MUFAP

MUTUAL FUNDS ASSOCIATION OF PAKISTAN

WHAT ARE MUTUAL FUNDS?

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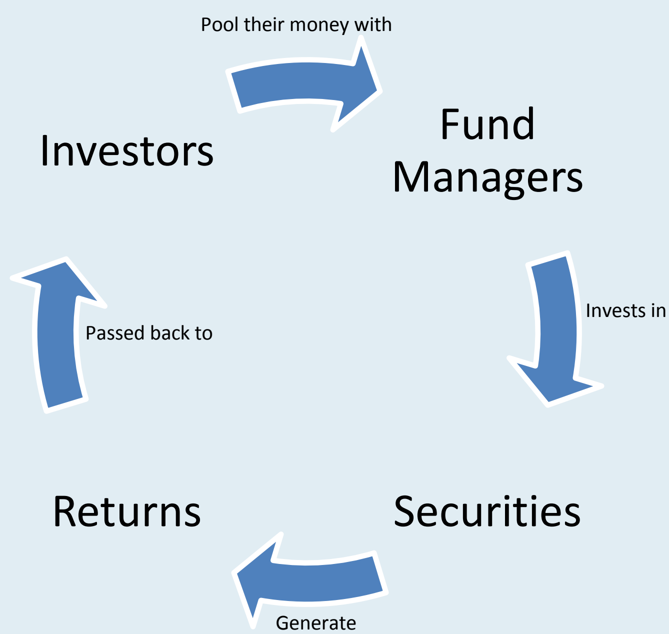
Mutual Funds Association of Pakistan is the trade body duly licensed by the Government of Pakistan for the mutual fund industry in Pakistan. All Asset Management Companies (AMCs) and Investment Advisory (IAs) licensed by SECP to launch Mutual Funds and perform Investment Advisory Services are required under NBFC Rules 2008 to become Members of MUFAP.

WHAT IS MUTUAL FUND

A mutual fund is a collective investment scheme, which specializes in investing a pool of money collected from investors for the purpose of investing in securities such as stocks, bonds, money market instruments and similar assets.

One of the main advantages of mutual funds is that they give small investors access to professionally managed, diversified portfolios of equities, debt instruments i.e. TFCs and Govt. Securities and other securities, which otherwise would be quite difficult (if not impossible) to create with a small amount of capital. The income earned through these investments and the capital appreciations realized are shared with its unit holders in proportion to the number of units owned by them.



TYPES OF MUTUAL FUNDS

There are basically two types of Mutual Funds:

- Open-Ended Mutual Funds
- Closed-Ended Mutual Funds

Open-ended

These are mutual funds which continually create new units or redeem issued units on demand. They are also called Unit Trusts. The Unit holders buy the Units of the fund or may redeem them on a continuous basis at the prevailing Net Asset Value (NAV). These units can be purchased and redeemed through Management Company which announces offer and redemption prices daily.

Close-ended

These funds have a fixed number of shares like a public company and are floated through an IPO. Once issued, they can be bought and sold at the market rates in secondary market (Stock Exchange). The market rate is announced daily by the stock exchange.

STRUCTURE OF MUTUAL FUND

Mutual Funds are operated by Asset Management Companies (AMCs) which exists in the form of a public limited company registered under Companies Ordinance, 1984. The AMC launches new funds through the establishment of a Trust Deed, entered between the Asset Management Company and the Trustee, with due approval from the SECP under the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003 (the "Rules"). The Trustee performs the functions of the custodian of the assets of the Fund. The trustee ensures that the Fund Manager takes the investment decisions within the defined investment policy of the mutual fund. Under Pakistan law, banks and central depository companies, approved by the SECP, can act as trustee.

At present Central Depository Company of Pakistan (CDC) is acting as Trustee of most of the funds of the industry.

The Securities & Exchange Commission of Pakistan (SECP) is the regulator of mutual funds industry and is very stringent in issuing licenses to fund management companies, especially in the case of Collective Investment Scheme (CIS). The SECP also carries out continuous monitoring of mutual funds through reports that the mutual funds have to file with the SECP on a regular basis. In addition, SECP conducts on-site inspections of the AMCs.

How do Mutual Funds determine their Unit Price?

A fund's Net Asset Value (NAV) represents the price per unit. The NAV is equal to the market worth of assets held in the portfolio of a Fund, minus liabilities, divided by the number of units outstanding.

$$\text{NAV} = \frac{\text{Current Market Value of all the Assets} - \text{Liabilities}}{\text{Total Number of Units Outstanding}}$$

In order to determine the sale price of the unit sales load is added to the NAV. In case there is no sales load the NAV will be the sale price as well as the redemption price. The sale and redemption price is declared on a daily basis by the Funds and can be viewed on their websites.

CATEGORIES OF MUTUAL FUND

SECP the Regulator has categorized the Schemes of mutual funds as under:-

Equity Scheme:
An equity scheme or equity fund is a fund that invests in Equities more commonly known as stocks. The objective of an equity fund is long-term growth through capital appreciation, although dividends and capital gain realized are also sources of revenue.

Balanced Scheme:
These funds provide investors with a single mutual fund that invests in both stocks and debt instruments and with this diversification aimed at providing investors a balance of growth through investment in stocks and of income from investments in debt instruments.

Asset Allocation Fund:
These Funds may invest its assets in any type of securities at any time in order to diversify its assets across multiple types of securities & investment styles available in the market.

Fund of Fund Scheme:
Fund of Funds are those funds, which invest in other mutual funds. These funds operate a diverse portfolio of equity, balanced, fixed income and money market funds (both open and closed ended).

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Shariah Compliant (Islamic) Scheme:
Islamic funds are those funds which invest in Shariah Compliant securities i.e. shares, Sukuk, Ijara sukuks etc. as may be approved by the Shariah Advisor of such funds. These funds can be offered under the same categories as those of conventional funds.

Capital Protected Scheme:
In this type of scheme, the payment of original investment is guaranteed with any further capital gain which may accrue at the end of the contractual term of the Fund. Such funds are for a specific period.

Index Tracker Scheme:
Index funds invest in securities to mirror a market index, such as the KSE 100. An index fund buys and sells securities in a manner that mirrors the composition of the selected index. The fund's performance tracks the underlying index's performance.

Money Market Scheme:
Money Market Funds are among the safest and most stable of all the different types of mutual funds. These funds invest in short term debt instruments such as Treasury bills and bank deposits.

Income Scheme:
These funds focus on providing investors with a steady stream of fixed income. They invest in short term and long term debt instruments like TFCs, government securities like T-bills/ PIBs, or preference shares.

Aggressive Fixed Income Scheme:
The aim of aggressive income fund is to generate a high return by investing in fixed income securities while taking exposure in medium to lower quality of assets also.

Commodity Scheme:
These schemes enable small investors to take advantage of gains in commodities such as gold through pooled investments. They invest at least 70%of their assets in commodity futures contracts, which include both cash-settled and deliverable contracts.

An investor can invest in any of the above categories of funds in accordance with his requirements and appetite for risk. For example those who want to earn high returns over a longer period can invest in Equity Funds whereas those who want to invest for short term with reasonable return can invest in Money Market Fund.

WHY INVESTMENT IN MUTUAL FUNDS:

Mutual funds make saving and investing simple, accessible, and affordable. The advantages of mutual fund include the following:-

- **Accessibility**
  Mutual funds units are easy to buy.
- **Liquidity**
  Mutual fund unit holders can convert their units into cash on any working day. They will promptly receive the current value of their investment. Investors do not have to find a buyer; the fund buys back (redeems) the units.

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- **Diversification**
  By investing the pool of unit holders' money across number of securities, a mutual fund diversifies its holdings. A diversified portfolio reduces the investors' risk. It would be difficult for an average investor to buy varied securities to achieve the same level of diversification as is available with investment in mutual fund.

- **Professional Management**
  Asset Management Company evaluates all the opportunities that arises in the market, carefully examines them and then takes decision for investing the mutual fund's money whereas it is not an easy task for an individual and even for corporate company if investing is not their core business.

TAX CREDIT ON INVESTMENT TO INDIVIDUAL

According to Section 62 of the Income Tax Ordinance, 2001, a "resident' tax payer other than a company, is entitled to tax credit on investment in new shares offered to public by a public company listed on a stock exchange in Pakistan. This tax credit is available on the lower of (a) the amount of actual Cost of Investment (b) 20% of Taxable Income for the tax year or (c) Rs. 1 million. The tax credit availed on acquisition of such shares will be need to be paid back, if such shares are disposed off within 24 months of the date of acquisition. Units of Mutual Funds are covered under the definition of shares as per Income Tax Ordinance, 2001.

In case of self employed individuals, the maximum tax credit of Rs. 220,417 is available on annual taxable income of Rs. 6 million or more at an average tax rate of 22% whereas Rs. 203,571 is the maximum tax credit available on annual taxable income of Rs. 7million or more at an average tax rate of 20%).

Self employed Individuals:

Annual Taxable Income (Upper Limits)	Average Rate of Tax [as per formula given in Section 62(2)]	Gross Tax Payable [as per rates given in First Schedule]	Amount of Investment eligible for tax credit	Tax Credit avalable as per Section 62(2)	Tax Saving as a % of Investment (i)
A	B (%)	C	D = A*20%	(A/B)*C	
750,000	5%	35,000	150,000	7,000	4.7%
1,500,000	10%	147,500	300,000	29,500	9.8%
2,500,000	14%	347,500	500,000	69,500	13.9%
4,000,000	18%	722,500	800,000	144,500	18.1%
6,000,000	22%	1,322,500	*1,200,000	220,417	22.0%

*Note: Maximum amount of investment that is avalable for tax credit is restricted to Rs. 1 million.

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Salaried Individuals:

Annual Taxable Income (Upper Limits)	Average Rate of Tax [as per formula given in Section 62(2)]	Gross Tax Payable [as per rates given in First Schedule]	Amount of Investment eligible for tax credit	Tax Credit avalable as per Section 62(2)	Tax Saving as a % of Investment (i)
A	B (%)	C	D = A*20%	(A/B)*C	
750,000	2%	17,500	150,000	3,500	2.3%
1,400,000	6%	82,500	280,000	16,500	5.9%
1,500,000	6%	95,000	300,000	19,000	6.3%
1,800,000	8%	140,000	360,000	28,000	7.8%
2,500,000	11%	262,500	500,000	52,500	10.5%
3,000,000	12%	362,500	600,000	72,500	12.1%
3,500,000	14%	475,000	700,000	95,000	13.6%
4,000,000	15%	600,000	800,000	120,000	15.0%
7,000,000	20%	1,425,000	*1,400,000	203,571	20.4%

*Note: Maximum amount of investment that is avalable for tax credit is restricted to Rs. 1 million.

For further details consult your Income Tax Advisor.

TAXATION

Rate of Withholding Tax on Dividend Income from Mutual Funds:

	Stock Funds	Tax Rate Applicable
(i)	Dividend received from stock fund if dividend receipts are less than capital gain	12.5%
	All other Mutual Funds Other than Stock Fund	
(ii)	For Banks and Companies: Dividend received by a company from collective investment scheme, or a mutual fund, other than stock fund	25%
(iii)	For Individuals and Other corporate and non-corporate unit holders	10% for filers and 15% for non-filers

Capital Gains Tax:

Mutual funds are required to withhold Capital Gains Tax (CGT) as per below:

Holding Period	Tax Rate
Where holding period of a security is less than twelve months.	12.5%
Where holding period of a security is twelve months or more but less than twenty-four months.	10%
Where holding period of a security is twenty-four months or more.	0%

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HOW TO INVEST AND DISINVEST IN MUTUAL FUNDS:

Individuals:

The individual investor is required to provide the following at the designated sales points of the Asset Management Company

- Copy of CNIC
- Application / Account opening Form
- Purchase of Units Form
- Zakat Affidavit (Optional)
- KYC Form
- FATCA Form
- Cheque in favour of Trustee of the Fund

Corporate:

The corporate/ Provident/ Pension Fund investors are required to provide the following-;

- Memorandum and Article of Association/ Trust deed
- Board / Trustee Resolution approving the investment
- Application/Account Opening Form
- Purchase of Units Form
- Power of Attorney and/or relevant resolution of board of directors/ trustee delegating authority to any of its officer to invest
- NTN of the institution with tax status
- CNIC of the officer to whom the authority has been delegated
- Cheque in favour of Trustee of the Fund

How to Disinvest in Mutual Fund?

Redemption payments are made to the investors within a period of a maximum 6 working days, either through a cross-cheque or through a bank transfer by submitting the Redemption form at designated Sales Points of an AMC.

DIVIDEND PAYMENT:

Dividend is paid in the form of cash on monthly/quarterly/ annual basis depending upon the category of the fund and from AMC to AMC. Any investor who wishes to re-invest the dividend amount has the option to inform the AMC beforehand so the dividend amount will be re-invested and new units will be issued.

CAPITAL GAINS TAX:

Mutual funds are required to withhold Capital Gains Tax (CGT) as per below:

- 12.5%, where holding period of a security is less than twelve months.
- 10%, where holding period of a security is twelve months or more but less than twenty-four months.
- Zero, where holding period of a security is twenty-four months or more.

Risk Disclaimer

All investments in mutual funds are subject to market risks. The NAV of units may go up or down based on market conditions. Past performance is not necessarily indicative of the future results. The investor are advised in their own interest to carefully read the Offering Document in particular the investment policies and risk disclosure and warning statements in their respective Offering Document.