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## **National Clearing Company of Pakistan Limited**

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

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**NCCPL/SLB/APRIL-14/01**

**April 8, 2014**

### **Modifications in Securities Lending and Borrowing System (“SLB”)**

Dear Clearing Members,

This is with reference to the implementation of Securities Lending and Borrowing System (“SLB”) by National Clearing Company of Pakistan Limited (“NCCPL”) in a capacity of an Authorized Intermediary effective from March 21, 2011.

In this respect, we are pleased to inform you that **effective from Monday April 14, 2014**, following changes will be implemented in SLB System so as to promote liquidity in SLB Market:

#### **A. Revision in Cash Retention Methodology:**

Presently, NCCPL holds 50% amount of lent securities and paid remaining 50% amount to the Lenders on the Settlement Date of SLB Transaction. Necessary amendments have been made in the NCCPL Regulations whereby, **100% amount of SLB Transaction value shall be paid to the Lenders** on the Settlement Date of SLB Transaction. Accordingly, in case of SLB(R) Transaction, Lenders shall be required to pay 100% amount of the lended Securities, along with the Premium adjustment to NCCPL on the Settlement Date of SLB(R) Transaction.

#### **B. Approved Form of Collateral against Exposure Margins and Special Margins:**

Deposit against Exposure Margins and Special Margins is accepted by NCCPL from SLB Participant in the form of cash only. However, following forms of collateral shall also be acceptable by NCCPL:

##### **1. Margin Eligible Securities**

The SLB Participants may also deposit Margin Eligible Securities, as declared by the stock exchange **for the purpose of Exposure Margins** in respect of their SLB Transactions. NCCPL shall apply conditions such as applicable Haircut, maximum limit of security deposit etc on Margin Eligible Securities in accordance with the NCCPL Regulations. In order to maintain Security Collateral Positions of SLB Participants, pledgee ID shall be issued by NCCPL upon receipt of written request by SLB Participant.



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### **2. Bank Guarantee**

The SLB Participants may also deposit a Bank Guarantee as collateral in the prescribed form for the purpose of **Exposure Margins and Special Margins** in respect of their SLB Transactions. However, such bank guarantee should be issued by a bank which is duly licensed to carry on banking business in Pakistan under the Banking Companies Ordinance, 1962 (LVII of 1962), or, being a statutory corporation, it is otherwise entitled to carry on banking business under the law by which it is created. Moreover, such Bank must be allocated minimum long term credit rating of “A”.

### **3. Treasury Bills (T-Bills)**

The SLB Participants may also deposit T-Bills for the purpose of **Exposure Margins and Special Margins** in respect of their SLB Transactions. For the purposes of T-Bills valuation, NCCPL shall apply conditions in accordance with the NCCPL Regulations.

### **4. Irrevocable Undertaking**

An irrevocable undertaking in the standard format may also be acceptable as collateral for the purpose of **Exposure Margins and Special Margins** in respect of SLB Transactions. Such irrevocable undertakings shall only be acceptable from:

- Banks/development financial institutions (“DFIs”) having minimum credit rating of AA; and
- Public sector entity owned or controlled by the Government of Pakistan

### **C. Exposure Margins and MTM Losses from Lenders:**

As per the revised mechanism, 100% amount of lent securities shall be paid to the Lenders on the Settlement Date. To cover the settlement risk, Lenders shall be required to pay VaR based Exposure Margins and Marked-to-Market Losses till the settlement of SLB Contracts. Such Exposure Margins and Marked-to-Market Losses shall be collected by NCCPL from Lenders in accordance with NCCPL Regulations.



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## National Clearing Company of Pakistan Limited

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We have also arranged a detailed presentation on the salient features of SLB for all Clearing Members as per the following schedule:

Participants	Location	Date	Time
TRE Certificate Holders of The Karachi Stock Exchange (KSE)	KSE Auditorium	April 09, 2014	04:00 p.m.
TRE Certificate Holders of The Lahore Stock Exchange (LSE)	LSE Auditorium	April 10, 2014	04:00 p.m.
TRE Certificate Holders of The Islamabad Stock Exchange (ISE)	ISE Auditorium	April 11, 2014	04:30 p.m.

Approved amendments in NCCPL Regulations pertaining to SLB is also attached herewith as (Annexure-A)

For any further queries or concerns, please feel free to contact the **Customer Support Department** of your respective locations:

City	Telephone Number	Fax Number
Karachi	021-32460811-19 Ext. 214, 217 & 218 Dir. 021-32438531-32-33	021-32462825
Lahore	042-36280815-7	042-36280818
Islamabad	051-2895460-62	051-2895463

Regards,

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**Rehan Saif**  
**Head of PD & CSS**

**CC:**

1. Executive Director (SMD) Securities and Exchange Commission of Pakistan - Karachi
2. Managing Director - The Karachi Stock Exchange Limited
3. Managing Director - The Lahore Stock Exchange Limited
4. Managing Director - The Islamabad Stock Exchange Limited
5. Chief Executive Officer - Central Depository Company of Pakistan Limited
6. Chief Executive Officer - Mutual Fund Association of Pakistan
7. Chairman - Pakistan Banking Association



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## National Clearing Company of Pakistan Limited

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### Annexure – A

## CHAPTER 7A SECURITIES LENDING AND BORROWING

### 7A.1. Definitions

Haircut		means the percentage rates on which the Margin Eligible Securities are discounted for valuation purposes based on their liquidity and volatility at the relevant Stock Exchange.
Margin Eligible Securities		means securities notified to be acceptable as Collateral pursuant to Regulation 7A.5.3. (Approved Collaterals).
VaR		Means the VaR Estimates as defined in the relevant regulations of the Karachi Stock Exchange.

### 7A.4.7 Settlement Mechanism

The SLB Transactions and SLB (R) Transactions shall be settled under Balance Order System as prescribed in these Regulations and the Procedures as follows:

- i) in the case of SLB Transaction, the Borrower shall be obliged to pay the SLB Transaction Value to the Company and the Lender shall be obliged to deliver the Borrowed Securities. Accordingly - 100% amount of such SLB Transaction Value shall be paid to the Lender by the Company.

Provided that, in case where SLB Transaction executed in SLB Spot Market, the Borrower shall be obliged to pay the SLB Transaction Value to the Company and the Lender shall be obliged to deliver the Borrowed Securities to the CDC account of the Company, within the time specified by the Company from time to time. Accordingly, the Company shall transfer such Borrowed Securities to the respective CDC main, house and sub-accounts, as the case may be, of the buyer Clearing Members. Accordingly -100% amount of that SLB Transaction Value shall be paid to the Lender by the Company.

- ii) in the case of SLB (R) Transaction, generated either on the basis of SLB Transactions in SLB Market or SLB Spot Market as the case may be,:
  - a. the Borrower shall deliver the SLB Securities and the Company shall pay the remaining amount of SLB Transaction Value to the Borrower after adjusting SLB Contract Price, provided that where SLB Contract Price exceeds the SLB



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## **National Clearing Company of Pakistan Limited**

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Transaction Value, the Borrower shall pay such excess amount to the Company in accordance with the procedures; and

- b. the Lender shall pay 100% amount of the SLB Transaction Value to the Company and the Company shall deliver the Borrowed Securities along with the adjusted SLB Contract Price to the Lender.

### 7A.5.3 Approved Collaterals

7A.5.3.1 The following shall be approved collaterals for the purpose of Exposure Margins, Marked-to-Market Losses, Special Margins and any other margins that may be required by the Company:

#### 1) Cash

Cash shall be acceptable collateral against any margin requirement under these Regulations and shall be the acceptable form for payment of Marked-to-Market Losses and Special Margins.

#### 2) Margin Eligible Securities

The Company shall notify from time to time, as declared by the stock exchange under their respective regulations, the securities that are acceptable to the Company for the purpose of Exposure Margins and any other margins-from time to time, except Marked-to-Market Losses and Special Margins.

#### 3) Bank Guarantees

A bank guarantee shall be an acceptable collateral for the purpose of Exposure Margins, Special Margins and any other margins that may be required by the Company from time to time, except Marked-to-Market Losses provided such bank guarantee is issued:

- i. in the form prescribed by the Company from time to time; and
- ii. by a bank which is:
  - a) is duly licensed to carry on banking business in Pakistan under the Banking Companies Ordinance, 1962 (LVII of 1962), or, being a statutory corporation, it is otherwise entitled to carry on banking business under the law by which it is created;



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- b) it has been allocated minimum long term credit rating of “A”. Provided that, where bank has been allocated minimum credit rating of “A” the amount of such Bank Guarantee per NCC Participant is limited up to Rs. 400 million, whereas, in case of “AA” and above credit rated bank the amount of such Bank Guarantee per NCC Participant is limited upto Rs. 1 billion; and it has a branch located in Karachi which is acceptable to the Company as such bank’s main contact branch;

The Company shall maintain a list of banks which satisfy the aforementioned eligibility criteria for issuing the bank guarantees acceptable to the Company for satisfying the Collateral requirements of SLB Participants. The said list shall be reviewed biannually by the Company and any change therein shall be disseminated accordingly.

#### 4) Irrevocable Undertaking

An irrevocable undertaking in the form prescribed by the Company from time to time shall be acceptable collateral for the purpose of Exposure Margins, Special Margins and any other margins that may be required by the Company from time to time, except Marked-to-Market Losses. Provided that such irrevocable undertakings shall be accepted only from the following SLB Participants for their own obligations:

- a) SLB Participants as are banks/development financial institutions (“DFIs”) having minimum credit rating of AA; and
- b) Any other public sector entity owned or controlled by the Government of Pakistan and approved by the Board from time to time.

#### 5) Treasury Bills (“T-Bills”)

T-Bills shall be acceptable collateral for the purpose of Exposure Margins, Special Margins and any other margins, except Marked-to-Market Losses, that may be required by the Company from time to time.

7A.5.3.2 All margins deposited by the SLB Participants with the Company in respect of SLB Market, shall be in the form of approved Collaterals and shall be subject to the following conditions:

- i. The Company shall not accept any Margin Eligible Security for the purpose of margin requirements if acceptance of Margin Eligible Security taken together with the margins already held will exceed SLB Participant wide and/or market wide limits of deposit of such Margin Eligible Security as prescribed below:



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## National Clearing Company of Pakistan Limited

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VaR Based Margin Percentage	Maximum Number of Margin Eligible Security that may be Deposited by SLB Participants
0<x>20%	1% of Free Float
x>20%	0.25% of Free Float

- ii. A maximum limit per Margin Eligible Security, as a percentage of free float, shall apply to all Margin Eligible Securities deposited as margin held by the Company i.e. margin held by the Company cannot exceed 25% of free float of such Margin Eligible Security.
- iii. The Margin Eligible Security is in book entry form.
- iv. The issuer of Margin Eligible Security is not placed on the defaulter's counter of any the Stock Exchanges.
- v. SLB Participants listed on Stock Exchanges will not be allowed to deposit their own deposits.
- vi. The Company may from time to time prescribe, with the prior approval of the Commission, the maximum number of acceptable Margin.
- vii. Any other criterion prescribed by the Company and approved by the Commission from time to time.

7A.5.3.3 The SLB Participant depositing margin in the form of Margin Eligible Securities shall always maintain the value thereof, after application of the relevant Haircuts, at not less than the margin amount for the time being required to be covered by them by providing further Margin Eligible Securities or depositing other approved Collaterals to the satisfaction of the Company which shall always determine the said value and whose valuation shall conclusively fix the amount of any deficiency to be made up from time to time. If at any time during a trading day, the required margins against Exposure of a SLB Participant exceed the already deposited margins, such SLB Participant shall deposit with the Company the margin computed by the Company within the time specified by the Company, but not later than opening of the market on.



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## **National Clearing Company of Pakistan Limited**

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### 7A.5.3.4 Valuation of Approved Collateral held by the Company as Margin

- i) Margin Eligible Securities shall be valued as per applicable Hair Cuts.
- ii) Bank Guarantees shall be taken at the amount guaranteed in such Bank Guarantees.
- iii) T-Bills shall be valued using the following valuation methodology while accepting as collateral:
  - a) 2.5% hair cut on daily valuation shall be applicable;
  - b) T-Bills can be of any tenure;
  - c) All T-Bills shall be released before 3-working days of their respective maturities; and
  - d) All T-Bills shall be valued on daily basis based on the prices published by the Reuter.

7A.5.3.5 All applicable margins on SLB Market shall be calculated on UIN wise in accordance with the client level margining regime applicable at the Stock Exchanges from time to time.

### 7A.5.4 Exposure and Margins

1. Security-wise and client-wise exposure of each SLB Participant will be calculated by the Company at any point in time, subject to the applicable netting rules as prescribed by these Regulations.
2. All SLB Contracts shall be subject to the margin requirements prescribed in these Regulations or such other additional margins as the Company may prescribe from time to time in addition hereto, with the prior permission of the Commission.



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## **National Clearing Company of Pakistan Limited**

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3. The VaR based margins for each SLB Eligible Security shall be calculated by the Company applying VaR Estimates calculated by the Risk Meter at the end of each trading day.
4. The SLB Participants shall deposit exposure margins in respect of their SLB Transaction on the day that the same is executed. Upon settlement of the SLB Transaction, the VaR based exposure margins shall be collected till settlement of SLB (R) Transaction.
5. (a) The exposure margins shall be deposited by a SLB Participant within such time as may be determined by the Company from time to time but in no case later than the opening of trade on the next trading day.  
  
(b) Exposure margins deposited by a SLB Participant under these Regulations must be kept separate by the Company, segregated from margins of all other Markets. Such SLB related margins will be utilized for the benefit of SLB Participants only in the event of default.
6. Margins payable by a SLB Participant under these Regulations will be accepted by the Company in the form of Acceptable Collaterals.
7. No netting such as across Markets, across clients, across different SLB Eligible Securities, across Settlement Dates or between exposure as Borrower and Lender shall be allowed whatsoever, to any SLB Participant.

### 7A.5.5 Marked-to-Market Losses

1. Marked-to-Market Loss shall be calculated, separately for each SLB Eligible Security, for each SLB Participant on the basis of the Closing Price.
2. The obligation of the SLB Participants to deposit their respective Marked-to-Market Losses shall commence from the SLB Transaction Date and shall continue till such time that SLB Transaction is settled. Thereafter, Marked-to-Market Losses shall be collected from the SLB Participants on SLB (R) Transaction till the settlement date of such SLB (R) Transaction.
3. Marked-to-Market Losses shall be deposited by each SLB Participant with the Company before such time as may be specified by the Company or at the end of each trading day but not later than prior to opening of trading on the next day.



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## **National Clearing Company of Pakistan Limited**

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4. While determining the Marked-to-Market Losses payable by SLB Participants, no netting such as across clients, across Markets, across contract periods, across securities, across Settlement Dates etc shall be allowed whatsoever.
5. Deposit against Marked-to-Market Losses will be accepted by the Company in the form of cash only.

### 7A.5.8 Lien on Deposits

The monies, SLB Eligible Securities, acceptable collateral and other assets deposited by a SLB Participant by way of exposure margins, Special Margins and Marked-to-Market Losses under these Regulations shall be subject to a first and paramount lien and pledge of the Company, with a right of sale and set off in each case in accordance with these Regulations, for any sum due to the Company by such SLB Participant and for the proper and punctual performance of such SLB Participant's engagements, obligations and liabilities arising out of or incidental to any SLB Contract and other contracts made subject to these Regulations or anything done in pursuance thereof.