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To: Securities and Exchange Commission of Pakistan

From: RIAA Barker Gillette, Advocates and Corporate Counsellors

Date: 9 September 2026

Re: Public and Stakeholder Comments on the Venture Capital Bill, 2026

A. INTRODUCTION

1. We thank the Securities and Exchange Commission of Pakistan ("**SECP**" or the "**Commission**") for placing the draft Venture Capital Bill, 2026 (the "**VC Bill**" or the "**Bill**") in the public domain and for inviting stakeholder comments before it is finalised and notified as the Venture Capital Act, 2026 (the "**VC Act**"). We set out below our comments and observations. They are offered in support of the Bill, not in opposition to it.

2. In our understanding, Venture capital in Pakistan is presently regulated not as a distinct activity but as a species of non-banking finance business. Under rule 2(1)(xxia) of the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003 (the "**NBFC Rules**"), made under Part VIII-A of the Companies Ordinance, 1984 (the "**1984 Ordinance**"), the notified forms of business include both "private equity and venture capital fund management services" and, separately, "venture capital investment". A "private fund management company" is a company licensed by the Commission to provide private equity and venture capital fund management services (rule 2(1)(xxxixc)), and the vehicle it manages is a "Private Fund" as defined in rule 2(1)(xxxixb): an arrangement pooling funds from eligible investors for investment in a portfolio of securities or other financial assets, whose participants have neither day-to-day control over the management of fund property nor the right to give directions in respect of that management.

3. That framework did not fall away with the repeal of the 1984 Ordinance. Section 509(1) of the Companies Act, 2017 repealed the 1984 Ordinance except Part VIII-A, consisting of sections 282A to 282N, and provided that the provisions of that Part, together with all related or connected provisions of the repealed Ordinance, apply mutatis mutandis to non-banking finance companies as if the Ordinance had not been repealed. The result is that non-banking finance regulation, including venture capital, is today governed by the sole surviving fragment of a statute otherwise repealed nine years ago, preserved by a savings clause pending replacement legislation that has not yet been enacted.

4. The consequence is that venture capital has, until now, been regulated by analogy. The licensing architecture, the capital adequacy concepts, and the supervisory apparatus were designed for balance-sheet lenders and asset managers, and venture capital has had to accommodate itself to a framework built for other businesses. A fund manager raising a Pakistani venture fund has had to explain to prospective limited partners why the vehicle sits under the one surviving Part of a 1984 Ordinance repealed in 2017, why its license category is shared with leasing and housing finance, and why its regulatory treatment is derived from rules addressed to collective investment schemes offering units to the public.

5. <u>What the Bill changes, and its importance</u>: The VC Bill addresses that directly, and its central design choices are sound:

   (a) it gives venture capital a dedicated primary statute, and begins to resolve the anomaly of an asset class regulated under subordinate legislation whose parent survives only as a Part expressly excepted from the repeal of the 1984 Ordinance;

   (b) it creates a purpose-built license for a venture capital fund management company ("**VCFMC**") and a distinct registration for the fund itself, so that the two are separately identified and separately supervised;

   (c) it recognises the mechanics of the asset class, in particular follow-on investment within a defined window and investment by one registered fund into another;

   (d) it restricts offering to eligible investors on a placement memorandum, correctly treating a venture fund as a private-placement product rather than a retail one;

   (e) it accommodates Shariah-compliant structures; and

   (f) it brings the regime within the Commission's administered legislation, with a defined appellate route.

6. Taken together, these give Pakistan the beginnings of a locally domiciled venture capital industry with a statutory identity of its own. That is a material advance and we support it.

7. In our considered view, a framework of this kind succeeds or fails on whether capital will actually use it. Our comments are therefore directed at a single question: what would prevent an institutional or foreign investor, or a domestic fund manager with a credible track record, from choosing to operate under this Act rather than around it? On our reading, there are a small number of issues capable of producing that outcome, and each is capable of being fixed at the drafting stage at no cost to the Bill's regulatory objectives. They concern, *inter alia*, the legal character and ring-fencing of the fund, the definition of control, the corporate identity of investee companies and cross-border structures, taxation, investor eligibility, the balance between criminal and administrative enforcement, fund-level integrity, and the constitutional discipline applicable to the Schedules.

B. COMMENTS

I. The legal character of a venture capital fund, and the absence of a statutory ring-fence

8. The Bill does not state what a venture capital fund is in proprietary terms. Section 2(1)(xv) read with Section 6(a) of the VC Bill establishes that the fund is a private or public limited company or a limited liability partnership, and that it is a legal entity separate from the VCFMC. It follows that legal title to the fund's assets vests in the fund itself. However, this aspect should be specified further, in particular, the mechanics of how the fund's assets should be treated, as is described below.

9. Instead, ring-fencing of the fund's assets should be ensured. Section 4(7)(a)(iii) requires the VCFMC to ensure that the assets of the fund are clearly segregated from its own, but that is an obligation on the manager, breach of which is addressed after the event by penalty under Section

10 of the VC Bill. It creates no proprietary consequence. We propose that the Bill include express provisions which protect the fund's assets in the event of the VCFMC's default on its obligations to the investors, such as providing that fund assets will be unavailable to the creditors of the VCFMC and will not require custody in the event of any breach of the provisions of the Bill. At present, the Bill does not address what happens to the fund's assets if the VCFMC becomes insolvent.

10. Comparatively, Regulation 41 of the Non-Banking Finance Companies and Notified Entities Regulations, 2008 obliges the trustee of an open-end or closed-end scheme to take under its control all the property of the scheme. The REIT framework under the REIT Regulations, 2022, separates scheme property, held by an independent trustee, from the management function exercised by the REIT management company. In both cases the separation is proprietary in nature, and is not merely a 'management function'. Investors in REITs and NBFCs are protected by the location of title of the assets, not only by the manager's compliance.

11. Ring-fencing is, in our view, the single most effective measure available to the Commission at no fiscal cost. We recommend that the VC Act expressly provide:

(a) that the assets of a registered venture capital fund are held for the account of that fund alone, are not available to the creditors of the VCFMC, and do not form part of its estate in liquidation or winding up;

(b) that securities capable of being held in book-entry form be held in an account with the Central Depository Company in the name of the fund, with equivalent custody or registration arrangements for assets that cannot be so held;

(c) that assets of each fund managed by the same VCFMC be segregated from those of every other fund it manages, with no commingling and no cross-collateralisation; and

(d) Section 9 of the VC Bill permits the Commission to suspend or cancel a license of the VCFMC. The Bill does not say what then becomes of the fund, who manages it, who issues capital calls, who executes an exit, and how a replacement VCFMC is appointed and on what terms. As drafted, the exercise of the Commission's supervisory authority over a fund manager can strand the fund and its investors in case of a cancellation or suspension of the VCFMC's license. We recommend a mechanism for the appointment of a replacement or interim manager by the fund itself through its board, or for a court-ordered winding up to take place, or alternatively a provision in the Act which empowers the Commission to prescribe regulations to this effect.

II. The definition of a venture capital fund is inconsistent with the Bill's own governance provisions and departs from settled Pakistani drafting

12. Section 2(1)(xv) of the VC Bill defines a venture capital fund as one in which "the unit holders shall have no control over management of the fund and the right to give directions in respect of such management". This potentially excludes funds which rely on directions of the unit-holders i.e., the investors. This is particularly true for institutional limited partners who routinely require protective rights, for instance, a limited partner advisory committee with consent over conflicts and valuation policy, key-man provisions, consent to extension of the fund's life, and no-fault removal rights. A fund carrying such terms arguably therefore has unit holders with "control" or

a "right to give directions" and so falls outside Section 2(1)(xv) of the VC Bill. If it falls outside that definition, it is not a venture capital fund and therefore falls outside the licensing requirement in Section 3(1) of the VC Bill and outside the offence in Section 3(3) of the VC Bill. The Bill would exclude from regulation the very funds that are most likely to be raised from sophisticated capital.

13. In this aspect, we recommend that Section 2(1)(xv) of the VC Bill adopts the established formulation, so that the law is predictable and consistent across the Commission's administered legislation. The proposed language is as follows:

> *"... and where the unit holders do not have any* ***day to day*** *control over the management of the fund, whether or not they have the right to be consulted or to give direction in respect of such management."*

14. If the Commission prefers to retain the stricter test, we recommend a proviso stating that the exercise of customary investor protections, including participation in an advisory committee, consent rights in respect of conflicts of interest, key-man and extension provisions, and rights of removal of the VCFMC, shall not of itself constitute control over the management of the fund.

III. The corporate identity of startups, holding structures, and the SBP–SECP coordination required to unlock global capital

15. Section 2(1)(xi) of the VC Bill defines a "startup company" as a company, and Section 2(2) of the VC Bill provides that expressions not defined take their meaning from, among other statutes, the Companies Act, 2017. That points to a company incorporated and registered in Pakistan. The definition of "eligible venture capital investments" in section 2(1)(iv)(a) refers to "startup companies and unlisted companies or businesses" without addressing jurisdiction of incorporation at all.

16. A substantial proportion of venture-backed Pakistani businesses are held through a foreign holding company, most commonly in Delaware, the Cayman Islands, Singapore or the ADGM, with a Pakistani operating subsidiary beneath it. That structure is not tax-driven, it is because that is where the instruments the asset class depends on are issued and enforced: preference shares with liquidation preferences, convertible instruments, option pools, drag and tag arrangements, and a capitalisation table that later-stage and international investors will underwrite. It is also where an exit occurs, whether by trade sale or by listing.

17. A registered venture capital fund that cannot subscribe at the holding-company level cannot participate in the rounds that actually fund Pakistani startups. The result would be that the Bill regulates only one portion of the transaction without considering the foreign holding and inevitably pushes the capital it is designed to attract back offshore.

18. In relation to the above, the Bill should recognise the holding structure expressly. We recommend that "eligible venture capital investments" and "startup company" be extended to include a company incorporated outside Pakistan which either (i) holds, directly or indirectly, a majority interest in a company incorporated in Pakistan that meets the startup company criteria, or (ii) itself satisfies a Pakistan-nexus test by reference to a specified proportion of its assets, revenue, employees or operations being located in Pakistan. A look-through approach should apply, with the turnover and age tests for determining the 'nexus' to be assessed at the level of the underlying

Pakistani operating business, rather than a newly incorporated holding company. Without a provision of this kind the Bill's definitions will be read as confined to domestically incorporated companies.

19. Secondly, it must be noted that an investment by a locally domiciled fund into a foreign holding company is an outward remittance governed by the Foreign Exchange Regulation Act, 1947 and the State Bank of Pakistan's Foreign Exchange Manual ("**Manual**"). Chapter 20 of the Manual contains provisions addressed to investment abroad by locally established mutual funds. It, however, contains nothing addressed to a registered venture capital fund, which should be addressed to consider the outward remittances that may be required to repatriate investments abroad into the foreign holding company.

20. We therefore recommend that the Act incorporates, and that SECP and the State Bank jointly develop and notify, a defined route for outward investment by registered venture capital funds. The key elements we would suggest are:

(a) a per-fund outward investment allocation, expressed either as a proportion of committed capital or as a monetary ceiling reviewable periodically;

(b) eligibility conditioned on a Pakistan-nexus test at the level of the underlying business, so that the facility funds Pakistani enterprise held offshore and not offshore enterprise generally;

(c) an automatic and documented right of repatriation of exit proceeds, dividends and distributions attributable to the permitted investment under the criteria specified above, without case-by-case approval;

(d) reporting through a designated authorised dealer, with the VCFMC accountable for compliance; and

(e) confirmation that units of a registered venture capital fund constitute securities eligible for investment by non-residents on a repatriable basis, so that the foreign individual and foreign corporate investors expressly contemplated by Schedule I can in fact invest and can in fact take their money out.

21. If a Singapore or ADGM holding company can be funded by a Pakistan-domiciled, SECP-registered venture capital fund, and if capital and returns can move in both directions along a defined and predictable route, then international partners can rely on the system and utilize the avenue to develop cross-jurisdictional capacity. In its absence, international partners either invest offshore into Pakistani founders without any Pakistani regulatory nexus, or they do not invest at all. A statute that recognises the corporate reality of how startups are held, coupled with an exchange-control route that recognises the same reality, converts the Bill into a channel for global capital with the local economy at its core.

IV. Investor eligibility under Schedule I

22. Schedule I to the VC Bill requires an individual investor, local or foreign, to have income of at least PKR 5 million in the preceding financial year and net assets of at least PKR 15 million excluding

the value of the personal residence. The test is cumulative and in our opinion, does not correspond with commercial reality.

23. The income threshold itself is not, in our view, excessive; a person earning at that level plausibly has the capacity to bear the loss of a venture investment. The potential difficulty is the conjunctive net-asset requirement. It excludes a category that may contribute significantly to venture capital investments i.e., experienced finance professionals, often early in their career, whose income qualifies but whose accumulated net assets do not. Globally, such a segment of the population invests significantly more in risk-based investments like venture capital funds.

24. Paragraph 2(ii) of Schedule I to the VC Bill meanwhile includes, as an institutional investor, "a company as defined in the Companies Act, 2017", with no income, net-asset, capital or assets-under-management requirement of any kind. A private limited company incorporated the previous week with nominal paid-up capital qualifies. Any individual who fails the Schedule I individual test can therefore incorporate a company and subscribe through it.

25. The two aspects highlighted above i.e., the individual and institutional investor eligibility must be reconciled. We recommend:

(a) For individuals: income of at least PKR 5 million in the preceding financial year, and either (i) net assets of at least PKR 15 million excluding the personal residence of the individual, or (ii) a prescribed qualification or experience — for example a person licensed or registered by the Commission in a relevant capacity, a holder of a certification issued by the Institute of Financial Markets of Pakistan, a CFA certificate-holder or a candidate having passed a specified level, a chartered or cost and management accountant, or a person with a specified minimum period of professional experience in fund management, investment banking, private equity or venture capital. This retains the income floor as the test of capacity to bear loss, while permitting demonstrable financial knowledge to substitute for accumulated wealth.

(b) A minimum subscription: Comparable regulatory regimes generally combine an investor eligibility test with a minimum investment threshold. In India, for example, an investor is required to commit at least INR 1 crore to an alternative investment fund. In the DIFC, the minimum investment is USD 500,000 for a Qualified Investor Fund and USD 50,000 for an Exempt Fund. In the United States, a fund relying on the Section 3(c)(1) exemption under the Investment Company Act of 1940 is generally limited to 100 beneficial owners. A minimum investment threshold provides a more practical safeguard than an income-based test, as it is easier to verify and helps ensure that a fund intended to remain privately held is not effectively offered to a broad investor base. We therefore recommend prescribing a minimum commitment for individual investors, with a lower threshold for employees and directors of the VCFMC; and

(c) Impose a minimum net-asset, paid-up capital or assets-under-management threshold on the institutional investor, or alternatively a look-through where a company has been incorporated or is being used principally for the purpose of making the investment in a venture capital fund.

V. Enforcement: separating criminal wrongdoing from regulatory failure

26. Section 3(3) makes operating without a license or registration an offence punishable with a fine which may extend to PKR 100 million, or imprisonment which may extend to three years, or both. The provision contains no requirement for such an action to be linked with criminal intent or *mens rea*. By contrast, Section 10(1)(a), which provides for administrative penalties, applies to a person who contravenes the Act and "knowingly authorizes or permits such failure, refusal or contravention", and it expressly excludes Section 3(3) from its scope.

27. The result is that the least culpable conduct addressed by the Bill, namely failure to obtain a license, is the only conduct for which no administrative penalty route exists at all. That is an unusual allocation and, in our respectful view, an unworkable one.

28. In our opinion, only actions such as fraud, investor deception and misappropriation of fund assets should attract criminal liability. Failure to obtain registration or a license for carrying out venture capital business should only attract civil liability. A criminal provision engages the presumption of innocence and requires every element to be proved beyond reasonable doubt. Where intent is the only available basis of liability and intent is difficult to prove, the practical outcome is not deterrence but under-enforcement, as this may result in individuals operating a venture capital business without license or registration to escape any form of liability solely due to the Commission being unable to prove intent.

29. Accordingly, we recommend the following amendments and additions to the Bill:

    (a) <u>A mental element in Section 3(3) of the Bill</u>: Section 3(3) should begin with the words "Any person knowingly carrying out…", so that the offence is committed by a person who knowingly carries on venture capital business without a license. In our view, such an amendment is essential since a criminal offence carrying imprisonment should not be capable of being made out on inadvertence.

    (b) <u>Imprisonment reserved for malice</u>: The penalty of imprisonment should be confined to cases involving fraud, deception, or misappropriation or misapplication of fund assets. Where the conduct is unlicensed/unregistered operation alone, the sanction should be financial alone, i.e., a fine.

    (c) <u>A regulatory tier for negligence</u>: Negligent and non-fraudulent contravention, including unlicensed operation, should be brought within Section 10 of the Bill as a civil or administrative wrong, determined by the Commission on the balance of probabilities after an opportunity of hearing. This gives the Commission a provable, usable instrument for routine supervision without the threat of imprisonment and reserves the criminal penalties for conduct that deserves such penalties. Where negligence is so gross as to be criminal, the criminal provision remains available.

    (d) <u>Procedural safeguards</u>: The Bill should specify the forum of trial, whether the offence is cognizable and bailable, and should require the Commission's recorded sanction before a prosecution is instituted. At present, the Bill is silent on these elements.

    (e) <u>A perimeter exemption</u>: We further recommend an exemption from Section 3(1) for investor pools below a threshold number of eligible investors participating in a fund which makes no public offer, coupled with a simplified notification-based registration, on the model of the exclusion in Section 3(c)(1) of the United States Investment Company Act of 1940 (under which, investor pools of up to one hundred investors are exempted from the registration requirement).

(f) The transition wind-down in Section 3(2): A person who does not apply within the twelve-month transition must wind down operations within thirty days of expiry of that period. In our considered opinion, thirty days is not a period in which a portfolio of unlisted, illiquid minority holdings can be realized. A forced sale in that window would destroy the investment value of the investors whom the same sub-section states an intention to protect. We recommend an orderly wind-down period linked to the realization of the portfolio, with the Commission empowered to supervise the process, to require reporting and to restrain new investment, but not to compel a distressed sale.

VI. Fund-level integrity: deployment, conflicts, valuation and leverage

30. The Bill imposes no minimum proportion of the fund that must be deployed in eligible venture capital investments, no limit on uninvested cash or liquid securities, and no investment diversification requirement. Comparably, the United States definition of a venture capital fund requires a substantial majority of the fund to consist of qualifying investments under Rule 203(l)-1(a)(2) of the Investment Advisers Act Rules, and India requires a Category I venture capital fund to invest a specified minimum proportion of its investable funds in unlisted equity or equity-linked instruments of venture capital undertakings under Regulation 16(2)(a) of the SEBI (Alternative Investment Funds) Regulations, 2012. Without such a requirement, a vehicle may register as a venture capital fund, hold government securities, and not materially function to provide venture capital to startups, or to hold investments in a venture capital fund in the manner or volume that the VC Bill envisions. We therefore recommend a minimum deployment percentage tested at the end of the investment period.

31. We further note that the Bill at present does not adequately address the issue of conflict of interest. The provisos to Section 6(d) of the VC Bill address disclosure of fees where one fund invests in another. However, the larger and more common conflict is the deployment of fund capital into companies affiliated with the VCFMC's own sponsors, directors or group. We recommend that a related-party investment be permitted only where the relationship is disclosed in the placement memorandum, follows the criteria specified under Section 208 of the Companies Act, 2017, and the investment is approved by a specified majority of unaffiliated unit holders or by an advisory committee of investors. Where a fund invests in another fund under common management, management fees should not be charged at both levels on the same deployment of capital.

32. In addition, we are of the opinion that the Bill may benefit from including valuation metrics for certain defined applications. Paragraph (xiii) of Schedule II to the VC Bill requires disclosure of valuation methodology, pricing of units and frequency of valuation, but the Bill imposes no independent valuation requirement, no minimum frequency and no standard. Net asset value determines the management fee, the carried interest and every investor's reported return, and the underlying assets are unlisted and illiquid. Self-valuation is the central conflict of interest in private funds, and it is unaddressed. We recommend an independent valuation of unlisted

holdings at least annually, by a valuer on a panel approved by the Commission, and mandatory disclosure of any departure from the stated valuation policy. Comparatively, India expressly regulates the valuation of alternative investment funds under Regulation 23 of the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012. Regulation 23(1) requires the fund to disclose its valuation procedure and methodology to investors, while Regulation 23(2) requires Category I and Category II AIFs to have their investments valued by an independent valuer at least once every six months. The frequency may be reduced to once a year only with the approval of investors representing at least 75% of the value of investments in the fund. We propose something similar to be factored into the VC Bill, to increase accountability and transparency from the perspective of stakeholders.

33. We further note that paragraph (ix) of Schedule II to the VC Bill requires a borrowing policy, but the Bill imposes no limit on the amount, purpose or duration of borrowing. A venture capital fund should deploy committed investor capital and should not expose its investors to open-ended leverage. That is particularly so in Pakistan, where exchange-rate volatility can convert foreign-currency borrowing into a loss independent of portfolio performance, in an asset class that is already at the high-risk end of the spectrum. The United States permits borrowing, guarantees and other leverage by a venture capital fund only up to a small proportion of aggregate contributed and uncalled committed capital under Rule 203(l)-1(a)(3) of the Investment Advisers Act Rules; India restricts Category I alternative investment funds to temporary borrowing, limited in duration, frequency and amount under Regulation 16(1)(c) of the SEBI (Alternative Investment Funds) Regulations, 2012. We recommend a statutory cap, and an express provision that borrowing may be used only to meet temporary shortfalls, to bridge capital calls or for working capital, and not to fund investments or distributions.

34. An additional recommendation to improve the Bill is the inclusion of a mandatory minimum sponsor or manager commitment to each fund a sponsor/manager manages, and mandatory disclosure in the placement memorandum of key-man provisions and of any advisory committee arrangements.

VII. The definition of a startup excludes the companies most likely to need venture capital

35. Section 2(1)(xi)(b) of the Bill defines a startup by reference to turnover "for any of the financial years since incorporation" not being greater than PKR 500 million. Under this definition, a company that has a single strong year early in its life may be permanently disqualified from being considered for a VC fund’s investment portfolio, regardless of how much capital it subsequently requires, provided that it does not fall within the ambit of Sections 2(1)(xi)(a), (c), and (d). The provision for follow-on investments provided in section 2(1)(iv)(b) of the Bill mitigates this risk only for companies already in the portfolio of a VC Fund, and only within ten years of initial investment.

36. The definition is also inconsistent with how venture-backed companies develop. A startup company typically raises successive rounds of capital, and by the later rounds is often approaching a listing, at which point its turnover will necessarily exceed any early-stage cap. A test tied to turnover in "any financial year" excludes precisely the later-stage, pre-IPO companies that still require venture capital before listing, and which represent the most realistic route to a domestic exit market.

37. We therefore recommend that:

(a) in the definition of a startup, turnover be tested at the date of the VC Fund's first investment in the company, rather than by reference to any financial year since incorporation; and

(b) in the alternative, or in addition, the definition include a company whose turnover exceeds the threshold, but which is not listed on the Pakistan Stock Exchange, aligning with the United States approach of testing whether the company is publicly traded at the time of investment rather than applying a revenue criterion at all.

VIII. A tiered framework proportionate to fund size and investor sophistication

38. The Bill applies substantially identical requirements to every venture capital fund regardless of size, number of investors, minimum commitment or strategy, while mature frameworks calibrate the requirements to the type of fund in question. For instance, the DIFC's framework distinguishes between Public Funds (which are subject to full prospectus and independent oversight requirements), Exempt Funds (which are offered by private placement to professional clients subject to a minimum subscription), and Qualified Investor Funds (investment in which is limited to professional clients subscribing at a substantially higher minimum and benefiting from an expedited and proportionate regime). Alternatively, the United States calibrates requirements by reference to investor eligibility and sophistication through the exclusions in Sections 3(c)(1) and 3(c)(7) of the Investment Company Act, 1940 and the accredited investor criteria.

39. In light of international best practices, we recommend the following three-tier structure creating different categories of venture capital funds, for adoption in the Bill:

(a) Category A: a registered venture capital fund, subject to the full regime;

(b) Category B: a Qualified Investor Venture Capital Fund, restricted to institutional and accredited investors meeting a substantial minimum commitment criterion, benefiting from expedited registration and proportionate ongoing obligations, while remaining subject to mandatory audit, independent valuation and disclosure; and

(c) Category C: a notification-based regime for small angel pools falling within the perimeter exemption proposed at paragraph 29(e) above, providing a route to regularization for small funds without placing the full licensing burden on such funds. The creation of such a category may be compared to the creation of the Growth Enterprise Market Board ("**GEM Board**") of the Pakistan Stock Exchange ("**PSX**"), which operates in parallel with the Main Board of the PSX. The creation of the GEM Board created an enabling market for small, medium, and high-growth startups to enable them to raise capital. Accordingly, we propose the creation of a similar enabling market for smaller venture capital funds.

IX. Process, timelines and internal inconsistencies

40. Fund formation is a jurisdictionally competitive activity, with some jurisdictions offering greater incentives for fund formation than others. Delay and indeterminacy in the formation, registration and licensing processes may themselves constitute a reason to domicile a fund elsewhere. In this regard, the following provisions of the VC Bill require attention:

(a) Section 4(4) of the Bill allows the Commission forty-five working days, approximately nine calendar weeks, for rendering a decision on a license application, and the period runs afresh from receipt of any additional information the Commission may seek, without limit on the number of such requests. There is no deemed approval for a licensing application. We recommend a single completeness review, an outer limit on the total period, and a deemed-approval mechanism for the qualified-investor tier of funds.

(b) Section 5(2) of the Bill prescribes no timeline at all for registration of a fund. One should be inserted.

(c) Section 7 of the Bill requires the VCFMC to submit the placement memorandum within three working days of circulating it to eligible investors, while the proviso requires that, prior to publication, the memorandum be amended in accordance with the Commission's comments. Circulation has by then already occurred. Further, no time limit is placed on the Commission's comments, which converts the proviso into an open-ended veto over the launch of a fund. We recommend that the section be amended to provide that a placement memorandum shall, before being circulated to the investors, be submitted to the Commission for its review and comments. After such submission, the Commission should be provided a defined time period (for instance, up to fifteen days) during which it shall review the memorandum and provide its comments on the same to the VCFMC. At this point, the VCFMC should be allowed up to, for instance, fifteen days during which it shall incorporate the Commission’s comments and obtain final approval of the Commission on the placement memorandum, to enable the VCFMC to circulate the same to the investors.

(d) Section 5(3)(b) of the Bill requires seven days' prior notice of the removal or replacement of the chief executive officer or designated partner. However, such a prior notice may not reasonably be given where a removal is summary, for example, a dismissal for misconduct. In our view, for Section 5(3)(b) alone, the notification obligation should arise after the occurrence of any removal or replacement. Alternatively, a proviso may be added after Section 5(3)(b) of the Bill, providing that where a replacement or removal is of a summary nature, such as in instances of replacement/removal for misconduct, the notification obligation shall be complied with within seven days of the replacement/removal.

(e) Section 5(4) of the Bill requires the approval of fifty-one per cent of unit holders by value for "any change in the placement memorandum under sub-section (3)". If this is a reference to Section 5(3)(a) of the Bill, we propose that the relevant sub-section, i.e., sub-section 3(a), be specified to avoid interpretative errors.

X. Delegation, the Schedules, and due process

41. Section 21 empowers the Commission, by notification in the official Gazette, to amend any Schedule to the Act, and provides that such amendment "shall have effect as if enacted in this Act". No prior publication, consultation or transitional protection is required. By contrast, section 18(2) requires that draft regulations be published in the Gazette and placed on the Commission's website for not less than fourteen days for public comment, and section 19(2) imposes the same discipline on rules made by the Federal Government.

42. The Bill therefore attaches consultation safeguards to the instruments that are lower in the legal hierarchy, and none at all to amendments that are declared to take effect as though contained in the primary statute. That inversion is difficult to justify on principle. It is more difficult still when regard is had to what these particular Schedules contain.

43. This distinction is particularly difficult to justify because the Schedules are not confined to administrative or technical matters. They prescribe substantive conditions which determine the rights and obligations of persons regulated under the Bill and, in several instances, are directly connected with contraventions carrying significant regulatory consequences. In particular:

    (a) Schedule I determines the persons eligible to invest. An amendment increasing the applicable thresholds or otherwise narrowing the eligibility criteria could, upon taking effect, render an existing unit holder ineligible. The Bill does not presently address the consequences for existing unit holdings, subsisting commitments, or the fund's continuing compliance with section 4(7)(b)(vi), which requires the VCFMC to ensure that subscriptions are invited only from eligible investors. The Bill should therefore provide expressly for the treatment of existing investors and investments where Schedule I is amended.

    (b) Schedule IV prescribes minimum equity or capital requirements. An amendment increasing those requirements could immediately place an existing licensee in breach of section 4(7)(a)(v), notwithstanding that the licensee was fully compliant immediately before the amendment. Such a contravention may attract the penalty contemplated by section 10, including a monetary penalty of up to PKR 50 million, reimbursement of profit gained or loss avoided and the Commission's costs, and may also have consequences for the continuation of the license. A reasonable statutory or regulatory compliance period should therefore be prescribed before an increase in the minimum capital requirement becomes enforceable against an existing licensee.

    (c) Schedule V sets out the fit and proper criteria applicable to relevant persons. An amendment adding a new criterion could cause an incumbent promoter, director or chief executive who was previously compliant to cease to satisfy the applicable requirements, thereby potentially triggering the three-working-day reporting obligation and the ninety-day replacement obligation under section 4(7)(b)(vii). The Bill should distinguish between a person becoming unsuitable by reason of conduct or circumstances warranting immediate regulatory intervention and a person becoming technically non-compliant solely because the applicable regulatory criteria have subsequently been amended. In the latter case, a reasonable transition or regularisation period should be provided, subject to the Commission's power to take immediate action where investor protection or market integrity so requires.

44. Further, the expression "as if enacted in this Act" also warrants reconsideration. The difficulty is not that such wording directly renders the resulting notification immune from judicial review, rather, it creates uncertainty as to the legal character and permissible scope of an executive instrument which may alter substantive conditions prescribed by the Act. A delegated power should remain confined to the policy, standards and limits established by Parliament and should not operate as an unrestricted power to alter substantive statutory obligations. The words "as if

enacted in this Act" should therefore be deleted or replaced with language making clear that an amendment to a Schedule takes effect only through the power vested in the Federal Government.

45. We recommend that section 21 be amended to provide that:

(a) the publication and consultation requirement in section 18(2) be applied to any amendment of a Schedule under section 21;

(b) the words "as if enacted in this Act" be deleted or qualified, as specified above;

(c) the Act provide expressly that no amendment of Schedule I, IV or V shall operate to place an existing licensee, registered fund or unit holder in contravention of the Act without a stated transitional period, which we would suggest should be not less than twelve months; and

(d) the Commission should not exercise the power under section 21 to impose, through an amendment to a Schedule, a substantive obligation which is not reasonably connected with and authorised by the provisions and policy of the Act.

46. Section 9(1) provides an opportunity of hearing before suspension or cancellation, but the proviso appears to confer that opportunity upon the venture capital fund management company alone. Where it is the registration of a fund that is to be cancelled, the fund itself should be afforded an opportunity of being heard because it is legally and economically distinct from its manager. The interests of the fund and its unit holders may also diverge from those of the VCFMC. The Bill should instead require appropriate notice to unit holders and provide for such mechanism of representation or protection of their interests as may be prescribed.

47. Section 11 confers extensive recovery powers, including attachment and sale of property, appointment of a receiver, and recovery as arrears of land revenue. The Bill contains no express provision staying recovery pending an appeal under section 10(2) read with section 33 of the Securities and Exchange Commission of Pakistan Act, 1997. Recovery effected before an appeal is decided is frequently irreversible in practice. We recommend an express provision that recovery is stayed pending disposal of an appeal, on such terms as the appellate forum considers appropriate.

48. Section 10(1)(ii) empowers the Commission to require reimbursement of any profit gained or loss avoided, but does not identify the recipient. Where the profit was gained at the expense of unit holders, the disgorged amount should be applied first in compensating them, and a mechanism for doing so should be provided. Section 15 should similarly specify responsibility for the cost of a special audit. In particular, where a special audit is necessitated by a breach attributable to the VCFMC, the cost should ordinarily be recoverable from the VCFMC rather than automatically being charged to the fund and thereby borne by investors.

XI. Parallel regimes, and the transition from the NBFC framework

49. The proviso to Section 3(1) of the Bill states that the Act shall not apply to private equity and venture capital fund management services carried on by a private fund management company before commencement of the Act, which shall continue to be governed by Part VIII-A of the Companies Ordinance, 1984 and the rules and regulations made thereunder.

50. On the other hand, Section 4(5) of the Bill deems an existing private fund management company carrying out private equity and venture capital fund management services to be licensed under the Act, subject to confirmation, while requiring clear segregation between the two businesses. Yet Section 3(2) of the Bill requires any person carrying on venture capital business at commencement to apply for a license within twelve months. Under these provisions, the relationship between a saving, a deeming provision and a mandatory transition is not made clear, and the same manager may be simultaneously preserved under the old regime, deemed licensed under the new one, and obliged to transition.

51. A further category is not addressed at all. Rule 2(1)(xxia) of the NBFC Rules notifies "venture capital investment" as a form of business distinct from "private equity and venture capital fund management services". The Bill's transitional provisions engage only with the latter, and make no reference to the former. The Commission should clarify in the Bill whether venture capital investment as a form of business is also covered by the Bill.

52. There is, however, an existing mechanism which may resolve much of this and which we would invite the Commission to make express. The proviso to rule 2(1)(xxxixb) of the NBFC Rules excludes from the definition of "Private Fund" any pool of funds which is "separately regulated by the Commission or which is already established under any other specific law". On the enactment of the VC Act, a fund registered under it would arguably cease to be a Private Fund under the NBFC Rules by operation of that proviso. Rather than leaving that to inference, we recommend that:

    (a) the Act state expressly that a venture capital fund registered under it, and a VCFMC licensed under it, are not a Private Fund and a private fund management company respectively for the purposes of the NBFC Rules;

    (b) consequential amendments to the NBFC Rules and to the Non-Banking Finance Companies and Notified Entities Regulations, 2008 be prepared and notified simultaneously with the commencement of the Act, rather than afterwards; and

    (c) the Act state, in terms, which activities must migrate, which may remain under the existing framework, whether a single entity may carry on both activities and on what conditions of segregation, and the position of the "venture capital investment" form of business.

53. We would add one further observation of a structural character. Because Part VIIIA was excepted from repeal rather than re-enacted, and applies as if the 1984 Ordinance had not been repealed, the enactment of the VC Act will produce a regime in which a 2026 statute operates alongside a preserved fragment of the 1984 Ordinance kept alive by Section 509(1) of the Companies Act, 2017, with the same subject matter divided between them. That is an unsatisfactory position for a market that is being asked to attract institutional and international capital, and it will be the first thing a foreign investor's counsel raises. The VC Bill is the first opportunity in nine years to begin retiring Part VIIIA in an orderly way. We recommend that the Act state expressly what it does to Part VIIIA and to the NBFC Rules in respect of venture capital, whether by way of partial disapplication, consequential amendment or a defined sunset for the venture capital forms of business, rather than leaving the two frameworks to coexist and be reconciled by inference.

XII. Taxation: the exemption as presently conditioned will not be available in the years in which it matters

54. The VC Bill contains no separate provision for the treatment of tax. Therefore, it is not clear within the intended drafting, whether tax is intended to arise at the level of the fund, at the level of the investor, or at both. For an asset class whose life-cycle depends entirely on the treatment of a long-dated, illiquid return profile that is loss-making for most of the fund's life except at the end, the treatment of tax is critical. Additionally, we note that the existing tax treatment of venture capital funds, namely the exemption granted to the same under Clause 99C of Part I of the Second Schedule to the Income Tax Ordinance, 2001 (the "**ITO**") is, in its present form, incompatible with the very structure of a venture capital fund regime, as will be discussed below.

55. We therefore suggest a series of possible interventions, which would require correspondence between the Federal Board of Revenue and the Commission to ensure that the tax treatment of venture capital funds can be effectively governed across the board. This has previously been incorporated within the REIT structure. The corporate architecture for REITs is governed by the REIT Regulations, but the fiscal treatment is separately covered under the ITO including the exemption for a REIT scheme, and the relief on transfer of immovable property into a scheme.

56. We respectfully suggest the same approach be adopted here and adopted now, rather than after enactment. In our view, a standing working group between the Commission, the Federal Board of Revenue and the Revenue Division, tasked with preparing the Finance Bill amendments in parallel with the VC Bill, should be constituted so that the Act and its fiscal counterpart commence together.

57. We note that the prevailing model for fund-level exemption in Pakistan conditions relief on distribution of not less than ninety per cent of accounting income, as reduced by accumulated losses and unrealised capital gains, to unit or certificate holders. This distribution condition, i.e., the tax exemption pre-condition under Clause 99C of Part I of the Second Schedule to the ITO, is borrowed from the REIT regime where such a condition is practically feasible. However, in our view, the distribution pre-condition for the application of the tax exemption is not practicable in the venture capital model.

58. A venture capital fund is structurally different from the REIT model of distribution. It draws down committed capital in tranches, acquires minority equity in loss-making unlisted companies which pay no dividends, and realises its return on exit, conventionally seven to ten years after first investment. In the intervening years there is characteristically neither accounting income at the level of the fund nor any amount actually received from the portfolio companies. The condition, therefore, may be impracticable for newly established venture capital funds.

59. Since accounting income is to be reduced by accumulated losses, and a venture fund accumulates losses precisely in its early years, a fund which does earn some gross income, for example return on undeployed capital held in government securities, will frequently have little to no accounting income once that reduction is applied.

60. Even where there is income, distributing it destroys the return the fund exists to generate. There is a second and independent objection, which arises in the years in which a fund does have accounting income. Amounts held by a venture capital fund are rarely free. They are typically

committed in one of three ways: as reserves for follow-on investment in existing portfolio companies, which in a conventionally constructed fund may account for a substantial proportion of committed capital; as amounts payable on the conversion or triggering of instruments already executed, including simple agreements for future equity and convertible notes, under which the fund has a subsisting obligation to fund; and as provision for management fees, expenses and unfunded commitments over the remaining life of the fund.

61. A condition requiring the distribution of ninety per cent of such amounts would compel a fund to distribute capital it has already committed, to forgo its pro-rata rights in the follow-on rounds where much of the return in this asset class is concentrated, and then to seek to re-call the same capital from its investors, which many fund agreements do not permit or permit only within narrow recycling limits. The condition would therefore not merely be difficult to satisfy; satisfying it would defeat the investment strategy and reduce investor returns. A fiscal condition that penalises the fund for behaving prudently is not a condition that should be applied to this asset class at all.

62. Additionally, the distribution model is not the international norm for venture capital. Leading fund jurisdictions condition relief on what the fund does and where its substance lies, not on whether it has moved cash to its investors in a given year. The following comparison is instructive:

Jurisdiction	**How fund-level relief is conditioned**	**Distribution required?**
Pakistan (REIT / CIS model, as proposed for VC)	Distribution of not less than 90% of accounting income, as reduced by accumulated losses and unrealised capital gains.	Yes — annually.
India	Statutory pass-through for SEBI-registered Category I and II Alternative Investment Funds (which include, without limitation, venture capital funds, private equity funds, and real estate funds) under s.115UB, Income-tax Act 1961: income other than business income is not taxed at the fund and is taxed in the unit holder's hands in the same character, as if invested directly.	No. Investors are taxed whether or not income is distributed.
United States	A venture fund is conventionally a fiscally transparent partnership. Relief is not conditioned on distribution; the qualifying tests that matter are portfolio-composition and leverage thresholds for the definition of a venture capital fund.	No.
Singapore	Sections 13O and 13U: exemption for specified income from designated investments, conditioned on a Singapore-based licensed fund manager, minimum assets under management, a minimum number of Singapore-resident investment professionals, tiered minimum local business spending, and (from 2025) deployment of at least 10% of AUM, or USD 10 million, whichever is lower, into qualifying local investments.	No. Conditions are substance- and deployment-based.
Hong Kong	Unified funds exemption: relief attaches to qualifying transactions carried out or arranged by a specified person, not to the movement of cash to investors.	No.

63. The above comparison highlights the following. First, no leading venture capital jurisdiction conditions fund-level relief on annual distribution. Second, the policy objective that the distribution condition serves, namely preventing indefinite deferral of tax, is achieved elsewhere by taxing the investor on accrual rather than by compelling the fund to move cash. Third, where jurisdictions wish to direct capital domestically, they do so through a deployment test measured as a proportion of assets, not through a test based on the corporate form or place of incorporation of the investee.

64. We recommend that the distribution condition be replaced, in the ITO and by way of the Finance Bill, with a set of conditions capable of being satisfied by an asset class without annual income. In our view, this would be vital to increasing engagement with the venture capital fund regime, as the offering of a practicable tax exemption would encourage greater participation in the market. The tax exemption as it presently stands may, in our opinion, actually disincentivize participation as fund managers may consider the distribution requirement to be too onerous to meet, especially in the initial years of a venture capital fund's operation. Our primary and alternative recommendations in this regard are as follows.

65. The primary solution, and the one which best protects the revenue, is to confer fiscal transparency on a registered venture capital fund on the model of section 115UB of the Indian Income-tax Act, 1961, which accords pass-through status to SEBI-registered Category I and Category II alternative investment funds. Income other than business income is not taxed at the fund level; it is taxed in the hands of the unit holders in the same character and proportion as if they had made the investments directly, whether or not it is distributed. The advantage of this approach for the Federal Board of Revenue is as follows: because the investor is taxed on accrual, there is no deferral for a distribution condition to prevent, and the condition becomes unnecessary. The revenue is protected, and the fund is not required to dismantle its own strategy to secure relief.

66. Alternatively, if fund-level exemption conditioned on eligibility is preferred to transparency, we recommend that the conditions be the following, in substitution for the distribution test:

(a) <u>A deployment test</u>: A minimum proportion of the fund's committed capital, tested at the end of the investment period rather than annually, must be invested in eligible venture capital investments. This is the condition which ensures that a vehicle claiming the relief is in fact a venture capital fund, and it addresses the concern identified at paragraph 30 above that nothing in the Bill presently requires a registered fund to invest in venture capital at all. The United States and India both apply a threshold of this kind.

(b) <u>A Pakistan-nexus deployment test</u>: A minimum proportion of the fund must be deployed into businesses whose substantive operations are in Pakistan, measured at the level of the operating business by reference to assets, employees, revenue or a combination of them. We emphasise that this test should be expressly neutral as to corporate structure: it should be satisfied whether the fund subscribes directly into a Pakistani company or into a foreign holding company whose operating business is in Pakistan. A test framed instead by reference to the place of incorporation of the investee, or which required direct-to-target investment, would cut directly against the recognition of holding structures recommended at paragraph 18 above; it would make the very structure the Act permits fiscally punitive, and would push funds back into the offshore arrangements that the Bill is intended to displace. Singapore provides the model: its fund exemption schemes were amended with effect from 2025 to require a proportion of assets under management to be deployed into qualifying local investments, expressed as a percentage of assets and not as a restriction on structure.

(c) A substance test: The fund must be managed by a VCFMC licensed under the Act and resident in Pakistan, employing a minimum number of investment professionals in Pakistan and incurring a minimum level of local business expenditure, including management fees paid to the Pakistani manager, local salaries and professional and operating costs incurred in Pakistan. This is the architecture of Singapore's Sections 13O and 13U, and it is directed at precisely the objective stated in the preamble to the Bill: not merely that Pakistani businesses receive capital, but that a domestic venture capital industry, with its people, its decision-making and its economic activity, is established in Pakistan. A substance condition rewards that outcome; a distribution condition does not measure it at all.

(d) A realisation-linked distribution obligation, with reinvestment relief: If the Federal Board of Revenue requires a distribution element, it should attach to realisation rather than to the accounting year: a specified proportion of the net realised proceeds of a disposal should be distributed within a defined period after that disposal, with an express carve-out for amounts reinvested in further eligible venture capital investments, or reserved for follow-on investment in or obligations to existing portfolio companies, within a defined window. Reinvestment relief of this character is well precedented; the United States permits a rollover of gain on qualified small business stock into further qualifying stock within a short window, and the United Kingdom's venture schemes contain analogous reinvestment provisions. This preserves the anti-deferral objective while removing the perverse incentive to break the fund's reserve policy.

(e) An express no-income proviso in any event: Whatever conditions are adopted, the ITO should state expressly that where a fund has no accounting income for a tax year, as reduced by accumulated losses and unrealised capital gains, no distribution is required in that year for the purposes of the exemption. Courts construing a fiscal statute apply the literal rule; a condition premised on the existence of accounting income and an act of distribution will not, in the absence of express words, be read as satisfied by a fund with neither. The absence of such words is the defect.

67. We would not recommend attempting to achieve any of this by a non-obstante provision in the VC Act. A court construing the ITO will look to the words of the taxing statute itself. Section 23 of the Bill in any event preserves rather than displaces other legislation, and an exemption granted otherwise than under the ITO is likely to be resisted by the department. The correct instrument is an amendment to the ITO through the Finance Bill.

68. The Bill permits a venture capital fund to be constituted as a company or as a limited liability partnership. However, the tax outcomes of those two vehicles diverge sharply: a company is a separate taxable entity whose distributions attract dividend treatment and withholding; an association of persons (which includes limited liability partnerships) is taxed at entity level with the members' share treated differently. The Bill should not offer a choice of vehicle without the fiscal consequence of each choice being settled and published. We recommend that the

treatment of a limited liability partnership registered as a venture capital fund be confirmed expressly in the ITO. If the pass-through recommendation above is adopted, this issue largely resolves itself, since transparency would apply to the registered fund irrespective of the vehicle chosen.

69. We would also invite the Commission to take up with the Federal Board of Revenue: relief against double taxation where one registered fund invests in another under section 2(1)(iv)(c) and section 6(d); the withholding position on distributions to resident and non-resident unit holders; double taxation treaty access for foreign limited partners investing through a Pakistani fund; the characterisation of gains on disposal of unlisted securities held by the fund; and the position under section 113 for a fund holding assets that generate no receipts.

C. CONCLUSION

70. The VC Bill is a substantial improvement on a framework in which venture capital has been regulated by analogy to businesses it does not resemble. Its architecture is sound. The comments above are directed at the small number of provisions which, in our assessment, would determine whether capital in fact uses the regime the Bill creates: the ring-fencing of fund assets, a definition of control that matches market practice and the Commission's own settled drafting, recognition of the holding structures through which Pakistani startups are actually funded, and a fiscal treatment that is capable of being relied upon without litigation.

71. Of these, the taxation issue and the exchange-control issue cannot be solved by the Commission acting alone. Both require the Commission to secure alignment with, respectively, the Federal Board of Revenue and the Revenue Division, and the State Bank of Pakistan. The REIT experience shows that such alignment is achievable when the regulatory and fiscal instruments are developed together. We would respectfully urge that the same course be followed here, and that the Finance Bill amendments and the exchange-control framework be settled before, not after, the Act is notified.

We would be pleased to assist the Commission further, including by participating in any consultative session or working group, or by providing draft language for any of the amendments proposed above.

We hope these comments assist the Commission in finalising the VC Bill.

Yours faithfully,

RIAA Barker Gillette

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Advocates and Corporate Counsellors