Study Notes for NISM Series VII : Securities Operations & Risk Management (SORM)

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NISM SERIES VII : SECURITIES OPERATIONS & RISK MANAGEMENT

Exam Details

Total Questions	**100 X 1 Marks**
Type	**Multiple Choice**
Pass Score	**50%**
Duration	**2 Hours**
Negative marks	**-0.25**

Chapterwise Weightages

Unit 1: Introduction to Securities Markets	**5%**
Unit 2: Market Participants in the Securities Markets	**10%**
Unit 3: Introduction to Securities Broking Operations	**20%**
Unit 4: Risk Management	**15%**
Unit 5: Clearing Process	**15%**
Unit 6: Settlement Process	**15%**
Unit 7: Investor Grievances and Arbitration	**10%**
Unit 8: Other Services Provided by Brokers	**10%**

Chapter 1: Introduction to the Securities Market

Financial market :

- Enables efficient **transfer** and **allocation** of financial resources for productive activities in the economy.
- **Providers of surplus funds** : Households, businesses and governments
- **Users of funds** : Businesses, governments and households
- **Intermediaries** : Banks, financial institutions, mutual funds and insurance companies, among others, channelize the available surplus funds from lenders to the users.
- Important function of financial markets – provide **liquidity** and exit **options**.
- Financial Market Comprises – **Securities Market** and **Money market**

Electronic Gold Receipt - an electronic receipt issued on the basis of deposit of physical gold in accordance with the SEBI regulations under section 31 of the said Act.

Securities Market : (Note : Securities as defined in the SCRA, 1956 includes - Shares, scrips, stocks, bonds, debentures, debenture stock,derivatives, Collective Investment Scheme, Security receipt, Mutual funds, Government Securities, Rights or interest in securities)
The securities market has two **interdependent** and **inseparable** segments :

- New issues (the primary market)
- Stock (secondary) market.

- Primary market ensures availability of adequate capital at reasonable rates to finance **expansion, diversification or consolidation** of companies.
- Issuer has direct contact with the investor – Primary market
- Lawyers, Bankers to the issue, Brokers, and Depository participants.

Methods of raising capital in primary market :

- **Initial Public Offer (IPO) or Further Public Offer (FPO)** : It is a public issue, anybody and everybody can subscribe for it.
- **Private Placement** : the issue is made to select group of people.
- **Rights Issue**: fresh shares are issued to existing shareholders at a particular price.
- **Bonus issue/stock split** : Issues without any cost to the existing shareholder(Free Shares).

The secondary market provides liquidity to these instruments (ie., IPO, FPO issued in primary market) through trading and settlement on the stock exchanges.

- An active secondary market promotes the **growth of the primary market** and **capital formation**.
- Provides primary market investors a **continuous market** where they have an option to liquidate their investments.
- Dealings are between two investors and the issuer are indirect - Secondary market

The secondary market operates through two mediums -

- **Over-The-Counter (OTC) market**
- **Exchange Traded Market / Screen Based Trading System** (SBTS).

OTC markets –

- Informal type of markets where trades are negotiated between the parties.
- Securities are traded and settled bilaterally over the counter

Exchange Traded Market

- Formal type of markets - Trading and settlement is done through the Stock Exchanges.

- The trades executed on the exchange are settled through the clearing corporation, who acts as a counterparty and guarantees settlement.

Capital market intermediaries - Registrars and Transfer Agents, Custodians and Depositories

- Provide important infrastructure services to both the primary and secondary markets.

Money market is divided into 2 segments:
(a) Borrowing and Lending segment with or without collaterals;
(b) Asset Market involving purchase and sale of money market instruments.

- It is a market for short term funds and instruments having a maturity period of <= 1 year.
- Deals primarily in short-term debt securities and investments, such as –
    - Term Money
    - Certificates of deposit (CDs)
    - Repos and Treasury Bills (T-bills)
    - Market Repo
    - Triparty Repo in Gsec
    - Cash Management Bills
    - Repo in Corp Bond
    - Call/Notice money market
    - Commercial papers

Equity Shares represents the form of **fractional ownership** in a business venture.

- Equity shareholders collectively own the company - bear its risk and enjoy the rewards of ownership.

Debentures are instruments for raising **long term deb**t.

- Secured by **tangible assets**.
- There are fully convertible, non-convertible and partly convertible debentures.
- NCDs are repayable on maturity.
- Debentures can be pure debt or quasi-equity

Government Securities issued by central and state government also traded on Equity segment of the Exchange.

Warrants entitle an investor to buy equity shares after a specified time period at a given price.

A Mutual Fund is an investment vehicle that pools money from numerous investors who wish to save or make investments having similar investment objective

Exchange Traded Fund :

- ETF is a marketable security that tracks an index, commodity, bonds, or a basket of assets
- Unlike regular mutual funds, an ETF trades like a common stock on a stock exchange.
- The traded price of an ETF changes throughout the day like any other stock, as it is bought and sold on the stock exchange.
- The trading value of an ETF is based on the net asset value of the underlying stocks that an ETF represents.

Indian Depository Receipt (IDR)

- IDR - an instrument denominated in Indian Rupees in the form of a depository receipt created by a Domestic Depository
- IDRs are issued by foreign companies to Indian investors.
- IDRs are depository receipts which have the equity shares of the issuing company as the underlying security.
- The underlying shares are held by a foreign custodian and the DRs are held in the Indian depository.
- IDRs are listed in the Indian stock exchanges.
- The investor can either hold the IDR, trade in them in the stock exchange or request for redemption into the underlying shares.
- Redemption is permitted after 1 year from the date of listing.
- Two-way fungibility of IDRs is permitted i.e. depository receipt can be converted into underlying shares and the underlying shares can be converted into depository receipt

Derivative Market and its Products

- Derivative is a product whose value is derived from the value of an underlying asset or group of assets—a benchmark.
- The derivative is a contract between two or more parties.
- The most common underlying assets for derivatives are stocks, bonds, commodities, currencies, interest rates, and market indexes.
- Derivative products are in the form of Forwards, Futures, Options and Swaps.
- Derivatives can trade over-the-counter (OTC) or on an exchange.

Forward contract is a promise to deliver an asset at a pre- determined date in future at a predetermined price.
Index/Stock Future is an agreement between two parties to buy or sell an asset at a certain time in the future at a certain price
Index / Stock Options are of two types - **Calls** and **Puts**. Calls give the buyer the right, but not the obligation, to **buy** a given quantity of the underlying asset, at a given price on or before a

given future date. Puts give the buyer the right, but not the obligation, to **sell** a given quantity of the underlying asset at a given price on or before a given date.

Weekly and monthly equity index futures & options contracts expire on the different days of expiry week or month.
In case the expiry day is a trading holiday, the contracts expire on the previous trading day.
A new contract is introduced on the next trading day following the expiry of the near month contract.

Currency Derivatives

- contracts are traded on four INR pairs i.e., USDINR, EURINR, GBPINR and JPYINR
- contracts are traded on 3 cross currency pairs i.e., EURUSD, GBPUSD and USDJPY
- The final settlement price for USDINR, EURINR, GBPINR and JPYINR is the FBIL (Financial Benchmarks India Pvt. Ltd.) reference rate.
- FBIL is an independent benchmark administrator for interest rates and foreign exchange.
- The final settlement price for cross currency pairs is derived from crossing respective FCY-INR rates.

Commodity Derivatives→raw or primary products (gold, silver, metal, energy and agricultural goods) are exchanged.

Interest Rate Derivatives
Interest Rate Futures (IRF) are standardized interest rate derivative contracts traded on a recognized stock exchange to buy or sell a notional security or any other interest-bearing instrument or an index of such instruments or interest rates at a specified future date, at a price determined at the time of the contract.
Interest rate futures are available on single GSec within maturity basket of 4-8 year, 8-11 year and 11-15 years, 91-day T-Bills and Overnight MIBOR

Debt Market →In India, the debt market is broadly divided into two parts: **government securities** (G-Sec) market and **the corporate bond market**.

Corporate Bond Market or corporate debt market is a market where debt securities of corporate such as corporate bonds, T-bills, commercial papers and certificate of deposits are issued and traded. Corporate Bond secondary market is mainly OTC market, where the trades are negotiated between the participants on phone or through intermediaries. In India, corporate bonds are issued mainly on private placement basis (around 95%) and only small part of the total issuances are through public offer.

Real Estate Investment Trusts (REIT) are trusts registered with SEBI that invest in commercial real estate assets. REIT assets" means real estate assets and any other assets held by the REIT, on a freehold or leasehold basis, whether directly or through a holding company and/or a special purpose vehicle

Infrastructure Investment Trusts (InvIT) are trusts registered with SEBI that invest in the infrastructure sector. The InvIT can raise funds through public issue and/or through private placement. The initial offer shall of atleast Rs. 250 crores and the value of the proposed assets of the InvIT shall minimum be of Rs. 500 crores

Sovereign Gold Bond Scheme (SGB) are government securities denominated in grams of gold. The bonds are issued in denomination of one gram of gold and in denominations thereof. The tenor of the bond is 8 years.

International Financial Services Centres (IFSC) - An International Financial Services Centre (IFSC) caters to customers outside the jurisdiction of the domestic economy.
All these Centres are 'international' in the sense that they deal with the flow of finance and financial products/services across borders

Chapter 2: Market Participants in the Securities Market

The four important participants of securities markets are the investors, the issuers, the intermediaries and regulators.

Investors in securities market (based on primary public issuance categorization) can be broadly classified into **Retail Individual Investors, Institutional Investors** and **Non-institutional investors (NII).**

Retail Investors are individual investors who buy and sell securities for their personal account, and not for another company or organization. This category also includes High Net worth Individuals (HNI) which comprise of people who invest above rupees 2 lakh in a single transaction.

Institutional Investors comprises domestic financial institutions (DFIs), banks, insurance companies, mutual funds, and Foreign Portfolio Investors (a FPI is an entity established or incorporated outside India that proposes to make investments in India) and any other entity specified by SEBI as an Institutional.

SEBI (Foreign Portfolio Investors) Regulations, 2019 - FPI categories

Category 1

(i) Govt and Govt related investors such as central banks, sovereign wealth funds, international or multilateral organizations etc.;
(ii) Entities controlled or at least 75% directly or indirectly owned by Govt
(iii) Pension funds and university funds;
(iv) Regulated entities such as insurance or reinsurance entities, banks, asset management companies, investment managers, investment advisors, portfolio managers, broker dealers and swap dealers;
(v) Entities from the Financial Action Task Force (FATF) member countries
(vi) An entity (A) whose investment manager is from the Financial Action Task Force (FATF) member country and such an investment manager is registered as a Category I foreign portfolio investor; or (B) which is at least 75 per cent owned, directly or indirectly by another entity, eligible under (ii), (iii)and (iv) and such an eligible entity is from a Financial Action Task Force member country

Category 2

i) Appropriately Regulated funds not eligible as Category-I foreign portfolio investor;
ii) Endowments and foundations;
iii) Charitable organizations;
iv) Corporate bodies;
v) Family offices;
vi) Individuals;
vii) Regulated entities investing on behalf of their client,
viii) Unregulated funds in the form of limited partnership and Trusts

Category-2 FPIs who are corporate bodies, individual and family offices are treated as non-institutional.

Non-Institutional investor means any investor other than retail individual investor and institutional investor such as Family offices, corporates, partnership firms etc.

Accredited Investors

- have an understanding of various financial products and the associated risks- returns
- able to take informed decisions regarding their investments
- recognized by many securities and financial market regulators around the globe

Eligibility

• Individuals, HUFs, Family Trusts and sole proprietorships, which meet the criteria as under:
• (i) Annual Income >= INR 2 Crore; OR

• (ii) Net Worth >= INR 7.5 Crore, out of which at least INR 3.75 Crore is in the form of financial assets; OR
• (iii) Annual Income >= INR 1 Crore+ Net Worth >= INR 5 Crore, out of which at least INR 2.5 Crore is in the form of financial assets;
• Partnership Firms set up under the Indian Partnership Act, 1932 in which each partner independently meets the Accredited Investor criteria for individuals
• Trusts (other than family trusts) AUM >= INR 50 Crore.
• Body corporate with net worth >= INR 50 Crore.
• Certain agency deemed to be accredited investors

Market Maker

- provide liquidity to facilitate efficiency in the functioning of the financial markets.
- for SME Exchange, market making has been made mandatory
- main responsibility is to provide two-way (buy as well as sell) quotes on a continuous basis with certain minimum amount and reasonable bid-ask spread

Global Depository Receipts (GDRs) is a negotiable financial instrument that is issued by a foreign depository bank other than the US representing a specified number of shares of a foreign company's stock. GDR are generally traded in European Stock Exchanges.

American Depository Receipts (ADRs) is a negotiable certificate issued by a U.S. depository bank representing a specified number of shares of a foreign company's stock. The ADR trades on U.S. stock markets as any domestic shares would.

Foreign Currency Convertible Bonds (FCCBs) are bonds issued by Indian companies and subscribed to by a non-resident in foreign currency. They carry a fixed interest or coupon rate and are convertible into a certain number of ordinary shares at a predetermined price.

External Commercial Borrowings (ECBs) are commercial loans (in the form of bank loans, buyers credit, suppliers credit, securitized instruments, floating rate notes and fixed rate bonds) availed from any internationally recognized source such as bank, export credit agencies, suppliers of equipment, foreign collaborators, foreign equity holders and international capital market. Indian companies have preferred this route to raise funds as the cost of borrowing is low in the international markets.

Masala Bonds are rupee-denominated bonds issued outside India by Indian entities. They are debt instruments which help to raise money in local currency from foreign investors.

The Securities Contract (Regulation) Act, 1956 (SCRA) defines '**Stock Exchange'** as a body of individuals, whether incorporated or not, constituted for the purpose of assisting, regulating or controlling the business of buying, selling or dealing in securities.

A Clearing Corporation performs three main functions, namely: **clearing** and **settlement** of all transactions executed in the stock market (i.e., completes the process of receiving and delivering shares/funds to the buyers and sellers in the market) and carrying out **risk management.**

The clearing corporation acts as a **central counterparty** to all the trades.

A Custodian is an entity that helps register and safeguard the securities of its clients. Besides safeguarding securities, a custodian also keeps track of corporate actions on behalf of its clients.

Pay-In is a process whereby a Clearing Member and Custodian (in case of Institutional deals) bring in money and/or securities to the Clearing House/ Corporation. This forms the first phase of the settlement activity.

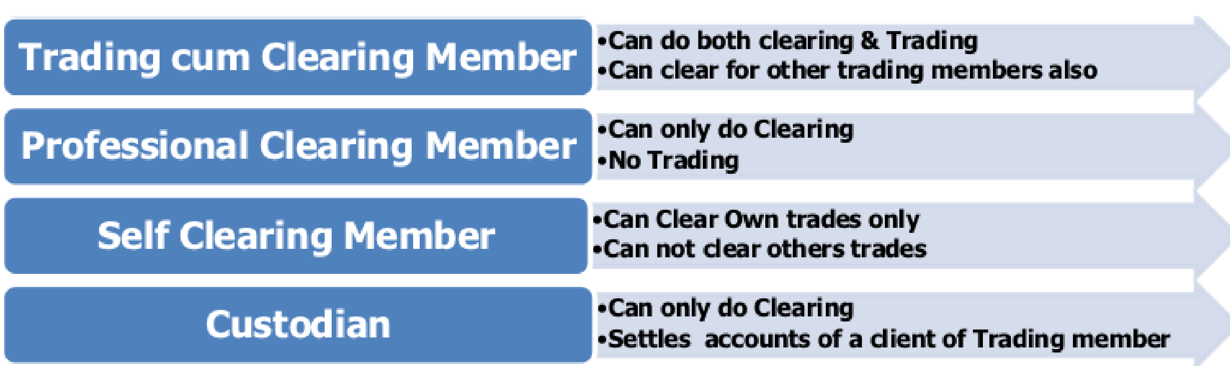
Pay-Out is a process where the Clearing House/ Corporation pays money or delivers securities to the Clearing Member and Custodians. This is the second phase of the settlement activity.

Depository is an entity facilitating holding securities in electronic form and enables transfer of securities by book entry

There are two Depositories in India, **Central Depository Services Limited (CDSL)** and **National Securities Depository Limited (NSDL)**.

The Depository provides its services to clients through its agents called **depository participants (DPs).**

Trading Member / Stock Broker - is a member of the stock exchange. A trading member is allowed to execute trades on his own account as well as on account of his clients. A trading member can be an individual (sole proprietor), a partnership firm, Limited Liability Partnership, Corporate or a bank who is a member of a Stock Exchange.



Authorized person is not a member of a Stock Exchange but is 'Any person, individual, partnership firm, LLP or body corporate, who is appointed as such by a Stock Broker and who provides access to trading platform of a Stock Exchange as an agent of the Stock Broker'.

Base Minimum Capital (BMC) is the deposit given by the member of the exchange against which no exposure for trades is allowed. It is maintained based on risk profile of the member

Custodian means any person/entity who carries on the business of providing custodial service. Custodians are also clearing members like PCMs but not trading members

Regulators

• Securities and Exchange Board of India (**SEBI**) regulates the Securities Industry.
• Reserve Bank of India (**RBI**) is the authority to regulate and monitor the Banking sector.
• Insurance Regulatory and Development Authority (**IRDA**) regulates the Insurance sector.
• Pension Fund Regulatory & Development Authority (**PFRDA**) regulate the pension fund.
• Ministry of Finance (**MOF**)
• Ministry of Corporate Affairs (**MCA**)

International Financial Services Centres Authority (IFSCA) is a is a unified authority for the development and regulation of financial products, financial services and financial institutions in the IFSC in India

SEBI Act, 1992 was enacted to empower SEBI with statutory powers for
(a) protecting the interests of investors in securities,
(b) promoting the development of the securities market,
(c) regulating the securities market.

Securities Contracts (Regulation) Act, 1956

It provides for direct and indirect control of virtually all aspects of securities trading and the running of stock exchanges. It gives Central Government regulatory jurisdiction over
(a) stock exchanges through a process of recognition and continued supervision
(b) contracts in securities
(c) listing of securities on stock exchanges.

Depositories Act, 1996

- The Depositories Act facilitated the establishment of 2 depositories - NSDL and CDSL.
- Only a company registered under the Companies Act, 2013 and sponsored by the specified category of institutions can set up a depository in India.

- A depository cannot directly open accounts and provide services to clients.

Companies Act, 2013

- deals with issue, allotment and transfer of securities and various aspects relating to company management.
- provides for standard of disclosure in public issues of capital, particularly in the fields of company management and projects, information about other listed companies under the same management, and management perception of risk factors.
- regulates underwriting, the use of premium and discounts on issues, rights and bonus issues, payment of interest and dividends, providing annual reports and other information
- Section 24 of the Companies Act 2013, delegates the power to regulate and transfer securities to SEBI

Securities Contract (Regulation) Rules, 1957 provide guidelines on

- application and recognition of stock exchanges
- qualifications for membership on a recognised stock exchange
- Books of account
- documents to be maintained and preserved by stock exchanges and stock brokers
- requirements regarding the listing of securities, units or a Collective Investment Scheme

Prevention of Money Laundering Act, 2002

Money laundering has been defined as “any process or activity connected with proceeds of crime including its concealment, possession, acquisition or use and projecting or claiming it as untainted property”.
Section 4 of the PMLA - punishment - imprisonment of 3 to 7 years and fines. 10 yr max
Section 6 - confers powers on the Central Govt to appoint an Adjudicating Authority
Section 9 - all the rights and title in confiscated property shall vest in the Central Govt
Section 11 - Adjudicating Authority has same powers as civil court under Code of Civil Procedure
Section 12 – record maintenance for 5 years by all reporting entities
Section 12 AA - enhanced due diligence by reporting entities.
Sections 16 and 17 - powers of the authorities to carry out summon, searches and seizures.
Section 24 - burden of proving that proceeds of alleged crime are untainted shall be on accused.
Sections 25 and 26 - establishment of Appellate Tribunal and appeal filing procedures
Section 42 - appeals to high court against order of the Appellate Tribunal.
Section 43 – empowers the Central Govt to designate Courts of Session as Special Courts for the trial of the offence of money-laundering

SEBI (Prohibition of Insider Trading) Regulations, 2015

Insider Trading denotes dealing in a company's securities on the basis of confidential information relating to the company which is not known to the public (**unpublished price sensitive information**), used to make profits or avoid loss.

Regulation 2(g) of the SEBI Insider regulations, defines an '**insider'** any person who is:
i) a connected person; or
ii) in possession of or having access to unpublished price sensitive information;

Regulation 2(n) defines unpublished price sensitive information as info related to -

- financial results;
- dividends;
- change in capital structure;
- mergers, de-mergers, acquisitions, delistings, disposals and expansion of business
- changes in key managerial personnel; and
- material events in accordance with the listing agreement.

The SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to the Securities Market) Regulations 2003 enable SEBI to investigate into cases of market manipulation and fraudulent and unfair trade practices.

Dabba trading is carried out by person not registered with SEBI wherein one person or group of persons carry out trading in securities by using price/quotes of securities available from the stock exchange trading platform / internet/tv screen etc

SEBI (Custodian) Regulation, 1996

A Custodian helps in -

- Maintaining a client's securities account
- Collecting the benefits or rights accruing to the client in respect of securities
- Keeping the client informed of the actions taken or to be taken by the issuer of securities, having a bearing on the benefits or rights accruing to the client.
- Maintaining and reconciling records of the above services.

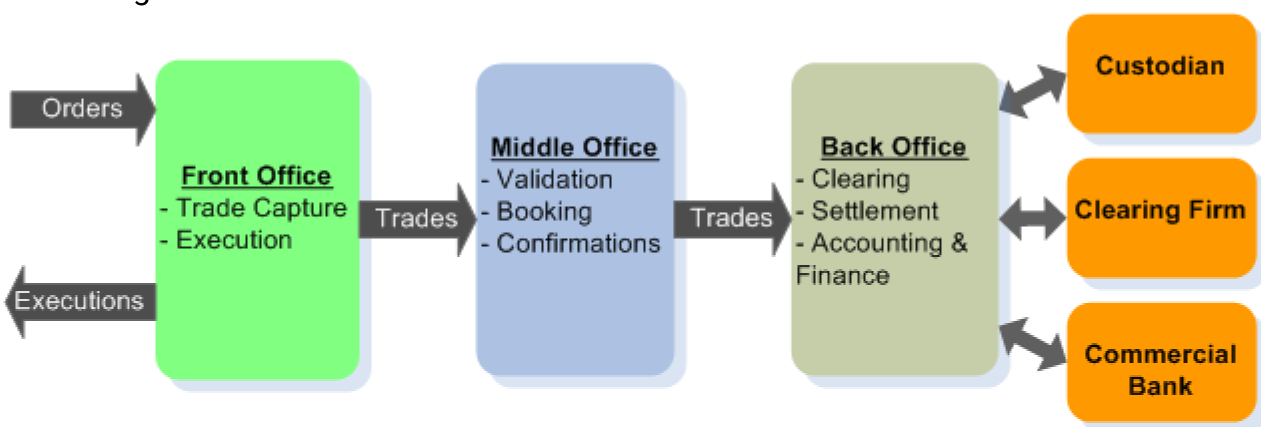
SEBI {KYC (Know Your Client) Registration Agency} Regulations, 2011

- After doing the initial KYC of the new clients, the intermediary shall forthwith upload the KYC information on the system of the KRA within 3 working days from the date of completion of KYC process.

- KRA shall send a letter to the client within 2 working days of the receipt of the initial/updated KYC documents from intermediary, confirming the details thereof and shall maintain the proof of dispatch.

Chapter 3: Introduction to Securities Broking Operations

A trade is the conversion of an order placed on the exchange which results into pay-in and pay-out of funds and securities. Trade ends with the settlement of the order placed.
The following steps are involved in a trade's life cycle:
1. Placing of Order
2. Risk management and routing of order
3. Order matching and its conversion into trade
4. Affirmation and Confirmation (only for institutional deals)
5. Clearing and settlement



Securities Trade Processing Flow

Clients have the option of placing their orders through various channels like internet, phone, direct market access (DMA) (for institutional clients), Securities trading using wireless technology facility (STWT)/ Automated /Algorithm Trading (ALGO)/ Smart order router (SOR).

All brokers shall execute trades of clients only after keeping evidence of the client placing such order in the form of
(a) Physical record written & signed by client
(b) Telephone recording
(c) Email from authorized email id

(d) Log for internet transactions
(e) Record of SMS messages
(f) Any other legally verifiable record.

Direct Market Access (DMA) is a facility which allows brokers to offer clients direct access to the exchange trading system through the broker's infrastructure without manual intervention by the broker

Algorithmic Trading – Any order that is generated using automated execution logic.
It shall mean and include any software or facility by the use of which, upon the fulfillment of certain specified parameters, without the necessity of manual entry of orders, buy/sell orders are automatically generated and pushed into the trading system of the Exchange for the purpose of matching**.**

High frequency trading (HFT) is a type of algorithmic trading which is latency sensitive and is characterized by a high daily portfolio turnover and high order-to trade ratio (OTR).

Affirmation and Confirmation (For Institutional Clients) –

- SEBI had mandated that all the institutional trades executed on the Stock Exchanges should be processed through the **Straight through Processing (STP) system**.
- STP is a mechanism that automates the end-to-end processing of transactions of the financial instruments.
- It involves use of a single system to process or control the work-flow of a financial transaction, including the Front, Middle, and Back office, General Ledger.
- STP can be defined as electronically capturing and processing transactions in one pass, from the point of first 'deal' to final settlement.

Contract Notes

- Contract note is the legal record of any transaction carried out on a stock exchange through a stockbroker. It serves as the confirmation of trade done on a day on behalf of a client on a stock exchange.
- Every stock broker shall issue a contract note to its clients for trades executed
- Contract note format is specified by the Exchanges.
- It establishes a legally enforceable relationship between the stock broker and the client in respect of settlement of trades executed on the Exchange as stated in the contract note.
- Contract note should be issued within 24 hours of the trade

- Stock brokers are required to maintain proof of dispatch of contract notes. In the case of Digitally Signed Electronic Contract Note (ECN), log of sending ECN to client's email id should be maintained
- The contract notes should be serially numbered starting from the beginning of the financial year. They should be issued with the client's name, PAN and client's code written on them. It should also contain the exact order number, order entry time, trade number, trade time, quantity of securities transacted, rates/price, etc.
- The contract notes should be signed by stock broker or by an authorised signatory of the stock broker.
- Contract should also mention all statutory charges like Securities Transaction Tax (STT), GST, stamp duty etc.), Regulatory levies / charges (e.g., SEBI turnover fees, Exchange transaction charges, etc.), Brokerage etc.

Front Office Operations

The front office is responsible for trade capture and execution. This is where the trade originates and the client relationship is maintained. The front office makes/takes orders and executes them. Traders and sales staff are considered front office staff.

Account Opening Kit

1) **Client Account Opening Form** which is in two parts.

a) Know Your Client (KYC) - form capturing the basic information about the client and instruction/check list to fill up the form and b) Additional Document capturing additional information about the client related to trading account.

2) Document stating the **Rights & Obligations of stock broker** (Member-Client Agreement), sub-broker and client for trading on Exchanges

3) **Uniform Risk Disclosure Documents (RDD**) for all segments/Exchanges.

4) **Guidance Note** detailing Do's and Don'ts for trading on Exchanges.

5) Document describing the **Policies and Procedures of the stock broker**

6) **A tariff sheet** specifying various charges, including brokerage, payable by the client to avoid any disputes at a later date.

SEBI has prescribed a new simplified **Account Opening Form ('AOF') or 'SARAL AOF'** for new individual investors participating in the cash segment of the Exchange but not availing facilities such as internet trading, margin trading, derivative trading and use of power of attorney.

KYC - "**Know your Client**" - Customer Identification Process.

For account opening purpose, stock brokers shall use the KYC templates provided by **Central Registry of Securitisation Asset Reconstruction and Security Interest of India (CERSAI)**
UID – Unique Identification Number (Aadhaar) can be a proof of Identity.
The **e-KYC** service launched by UIDAI is accepted as a valid process for KYC verification, provided the client has authorized the intermediary to access his data through UIDAI system.
e-KYC through Aadhaar Authentication service of UIDAI (e-KYC) or offline verification through **Aadhaar QR Code/XML** file shall be undertaken

Authority Letter for settle account

- The settlement of funds shall be done within 24 hours of the payout
- The client can authorize the Broker to retain funds in his Trading Account and maintain it as Running Account. This is called Running Account Authorization.
- Authorization shall be signed by the client only & not by any POA holder.
- In spite of this letter, actual settlement of funds shall be done by the broker, at least once in a calendar quarter or month depending on preference of the client.

KRA – Know Your Client Registration Agency

The new KRA system was developed for centralization of KYC records in the securities markets. It is applicable from January 1, 2012.
The brokers or trading members shall upload the KYC information on the system of the KRA within **3 working days** from the date of completion of KYC process.
The KRAs shall verify the necessary attributes of records of all clients within 2 days of receipt of KYC records

Central Know Your Client (CKYC)

CKYC refers to Central KYC (Know Your Customer)
Same KYC applies to various entities across the financial sector.
CKYC is managed by **CERSAI**, which is authorized by Govt. to function as the **Central KYC Registry (CKYCR**).

Stock brokers shall within **10 days** after the commencement of an account-based relationship with a client, file the electronic copy of the client's KYC records with the CKYCR.

Unique Client Code

Once the formalities of KYC and other details thereon are complete, each client is assigned a unique client code (UCC) by the broker. This acts as an identity for the client with respect to the broker. The unique client code should be mapped with the PAN number of the client

Brokerage rule for equity segment:

- Maximum brokerage - 2.5% of the trade value.
- If the value of share is Rs.10/- or less, a maximum brokerage of 25 paise per share can be collected.

There is no minimum brokerage requirement specified.

Brokerage rule for F&O segment:

- Brokerage for F&O is similar to the equity segment except for options contract
- Options contracts - maximum brokerage can be 2.5% of the option premium or Rs.100/- per contract whichever is higher.

Trading member can be a full service broker, discount broker or an online broker.

- Full service broker charges higher commission
- Discount brokers charge a much lower commission
- Online brokers cater to niche segment of retail clients.

Order Management consists of entering orders, order modification, order cancellation and order matching. The main components of an order are: Price, Time, Quantity, Security (What to buy and what to sell)), Action (Buy / Sell) & Client identity (UCC)

Types of order

A market order is where a trader purchases or sells their security at the best market price available. In the market order there is no need to specify the price at which a trader wants to purchase or sell.

Market order without Protection – Best available price in the market at that time

Market order with Protection – Best Available price within a specified range

Limit Order - the trader here needs to specify the price.

Stop Orders (orders with stop loss triggers) –an order which gets activated only when the market price of the security reaches or crosses a threshold price. Until then the stop order does not enter the market.

Time Condition

DAY - An order which is valid for the day on which it was entered.

IOC - Immediate or Cancel

GTC - A Good Till Cancelled

GTD - A Good Till Days/Date (GTD) order allows the Trading Member to specify the days/date up to which the order should stay in the system

Quantity Condition

Disclosed Quantity (DQ)- An order with a DQ condition allows the Trading Member to disclose only a part of the order quantity to the market

MF - Minimum Fill (MF) orders allow the Trading Member to specify the minimum quantity by which an order should be filled.

AON - All or None orders allow a Trading Member to impose the condition that only the full order should be matched against. If the full order is not matched it will stay in the books till matched or cancelled.

Proprietary Trading

Trading members are also allowed to trade on own behalf.

Stock Exchanges provide facility of placing order on proprietary (pro) account.

Facility of placing orders on proprietary account through trading terminals shall be extended only at one location of the members as specified / required by the members

SEBI permission required for multiple location Pro-Trading

Trade modification is allowed for parameters like client code and custodian participant code.

Stock Exchanges may allow modifications of client codes of non-institutional trades only to rectify a genuine error in entry of client code at the time of placing/modifying the related order.

Brokers shall disclose the codes of accounts which are classified as 'error accounts' to the Stock Exchanges

The Stock Exchanges shall levy a penalty on trading members wherever applicable and credit the same to its Investor Protection Fund.

Trade annulment

- Trading members are allowed to provide trade annulment request on trading system.
- The request should be submitted within 30 minutes from trade execution.
- Stock exchange may consider requests received after 30 minutes, but no longer than 60 minutes, only in exceptional cases and after examining and recording reasons for such consideration.

Middle Office is a hybrid function between the front and back office.

The middle office handles **validations, bookings** and **confirmations**.

Risk Management and **Surveillance** forms the main function of the middle office.

Types of Risk

Operational risk - Risk of monetary loss resulting from inadequate or failed internal processes, manual and systems error or external events.

Operational Risks for stock broker - risk arising on handling of client assets, regulatory non-compliance, trading error, non-payment, non-delivery of scrip(s), denial of matched order by clients, sudden closure of banks, unauthorized trading, fraud in trading or in back office functions, inexperienced personnel and compromised PC's.

Market risk - Loss from adverse changes in financial asset prices such as stock.
For the stock broker, market risks are essentially risk arising on account of concentration of client collateral in stocks/sectors, brokers own investment in stocks/sectors etc.
This risk entails the erosion of value of marketable securities and assets, due to factors beyond an enterprise's control.
Market risk is usually affected by economic developments, political destabilization, rising fiscal gap, and national debt, terrorism, energy price shocks, increase in interest rates, all resulting in a drop inequity prices.

Credit risk - risk of default on a debt that arise from a borrower failing to make required payments. The credit risk for broker can arise on account of Loans to Group Companies/ Related Parties, debit balance of clients, funding of clients, short collection of margins, Non-confirmation of DVP trade by custodian etc.

Legal risk arises from the possibility that an entity may not be able to enforce a contract against another party

Systemic Risk
(1) a disruption at a firm, in a market segment, or to a settlement system could cause a "domino effect" throughout the financial markets toppling one financial institution after another
(2) a "crisis of confidence" among investors, creating illiquid conditions in the marketplace.

Technology risk which includes technical glitches and cyber-attacks.

Back Office - confirmation, payments, settlements & accounting.
The back office monitors the post-market processing of transactions.
The back office is where the trade ends.

Trade Enrichment is defined as process of including additional information in a trade which is already executed.
Trade enrichment is performed automatically after each trade execution.

Trade Allocation - In the case of institutional trades, the front office may enter a single order for a particular client with **CP code** "**INST**" and subsequently distribute it across various sub schemes of the client at the back office end. For example, hedge fund makes a trade, and manages several portfolios. Often, they will choose to allocate their trade to various portfolios for a number of reasons

Clearing and Settlement Process is a post trading activity that constitutes the core part of equity trade lifecycles. Clearing house/corporation is an entity through which settlement of securities takes place. The details of all transactions performed by the brokers are made available to the Clearing House/Corporation by the Stock Exchange.
The Clearing House/Corporation gives an obligation report to the brokers and custodians who are required to settle their money/securities obligations within the stipulated time period, failing which they are required to pay penalties. This obligation report serves as statement of mutual contentment.
T+1 rolling settlement was implemented in the Indian securities market w.e.f January 27,2023. Currently, all cash market segment settlements are on T+1 day rolling basis.

Accounting
The stock brokers are required to maintain books of account as prescribed by the Securities Contracts (Regulation) Rules, SEBI (Stock brokers) Regulations and requirements of Exchanges. These are to be maintained for a minimum period of 5 years.

The **register of transactions** (**sauda book**) - Details of each transaction with the name of the security, its value, rates gross and net of brokerage and names of the clients.
• The **client's ledger** - has the details of all clients and their transactions
• The **general ledger** - transactions including expenses, overheads salaries, petty cash, etc.
• The **journal** is the accounting book of the general ledger. Any adjustment entries for e.g., interest receivable, etc., is accounted here.
• **The cash and bank book** contain records of all cash and cheque transactions and are normally balanced daily.
• **The securities register** is required to be maintained client-wise and scrip-wise. The detailsprovided would include date of receipt/delivery of the security, quantity received/delivered, party from whom delivered/to whom delivered, the purpose ofreceipt/delivery and the balance quantity.
• **A contract note** is a confirmation of trade done on a day for and on behalf of aclient.
• **The margin deposit book**- details of margins paid/collected/payable/ collectable.

Investor Risk Reduction Access (IRRA) platform

A joint platform to provide Investor Risk Reduction Access (IRRA) service shall be developed by the exchanges to provide investors an opportunity to square off/close the open positions and /or cancel pending orders in case of disruption of trading services provided by the Trading Member

Stock brokers shall inform about the technical glitch to the stock exchanges immediately but not later than **1 hour** from the time of occurrence of the glitch.

Stock brokers shall submit a Preliminary Incident Report to the Exchange within **T+1** day of the incident

Stock brokers shall submit a **Root Cause Analysis (RCA)** Report (as per format specified by SEBI) of the technical glitch to stock exchange, within **14 days** from the date of the incident.

Cyber Security & Cyber Resilience framework

The objective of CSCRF is to address evolving cyber threats, to align with the industry standards, to encourage efficient audits, and to ensure compliance by SEBI REs.

As per the CSCRF, Market Infrastructure Institutions (MIIs) are:

a. Stock Exchanges
b. Depositories
c. Clearing Corporations
d. KYC Registration Agencies (KRAs)
e. Qualified Registrars and Transfer Agents (QRTAs**)**

Securities Transaction Tax

S.No.	Taxable securities transaction	Rates	Payable by
1	Purchase of an equity share	0.1 Percent	Purchaser
2	Sale of an equity share	0.1 Percent	Seller
3	Sale of a unit of an equity oriented fund	0.001 Percent	Seller
4	Sale of an equity share where there is no delivery	0.025 percent	Seller
5	Sale of an option in securities	0.0625 per cent on premium	Seller
6	an option in securities, where option is exercised	0.125 per cent	Purchaser
7	Sale of a futures in securities	0.0125 percent	Seller

STT is not applicable on Currency Derivatives, Interest Rate Derivatives and Debt Securities transactions

Bulk Deal is defined as “all transactions in a scrip (on an Exchange) where the total quantity of shares bought/sold is more than 0.5% of the number of equity shares of the company listed on the Exchange”. However, the quantitative limit of 0.5% could be reached through one or more transactions executed during the day in the normal market segment.

Block Deals - A trade, with a minimum value of Rs. 10 crore executed through a single transaction on this separate window of the stock Exchange constitutes a "block deal"

Block Deal Windows – 8.45am to 9am & 2.05pm to 2.20pm
The orders may be placed in this window at a price not exceeding **+1%** of the applicable reference price in the respective block deal window

Chapter 4: Risk Management

Risk Management framework consists of the following components:
• Margin • Liquid Asset • Base minimum capital • Pre-trade risk control • Risk Reduction mode

Margining is a process by which a clearing corporation computes the potential loss that can occur to the open positions (both buy and sell) held by the members

In Cash/Equity Segment the clearing corporation computes and collects 3 kinds of margins:

- **Value at Risk Margin** (VaR) to cover potential losses for 99.9% of the days.
- **Mark to Market (MTM) Loss Margin**: Mark to market losses on outstanding settlement obligations of the member.
- **Extreme loss margin**: Margins to cover the loss in situations that lie outside the computation of the VaR margin.

Scrip sigma means the volatility of the security computed as at the end of the previous trading day. The computation uses the exponentially weighted moving average method applied to daily returns in the same manner as in the derivatives market.

Liquidity Categorization	VaR Margin
Group I (Liquid Securities)	Based on 6σ, subject to minimum of 9%
Group II (Less Liquid Sec.)	Based on 6σ, subject to minimum of 21.5%
Group III (Illiquid Securities)	50% if traded at least once per week ; 75% otherwise

Mark to Market Margin/ Loss is calculated by marking each transaction in security to the closing price of the security at the end of trading.

In case the net outstanding position in any security is NIL, the difference between the buy and sell values is considered as notional loss for the purpose of calculating the mark to market margin payable.

Extreme Loss Margin (ELM)

- ELM covers the expected loss in situations that go beyond those envisaged in the 99% value at risk estimates used in the VaR margin.
- ELM shall be 3.5% for any stock and 2% for ETFs that track broad based market indices and do not include ETFs which track sectoral indices.
- ELM shall be collected/ adjusted against the total liquid assets of the member on a real time basis.
- ELM shall be collected on the gross open position of the member. there would be no netting off of positions across different settlements. The Extreme Loss Margin collected shall be released on completion of pay-in of the settlement.
- Upfront margin rates (VaR Margin + Extreme Loss Margin) applicable for all securities in the TFTS shall be 100%.

Acceptable Liquid assets along with haircuts and limits

Item	Haircut
Units of growth plans of overnight mutual fund scheme	5 percent
Units of overnight mutual fund schemes (other than growth plans), liquid mutual fund schemes or gsec mutual fund schemes	10 percent
Equity shares with impact cost of upto 0.1% for an order value of Rs. 1 lakh and traded for atleast 99% of days over the period of previous 6 months	VaR margin based on 6 sigma subject to minimum of 9%.
Units of Mutual fund schemes other than those listed under cash equivalents	VaR margin based on 6 sigma subject to minimum of 9%.

Corporate Bonds	Min 10% or VaR based Haircut. A higher haircut may be considered to cover the expected time frame for liquidation.

Type and Tenor of Securities	Haircut
Treasury Bills and liquid GSec with residual maturity < 3 yrs	2%
Liquid GSec having residual maturity > 3 yrs	5%
For all other semi-liquid and illiquid GSec	10%

Liquidity Categorization	Trading Frequency	Impact Cost
Group I (Liquid Securities)	At least 80 percent of the days	<= 1%
Group II (Less Liquid Sec.)	At least 80 percent of the days	> 1%
Group III (Illiquid Securities)	Less Than 80 percent of the days	n/a

Calculation of mean impact cost

- Impact cost shall be calculated by taking 4 snapshots in a day from the order book in the past 6 months. These 4 snapshots shall be randomly chosen from within 4 fixed 10-minutes windows spread through the day.
- The impact cost shall be the percentage price movement caused by an order size of Rs.1 lakh from the average of the best bid and offer price in the order book snapshot. The impact cost shall be calculated for both, the buy and the sell side in each order book snapshot.
- The stock exchanges which are unable to compute the mean impact cost calculations at their exchanges shall use the impact cost calculations of BSE/NSE.

Base minimum capital is the deposit a stock broker has to make with the stock exchange to get trading rights on the exchange.

Categories	BMC Deposit
Only Proprietary trading without Algorithmic trading (Algo)	Rs.10 Lacs
Trading only on behalf of Client (without proprietary trading) and without Algo	Rs.15 lacs
Proprietary trading and trading on behalf of Client without Algo	Rs.25 lacs
All Trading Members/Brokers with Algo	Rs.50 lacs

Dynamic Price Bands

Stock Exchange shall set the dynamic price bands at **10 percent** of the previous closing price for the Stocks on which derivatives products are available
In the event of a market trend in either direction, the dynamic price bands shall be relaxed by the Stock Exchanges in increments of **5 percent**.
There are no day minimum/maximum price ranges applicable for index futures and stock futures. In order to prevent erroneous order entry by trading members, dynamic price band/operating ranges are kept at **+/- 10%.**
UCC/PAN check - Trading member can put this check to ensure that order is not entered for unregistered client. Exchange system does not allow order entry for those clients whose UCC/PAN is not uploaded on Exchange system
Initial margin is payable on all open positions of clearing members, up to client level and shall be payable upfront by Clearing Members in accordance with the margin computation mechanism adopted by the Clearing Corporation. Initial margin shall include SPAN margins, Margin on consolidated crystallized obligation, delivery margins

Margin Period of Risk (MPOR)
SEBI has advised Clearing corporation to estimate appropriate MPOR, subject to minimum of 2 days, for equity derivatives based on liquidity therein and scale up the initial margins

Calendar Spread Charge
Index Derivatives - 1.75% of the far month contract
Single Stock Derivatives - 2.2% of the far month contract

Net Option Value is computed as the difference between the long option positions and the short option positions, valued at the last available closing price of the option contract and shall be updated intraday at the current market value of the relevant option contracts at the time of generation of risk parameters.
The Net Option Value shall be added to the Liquid Net Worth of the clearing member. Thus, mark to market gains and losses shall not be settled in cash for options positions.

Delivery Margins shall be levied on lower of potential deliverable positions or in-the-money long option positions four (4) days prior to expiry of derivative contract which must be settled through delivery.

Extreme Loss Margin

Product	Extreme Loss Margin
Index Futures	2% of the notional value of the gross open positions in futures
Single Stock Futures	3.5% of the notional value of the gross open positions in futures

Short Index Options	2% of the notional value of the short open position
Short Stock Options	3.5% of the notional value of the short open position

Cross Margining introduced by SEBI to improve the efficiency of the use of the margin capital by market participants. Cross margining across Cash and Derivatives segment are available to all categories of market participants. The positions of clients in both the Capital market and F&O segments to the extent they offset each other shall be considered for the purpose of cross margining.

Graded Surveillance Measure (GSM) and Additional Surveillance Measure (ASM)
To enhance market integrity and safeguard interest of investors, SEBI has introduced Graded Surveillance Measures (GSM) on securities which witness an abnormal price rise not commensurate with financial health and fundamentals like Earnings, Book value, Fixed assets, Net-worth, P/E multiple, etc.
Similarly, 'Additional Surveillance Measures' (ASM) on securities with surveillance concerns viz. Price variation, Volatility etc. have been introduced too.
The main objective of these measures is:

- To alert and advice investors to be extra cautious while dealing in these securities
- To advice market participants to carry out necessary due diligence while dealing in these securities.

Trading supported by Blocked Amount in Secondary Market - SEBI has introduced a process for trading in secondary market based on blocked funds in investor's bank account, instead of transferring them upfront to the trading member.

The said facility shall be provided by integrating RBI approved Unified Payments Interface (UPI) mandate service of single-block-and-multiple-debits with the secondary market trading and settlement process and hereinafter referred as 'UPI block facility'.

The parameters considered for designating a stockbroker as **QSB** :
(a) the total number of active clients of the stock broker
(b) the available total assets of clients with the stock broker
(c) the trading volumes of the stock broker
(d) the end of day margin obligations of all clients of a stock broker
(e) the proprietary trading volumes of the stock broker
(f) compliance score of the stock broker
(g) grievance redressal score of the stock broker

Core Settlement Guarantee Fund - SEBI has directed clearing corporation to have a fund called Core SGF (Settlement Guarantee Fund) for each segment of each Recognized Stock Exchange (SE) to guarantee the settlement of trades executed in respective segment of the Stock Exchange. In the event of a clearing member (member) failing to honour settlement commitments, the Core SGF shall be used to fulfill the obligations of that member and complete the settlement without affecting the normal settlement process.

Chapter 5: Clearing Process

General Clearing process in Cash Segment for T+1 rolling settlement

1. At the end of the day's trade (T Day), all trades details are sent by the stock Exchanges to the clearing house/corporation.
2. Modification of Custodial Participant (CP) code (T day) upto 4:15 pm.
3. Allocation of "INST" trade on T day.
4. The clearing corporation/house then groups the trades under the various clearing members/custodians and informs them about the transactions of their respective clients.
5. The clearing members/custodians then confirm back institutional/Custodian Participant trades by 7:30 a.m. on T+1 day.
6. The clearing house/corporation then performs **multilateral netting** and determines the final obligations of all clearing members & custodian for funds and securities on T+1 by 9:00 a.m.

Role of the Clearing Agency / Corporation/House

When a trade occurs on the Stock Exchange it is a legal contract between the buyer and seller. Clearing Corporation ensures that members meet their fund/security obligations. It acts as a legal counterparty to all trades through the process called novation.

Clearing Corporation becomes the buyer to every seller and seller to every buyer.

If there is a default by either the buyer or the seller the counter party to the trade will have to bear the loss. The process of "novation" addresses this risk.

Novation - The Act of a clearing corporation interposing itself between both parties of every trade, being the legal counterparty to both.

In India, there are 2 major clearing corporations - **NSE Clearing Limited (NCL) & Indian Clearing Corporation Limited (ICCL)**

Interoperability among Clearing Corporations - SEBI introduced the concept of Interoperability among Clearing Corporations which necessitates linking of multiple Clearing Corporations. Inter-operability among Clearing Corporation (CC) will enable a Clearing Member to select the Clearing Corporation of its choice to clear and settle trades executed in multiple exchanges. It allows market participants to consolidate their clearing and settlement functions at a single Clearing Corporation, irrespective of the stock exchange on which the trade is executed

Clearing Banks acts as an important intermediary between a clearing member(s) and the clearing corporation. Every clearing member needs to maintain an account with any of the empaneled clearing banks at the designated clearing bank branches. The clearing accounts are to be used exclusively for clearing & settlement operations.
It is mandatory for CM to open demat accounts with both CDSL and NSDL. This account is called a **clearing member settlement pool account**. Separate accounts are to be opened for all the exchanges

Depositories & Depository Participants
A "Depository" is an entity facilitating holding securities in electronic form and enables transfer of securities by book entry.
In the depository system both transferor and transferee have to give instructions to its depository participants [DPs] for delivering [transferring out] and receiving of securities. However, transferee can give **'Standing Instructions' [SI]** to its DP for receiving in securities. If SI is not given, transferee must give separate instructions each time securities have to be received.

Transfer of securities may be done for any of the following purposes:
a. Transfer due to a transaction done between 2 persons (off-market transaction)
b. Transfer arising out of a transaction done on a stock exchange.
c. Transfer arising out of transmission and account closure.

A beneficiary account can be debited only if the beneficial owner has given **'Delivery Instruction Slip' [DIS] .**

Demat Debit and Pledge Instruction (DDPI) - under which the clients shall explicitly agree to authorize the stock broker/stock broker and depository participant to access their BO account for the limited purpose of meeting pay-in obligations for settlement of trades executed by them. The DDPI shall serve the same purpose of PoA and significantly mitigate the misuse of PoA.

Any trade that is cleared and settled without the participation of a clearing corporation is

called **off-market trade**.
A **market trade** is one that is settled through participation of a Clearing Agency

Clearing Process
The clearing function of the clearing corporation is designed to work out a) what members are due to deliver and b) what members are due to receive on the settlement date.
In the stock exchanges this is done by a process called **multilateral netting**. This process is performed by the clearing agency (clearing corporation/clearing house). The clearing agency guarantees that all contracts which are traded will be honoured.

Clearing Process for Derivatives
The clearing mechanism essentially involves working out open positions and obligations of clearing members. This position is considered for exposure and daily margin purposes. The open positions of clearing members are arrived at by aggregating the open positions of all the brokers/trading members and all custodial participants clearing through them.
A trading member's open position is arrived at by summing up his proprietary and client's open positions. Proprietary positions are calculated on net basis (buy - sell) for each contract88. Clients' positions are arrived at by summing together net (buy - sell) positions of each individual client. Please note that positions are only netted for each client at contract level and not netted across clients and are rather added up across clients. A TM's open position is the sum of proprietary open position, client open long position and client open short position.

The stock brokers are allowed to net the clients account within the firm

Chapter 6: Settlement Process

The daily & final settlement of derivative trades is done on T+1 working day basis except for final settlement of currency derivatives segment, where final settlement take place on a T+2 basis.

In case of exchange-traded equity derivatives contracts in India, some of the derivatives contracts (such as those based on the Indices) are **cash-settled** and some of the contracts (such as those based on individual securities) are **physically settled**.

The daily & final settlement of derivative trades is done on T+1 working day basis except for final settlement of equity derivatives contracts which are settled by delivery and are effected on Expiry+2 days. The final settlement in currency derivatives segment place on a T+2 basis.

Product	Settlement	Price
Futures Contracts on Index or Individual Security	Daily	Closing price of the futures contracts on the trading day (closing price = last half an hour weighted average price of the contract)
Un-expired illiquid futures contracts	Daily	Theoretical Price $F=S*e^{rt}$
Futures & Options Contracts on Index or Individual Securities	Final	Closing price of the relevant underlying index / security in the Capital Market segment of NSE, on the last trading day of the futures contracts.
Currency Futures	Daily	Last half an Hour weighted avg price
Un-expired illiquid futures contracts	Daily	$F=S*e^{(r-rf)t}$
Currency Futures and Options	Final	FBIL reference rate / Rate derived from FBIL reference rate
Cash Settlement GOI Bond Futures	Daily	Last half an Hour weighted avg price
Un-expired illiquid futures contracts	Daily	Theoretical price = Cash Price + Financing cost – Income on cash position
Cash Settlement GOI Bond Futures & Options	Final	Last 2 Hours Weighted avg price on NDS-OM (min 5 trades) or FBIL price

Corporate Actions to be adjusted

The corporate actions may be broadly classified under **stock benefits and cash benefits**.
The various stock benefits declared by the issuer of capital are:
• Bonus • Rights • Merger / De-merger • Amalgamation • Splits • Consolidations • Hive-off
• Warrants, and • Secured Premium Notes (SPNs) among others.

The cash benefit declared by the issuer of capital is cash dividend

Any adjustment for corporate actions would be carried out on the last day on which a security is traded on a cum basis in the underlying equities market after the close of trading hours.
Adjustment - Modifications to positions / contract specifications listed below

- Strike Price , Position , Market Lot / Multiplier

Bonus - Ratio A:B	**Adjustment factor : (A+B)/B**
Stock Splits / Consolidations Ratio - A : B	**Adjustment factor : A/B**

Dividends which are **below 2% of the market value** of the underlying stock, would be deemed to be **ordinary dividends** and no adjustment in the Strike Price would be made for ordinary dividends.

For **extra-ordinary dividends**, **>=2% of the market value** of the underlying security, the total dividend amount would be reduced from all the strike prices of the option contracts on that stock.

Chapter 7: Investor Grievances and Arbitration

Grievance Redressal Mechanism:

Investor grievance is handled at the **trading member level, stock exchange level** and **the regulator level**

Investor Grievance handling at the trading member level

All the trading firms have a designated cell/person for redressing investor grievances.

When a complaint is filed by the investor, matter has to be resolved at the branch level or the firm level depending upon the nature of the complaint.

Investor Grievance handling at the Stock Exchanges and SEBI

In case the complainant or the aggrieved investor is unsatisfied with the redressal process of the trading member then the investor can take his grievance to the stock exchange or SEBI.

SEBI Complaints Redressal System (SCORES https://scores.sebi.gov.in/)

- SEBI handles the investor grievances through a system called SEBI Complaints Redressal System (SCORES) .Its a 24x7, web based centralized system to capture investor complaints against listed companies and registered intermediaries.
- It allows the investors to lodge their complaints and track the status online. When a complaint is lodged on SCORES, an email acknowledgement is generated for reference and tracking.
- All Entities who are in receipt of the complaints of the investors through SCORES, shall resolve the complaint within 21 calendar days of receipt of such complaint.
- The Complaints lodged on SCORES against any Entity shall be automatically forwarded to the concerned Entity through SCORES for resolution and submission of Action Taken Report (ATR).

- If the complainant is not satisfied, the complainant may request for a review of the resolution provided by the entity within 15 calendar days from the date of the ATR.
- The Designated Body may seek clarification on the ATR submitted by the Entity for the first review. The Designated Body submits the revised ATR to the complainant on SCORES within 10 calendar days of the review sought

Investor Service Centres (ISCs) of Stock Exchanges
SEBI has advised all stock exchanges to open or maintain atleast 1 Investor Service Centre (ISC) for the benefit of the investors.
Such centres are required to provide counseling service and provide certain basic minimum facilities to the investors.
SEBI has mandated Exchanges to open ISCs in metro cities

Online Resolution of Disputes in the Indian Securities Market
SEBI has notified and put in place an "Online Dispute Resolution process" by establishing a common Online Dispute Resolution Portal (ODR Portal). The ODR portal harnesses online conciliation and online arbitration for resolution arising in the securities markets**.**

Arbitration which is a quasi judicial process, is an alternate dispute resolution mechanism prescribed under the Arbitration and Conciliation Act, 1996
When the investor/client and/or the Market Participant pursue online arbitration, the ODR Institution shall appoint a sole independent and neutral arbitrator from its panel of arbitrators within 5 calendar days of reference and receipt of fees, cost and charges as applicable.
Claim >Rs.30 lakh → Arbitral Tribunal of **3 arbitrators**.
Claim > Rs. 1 Lakh → the **Sole Arbitrator** or Arbitral Tribunal shall conduct one or more hearing/s and pass the arbitral award within 30 days.
Claim < Rs. 1 Lakh → the Sole Arbitrator shall conduct a document-only arbitration process and pass the arbitral award within 30 calendar days

If the Market Participant wishes to challenge an arbitral award, then the Market Participant must deposit 100% of the amounts payable in terms of the arbitral award with the relevant MII prior to initiation of the challenge

he stock exchange must ensure that the process of appointment of arbitrator(s) is completed within 30 days from the date of receipt of application from the applicant.

Investor Protection Fund

1. All stock exchanges and depositories shall establish an IPF. The IPF of the stock exchange and depository shall be administered through separate trusts
2. The following contributions shall be made by the Stock Exchange to the IPF:
   a) 1% of the listing fees received , on a quarterly basis.
   b) 100% of the interest earned on the 1% security deposit kept by the issuer companies at the time of public offers
   c) Penalty collected by stock exchanges from Trading Members(TMs) for deficiency in modification of client code
   d) Penalty collected by stock exchanges from TMs for default in pay-in for certain trades during periodic call auction for Illiquid scrips
   e) Penalties collected by stock exchanges from their listed companies for non-compliance with various requirements of the SEBI
   f) Penalty collected from TMs for default in pay-in by an investor in an Offer For Sale (OFS)transaction
   g) Contribution towards the IPF based on the transaction charges collected from the members of the exchange
   h) 70% of interest or income received out of any investments made from the IPF.
3. The amount in IPF and any interest or income generated from the IPF of the stock exchanges shall be utilized to meet the legitimate investment claims of the clients of the defaulting TMs and to pay interim relief to investors

4. Interest or income received out of any investments made from the IPF : At least 70% of interest or income from IPF received every year shall be ploughed back to IPF; 25% can be utilised for promotion of investor education and investor awareness.

5. The stock exchanges and depositories shall conduct half-yearly review to ascertain the adequacy of the IPF corpus.

6. The claims received against the defaulter TMs during the specified period shall be eligible for compensation from the IPF.

Chapter 8: Other Services provided by Brokers

- Investment advice & Research reports and market review * Depository services
- Direct Market Access (DMA) * Mobile trading & Smart Order Routing (SOR)
- Algorithmic trading * IPOs & Mutual Funds Distribution
- Internet-based Online Trading (IBT) * Margin funding

"Application Supported by Blocked Amount (ASBA)" - The application money remains in the investor's account till finalization of basis of allotment in the issue. If an investor is applying through ASBA, his application money is debited from the bank account only if the investors application is selected for allotment after the basis of allotment is finalized, or the issue is withdrawn/failed.

Trading of Mutual Fund Units - The Exchanges provides platform (e.g. Mutual Fund Service System of NSE and BSE Star MF) to trading member and mutual fund distributors for trading in open ended mutual fund scheme. The trading members who are AMFI Registration Number (ARN) holders and have passed the NISM certification examination are permitted to participate in the trading of the mutual funds units through the exchange trading platform

MF Settlement Procedure - The settlement for MF platform provided by Exchanges is carried out by Clearing Corporations (CCs) through the depository and bank interface. The Exchange/CCs does NOT offer any settlement guarantee as the respective AMC is the counterparty for all transactions

PMS - Many stock brokers also offer Portfolio Management Services (PMS) to their High NetWorth clients. Portfolio manager can be discretionary or non-discretionary.

The **discretionary** portfolio manager **individually** and **independently manages** the funds of each client
The **non-discretionary** portfolio manager manages the funds in **accordance with the directions of the client.**

Co-investment Portfolio Manager" means a Portfolio Manager who is a Manager of a Category I or Category II Alternative Investment Fund(s); and:
(i)provides services only to the investors of such Category I or Category II Alternative Investment Fund(s);
(ii)makes investment only in unlisted securities of investee companies where such Category I or Category II Alternative Investment Fund(s) make investments

SEBI fee structure & Eligibility criteria

- Non-refundable Application fee (Renewal / Registration)- Rs. 1 lakh.
- Initial Registration fee – Rs10 Lakhs
- Renewal Fees – Rs 5 Lakhs every 3 years.
- Minimum networth of portfolio manager - 5 crore rupees.

The portfolio manager shall not accept from the clients, funds or securities worth less than **Rs.50 lakh**

Margin Trading - Only corporate brokers with networth of at least Rs.3 crore are eligible for providing margin trading facility to their clients.

Securities eligible for margin trading

Group 1 stocks in F&O - VaR + (3 x Extreme Loss Margin)
Group 1 stocks NOT in F&O - VaR + (5 x Extreme Loss Margin)

Leverage and Exposure Limits - At any point of time, the total indebtedness of a broker for the purpose of margin trading shall not exceed 5 times of his net worth and the maximum allowable exposure of the broker towards the margin trading facility shall not exceed the borrowed funds and 50% of his "net worth".

Broker providing the margin trading facility shall ensure that:

a) Exposure to any single client shall not exceed 10% of the broker's max allowable exposure.

b) Exposure towards stocks purchased under margin trading facility and collateral kept in the form of stocks are well diversified.

The stock exchange should grant approval or reject the application as the case may be and communicate its decision to the member within **7 calendar days** of the date of completed application submitted to the exchange.

The broker must have a minimum net worth of **Rs.50 lacs** if the broker is providing the Internet based facility on his own

IMPORTANT NOTE :

1. Attend ALL Questions
2. For the questions you don't know the right answer – Try to eliminate the wrong answers and take a guess on the remaining answers.
3. DO NOT MEMORISE the question & answers. It's not the right to way to prepare for any NISM exam. Good understanding of Concepts is essential.

All the Best ☺

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