



National Clearing Company of Pakistan Limited

8th Floor, Pakistan Stock Exchange Building, Stock Exchange Road, Karachi

NCCPL/CM/OCTOBER-20/11

October 23, 2020

Implementation of Close-Out mechanism in Deliverable Future Contract (DFC) Market

Dear Market Participants,

This is in continuation to our earlier circulars No. NCCPL/CM/MARCH-20/07 dated March 04, 2020 & NCCPL/CM/OCTOBER-20/10 dated October 22, 2020 regarding approved amendment in NCCPL Regulations 2015 (Annexure 'A') and National Clearing & Settlement System "NCSS" Procedures 2018 ((Annexure 'B') respectively (attached herewith for ready reference) regarding implementation of close-out mechanism in DFC Market.

In this respect, all Market Participants are hereby informed that necessary system development has been completed at National Clearing Company of Pakistan Limited and Pakistan Stock Exchange end and will be implemented effective from November 9, 2020.

This for information and record of the Market Participants.

For any further queries or concerns, please feel free to contact the Customer Support Department at UAN No. 021-111-111-622.

Regards,

Sd

Muhammad Asif
Head of Operations

CC:

- 1. Executive Director/HOD - Policy, Regulation and Development Department - SMD
Securities & Exchange Commission of Pakistan - Islamabad**
- 2. Chief Executive Officer - Pakistan Stock Exchange Limited**
- 3. Chief Executive Officer - Central Depository Company of Pakistan Limited**
- 4. Chief Executive Officer - Mutual Fund Association of Pakistan**
- 5. Chairman - Pakistan Banking Association**

**APPROVED AMENDMENTS IN NCCPL REGULATIONS, 2015 PERTAINING TO
CLOSE-OUT MECHANISM OF DELIVERABLE FUTURE CONTRACT MARKET**

Approved Regulations

**CHAPTER 13: MONEY DEFAULT MANAGEMENT (OTHER THAN TRADE-FOR-TRADE
SETTLEMENT)**

13.2.6 The Final loss of the Suspended Clearing Member shall be determined after utilizing of and application of the funds realized by the Company through squaring-up / closing-out of the Suspended Clearing Member's unsettled Balance Orders and Positions and liquidation and encashment of Margins, as above stated.

However, in case where Suspended Clearing Member is also a Trading Financier, the settlement obligation pertaining to the MT Market and MT Financed Securities held in Blocked Status of such suspended Trading Financier shall be dealt in accordance with the Regulation 7C.6.14-1 and Chapter 12 of these Regulations. In case where such Suspended Clearing Member is also a Finantee in MT Market, the settlement obligation pertaining to the MT Market shall be dealt in accordance with the Regulation 7C.6.14-21 and Chapter 12 of these Regulations.

Whereas, in case such Suspended Clearing Member is also a MF Participant in MF Market, the settlement obligation pertaining to the MF Market shall be dealt in accordance with the ~~Regulation 7B.10~~ **Chapter 7B** and Chapter 12 of these Regulations.

The relevant provisions of the Procedures dealing with squaring-up / closing-out process are contained in Chapter 4 of the Procedures except in case of Position in Deliverable Future Contracts "DFC" following additional measures will be taken to square-up or close-out the Position of the Suspended Clearing Member in DFC:

- a. **The Position in DFC (buy or sell positions) shall be liquidated in the Market by placing only reverse orders of open Position through Trading ID of Suspended Clearing Member in an un-disclosed manner through Deliverable Future Contract market. The liquidation of Position through this mechanism will be initiated on the day of default or next Business Day from the day of default;**
- b. **Where the Position in DFC is not fully liquidated after applying the mechanism explained in point (a) above, the remaining Position in DFC shall be squared-up through an open auction session through the Exchange by offering the market participants DFC Position of Suspended Clearing Member at such auction price as prescribed under the Procedures. The maximum auction price may be set at a discount of 15% less than the Closing Price of the DFC on the last Business Day before the open auction. The remaining Position in DFC shall be squared-up using this option on the next Business Day or second Business day, as the case may be, from the day of default during business hours, the mode and manner of the auction shall be as per the regulations of the Exchange and as prescribed in Procedures;**
- c. **Where the Position in DFC is not fully squared-up after applying the mechanism explained in point (a) and (b) above, the Company shall close – out the Position of the Suspended Clearing Member in DFC at the close-out price computed in the manner prescribed in the Procedures. As a consequence of the close-out of the Position in DFC of the Suspended Clearing Member, the Company, to the extent practicable, shall allocate among the Clearing Accounts of the non-defaulting Clearing Members the closed-out DFC position on a pro-rata basis in the manner prescribed in Procedures. The remaining Position in DFC shall be closed-out using this option on the second Business day from the day of default.**

Annexure – A

Upon determination of a Suspended Clearing Member's final loss, a loss notice demanding payment during the banking hours on the next **third** Business Day **of default** shall be served on the Suspended Clearing Member, by the Company in accordance with these Regulations. Copies of the loss notice shall be sent to the Exchange and the CDC. On non-compliance of any such notice, the Company shall declare such Clearing Member as a defaulter (hereinafter in this Chapter referred to as the "Defaulter Clearing Member") and the Company shall terminate the Defaulter Clearing Member's admission to NCC Systems and his access to the services offered by the Company. The Company shall serve a notice declaring the Clearing Member as a defaulter to the Defaulter Clearing Member, the Exchange, all Clearing Members, CDC and the Commission.

13.2.9 After the Company's declaration of a Non-Broker Clearing Member as a Defaulter, all the assets of such defaulting Non-Broker Clearing Member under the control of the Company shall be liquidated by the Company and the proceeds shall be made available to meet any shortfall in the replenishment of SGF.

~~The Company shall not be liable towards a Clearing Member or any of its client in the event that it takes any action as prescribed under clause 13.2 of this Chapter which is taken as a result of a Clearing Member's failure to settle its money obligations, Margin and Mark to Market Losses, including but not limited to, actions taken by the Company to satisfy a Clearing Member's net money obligations. For the avoidance of doubt, no suit or claim shall lie against the Company in this regard.~~

13.3 The Company shall not be liable towards a Clearing Member or any of its client in the event that it takes any action as prescribed under **clause 13.2 of this Chapter of the Regulations** which is taken as a result of a Clearing Member's failure to settle its money obligations, Margin and Mark-to-Market Losses, including but not limited to, actions taken by the Company to satisfy a Clearing Member's net money obligations. For the avoidance of doubt, no suit or claim shall lie against the Company in this regard.

15.1.1 When the Company takes any action in respect of a NCC Participant pursuant to Chapter 18 (RESTRICTION, SUSPENSION OR TERMINATION OF ACCESS TO SERVICES OFFERED BY THE COMPANY), it shall provide to that NCC Participant with a notice to this effect and general notice to all NCC Participants, the Exchange, Commission and CDC of the action taken by the Company. Such notice shall also be placed on the Company's website preferably on the same day on which the action is taken. ~~In addition to the above, the Company shall also provide above referred notice to the eligible UIN Holders who have subscribed for UIN Information Systems in accordance with Regulation 9.12.~~

In addition to the above, the Company shall also provide above referred notice to the eligible UIN Holders who have subscribed for UIN Information Systems in accordance with Regulation 9.12.

15.1.3 When the Company has taken any action in respect of a NCC Participant, as aforesaid, the NCC Participant may be permitted restricted access to the NCC Systems within the limitations prescribed by the Company to the **intent extent** that the liability of the NCC Participant is reduced. Any further Exchange trades and/or Non-Exchange Transactions of the NCC Participant Transmitted to the Company or recorded with the Company during such restricted access to NCC Systems and which have the effect of increasing the liability of the NCC Participant may be ignored and excluded from all operations of the Company.

15.2.1 Except as otherwise may be determined by the Company in any particular case, Balance Order Securities deliverable to the Clearing Member in respect of whom the Company has taken any action pursuant to Chapter 18 (RESTRICTION, SUSPENSION OR TERMINATION OF ACCESS TO SERVICES OFFERED BY THE COMPANY) shall be retrieved by NCSS and the Company shall cause sell-out of such Securities in accordance with the Procedures. The Balance Order Securities deliverable by such a Clearing Member shall be caused to be bought-in by the Company in accordance with the Procedures and delivered to the Clearing Member to whom such Securities are to be delivered. If any profit or loss, as the case may be, accrues to the Company as a result of the purchases or sales effected as above stated under the Balance Order Settlement System, such profit or loss shall be credited or debited to the Clearing Member's Money Account, provided that payment of profit shall be subject to the approval of Exchange. **Similarly, where any gain is realized on the square-up or close-out of the Position of such Clearing Member in Deliverable Future Contracts, the same shall netted against any loss of the Suspended Clearing Member in any other**

Annexure – A

Market(s) and balance will be retained by the Company and made part of the Settlement Guarantee Fund.

Revision in NCCPL procedures related to “Close-out of Deliverable Future Contract” in case of default by Clearing Participant(s)

NCCPL’s Risk Management proposed regulations with reference to market reform committee recommendations for “Deliverable Future Contract (DFC) close-out mechanism”. Which was shared with Risk Committee “RC” via circular resolution dated December 11, 2020. Subsequently RC and NCCPL board approved the same. The proposed regulations were submitted to SECP dated December 30, 2019.

Accordingly, NCCPL Procedures covering operational aspects of the close out procedures were detailed and presented to RC in its 13th meeting held on February 21, 2020. Subsequently, the system development started with Operations, IT and Finance team indulged and in the process they identified few more details that needs to be added in the existing procedures. Therefore, the revised procedures are presented for Risk Committee’s consideration and approval.

ORIGINAL PROCEDURES	PROPOSED PROCEDURES
<p>4a.1 Liquidation of Deliverable Future Contracts (DFC):</p> <p>4a.1.1 The Position in DFC (buy or sell positions) of a Suspended Clearing Member shall be liquidated in the DFC Market by placing only reverse orders of open Position through Trading ID of Suspended Clearing Member in an un-disclosed manner.</p> <p>4a.1.2 The Company shall send a notice to the Exchange identifying the securities wise net long/short position of the Suspended Clearing Member that needs to be liquidated within the time prescribed in the Designated Time Schedule. The Exchange shall facilitate the Company in liquidating the position whereby reverse side orders in an un-disclosed manner shall be executed in the DFC Market at market price through the Trading ID of the Suspended Clearing Member.</p> <p>4a.1.3 Upon completion of liquidation (even in part) the Exchange shall provide liquidation results to the Company immediately after close of the DFC Market.</p> <p>4a.1.3 The net profit or loss booked on the liquidation of DFC position shall be calculated by the Company.</p>	<p>4a.1.2 The Company shall send a notice to the Exchange identifying the securities wise Sub A/c and UIN wise outstanding net long/short position of the Suspended Clearing Member that needs to be liquidated within the time prescribed in the Designated Time Schedule. The Exchange shall facilitate the Company in liquidating the position whereby reverse side orders in an un-disclosed manner shall be executed in the DFC Market at market price through the Trading ID of the Suspended Clearing Member.</p> <p>4a.1.3 Upon completion of liquidation (even in part) the Exchange shall provide liquidation results to the Company immediately after close of the DFC Market.</p>
<p>4a.2 Square-up of open Deliverable Future Contracts:</p> <p>On completion of the liquidation process, as explained in Procedure 4a.1, the remaining net long/short position in DFC of a Suspended Clearing Member shall be squared-up through an open auction session in the DFC square-up</p>	<p>4a.2 Square-up of open Deliverable Future Contracts:</p> <p>On completion of the liquidation process, as explained in Procedure 4a.1, the remaining Sub A/c and UIN wise net long/short position in DFC of a Suspended Clearing Member shall be squared-up through an open auction</p>

<p>market of the Exchange in an un-disclosed manner through the Trading ID of the Suspended Clearing Member.</p>	<p>session in the DFC square-up market of the Exchange in an un-disclosed manner through the Trading ID of the Suspended Clearing Member.</p>
<p>4a.3 Notices of Squaring-up DFC Contracts to the Exchange:</p> <p>The Company for squaring-up the net long/short position of the Suspended Clearing Member in DFC shall send a notice to the Exchange highlighting the details of security-wise unsettled net long or net short DFC positions that are required to be squared-up by the Exchange. The Exchange shall initiate the squaring-up process within the time frame set out in or determined under the squaring-up procedures of the Exchange.</p>	<p>4a.3 Notices of Squaring-up DFC Contracts to the Exchange:</p> <p>The Company for squaring-up of Sub A/c and UIN wise net long/short position of the Suspended Clearing Member in DFC shall send a notice to the Exchange highlighting the details of security-wise Sub A/c and UIN wise unsettled net long or net short DFC positions that are required to be squared-up by the Exchange. The Exchange shall initiate the squaring-up process within the time frame set out in or determined under the squaring-up procedures of the Exchange decided mutually by the Company and Exchange.</p>
<p>4a.4 Eligibility to Bid and Offer by Buyer or Seller:</p> <p>Any TRE Certificate Holder who is also a CM (excluding Suspended Clearing Member) shall be permitted to make a bid or offer in squaring-up process either on proprietary account and/or for and behalf of its clients.</p>	
<p>4a.5 Actions on Completion of Squaring-Up (Even in Part):</p> <p>4a.5.1 The Exchange shall complete the square-up process as per its rules and regulations and in accordance with the following mechanism:</p> <p>a) The securities wise net long position in DFC of the Suspended Clearing Member may be offered in DFC square-up market by the Exchange at last day closing price of contract in DFC Market. Likewise, the securities wise net short position in DFC of the Suspended Clearing Member may be</p>	<p>4a.5 Actions on Completion of Squaring-Up (Even in Part):</p> <p>a) The securities Sub A/c and UIN wise net long position in DFC of the Suspended Clearing Member may be offered in DFC square-up market by the Exchange at last day closing price of contract in DFC Market. Likewise, the Sub A/c and UIN wise net short position in DFC of the</p>

<p>offered in DFC square-up market by the Exchange at last day closing price of contract in DFC Market. All such bids and offers shall be placed in an un-disclosed manner through the Trading ID of the Suspended Clearing Member.</p> <p>b) For the purpose of determination of square-up price, a maximum discount or premium of 15% may be allowed in bid/offer prices of the last day closing price of the same contracts in DFC market, depending upon the outstanding position of the Suspended Clearing Member.</p> <p>4a.5.2 Upon completion of squaring-up (even in part) the Exchange shall provide squaring up results to the Company immediately after close of the DFC square-up market of the Exchange.</p> <p>4a.5.3 The net profit or loss booked on the squaring up of the DFC position would be calculated by the Company.</p>	<p>Suspended Clearing Member may be offered in DFC square-up market by the Exchange at last day closing price of contract in DFC Market. All such bids and offers shall be placed in an un-disclosed manner through the Trading ID of the Suspended Clearing Member.</p>
<p>4a.6. Close-out of Outstanding Defaulted DFC Position:</p> <p>4a.6.1 If the net outstanding short/ long position of the Suspended Clearing Member is not completely liquidated or squared-up in accordance with the Procedures, or where these processes could not be initiated within the time prescribed in NCCPL Regulations, 2015, the net open long / short position in DFC of Suspended Clearing Member shall be closed out by the Company as follows:</p> <p>a. The Company shall prepare a securities wise list of net long or net short outstanding DFC position of all non-defaulted CMs and their respective investors' at Unique Identification Number "UIN" level, based on</p>	

<p>the securities wise net open long / short position in DFC of the Suspended Clearing Member.</p> <p>b. Net open long / short position in DFC in a particular security of Suspended Clearing Member would be allocated to non-defaulting CMs proprietary UINs having open reverse positions in DFC of that particular security on the date of close out on pro rata basis, whereby the net long position of non-defaulting CMs proprietary UINs would be offset against net short DFC position of Suspended Clearing Member. Likewise, net short position of non-defaulting CMs proprietary UINs would be offset against net long position of Suspended Clearing Member.</p> <p>c. The remaining net long / short position of the Suspended Clearing Member in DFC, if any, after the allocation to proprietary UINs of the non-defaulting CMs as explained in b above, shall then be offset against the open position of investors' on UIN basis having exposure in that particular security on pro rata basis, whereby net long position of non-defaulted investors' UINs would be offset against net short DFC position of Suspended Clearing Member. Likewise, net short position of non-defaulted investors' UINs would be offset against net long position of Suspended Clearing Member.</p> <p>d. All allocations made as per the mechanism provide in points "b" and "c" above will be based on lot size of a particular security at a</p>	
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<p>maximum discount or premium of 15% of the last day closing price of the same contract in DFC market, as the case may be.</p> <p>4a.6.2 The net profit or loss booked on the close out of the DFC position would be calculated by the Company.</p>	
<p>4a.7. Circumstances where Square-up process may not be initiated;</p> <p>4a.7.1 The net long / short position in DFC of a Suspended Clearing Member shall not be squared-up in accordance with Procedures 4a.1 to 4a.5, where CM has failed to pay MTM losses, margins or money obligation in accordance with Chapter 13 of NCCPL Regulations, 2015, two days before the Settlement Date of the open position in DFC market (i.e. last day of the contract). Under such circumstances the net open long / short position of Suspended Clearing Member in DFC will be closed out in accordance with Procedure 4a.6.</p> <p>4a.7.2 The net long/short position in DFC of a Suspended Clearing Member that will be settled earlier due to announcement of corporate entitlement shall not be squared-up in accordance with Procedures 4a.1 to 4a.5 where two days are left in the Settlement Date. Under such circumstances the net open long / short position of defaulting CM in DFC will be closed out in accordance with Procedure 4a.6.</p>	
<p>4a.8 Profit arising from liquidation, square-up or close out</p> <p>The CM on whose account liquidation, square-up or close out-out is effected will, notwithstanding that he is in default, is entitled to profit which may arise by such processes.</p>	