Are you an investor? Think about these points

Before an investor buys or sells shares, he needs to contact a stockbroker, licensed with the Securities and Exchange Commission of Sri Lanka (SEC) to carry out the transactions on the Colombo Stock Exchange (CSE).

Clients enter into a written agreement with the broker prior to obtaining services from them, for the purpose of engaging that broker to execute trades on behalf of them. The type of client agreement may vary depending on the services provided by the broker. This agreement contains clauses defining the rights and responsibilities of the client vis-à-vis broker.

Stockbroker firms are required to provide a copy of the client agreement to the client and draw the client's attention to the risks that are described in the appropriate risk disclosure statements. The client agreement includes a written 'risk acknowledgement statement' which the client is expected to acknowledge by placing his signature and date confirming that he is aware of the basic risks involved in trading in securities.

Confirmation of trades

Confirmation of trades is also referred to as bought/sold notes. When a client trades through his brokerage account, he receives a trade confirmation mailed/emailed to him indicating a buy or sell order by the end of the trade day. Prior to issuing a bought note/sold note to the client in electronic form, the broker needs to obtain the client's consent and the broker needs to retain evidence of such consent. The bought note/sold note also indicates that the purchase/sale is subject to the CSE and Central Depository Systems (Pvt.) Ltd. (CDS) rules.

A trade confirmation is extremely important because it is the client's way of verifying that the broker has filled an order according to his instructions. It also helps provide documentation for taxes and enables clients to keep track of their gains and losses. Furthermore, it is important to keep copies of all trade confirmations to detect possible errors. In case an error is detected, the client must contact the broker and attempt to get it corrected immediately.

A bought note/sold note should not be amended by a stockbroker unless there is a valid reason for the amendment. The chief executive officer/the compliance officer is permitted to amend such notes and they are required to approve such amendments.

CDS account statements

CDS shall send account holders a CDS account statement which includes all listed securities held in the account and the quantity of such shares.

The CDS account statement is forwarded to the account holder directly by CDS and if the client's account is maintained through a custodian bank, the statement is forwarded to the account holder through the relevant custodian bank. The CDS statement is forwarded in the electronic form if the account holder makes a request in writing.
The CDS account statements are forwarded in the following manner:

a. A statement is forwarded to the account holder on a monthly basis if such account was active during a particular month.
b. A statement is forwarded to the account holder on a quarterly basis if such account was active during the preceding three months.
c. A statement is forwarded annually as at March 31 to inactive account holders (accounts with no transactions for a period of 12 months).

Statement of accounts to clients

A statement of accounts is sent to all clients who are debtors beyond Trade Day + 3 (T+3) by the stock broking firm on a monthly basis by the seventh day of the following month. This should apply to all debtors over T+3 who have had transactions during the month and the 'interest charged on delayed payment' should also be considered a transaction for this purpose.
A statement of accounts should specify the transactions in the account including receipts and payments during the month under reference. Prior to issuing a statement of accounts in electronic form, a stockbroker should obtain the consent of the client.

Payment by buyer

The buyer shall ensure that 'Cleared Funds' i.e. funds that are realized and available for drawing in the payee's bank account, are made available to the buying broker by 09.00 hours on the settlement date, which is T+3, for the purchase of securities. When a sale and purchase settlement falls on the same settlement date or when the client gives written instructions to hold sales proceeds to meet the settlement of future purchases.

Buyer in default

Where the buyer fails to make payment by 09.00 hours on the settlement date, which is T+3;

- The buying stockbroker firm may pledge subject to the applicable CDS rules, the securities in which the payment is in default to a commercial bank, licensed under the Banking Act No. 30 of 1988 (as amended), as collateral, for the purpose of obtaining an immediate credit facility from the bank in order to meet the settlement obligations of the buying stockbroker firm on the settlement date.
- The buying stockbroker firm may, at its absolute discretion, recover interest commencing from the day after the settlement date up to the date of final settlement. If interest is charged it shall not exceed 0.1% per day.
- The buyer shall be liable for all losses and damages sustained or incurred by the buying stockbroker firm.
- The buying stockbroker firm may set off any amount due from the buyer, against sales proceeds due to the buyer.
- Any surplus arising on the sale of securities in respect of which the payment is in default shall accrue to the buying stockbroker firm, unless such surplus arises from the sale of other securities deposited by the buyer as collateral with the buying stockbroker firm, in which event the surplus shall be remitted to the buyer after settlement date of the relevant sale(s).

Payment to seller

- Settlement to the seller could be made either by cheques or electronic fund transfers to the seller's bank account. If payment is made to sellers by way of cheques, such cheques shall be duly crossed as 'Account Payee'. If the client requests that the crossing to be cancelled, the request shall be made in writing by the client and authorized, in writing, by the chief executive officer of the stockbroker firm.
- The selling broker firm shall ensure that 'Cleared Funds' are made available to the seller on the settlement date, which is T+3 unless expressly permitted by the seller in writing to do otherwise. If for any reason, payment has not been made by the stockbroker firm to the seller on the settlement date without a written request of the client in terms of the stockbroker rule, the seller shall be entitled to interest from the day after the settlement date on the outstanding amount at 0.1% per day.
- No cash cheques shall be issued to clients.

Extending credit limit

- In the event the client fails to meet the shortfall on the next market day, the stockbroker firm shall immediately sell the securities which have been pledged by the client, in order to ensure compliance with the stockbroker rules of the CSE
- The credit extended to a client shall not exceed 50% of the market value of the securities i.e. value of the securities pledged by the client marked to market at the end of each market day, which are pledged by the client, to secure the credit.
- This agreement needs to clearly set out the terms and conditions entered into between the client and the stockbroker firm. Amendments to the agreement will be in writing.
- A stockbroker firm may extend credit to its clients for the sole purpose of purchasing securities traded on the CSE, provided that the total value of the credit extended shall not exceed three times of the 'Adjusted Net Capital ' of the stockbroker firm. Stockbroker firms are required to enter into a written agreement with each client when credit is extended.
- The credit extended to a client of the stockbroker firm shall be secured by collateral obtained from such client, which shall comprise of securities held in the client's CDS account.
- When the market value of the securities pledged by the client falls by 25%, the stockbroker firm is required to inform the client to meet the shortfall by the next market day.
- A stockbroker firm shall ensure that the credit extendable to a 'Single Client' does not exceed 15% of the total value of credit extendable by the stockbroker firm.

(Sources: Securities and Exchange Commission of Sri Lanka/Central Depository Systems (Pvt.) Ltd. /Rules (December 2010) Stock broker Rules (effective from February 14, 2012)