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The Board of Directors
MCB-Arif Habib Savings and Investments Limited
2nd Floor, Adamjee House
I.I. Chundrigar Road
Karachi

August 4, 2021

ASR 0265

Dear Board members

AUDIT FOR THE YEAR ENDED JUNE 30, 2021

MCB CASH MANAGEMENT OPTIMIZER (CMOP);
MCB DCF INCOME FUND (DCFIF);
ALHAMRA ISLAMIC ASSET ALLOCATION FUND (ALHAA);
PAKISTAN CASH MANAGEMENT FUND (PCF);
PAKISTAN CAPITAL MARKET FUND (PCMF); and
PAKISTAN INCOME ENHANCEMENT FUND (PIEF).

We have pleasure in enclosing three copies of the draft financial statements of CMOP, DCFIF, ALHAA, PCF, PCMF and PIEF (collectively referred to as 'the Funds') being managed by MCB-Arif Habib Savings and Investments Limited (the Management Company) along with our draft reports thereon initialled by us for identification purposes. We shall be pleased to sign our draft audit reports in their present or amended forms after:

(a) the draft financial statements of the Funds have been approved by the Board of Directors of the Management Company and signed by the Chief Executive Officer, Chief Financial Officer and any one of the directors of the Management Company authorised by the Board in this behalf;

(b) we have seen the Board's specific approval for:

- transactions with connected persons / other related parties as disclosed in the enclosed financial statements of the respective Funds; and
- amounts stated in Annexure 'A' to this letter;

(c) we have received direct responses to our requests for confirmations from the Funds tax advisors, Funds legal advisors, banks, Central Depository Company of Pakistan Limited and IPS maintained with Habib Metropolitan Bank Limited for CMOP, DCFIF, PCF, PCMF and PIEF and United Bank Limited for ALHAA. A list of these outstanding confirmations have been shared with the management.

(d) we have seen a copy of the Trustee reports for each of the Funds and Shariah report for ALHAA for the year ended June 30, 2021;

(e) we have received the final drafts of "other information" to be printed in the annual reports of the Funds signed by the Chief Executive Officer and the Company Secretary of the Management Company to consider whether these, including the manner of their presentation, are materially consistent with the information appearing in the enclosed draft financial statements; and

(f) we have received appropriately signed letters of representation for each Fund. The draft representation letters are enclosed with this letter, which contain certain written representations being sought from the Management Company.

We take this opportunity to draw your attention to certain accounting and related matters which are set forth in the following paragraphs:

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2. RESPONSIBILITIES OF THE MANAGEMENT AND AUDITORS IN RELATION TO THE FINANCIAL STATEMENTS

The responsibilities of the independent auditors, in a usual examination of the financial statements are explained in International Standard on Auditing 200, "Overall objectives of the independent auditor and the conduct of an audit in accordance with international standards on auditing." While the auditors are responsible for forming and expressing their opinion on the financial statements, the responsibility for the preparation of the financial statements is primarily that of the management in accordance with the applicable financial reporting framework, which includes the design, implementation and maintenance of internal control relevant to the preparation and presentation of the financial statements that are free from material misstatement, whether due to fraud or error. The management's responsibilities include to provide the auditor with (i) all information, such as records and documentation, and other matters that are relevant to the preparation and presentation of the financial statements; (ii) any additional information that the auditor may request from the management and, where appropriate, those charged with governance; and (iii) unrestricted access to those within the entity from whom the auditor determines it necessary to obtain audit evidence. The audit of the financial statements does not relieve the management of its responsibilities. Accordingly, our examination of the books of accounts and records should not be relied upon to disclose all the errors or irregularities in relation to the financial statements.

We would like to inform the Board that unless we have signed the auditors' reports on these financial statements, the same shall remain and be deemed unaudited.

3. FEDERAL EXCISE DUTY (FED) ON REMUNERATION OF THE MANAGEMENT COMPANY

We refer to our covering letter ASR 0290 dated August 11, 2020 issued on the financial statements of the Funds for the year ended June 30, 2020 wherein the matter related to retaining the provision in respect of FED on remuneration of the Management Company was highlighted to the Board of Directors of the Management Company. The provision against FED on remuneration of the Management Company has been retained in the financial statements of the respective Funds as at June 30, 2021 as the matter is currently pending before the Supreme Court of Pakistan. There has been no change during the current year.

4. SINDH WORKERS' WELFARE FUND

As a consequence of the 18th amendment to the Constitution of Pakistan, in May 2015 the Sindh Workers' Welfare Fund Act, 2014 (SWWF Act) had been passed by the Government of Sindh as a result of which every industrial establishment located in the Province of Sindh, the total income of which in any accounting year is not less than Rs 0.50 million, is required to pay Sindh Workers' Welfare Fund (SWWF) in respect of that year a sum equal to two percent of such income. The matter was taken up by the Mutual Fund Association of Pakistan (MUFAP) with the Sindh Revenue Board (SRB) collectively on behalf of various asset management companies and their CISs whereby it was contested that mutual funds should be excluded from the ambit of SWWF Act as these were not industrial establishments but were pass through investment vehicles and did not employ workers. The SRB held that mutual funds were included in the definition of financial institutions as per the Financial Institution (Recovery of Finances) Ordinance, 2001 and were, hence, required to register and pay SWWF under the SWWF Act. Thereafter, MUFAP has taken up the matter with the Sindh Finance Ministry to have CISs / mutual funds excluded from the applicability of SWWF. In view of the above developments regarding the applicability of SWWF on CISs / mutual funds, MUFAP recommended that as a matter of abundant caution provision in respect of SWWF should be made on a prudent basis with effect from the date of enactment of the Sindh WWF Act, 2014 (i.e. starting from May 21, 2015). The Funds have, accordingly, made provision in respect of SWWF as recommended by MUFAP.

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5. BONUS SHARES WITHHELD

The Finance Act, 2014 introduced a levy of 5% income tax on bonus shares and made every company responsible to withhold and deposit 5% of total bonus shares into the Government treasury after selling them into the Stock Exchange. Consequently, shares withheld were only to be released once the recipients of bonus shares deposit tax equivalent to 5% of the value of the bonus shares issued. The value of tax is computed on the basis of day-end price on the first day of book closure.

In this regard, a constitutional petition had been filed by Collective Investment Schemes (CISs) through their Trustees in the High Court of Sindh, challenging the applicability of withholding tax provisions on bonus shares received by CISs. The petition was based on the fact that because CISs are exempt from deduction of income tax under Clause 99 of Part I of the Second Schedule to the Income Tax Ordinance 2001, the withholding tax provision should also not be applicable on bonus shares received by CISs. A stay order had been granted by the High Court of Sindh in favour of CISs.

During the year ended June 30, 2018, the Supreme Court of Pakistan passed a judgement on June 27, 2018 whereby the suits which are already pending or shall be filed in future must only be continued / entertained on the condition that a minimum of 50 percent of the tax calculated by the tax authorities is deposited with the authorities. Accordingly, the CISs were required to pay minimum 50% of the tax calculated by the tax authorities for the case to remain continued. The CISs failed to deposit the minimum 50% of the tax liability and accordingly the stay got vacated automatically during the year ended June 30, 2019. During the year ended June 30, 2020, the CISs have filed a fresh constitutional petition via CP 4653 dated July 11, 2019. Subsequently, in this regard, on July 15, 2019, the Honourable High of Sindh has issued notices to the relevant parties and has ordered that no third party interest on bonus shares issued to the Funds in lieu of their investments be created in the meantime. The matter is still pending adjudication and the Funds included these shares in their portfolio, as the management is confident that the decision of the constitutional petition will be in favour of the CISs. During the current year, the Fund has reclassified the amount of these shares from "investments" to "advances, deposits and other receivables" based on the market values of these shares on November 13, 2020.

We would like to highlight that the Finance Act, 2018 (effective from July 1, 2018) has omitted Section 236M of the Income Tax Ordinance, 2001 requiring every company quoted on stock exchange issuing bonus shares to the shareholders of the company, to withhold five percent of the bonus shares to be issued. Accordingly, post July 1, 2018 shares are not being withheld at the time of bonus issue.

The table presenting details of bonus shares withheld in respect of each Fund as at June 30, 2021 is disclosed in Annexure B to this letter.

6. ALLOCATED EXPENSES AND SELLING AND MARKETING EXPENSES

(i) Allocated Expenses

In accordance with the provisions of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 (amended vide S.R.O 1160(1) / 2015 dated November 25, 2015), the Management Company was entitled to reimbursement of fee and expenses in relation to registrar services, accounting, operation and valuation services related to the Fund up to a maximum of 0.1% of the average annual net assets of its Collective Investment Schemes (CISs) or actual, whichever is less.

During the year ended June 30, 2019, the Securities and Exchange Commission of Pakistan (SECP) vide SRO 639 of 2019 dated June 20, 2019 introduced amendments in Regulation 60 of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 whereby the maximum limit of 0.1% was removed. However, capping of Total Expense Ratio (TER) of the Fund is in place according to different categories of the Funds.

In this connection, the Management Company has allocated such expenses to the Fund based on its discretion subject to not being higher than actual expenses, which have also been approved by the Board of Directors of the Management Company.

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We have been informed by the management that the total expenses allocated to all the Funds do not exceed the total eligible allocable expenses incurred by the Management Company during the year.

(ii) Selling and Marketing Expenses

The SECP had allowed the Asset Management Companies to charge selling and marketing expenses to all categories of open-end mutual funds (except fund of funds) initially for a period of three years (i.e. from January 1, 2017 till December 31, 2019). The maximum cap of selling and marketing expense was 0.4% per annum of the net assets of the Fund or actual expenses whichever is lower.

During the year ended June 30, 2020, the SECP through its circular 11 dated July 5, 2019 has revised the conditions for charging of selling and marketing expenses to a Fund. As per the revised guidelines, the maximum cap of 0.4% per annum has been lifted and now the asset management company is required to set a maximum limit for charging of such expense to the Fund and the same should be approved by the Board of Directors of the Management Company as part of an annual plan.

The Management Company has charged selling and marketing expenses to the Fund based on its discretion subject to not being higher than actual expenses. We suggest that the Management Company should set a mechanism and threshold for chargeability of selling and marketing expenses for each fund to completely comply with the requirements of Circular 11 of 2019.

The SECP's circular further mentions that the selling and marketing expenses are to be reimbursed by the Funds to the Management Company at the end of each quarter subject to verification of documentary evidence by the Trustee and ensuring that the expenses are used for the purpose allowed. In case of dispute between the Asset Management Company and the Trustee, the matter shall be referred to the SECP and the decision of the SECP shall be binding on both the Asset Management Company and the Trustee.

We would like to highlight that the Management Company has submitted details of selling and marketing expenses for DCFIF, ALHAA, PCMF and PIEF from July 01, 2020 to March 31, 2021 and is in the process of submitting documents for the period from April 01, 2021 to June 30, 2021 with the trustees. No dispute with the Trustee has arisen on information submitted from July 01, 2020 to March 31, 2021 and the management company is confident that no dispute is likely to arise on reimbursement of payment for selling and marketing expenses for the period from April 01, 2021 to June 30, 2021.

7. WITHHOLDING TAX DEDUCTION BY COMPANIES

As per clause 47(B) of part IV of the Second Schedule to the Income Tax Ordinance, 2001 (the Ordinance), payments made to collective investment schemes (CISs) are exempt from withholding tax under sections 150 and 151 of the Ordinance. However, during the course of our audit, we noted that certain withholding agents had deducted withholding tax on profit on bank balances, profit on debt securities and dividend received by the Funds in current and prior years citing that a valid exemption certificate under section 159(1) issued by the concerned Commissioner of Inland Revenue (CIR) had not been submitted to them by the Funds at the time the profit on bank balances, profit on debt securities and dividends were paid. The cumulative amount of tax withheld has been shown as advance tax in the financial statements of the respective Funds for the year ended June 30, 2021 as, in the opinion of the management, the Funds will be able to obtain refunds against the tax so withheld.

The table below presents details of taxes withheld in respect of each Fund as at June 30, 2021:

Name of Fund	Amount
	(Rupees in '000')
MCB Cash Management Optimizer	1,411
MCB DCF Income Fund	1,607
Alhamra Islamic Asset Allocation Fund	1,205
Pakistan Cash Management Fund	386
Pakistan Capital Market Fund	466
Pakistan Income Enhancement Fund	303

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8. TAXATION MATTERS

a. Show cause notice issued to DCFIF for tax year 2017

During the year, the DCFIF has received a show cause notice on October 17, 2020 from the Additional Commissioner (Inland) Revenue (ACIR) in respect of tax year 2017. ACIR has raised objections on claiming of "provision against debt securities" amounting to Rs. 7,943,000 and adjustment of the "Element of loss and capital losses" amounting to Rs. 151,140,000 while arriving at the declared accounting income of the Fund and has challenged the distribution of 90 percent of income and the Fund's eligibility for exemption from tax. The Management Company through its tax advisor has submitted a response on December 9, 2020 in respect of objections raised by ACIR. We have been informed by the Management Company that no further communication has been received from ACIR after the submission of the Management Company's response through its tax advisor.

We have been informed by the Management Company that the matter is likely to be decided in favour of the Fund as the treatment adopted by the Fund is in line with the applicable regulations, the Income Tax Ordinance, 2001 and is consistent with the industry practices. Accordingly, no provision has been recognised in respect of the above tax matter in the financial statements of DCFIF for the year ended June 30, 2021.

b. Show cause notices issued to certain collective investment schemes in the industry

The Securities and Exchange Commission of Pakistan (SECP) vide SRO 756(I)/2017 dated August 3, 2017 made amendments in the Schedule V of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 and introduced the following disclosure:

- **Allocation of net income for the year:**
  - Income already paid on units redeemed; and
  - Accounting income available for distribution.

The above implies that the Fund is required to deduct "income already paid on units redeemed" in order to arrive at the amount of "accounting income available for distribution" to be disclosed in the Income Statement. "Income already paid on units redeemed" represents the portion of income paid to outgoing unit holders (relevant share in the income statement) during the year while the Fund is in profit.

The above disclosure was applicable for the first time for the financial year ended June 30, 2018. As per the common practice in the industry the amount of "income already paid on units redeemed" is deducted while determining the amount available for distribution.

During the current year, certain CISs in the industry (including certain other funds managed by the management company and which are not audited by us) have received notices from the Additional Commissioner (Inland) Revenue (ACIR), whereby ACIR has raised an objection on claiming of "income already paid on units redeemed" as part of distribution and has thereby challenged the distribution of 90 percent of income and the Fund's eligibility for exemption from tax. ACIR is of the view that the amount of "Cash Dividend" paid can only be treated as part of distribution and the amount of "income already paid on units redeemed" is not a "Cash Dividend".

We have been informed by the management that the Federal Board of Revenue (FBR) has approached the Institute of Chartered Accountants of Pakistan (ICAP), Institute of Cost and Management Accountant of Pakistan (ICMAP) and the Securities and Commission of Pakistan (SECP) in respect of the above matter.

The Management Company in case of one of the aforementioned funds (where notice was received) has filed an application under section 7 of the Federal Board of Revenue Act, 2007 with the chairman FBR on January 4, 2021 in respect of objections raised by ACIR. The Management Company has received a response from the FBR dated February 25, 2021 whereby the FBR has stated that they referred the matter

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to ICAP, ICMAP and SECP for their expert opinion. All of the three bodies have opined that the positive differential between original cost incurred by a unit holder and the amount received by the unit holder from the mutual fund on redemption of such units can be construed as "distribution of profits". Subsequently, the Chairman of the FBR advised that the concerned field staff to evaluate the case based on practice prescribed by these bodies.

9. REGISTRATION OF CIS UNDER THE NEW PROVINCIAL TRUST ACTS

As a result of the Eighteenth Amendment to the Constitution of Pakistan, certain legislative powers have been vested with the provinces. Prior to this, the Constitution of Pakistan (Constitution) contained two legislative lists i.e. the "Federal Legislative List" and the "Concurrent Legislative List". The Parliament had the exclusive power to make laws with respect to any matter contained in the "Federal Legislative List" whereas the Parliament as well as the Provincial Assemblies, both had the power to make laws contained in the "Concurrent Legislative List".

"Trusts and Trustees" were covered under the "Concurrent Legislative List" and therefore prior to the Eighteenth Amendment, the Federation (i.e Parliament) as well as the provinces were empowered to make laws relating to "Trusts and Trustees". The "Concurrent Legislative List" contained in the Constitution prior to the Eighteenth Amendment has been omitted. However, post Eighteenth Amendment, Trust Act, 1882 was considered as a valid legislation since provincial acts were not issued by the provinces.

During the current year, the Trust Act, 1882 has been repealed and is now replaced by the Trust Acts for the respective provinces [i.e. Sindh Trust Act, 2020, Punjab Trust Act, 2020, Balochistan Trust Act, 2020, KPK Trust Act, 2020 and Islamabad Capital Territory (ICT) Trust Act, 2020, hereinafter collectively known as the Trust Acts, 2020] which have been issued as required under the Eighteenth Amendment to the Constitution.

Regulation 39 of the Non-Banking Finance Companies and Notified Entities Regulation, 2008 requires that a Collective Investment Schemes (CISs) can only be established as a registered trust in accordance with the provisions of the Trust Act, 1882. Therefore, after the enactment of the Trust Acts, 2020, the CISs are now required to be registered under the relevant provincial acts.

The Trust Acts, 2020 initially issued by the provinces had the following main conditions / implications:

S.No	Conditions	Implications
1	Only natural person can create a trust	This is not possible in the case of Collective Investment Schemes (CISs) since the Asset Management Company creates the trust for a CISs.
2	Legal person cannot be a beneficiary	This can have implications in the case of CISs since the beneficiaries i.e, unit holders can be corporate entities.
3	Legal person cannot be a trustee	This will have implications as all the CISs have appointed corporate entities most notably Central Depository Company of Pakistan Limited or MCB Financial Services Limited as the trustee

Moreover, the Trust Acts, 2020 have also given the power to the Assistant Director / Commissioner to inspect the records of the Trusts, impose penalties of upto Rs 1 million, summon and provide information to the competent authorities and certain other clauses which will be difficult to apply considering the nature of operation of CISs.

The Trust Acts of all other provinces except the province of Sindh require fresh registration of all the trusts (that existed under the repealed act) within six months of the commencement of the relevant acts whereas the Sindh Trust Act, 2020 did not specify any timeline for registration of the existing trusts. A second public notice was issued on January 24, 2021 under the Sindh Trust Rules, 2020 whereby all the registered Trusts operating in the province of Sindh have been given an extension of fifteen days to register themselves under the Sindh Trust Act, 2020.

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We understand from our discussions with the Management Company and the Mutual Funds Association of Pakistan (MUFAP) that a Committee was formed at MUFAP level to deal with this issue.

Recently, the provincial assembly of Sindh through its notification on April 28, 2021 published 'The Sindh Trusts (Amendment) Act, 2021' to amend the Sindh Trusts Act, 2020. The major amendments with respect to the requirement of a natural person to create a Trust and inability of legal persons to be beneficiaries or Trustees of the Funds have been removed vide sections 3, 4 and 5 of "The Sindh Trusts (Amendment) Act, 2021".

We have been informed by the management that the Management Company has submitted the trust deeds of the Funds to the Registrar (acting under Sindh Trusts Act 2020) to fulfil the requirements for registration of Trust Deed under Sindh Trusts Act 2020.

10. CONTINGENCIES AND COMMITMENTS AND TRANSACTIONS WITH CONNECTED PERSONS / RELATED PARTIES

We have been informed by the management that there were no contingencies and commitments and transactions with connected persons / related parties other than those already disclosed in the financial statements of the Funds.

We wish to place on record our appreciation of the courtesy and cooperation extended to us during the course of our audit.

Yours truly

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ANNEXURE A

DETAILS OF ITEMS FOR WHICH SPECIFIC APPROVAL IS REQUIRED AS REFERRED TO IN PARAGRAPH 1(b) OF OUR LETTER ASR 0265 DATED AUGUST 4, 2021

Name of the Fund	Remuneration of the Management Company (including indirect taxes)	Remuneration of the Trustee (including indirect taxes)	Allocated Expenses	Selling and marketing expenses	Provision against Sindh Workers' Welfare Fund
	------------------------- (Rupees in 000) ----------------------				
MCB Cash Management Optimiser	113,912	23,608	23,728	-	44,371
MCB DCF Income Fund	68,376	3,419	4,034	15,732	5,273
Alhamra Islamic Asset Allocation Fund	69,112	3,889	2,442	19,428	10,759
Pakistan Cash Management Fund	3,677	1,017	1,164	-	3,310
Pakistan Capital Market Fund	13,230	1,060	469	3,879	1,938
Pakistan Income Enhancement Fund	7,928	582	686	3,196	982

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ANNEXURE B

DETAILS OF BONUS SHARES WITHHELD AS REFERRED TO IN PARAGRAPH 5 OF OUR LETTER ASR 0265 DATED AUGUST 4, 2021

Particulars	Bonus shares withheld	Carrying value of shares withheld
	(Number of shares)	(Rupees in 000)
Pakistan Capital Market Fund		
The Searle Company Limited	209	51
Al Shaheer Corporation Limited	805	18
Faysal Bank Limited	8,250	134
Alhamra Islamic Asset Allocation Fund		
IBL Healthcare Limited	691	59
The Searle Company Limited	196	46

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