rules, 2010.

(2) They shall come into force at once.

2. Definitions.— (1) In these Rules, unless there is anything repugnant in the subject or context,-

(a) "authorized intermediary" means a stock exchange, central depository or clearing company registered with the Commission under these rules;

- (b) “authorized financier” means such person registered and allowed under these rules to provide margin financing;
- (c) "borrower" means a person who borrows securities under these rules through an authorized intermediary;
- (d) “clearing company” means a company registered as a clearing house under the Clearing Houses (Registration and Regulation) Rules, 2005;
- (e) “Commission” means the Securities and Exchange Commission of Pakistan established under the Securities and Exchange Commission of Pakistan Act, 1997 (XLII of 1997);
- (f) “finanee” means the person availing the facility of margin financing;
- (g) "lender" means a person who makes securities available with an authorized intermediary for the purpose of lending;
- (h) “margin financing” means extension or maintenance of credit for the purpose of purchasing or carrying any security through an authorized intermediary;
- (i) “margin financing agreement” means an agreement executed between the authorized financier and the finanee for the purpose of margin financing;
- (j) “Ordinance” means the Securities and Exchange Ordinance, 1969 (XVII of 1969);
- (k) “securities lending and borrowing” means lending of securities by the lender and borrowing of securities by the borrower, through the platform provided by the authorized intermediary; and
- (l) “spot period” means the trading period as notified by the stock exchanges prior to the commencement of book closure date.

(2) All other words and expressions used, but not defined in these rules, shall have the same meanings as are assigned to them under the Ordinance, the Companies Ordinance, 1984 (XLVII of 1984), and the Central Depositories Act, 1997 (XIX of 1997).

CHAPTER.- II. - AUTHORIZED INTERMEDIARIES

3. Authorized intermediary.- (1) The Commission shall determine the number and places for the establishment of authorized intermediaries.

(2) A stock exchange, central depository or clearing company desirous of providing a platform to facilitate the activities of margin financing and securities lending and borrowing may make an application to the Commission for the purpose of acting as an authorized intermediary.

(3) The application under sub-rule (2) shall be accompanied by,-

- (a) documents showing that satisfactory internal controls and written compliance procedures are available to act as authorized intermediary for margin financing and securities lending and borrowing;
- (b) documents showing that adequate financial, technical, organizational and human resources are available to facilitate the activity of margin financing

and securities lending and borrowing in a proper and efficient manner, on an ongoing basis;

- (c) the fee specified by the Commission; and
- (d) such other document as may be required by the Commission.

(4) Upon receipt of the application under sub-rule (2) and the documents and fee specified under sub-rule (3), the Commission, if satisfied that -

- (a) the applicant is eligible for acting as authorized intermediary;
- (b) the applicant is in compliance with all applicable regulatory requirements; and
- (c) it is in the interest of the capital market for the applicant so to do,

may register the applicant as an authorized intermediary in the manner specified Form I to these rules.

4. Suspension of registration of authorized intermediary.- (1) The Commission may by an order in writing suspend the registration of an authorized intermediary, if-

- (a) the Commission, on reasonable grounds, believes that such action is in the best interest of the capital market;
- (b) the authorized intermediary fails to comply with the provisions of the Ordinance, these rules, any regulations or any directive or circular given by the Commission;
- (c) the authorized intermediary does not furnish the information required by

the Commission or furnishes wrong or false information; or

- (d) the authorized intermediary does not cooperate in any enquiry or inspection conducted by the Commission.

(2) The order of the Commission suspending the registration of the authorized intermediary shall state the period of suspension and such period may be extended by the Commission upon the expiry of the initial period of suspension.

(3) The Commission while suspending the registration of an authorized intermediary may impose such restrictions and conditions, as it deems proper, on the authorized intermediary.

5. Cancellation of registration of Authorized Intermediary.- The Commission may cancel the registration of an authorized intermediary after providing an opportunity of hearing to the authorized intermediary, if-

- (a) the cause of suspension of registration under rule 4 continues during the period of suspension or extension thereof, if any;
- (b) the authorized intermediary does not pay the penalty, if any, imposed by the Commission;
- (c) the Commission determines that cancellation of registration will be in the best interest of the capital market;
- (d) a court of competent jurisdiction passed a winding up order of the authorized intermediary;
- (e) the Commission, on reasonable grounds, believes that any other entity will

perform the functions of the authorized intermediary in a better and effective manner;

- (f) the authorized intermediary does not comply with the restrictions or conditions imposed by the Commission at the time of suspension; or
- (g) the authorized intermediary request the Commission, on reasonable grounds, to cancel its registration.

6. Conditions applicable to authorized intermediary.- An authorized intermediary shall,-

- (a) provide a platform to facilitate the activity of margin financing and securities lending and borrowing and modules to facilitate the activity and ensure that the requirements of these rules and the requirements specified by the Commission and directions of the Commission are being complied with;
- (b) ensure that a fair, transparent and efficient system for the activity of margin financing and securities lending and borrowing is provided;
- (c) ensure that the risks associated with providing the facility of margin financing and securities lending and borrowing are managed prudently;
- (d) ensure that systems and procedures developed by it for providing the facility of margin financing and securities lending and borrowing are effective;
- (e) correctly record all transactions relating to margin financing and securities lending and borrowing;
- (f) submit to the Commission such periodic returns and information as specified by the Commission;

- (g) correctly disclose such information as specified by the Commission, to the public relating to the activity of margin financing and securities lending and borrowing;
- (h) collect and maintain margins as specified by the Commission;
- (i) ensure that the total margin financing provided by an authorized financier at any point in time, in a particular security, or to a single finantee, does not exceed the limits specified by the Commission;
- (j) ensure that total lending by a lender or borrowing by a borrower at any point in time, in a particular security, or to a single lender or borrower, or client, does not exceed the limits specified by the Commission;
- (k) correctly provide information to the Commission;
- (l) cooperate in any enquiry or inspection conducted by the Commission; and
- (m) comply with such other condition as may be specified by the Commission.

CHAPTER.- III - MARGIN FINANCING

7. Eligibility criteria for authorized financier.- A person shall be eligible to apply for registration as an authorized financier, if such person, -

- (a) is-
 - (i) a broker;

(ii) Scheduled bank licensed under the Banking Companies Ordinance, 1962 (LVII of 1962), with a minimum credit rating as specified by the Commission;

(iii) a financial institution covered under section 3A of the Banking Companies Ordinance, 1962 (LVII of 1962); or

(iv) such other person as the Commission may, through circular from time to time, notify.

- (b) meets the minimum net capital and capital adequacy requirements specified by the Commission;
- (c) has financial, technical, organizational and human resources for extension or maintenance of credit for the purpose of purchasing or carrying any security;
- (d) is not in default of any regulatory requirement;
- (e) has not been convicted of any fraud or criminal offence or has been penalized for any offence;
- (f) has not been subject to any adverse findings in an inquiry or investigation;
- (g) is not undergoing any proceedings with respect to winding-up or insolvency;
- (h) has trading rights, the rights have not been suspended;
- (i) is a CDC Participant, eligibility of such person as a participant has not been suspended;
- (j) is a clearing member of a clearing company, eligibility of such person as a clearing member has not been suspended; and

(k) meets any other requirement specified by the Commission.

8. Registration of authorized financier.- (1) A person eligible for registration under rule 7 shall make an application to the authorized intermediary for registration along with the following documents,namely:-

- (a) documents showing that the requirements of rule 7, clauses (a), (b) (c), (g), (h), (i) and (j) have been fulfilled;
- (b) an affidavit, in the manner specified in Form-II to these rules, that the applicant is not in violation of the requirements of rule 7, clauses (d), (e) and (f);
- (c) in the case of a company, a copy of the latest audited financial statement or in the case of an individual a copy of the income tax return as submitted to the Federal Board of Revenue;
- (d) application fee as specified by the Commission; and
- (e) any other document specified or required by the Commission.

(2) If the authorized intermediary is satisfied that the eligibility criteria under rule 7 has been satisfied and the documents required under rule 8 have been submitted, the authorized intermediary shall register the applicant as an authorized financier.

Explanation- For the purpose of clause (b) of sub-rule (1) where the applicant is a body corporate the deponent shall be the company secretary or equivalent of the applicant, and where the applicant is a natural person the deponent shall be the applicant himself.

9. Restriction of activities of authorized financier. (1) The authorized intermediary shall immediately restrict an authorized financier from the activity of margin financing if the authorized financier,-

(a) after registration is not in compliance with the eligibility conditions specified in rule 7; or

(b) is in violation of any provision of these rules,

and the authorized intermediary shall immediately notify the Commission of the restriction.

(2) Where the authorized intermediary fails to restrict an authorized financier under sub-rule (1), the Commission shall restrict the activities of the authorized financier.

10. Cancellation of registration of authorized financier.- The authorized intermediary shall after providing an opportunity of hearing to the authorized financier cancel the registration of an authorized financier,-

(a) if the cause of restriction under rule 9 continues for more than 45 days;

(b) the authorized financier does not furnish the information required by the Commission or furnishes wrong or false information;

(c) does not cooperate in any enquiry or inspection conducted by the Commission;

(d) a court of competent jurisdiction passed a winding up or liquidation order of the authorized financier; or

- (e) the Commission directs the authorized intermediary to cancel the registration of the authorized financier on the grounds stated in the direction.

11. Conditions applicable to authorized financier. (1) An authorized financier shall, -

- (a) only extend margin financing to finance purchases or carrying securities in respect of trades carried out on a stock exchange;
- (b) not extend financing without first executing a margin financing agreement which shall *interalia* contain provisions prescribed in Form IV to these rules;
- (c) at all times comply with all directives or circulars as may be issued by the Commission; and
- (d) ensure that true and correct information is passed on to the authorized intermediary.

12. Conditions applicable to brokers who are authorized financier.- (1) In addition to the provisions of rule 11, a broker who is registered as an authorized financier shall also comply with the following conditions, -

- (a) the broker may use his own funds for the purpose of providing margin financing or borrow funds from financial institutions approved by the Commission;
- (b) the broker shall not use the funds of any client for providing margin financing to another client or for proprietary account;

- (c) the broker shall not extend financing for purchases of securities which are not through the platform provided by the authorized intermediary; and
- (d) the broker shall not extend margin financing to any client without evaluating the creditworthiness of the client through a credit risk assessment system.

13. Regulatory requirements for Margin Financing.- The Commission shall through directives or circulars specify the following matters, namely:-

- (a) the selection criteria, including the minimum liquidity requirements, for securities for which margin financing can be obtained;
- (b) risk management systems;
- (c) the limits under which margin financing may be obtained by a broker for its proprietary position, by a single client of a broker or by all the clients of a single broker, or by the broker collectively for proprietary trading and trading for client, at any point of time in a particular scrip;
- (d) the limit beyond which the collective outstanding balances of margin financing obtained by the clients of a broker, including margin financing obtained by the broker for proprietary trading shall not exceed;
- (e) the manner in which the percentage of the total value of securities financed under margin financing as equity participation shall be paid by the financee;

- (f) suspension or disciplining of authorized financier for conduct inconsistent with just and equitable principles in connection with providing margin financing;
- (g) terms and conditions under which margin financing may be provided;
- (h) with respect to the recording and publishing of details of margin financing by the authorized intermediary;
- (i) with respect to the fee and charges payable for facilities and services provided for margin financing by the authorized intermediary;
- (j) reporting details relating to margin financing from authorized financier and such brokers who are financees; and
- (k) any other matter as deemed necessary for the effective enforcement and regulation of these rules.

CHAPTER,- IV - SECURITIES LENDING AND BORROWING

14. Eligibility criteria for securities lender and borrower.- (1) A person shall be eligible to apply for registration as a securities lender and borrower if such person, -

- (a) is,
 - (i) a broker;
 - (ii) financial institutions approved by the Commission; or
 - (iii) such other person as the Commission may specify through a circular;

- (b) meets the minimum net capital and capital adequacy requirements specified by the Commission;
- (c) is not in default of any regulatory requirement;
- (d) has no pending enquiries and has not been convicted of any fraud;
- (e) is not undergoing any proceedings with respect to winding-up or insolvency;
- (f) has trading rights, the rights have not been suspended;
- (g) is a CDC participant, eligibility of such person as a participant has not been suspended;
- (h) is a clearing member of a clearing company, eligibility of such person as a clearing member has not been suspended; and
- (i) meets any other requirement specified by the Commission.

15. Registration of a securities lender and borrower.- (1) A person eligible for registration under rule 14 shall make an application to the authorized intermediary for registration along with the following documents, namely:-

- (a) documents showing that the requirements of rule 14, clauses (a), (b), (f), (g), (h) and (i) have been fulfilled;
- (b) an undertaking, in the manner specified in Form-III to these rules, that the applicant is not in violation of the requirements of rule 14, clauses (c), (d), and (e);
- (c) in the case of a company, a copy of the latest audited financial statement or in the case of an individual a copy of the income tax return as submitted to the Federal Board of Revenue;

- (d) application fee as specified by the Commission; and
- (e) any other document specified or required by the Commission.

(2) If the authorized intermediary is satisfied that, the eligibility criteria under rule 14 has been satisfied and the documents required under rule 15(1) have been submitted, the authorized intermediary shall register the applicant as a securities lender and borrower.

Explanation:- For the purpose of clause (b) of sub-rule (1) where the applicant is a body corporate, the deponent shall be the company secretary or equivalent of the applicant, and where the applicant is a natural person, the deponent shall be the applicant himself.

16. Restriction of activities of a securities lender and borrower. (1) The authorized intermediary shall immediately restrict a securities lender and borrower from the activity of securities lending and borrowing if the securities lender and borrower,-

- (a) after registration is not in compliance with the eligibility conditions specified in rule 14; or
- (b) is in violation of any provision of these rules;

and the authorized intermediary shall immediately notify the Commission of the restriction.

(2) Where the authorized intermediary fails to restrict a securities lender and borrower under sub-rule (1) of rule 16, the Commission shall restrict the activities of the securities lender and borrower.

17. Cancellation of registration of a securities lender and borrower.- The authorized intermediary shall, after providing an opportunity of hearing to the securities lender and borrower, cancel the registration of the securities lender and borrower,-

- (a) if the cause of restriction under rule 16 continues for more than forty-five days;
- (b) the securities lender and borrower does not furnish the information required by the Commission or furnishes wrong or false information;
- (c) does not cooperate in any enquiry or inspection conducted by the Commission;
- (d) a court of competent jurisdiction passed a winding up or liquidation order of the securities lender and borrower; or
- (e) the Commission directs the authorized intermediary to cancel the registration of the securities lender and borrower on the grounds stated in the direction;

18. Conditions applicable to securities lender and borrower.-(1) A securities lender and borrower shall, -

- (a) only lend or borrow securities through the platform provided by the authorized intermediary;
- (b) not lend or borrow securities for own benefit or on behalf of a customer, whether directly or indirectly, of any company where the such lender and borrower or the customer is,
 - (i) a director or sponsor;
 - (ii) an associated company and associated undertaking;

- (iii) a shareholder who is barred from selling such securities; or
- (iv) any other person as may be specified by the Commission;
- (c) be eligible to lend or borrow any security or arrange for lending or borrowing of any security for his own benefit or in the case of a broker registered as a securities lender and borrower on behalf of its clients;
- (d) at all times comply with all directives or circulars as may be issued by the Commission; and
- (e) ensure that true and correct information is passed on to the authorized intermediary.

(2) All Securities lending and borrowing contracts shall be forced released on the working day before the start of a spot period relating to that security and lenders and borrowers shall not lend or borrow securities during the spot period.

19. Regulatory requirements for securities lending and borrowing.- The Commission shall through directives or circulars specify the following matters, namely:-

- (a) risk management systems, including but not limited to collateral and margin requirements, exposure margins, position limits, collection of mark to market losses, forms of deposits, etc. ;
- (b) the manner in which a securities lender and borrower shall put in place a system whereby the-
 - (i) lender agrees to deposit the specific number and class of securities with the authorized intermediary for lending the same to the borrower, against an agreed rate of return; and

- (ii) borrower agrees to borrow specific number and class of securities and to return the same to the authorized intermediary, for onward transfer to the lender, together with the agreed return.

- (c) selection criteria for securities which shall be available for lending and borrowing;
- (d) the manner in which the margins including marked-to-market losses shall be deposited by the lender and borrower;
- (e) terms and conditions under which securities lending and borrowing may be provided;
- (f) with respect to the recording and publishing of details of securities lending and borrowing;
- (g) with respect to the fee and charges payable for facilities and services provided for securities lending and borrowing; and
- (h) any other matter as deemed necessary for the effective enforcement and regulation of these rules.

CHAPTER.- V - PLEDGING

21. Conditions applicable for pledge of securities.- No broker shall pledge or deposit any security on account of a client as collateral except as provided below, namely:-

- (a) the pledge is in favour of or with a stock exchange or a clearing company in respect of margin requirements relating to the transactions or trades of such client as required under the relevant regulatory framework;
- (b) the pledge is in favour of or with a financial institution in respect of margin financing extended by such financial institutions in respect of transactions of such clients under the margin financing facility or any other form of financing as allowed by the Commission;
- (c) the pledge is in favour of or with a financial institution to borrow funds, provided that the client has authorized the broker in the manner specified by the Commission; and
- (d) the pledge is for any other purpose as permitted under applicable laws and regulations, provided the client has authorized the broker in the manner specified by the Commission.

PART,- VI - GENERAL

22. Power of the Commission to issue directives, circulars, etc. - (1) The Commission may issue such directives, circulars, etc. as are necessary to carry out the purposes of these rules.

- 23. Prohibition.-** No person shall carry on any activity, or purport to do so, which is covered under these rules except in accordance with the provisions of these rules or any directives or circulars issued by the Commission.
- 24. Penalty.-** If any person contravenes or fails to comply with any provision of these rules, the Commission may, in addition to any action authorized under these rules, impose upon such person a penalty under the Ordinance, for violations of these rules.
- 25. Recession ..-** The Margin Trading Rules, 2004 are hereby rescinded.

FORM I

[See Rule 3(4)]

SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

**CERTIFICATE OF REGISTRATION
AUTHORIZED INTERMEDIARY**

In exercise of the powers conferred by rule 3 of Securities (Margin Financing, Lending, Borrowing and Pledging Rules, 2010 the Securities and Exchange Commission of Pakistan hereby grants a certificate of registration to _____, as an Authorized Intermediary subject to the conditions prescribed under the Securities (Margin Financing, Lending, Borrowing and Pledging Rules, 2010 or as may be specified or imposed hereafter by the Commission.

The registration number of the authorized intermediary is _____.

Dated: _____

Place: ISLAMABAD

By order

Sd/-

For and on behalf of

THE SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

FORM II

[See rule 8 (1) (b)]

AFFIDAVIT

Before the Securities and Exchange Commission of Pakistan

Affidavit of _____ son of _____ resident of _____ and holding CNIC/Passport No. _____

I the above named deponent, do hereby solemn affirm and state on oath as under:-

1. That I am the company secretary of _____, and I am well conversant with the facts deposed below. (Where the application is by a body corporate).
2. _____(Name of the applicant) is not in default of any regulatory requirement.
3. _____(Name of the applicant) has not been convicted of any fraud or criminal offence or has been penalized for a civil offence nor has been subject to any adverse findings in an inquiry or investigation .
4. _____(Name of the applicant) is not undergoing any proceedings with respect to insolvency.
5. The statements made and the information given along with the application under rule 8 of the Securities (Margin Financing, Lending, Borrowing and Pledging Rules, 2010 is correct and that there are no facts which have been concealed.
6. That I have no objection if the Securities and Exchange Commission of Pakistan requests or obtains information about me from any third party.
7. That all the documents provided to Securities Exchange Commission of Pakistan are true copies of the originals.

DEPONENT

The Deponent is identified by me

Signature _____
ADVOCATE
(Name and Seal)

Solemnly affirmed before me on this _____ day of _____ at _____ by the Deponent above named who is identified to me by _____, Advocate.

Signature _____
OATH COMMISSIONER FOR TAKING AFFIDAVIT
(Name and Seal)

FORM III
[See rule 15(1) (b)]

AFFIDAVIT

Before the Securities and Exchange Commission of Pakistan

Affidavit of _____ son of _____ resident of _____ and holding CNIC/Passport No. _____

I the above named deponent, do hereby solemn affirm and state on oath as under:-

8. That I am the company secretary of _____, and I am well conversant with the facts deposed below. (Where the application is by a body corporate)
9. _____(Name of the applicant) is not in default of any regulatory requirement.
10. _____(Name of the applicant) has not been convicted of any fraud or criminal offence or has been penalized for a civil offence nor has been subject to any adverse findings in an inquiry or investigation;
11. _____(Name of the applicant) is not undergoing any proceedings with respect to insolvency.
12. The statements made and the information given along with the application under rule 15 of the Securities (Margin Financing, Lending, Borrowing and Pledging Rules, 2010 is correct and that there are no facts which have been concealed.
13. That I have no objection if the Securities and Exchange Commission of Pakistan requests or obtains information about me from any third party.
14. That all the documents provided to Securities Exchange Commission of Pakistan are true copies of the originals.

DEPONENT

The Deponent is identified by me

Signature _____
ADVOCATE
(Name and Seal)

Solemnly affirmed before me on this _____ day of _____ at _____ by the Deponent above named who is identified to me by _____, Advocate.

Signature _____
OATH COMMISSIONER FOR TAKING AFFIDAVIT
(Name and Seal)

