



UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

DIVISION OF  
CORPORATION FINANCE

May 15, 2018

Mr. Sandeep Parekh  
Finsec Law Advisors  
C-1419, One BKC  
Bandra Kurla Complex  
Mumbai 400051

Re: BSE Limited  
Incoming Letter dated May 3, 2018

Dear Mr. Parekh:

This letter will confirm the response of the Division of Corporation Finance to your request that the Division designate BSE Limited as a “designated offshore securities market” within the meaning of Rule 902(b) of Regulation S under the Securities Act of 1933. A copy of your letter is enclosed in order to avoid having to recite or summarize the facts set forth therein. On the basis of the facts presented, we hereby so designate BSE Limited.

For the Commission  
by the Division of Corporation Finance  
pursuant to delegated authority,

/s/ Michael Coco

Michael Coco  
Chief (Acting)  
Office of International Corporation Finance

Chief, Office of International Corporate Finance  
Securities and Exchange Commission  
Room 3628  
100 F Street NE  
Washington, DC 20549  
USA

May 03, 2018

**Re: Application for Designation of BSE Limited as a “Designated Offshore Securities Market”**

Dear Ma’am/Sir,

We are writing on behalf of BSE Limited (“**BSE**”) to request that it be recognized as a “Designated Offshore Securities Market” (“**DOSM**”). This designation is sought within the meaning of Rule 902(b) of Regulation S (“**Regulation S**”), issued under the Securities Act of 1933, as amended (“**Securities Act**”). The designation is being sought in order to assist market participants who are eligible for the safe harbor provided by Rule 904 of Regulation S in satisfying the requirements specified in that rule when reselling securities “*in, on or through the facilities of*” BSE.

Currently, equity and bond securities listed on BSE and issued in the United States of America (“**U.S.**”), that are traded on BSE cannot generally be resold in non-prearranged trades executed through the facilities of BSE’s trading platform, without requiring that the seller forms a reasonable belief that the buyer is outside the U.S. Thus, effecting such transactions with U.S. persons without any restrictions under the Securities Act becomes a problem. The status of DOSM will provide several advantages that can facilitate securities offerings by BSE-listed companies, particularly to U.S. investors. For instance, BSE-listed securities, originally issued in the U.S., in transactions that are exempt from SEC registration, may be freely resold on BSE. This is expected to primarily benefit securities issued in U.S. private placements to institutional investors. The availability of a liquid resale market is expected to make exempt offerings by BSE-listed companies more attractive to U.S. investors. BSE’s new status will provide additional benefits to companies whose securities are traded both in the U.S. and on BSE. Certain directors and officers of dual-listed companies will generally be permitted to resell

their securities on BSE, regardless of any restrictions or holding periods that may apply under U.S. securities laws.

Seeking DOSM recognition is yet another step in BSE's internationalization strategy. BSE has applied to the US Commodity Futures Trading Commission for a Rule 30.10 exemptive relief in a representative capacity on behalf of its members. The designation of BSE as a DOSM would be of significance to both BSE and the Indian capital markets as a whole. Once the recognition is granted, U.S. based investors will be able to trade in securities listed on BSE without taking their own measures to ascertain that the purchaser is outside the U.S. and without having to meet the registration requirements imposed by the U.S. federal securities laws. While BSE already has the attention of key institutional investors from the U.S., having the designation will ease the trading processes for those investors based in the U.S. The recognition will go a long way in facilitating trading between both jurisdictions. While BSE has long maintained the highest standards of oversight, reporting and technological innovation, the SEC's designation would recognize these standards and place BSE among the world's leading securities markets who have already earned such designation.

BSE is a public limited company incorporated under the provisions of the Indian Companies Act, 1956<sup>1</sup> ("**Companies Act, 1956**") and licensed under the provisions of Securities Contracts (Regulation) Act, 1956 ("**SCRA**") as a recognized stock exchange of India. [The SCRA has been annexed hereto as **Annexure 1.**] BSE is a premier Indian stock exchange with the best global practices in technology, product innovation, compliance and monitoring and customer service. BSE provides an efficient and transparent market for trading in equity, debt instruments, derivatives on equities and currencies, interest rate derivatives and mutual funds. BSE also has a platform for trading in equities of small-and-medium enterprises ("**SME**"). BSE is a fully-integrated exchange which offers the complete range of general exchange-related services, including trading, clearing, settlement<sup>2</sup> and depository services<sup>3</sup>. As a stock exchange, BSE falls within the regulatory purview of the Securities and Exchange Board of India ("**SEBI**"), India's capital market regulator.

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<sup>1</sup> Available at [http://www.mca.gov.in/Ministry/pdf/Companies\\_Act\\_1956\\_13jun2011.pdf](http://www.mca.gov.in/Ministry/pdf/Companies_Act_1956_13jun2011.pdf)

<sup>2</sup> Through its wholly owned subsidiary Indian Clearing Corporation Limited (**ICCL**). The functions of clearing, settlement, collateral management and risk management for various segments of BSE are carried out by ICCL.

<sup>3</sup> Through its associate company Central Depository Services (India) Limited (**CDSL**).

## I. BACKGROUND

### A. BRIEF DESCRIPTION OF THE INDIAN ECONOMY

The Indian economy is a mixed economy, a blend of public and private sector. It is also a dualistic economy, wherein both modern industries and traditional agricultural activities co-exist. India has a stable economic and political environment with a democratically elected parliament. Even in 2008-09, while advanced developed countries were experiencing recession, India succeeded in achieving 6.7% growth, which further rose to 8.4% in 2009-10 and 2010-11. In the last decade, India has emerged as one of the fastest growing large economies of the world. Both the long-term and short-term growth prospective of the Indian economy are positive. The Organization for Economic Cooperation and Development in its interim economic outlook report, has stated that the country is “*expected to be the fastest-growing major economy over the coming two years*”.<sup>4</sup>

India has a diversified financial sector, which is undergoing rapid expansion. It comprises commercial banks, insurance companies, non-banking financial companies, co-operatives, pension funds, mutual funds and other smaller financial entities etc. The introduction of several new instruments in the banking and capital markets space has helped to broaden and deepen the financial markets. New players seek to adopt international best practices to offer a sophisticated range of financial services to corporate, retail and institutional customers. Financial sector regulators too have been proactive in ensuring that new regulations and guidelines are more or less in tandem with the growth in the financial sector.

In India, monetary policy of the Reserve Bank of India (“**RBI**”), India’s central bank, is aimed at managing the quantity of money in order to meet the requirements of different sectors of the economy and to stabilize the pace of economic growth and inflation management. The RBI implements the monetary policy through open market operations, bank rate policy, reserve system, credit control policy and other instruments. At present, India is undoubtedly one of the world’s most vibrant capital markets. Financial intermediaries have gradually moved to internationally acceptable norms for income recognition, asset classification, provisioning and capital adequacy. India can legitimately claim that the rates of domestic saving and investment

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<sup>4</sup> *OECD Interim Economic Outlook*, September 16, 2015, available at <http://www.oecd.org/economy/economicoutlook.htm>

are fairly high. The market will develop with better awareness of the opportunities for investment.

India has moved a step closer to having a Singapore or Dubai-like financial hub, with SEBI approving a framework for international financial centres (IFC). The state of Maharashtra's plans to promote Mumbai as a global financial centre have received further encouragement as Wall Street firm JPMorgan Chase & Co. and the Japanese government arm Japan External Trade Organization (JETRO) agreed to partner with the state government to hold road shows to attract financial services companies to Mumbai. Given the relatively stable economy and the focus on quality in the area of financial services, many American and European banks and accounting firms have established subsidiaries in India.

India is a signatory to various treaties and a part of several multinational organizations, including the United Nations and the World Trade Organization. As a major international financial centre, India maintains the highest standard of compliance with international Anti-Money Laundering (AML) standards as well as those standards that relate to Combating the Financing of Terrorism (CFT). SEBI is a member of the International Organization of Securities Commissions ("IOSCO") and signatory to the IOSCO Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information. Reforms initiated by the Government and other regulatory mechanisms have helped ensure that the new emerging face of the Indian financial services sector will culminate in a strong, transparent and resilient system.

## **B. BRIEF DESCRIPTION OF THE SECURITIES AND EXCHANGE BOARD OF INDIA**

### ***About SEBI- Establishment of SEBI***

SEBI is the home regulator of BSE. Initially SEBI was formed as a non-statutory body in 1988 for regulating the securities market. The Parliament of India, for the regulation and development of the securities market in the country, enacted the Securities and Exchange Board of India, Act 1992 ("**SEBI Act**") on April 04, 1992. [The SEBI Act has been annexed hereto as **Annexure 2.**] The preamble of the SEBI Act states that the objective of the statute is to protect the interest of the investors in securities and to promote the development of, and to regulate, the securities market and for matters connected therewith or incidental thereto. Pursuant to the enactment of the SEBI Act, SEBI was established on April 12, 1992. SEBI is

responsible for the regulation, supervision and development of the securities market in India. The head office of SEBI is located in Mumbai. As on March 31, 2017, SEBI had a total of 788 employees in various grades, out of which 692 were officers and 96 were secretaries and other staff.<sup>5</sup>

### ***Autonomy of SEBI***

SEBI as a statutory regulator, has independent legislative, executive and quasi-judicial powers. SEBI is managed by a board which comprises eight members, including the chairman. SEBI functions in an autonomous manner except where the Central Government of India (“**Central Government**”) may issue directions on questions of policy as provided under Section 16 of the SEBI Act. Section 29 and Section 30 of the SEBI Act empower SEBI to make rules and regulations, respectively. The rules and regulations framed by SEBI are required to be laid before the Parliament of India under Section 31 of the SEBI Act and are subject to modification that may be done by the Parliament of India. SEBI has been given financial autonomy by means of a separate fund under Section 14 of the SEBI Act, which primarily comprises grants, fees and charges received by SEBI under the SEBI Act.

### ***Powers and Functions of SEBI***

SEBI is empowered to take appropriate measures under Section 11(1) of the SEBI Act for the purposes of discharging its duties and functions. Further, SEBI is vested with the power to grant registration to different classes of market participants under Section 12. The quasi-judicial powers of SEBI can be traced to Section 11(4), Section 11B, Section 11D, Section 12(3) and Chapter VI-A of the SEBI Act. Under Chapter VI-A, SEBI can impose monetary penalties through a process of adjudication. All quasi-judicial functions of SEBI can be appealed under Section 15T of the SEBI Act before the Securities Appellate Tribunal (“**SAT**”), an expert tribunal comprising three members. SAT has been established under the provision of Section 15K of the SEBI Act to hear and dispose of appeals against the orders passed by SEBI or by an adjudicating officer under the SEBI Act. Apart from the jurisdiction vested under Section 15T of the SEBI Act, a listed company or any person aggrieved by a decision of a

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<sup>5</sup> SEBI Annual Report, 2016-2017, August 14, 2017, available at [https://www.sebi.gov.in/reports/annual-reports/aug-2017/annual-report-2016-17\\_35618.html](https://www.sebi.gov.in/reports/annual-reports/aug-2017/annual-report-2016-17_35618.html)

recognized stock exchange can also appeal before SAT under Section 22A of SCRA or Section 23L of SCRA respectively.

SEBI performs protective, developmental and regulatory functions. As a regulator, it plays a pro-active role. SEBI protects the interests of investors, for instance, by prohibiting insider trading, checking price rigging, fraudulent and unfair trade practices. SEBI undertakes several developmental functions such as, promoting training of intermediaries in the securities market and promoting activities in stock exchanges. In discharging its regulatory functions, SEBI has framed rules and regulations to govern intermediaries such as merchant bankers and brokers and it conducts inquiries and audit of stock exchanges. SEBI also adopts a public consultative process while framing its regulations. Further, pursuant to the merger of the Forward Markets Commission, the commodities futures regulator in India, with SEBI on September 28, 2015, commodities derivatives also fall within the regulatory purview of SEBI.

#### ***Memoranda of Understanding entered into by SEBI***

SEBI is an ordinary member of the IOSCO and is one of the board members of IOSCO. SEBI generally seeks to ensure that BSE, as a recognized exchange, complies with IOSCO standards. SEBI regularly undertakes review of its regulations to test against the IOSCO Principles as necessary. As an active member of IOSCO, SEBI is committed to ensuring orderly growth of the securities market and cooperation with other global regulators. In the past, SEBI's erstwhile chairmen have been chairmen of the Emerging Markets Committee and the Asia-Pacific Regional Committee of the IOSCO.

Further, since April 22, 2003, SEBI has been a signatory to the IOSCO Multilateral Memorandum of Understanding Concerning Consultation and Cooperation and the Exchange of Information ("MMOU"). Pursuant to the MMOU, SEBI has agreed to provide mutual assistance and exchange information for the purpose of enforcing and securing compliance with applicable securities and derivatives laws. The scope of assistance includes providing information and documents held in the files of the requested authority, obtaining information and documents from persons and taking or compelling a person's statement. The authorities represent that no domestic secrecy or blocking laws or regulations would prevent the collection or provision of information, however, a request may be denied if it would require the authority to act in a manner violating its domestic law or on grounds of public interest or essential national interest.

On March 06, 1998, SEBI and the SEC signed a memorandum of understanding Regarding Cooperation, Consultation and the Provision of Technical Assistance (“**SEBI – SEC MOU**”). A copy of the SEBI – SEC MOU is annexed hereto as **Annexure 3**. Clause II (4) of the SEBI – SEC MOU states as follows,

*“The Authorities declare their intent to provide each other assistance in obtaining information and evidence to facilitate the enforcement of their respective laws relating to securities matters. The Authorities recognise that such assistance will be particularly important in matters involving possible fraud in the offer, purchase or sale of securities. Where necessary, the Authorities will use all reasonable efforts to obtain the cooperation of other domestic governmental agencies to provide assistance pursuant to this Memorandum of Understanding.”*

Further on April 28, 2004, SEBI and the U.S. Commodity Futures Trading Commission (“**CFTC**”) signed a memorandum of understanding Regarding Futures Regulatory Cooperation, Consultation and the Provision of Technical Assistance (“**SEBI – CFTC MOU**”). A copy of the SEBI – CFTC MOU is annexed hereto as **Annexure 4**. The following is the purpose for which the SEBI – CFTC – MOU was entered into:

*“Sharing the goal of building and maintaining open, fair, efficient and sound futures markets,*

- a. Recognizing that the development of effective domestic legal and regulatory structures is essential to market integrity and investor protection,*
- b. Believing that international cooperation can facilitate the development and effective operation of futures markets, and*
- c. Desiring to establish a mutually acceptable basis for cooperation and consultation.”*

Section 3 under Clause I of the SEBI – CFTC MOU provides that both SEBI and CFTC intend to share information on each other’s laws, rules and regulations pertaining to futures and options markets, if applicable, and how those laws, rules and regulations are implemented and interpreted. Clause III of the SEBI – CFTC MOU states that each authority may give assistance as to:

- a. The granting of licenses, waivers, or exemptions for the conduct of futures business;
- b. The laws and regulations applicable to futures business;
- c. The laws and regulations applicable to futures exchanges and other types of markets;
- d. The oversight of futures exchanges by regulatory and market authorities;
- e. The prevention and detection of futures and options fraud and other irregularities or unlawful activities in connection with the offer, purchase or sale of any futures or options contract; and
- f. The prevention and detection of market manipulation.

### **C. BSE LTD. (FORMERLY KNOWN AS BOMBAY STOCK EXCHANGE LTD)**

#### ***About BSE- Establishment and Milestones***

The journey of BSE, the first stock exchange in Asia, is as eventful and interesting as the history of India's securities market. BSE was established in 1875 as the "Native Share & Brokers' Association". On August 31, 1957, BSE became the first stock exchange in the country to be granted permanent recognition under the SCRA. A copy of the notification published in the Official Gazette of India on August 31, 1957 regarding the grant of recognition to BSE under Section 4 of the SCRA by the Central Government is annexed hereto as **Annexure 5**.

Over the past 140 years, BSE has facilitated the growth of the Indian corporate sector by providing it an efficient capital-raising platform. In 1986, BSE launched the S&P BSE SENSEX, which was India's first equity index and is still considered as a benchmark equity index that reflects the health of the Indian economy. Further, S&P BSE SENSEX index is traded internationally on the Eurex Exchange as well as on other leading exchanges of the BRICS nations (Brazil, Russia, China and South Africa). Based on this index, BSE, in the year 2000 opened its derivatives market, trading SENSEX futures contracts. The development of SENSEX options along with equity derivatives followed in 2001 and 2002, expanding BSE's trading platform.

BSE, previously mutually owned and un-incorporated, was incorporated on August 08, 2005 under the provisions of the Companies Act, 1956 as a public limited company. The Corporate

Identity Number of BSE is U67120MH2005PLC155188. Its erstwhile name was Bombay Stock Exchange Limited. [The Certification of Incorporation and the Fresh Certificate of Incorporation pursuant to change of name are annexed hereto as **Annexure 6**. The Memorandum of Association and the Articles of Association of BSE are annexed hereto as **Annexure 7**.] BSE is located on Dalal Street, Mumbai, Maharashtra. Mumbai is referred to as the financial capital of India. In 2007, BSE became a corporatized and demutualised entity.<sup>6</sup>[The BSE (Corporatisation and Demutualisation) Scheme, 2005 is annexed hereto as **Annexure 8**.] BSE has a nation-wide presence and a global reach with customers around the world. BSE has been a driver of several key initiatives and developments in the Indian capital market. Some of the key milestones achieved by BSE have been annexed hereto as **Annexure 9**.

BSE is one of the leading stock exchanges in the world and has fared remarkably well in the World Federation Exchanges Rankings in the following categories<sup>7</sup>:

Sl. No.	Particulars	Rank
1	Number of Listed Companies	1
2	Currency Options- Number of Contracts Traded	2
3	Currency Options- Notional Turnover	3
4	Currency Futures- Number Of Contracts Traded	3
5	Number of New Bonds Listed	6
6	Stock Index Options- Number of Contracts Traded	6
7	Number of Bonds Listed	7
8	Stock Index Options- Notional Turnover	7
9	Currency Futures- Notional Turnover	7
10	Number of Other Companies Listed	9
11	Number of New Companies Listed Through An IPO	10
12	Interest Rate Futures- Number of Contracts Traded	10
13	Market Capitalization	11

<sup>6</sup> Its shareholding, management and ownership are segregated from one another, thereby ensuring a minimally conflicted model.

<sup>7</sup> These rankings are as on December 2015/YTD 2015.

14	Number of Trades in Equity Shares	11
15	Bond Trades- Electronic Order Book Trades	11
16	Stock Options- Notional Turnover	11

BSE is subject to the regulatory oversight of SEBI. BSE is also a Partner Exchange of the United Nations Sustainable Stock Exchange initiative, joining it in September 2012.<sup>8</sup> BSE is an affiliate member of the IOSCO. Mr. Nehal Vora, the Chief Regulatory Officer of BSE, chairs the Task Force on Cyber Crime for the Affiliate Members Consultative Committee as a part of IOSCO deliberations. BSE is a signatory to the International Information Sharing Memorandum of Understanding and Agreement.

***Ownership and Corporate Structure of BSE***

Pursuant to a ‘no observation letter’ issued by SEBI, BSE launched its initial public offering (“IPO”) on January 23, 2017. Consequently, BSE became India’s first listed stock exchange on February 3, 2017. BSE’s shares are now listed on the National Stock Exchange of India Ltd having a broad shareholder base of approximately 1,75,091 shareholders as on March 31, 2018 shareholders, which includes leading global exchange, Deutsche Börse AG. The five largest shareholders of BSE with their respective shareholding are as follows:- Deutsche Börse AG (4.78 %), State Bank of India (4.78%), Life Insurance Corporation of India (4.73 %), GKFF Ventures (2.30%) and Caldwell India Holdings Inc. (2.20%) as on March 31, 2018.

As on March 31, 2018, the subsidiaries and step down subsidiaries of BSE are as follows:- Indian Clearing Corporation Limited (“ICCL”), India International Clearing Corporation (IFSC) Limited, India International Exchange (IFSC) Limited, BSE Institute Limited (BIL), Marketplace Technologies Private Limited (MTPL), BFSI Sector Skill Council of India (BFSI), Marketplace Tech Infra Services Private Limited (MTISPL), BSE Investments Limited (BIL), BSE SAMMAAN CSR Limited, BIL – Ryerson Technology Startup Incubator Foundation (BRTSIF), BSE CSR Integrated Foundation and BSE Skills Limited (BSL). The joint ventures of BSE are Asia Index Private Limited (AIPL). Central Depository Services (India) Limited (“CDSL”), CDSL Ventures Limited (CVL), CDSL Insurance Repository

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<sup>8</sup> “Bombay Stock Exchange (BSE) commits to promoting sustainability”, September 27, 2012, available at [http://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=310&Sitemap\\_x0020\\_Taxonomy=ISAR%20-%20Corporate%20Transparency%20-%20Accounting:#6:#Investment](http://unctad.org/en/pages/newsdetails.aspx?OriginalVersionID=310&Sitemap_x0020_Taxonomy=ISAR%20-%20Corporate%20Transparency%20-%20Accounting:#6:#Investment)

Limited (CIRL), CDSL Commodity Repository Limited and BSE EBIX Insurance Broking Private Limited are associate companies of BSE.

BSE has a vertically integrated market infrastructure with ICCL as its fully owned Central Counter Party (“CCP”) and has a 24% stake in CDSL, one of the two central securities depositories in India. CDSL has undergone an IPO in June 2017 and pursuant to the same, BSE has divested its shareholding in CDSL from 50.05% to 24%. Further, Regulation 7 of the SEBI (Depositories and Participants) Regulation 1996 requires that a recognised stock exchange that is a sponsor of any depository shall not hold more than 24% of the paid-up equity share capital of that depository. The change in shareholding of BSE in CDSL is in line with this regulatory requirement. BSE is a promoter and sponsor for CDSL, and BSE and CDSL are associate companies.

BSE also operates BSE Institute Limited, which is one of the most respected capital market educational institutes in the country.

The depository facilities of holding of securities in electronic form and enabling securities transactions to be processed by book entry are carried out by CDSL. CDSL is an associate company of BSE and was promoted by BSE jointly with leading banks in India such as, State Bank of India, Bank of India, Bank of Baroda, HDFC Bank, Standard Chartered Bank and Union Bank of India. BSE is the largest shareholder of CDSL and holds shares amounting to 24% of the total paid-up equity share capital of CDSL.

CDSL was set up with the objective of providing convenient, dependable, and secure depository services at affordable costs to all market participants. Some of the important statistics in relation to CDSL are as follows:-<sup>9</sup>

Securities available for Demat	
Equity	9,938
Debt instruments including debentures, bonds, Government securities, certificates of deposits, commercial paper, pass through certificates and others.	14,513
Mutual fund units	16,247

<sup>9</sup> These statistics are as on March31, 2018.

Depository Participants	
Number of Depository Participants	594
Number of branches with LIVE Connectivity	209
Number of cities/ towns with LIVE connectivity	103
Number of locations with LIVE connectivity	294
Demat Custody	
Number of securities (in billion)	283.92
Value (Rs. in billion)	19,839.81

***Overview of the Rules, Bye Laws and Regulations of BSE***

BSE has established rules, policies and other similar instruments that are necessary or appropriate to govern and regulate all aspects of its affairs and business. In fact, much before the actual legislations were enacted, BSE had formulated a comprehensive set of Rules, Bye-laws and Regulations that govern various aspects of its functioning and management as a stock exchange and the securities market. It had also laid down best practices which were adopted subsequently by 23 stock exchanges which were set up after India gained its independence. The Trading Members of BSE are governed by Rules, Bye-laws and Regulations of BSE made pursuant to the SCRA and in accordance with the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 (“**SECC Regulations**”).

BSE was the first stock exchange to get recognition from the Central Government in the year 1957. Over the years, several legislative amendments issued by the Central Government / SEBI resulted in a series of changes to the Rules, Bye-laws, and Regulations of BSE. These successive changes had led to duplication of provisions and inconsistencies in certain terms of the Rules, Bye-laws, and Regulations of BSE.

In light of the above and to streamline the Rules, Bye-laws, and Regulations of BSE as per the present regulatory framework, BSE has revamped its Rules, Bye-laws, and Regulations and accordingly, after receiving SEBI’s approval and publication in the Official Gazette, BSE has issued a notice dated April 19, 2017, inter alia, informing the market participants about the applicability of the current Rules, Bye-laws, and Regulations of BSE.

- a. Rules of BSE: They deal with the overall functioning, constitution and governance of BSE. They also deal with admission of member brokers on BSE, disciplinary proceedings against the member brokers and penalties etc.
- b. Bye-Laws of BSE: They, *inter alia*, deal with dealings in securities on BSE, entering into contracts, margin requirements, rights and obligations of member brokers and investors, arbitration mechanism, declaration of defaulter etc.
- c. Regulations of BSE: They envisage the procedural aspects, day-to-day operations, processes, formats relating to the arbitration mechanism, dealing in contracts etc.

The SECC Regulations are annexed hereto as **Annexure 10**. The Rules, Bye-laws and Regulations of BSE for the cash segment and the derivatives segment have been annexed hereto as **Annexure 11** and **Annexure 12** respectively.

Section 9 of the SCRA specifically empowers recognised stock exchanges to make Bye-laws. In addition, Section 23H of the SCRA provides for statutory penalty for the breach of rules, articles of association, bye-laws and regulations of any recognised stock exchange. Section 23H states as follows,

*“23H. Whoever fails to comply with any provision of this Act, the rules or articles or bye-laws or the regulations of the recognised stock exchange or directions issued by the Securities and Exchange Board of India for which no separate penalty has been provided, shall be liable to a penalty which shall not be less than one lakh rupees (one hundred thousand rupees) but which may extend to one crore rupees (Rs. 10 million).”*

Under Indian law, no recognised stock exchange can amend its Bye-laws on its own volition. To amend its Bye-laws, the recognised stock exchange is required to take prior approval of SEBI and provide reasons for such amendment to the Bye-laws. The general procedure on amendment of the Rules, Bye-Laws and Regulations of BSE is as follows:-

- a. Rules: Pursuant to the regulatory changes suggested by SEBI or otherwise, the draft rules are placed before the Board of Directors of BSE for their approval. On receipt of the approval, the proposed rules are forwarded to SEBI for its approval. On receipt of the approval from SEBI, the proposed rules are published in the Official Gazette of India and State Gazette. The proposed rules come into force on such publication.

- b. Bye laws: After carrying out regulatory changes, the proposed Bye- laws are placed before the Board of Directors of BSE for their approval. On receipt of the approval, the proposed Bye-laws are published for public comments unless a waiver is granted by SEBI. After expiry of period for inviting public comments, the proposed Bye-laws and public comments, if any, are forwarded to SEBI for its approval. In case, no changes are suggested by SEBI, then the proposed Bye-laws are published in Official Gazette of India and State Gazette. The proposed Bye-laws come into force on such publication.
- c. Regulations: Pursuant to powers vested under the Rules and Bye-laws of BSE, the Board of Directors of BSE is empowered to make/amend the Regulations of BSE. On receipt of the approval of Board of Directors, the proposed regulations come into force.

### ***Organizational and Governance Structure of BSE***

BSE is governed by its Board of Directors (“**Board or Board of Directors**”), the composition of which is regulated by the SECC Regulations. The requirements under Regulation 23 of the SECC Regulations which deals with the composition of the Governing Board (i.e., the Board of Directors) of a recognised exchange are as follows:-

- i. subject to prior approval of SEBI, the chairperson shall be elected by the governing board from amongst the public interest directors;
- ii. the number of public interest directors shall not be lesser than the number of shareholder directors in a recognized stock exchange;
- iii. the managing director shall be an ex-officio director on the governing board and shall not be included in either the category of public interest directors or shareholder directors;
- iv. any employee of a recognized stock exchange may be appointed on the governing board in addition to the managing director, and such director shall be deemed to be a shareholder director;
- v. no Trading Member or their associates and agents shall be on the governing board of a recognized stock exchange;

- vi. no foreign institutional investor shall have any representation in the governing board of a recognized stock exchange.

Regulation 23 of SECC Regulations effectively requires BSE to have a Board of Directors comprising:-

- i. Shareholder directors;
- ii. Public interest directors; and
- iii. Managing director.

A 'public interest director' is defined under Regulation 2(n) of the SECC Regulations as an independent director, representing the interests of investors in securities market and who does not have any association, directly or indirectly, which in the opinion of SEBI, is in conflict with such director's role. A 'shareholder director' is defined under Regulation 2(r) of the SECC Regulations as a director who represents the interest of shareholders, and elected or nominated by such shareholders who are not Trading Members or their associates and agents. Further, the chairperson shall be elected by the board of directors from amongst the public interest directors, subject to the prior approval of SEBI.

Regulation 24 of the SECC Regulations provides the following conditions for the appointment of directors:-

- i. the appointment and re-appointment of all shareholder directors on the governing board of a recognized stock exchange shall be with the prior approval of SEBI;
- ii. the public interest directors on the governing board of a recognised stock exchange shall be nominated by SEBI;
- iii. the public interest directors shall be nominated for a fixed term of three years, or for such extended period, as may be approved by SEBI;
- iv. if any issue arises as to whether an assignment or position of a public interest director is in conflict with his role, the SEBI's decision shall be final;
- v. a public interest director may be re-nominated after a cooling-off period of one year or such period as the SEBI may deem fit in the interest of the securities market.

Further, SEBI circular dated December 13, 2012 on Procedural Norms on Recognitions, Ownership and Governance for Stock Exchanges and Clearing Corporations<sup>10</sup> [annexed hereto as **Annexure 13**], requires that the stock exchange shall ensure that public interest directors are selected from diverse fields of work. While deciding to propose a particular person as a public interest director, the stock exchange shall also take into account the following factors:-

- a) Qualification in the area of law, finance, accounting, economics, management, administration or any other area relevant to the financial markets.
- b) At least one person may be inducted having experience and background in finance / accounts who may preferably be inducted in the audit committee.
- c) Persons currently holding positions of trust and responsibility in reputed organizations or person who have retired from such positions.
- d) Persons who are likely to have interested positions in commercial contracts and financial affairs of stock exchanges, may be excluded. Also, persons who are regular traders/ speculators in the market or are director in the board of the promoter entity of the stock exchange or clearing corporation, shall be excluded.

For the appointment of a managing director, BSE has to comply with the following requirements, as laid down under Regulation 25 of the SECC Regulations:-

- i. the appointment, renewal of appointment and termination of service of the managing director of a stock exchange shall be subject to prior approval of SEBI;
- ii. every recognized stock exchange shall, subject to the guidelines issued by SEBI from time to time, determine the qualification, manner of appointment, terms and conditions of appointment and other procedural formalities associated with the selection/ appointment of the managing director;
- iii. the appointment of the managing director shall be for a tenure not less than three years and not exceeding five years;

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<sup>10</sup> Circular bearing reference number CIR/MRD/DSA/33/2012, dated December 13, 2012, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1355463824798.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1355463824798.pdf)

- iv. the managing director of a recognized stock exchange shall not –
  - a. be a shareholder or an associate of a shareholder of a recognized stock exchange;
  - b. be a Trading Member or his associate and agent, or shareholder of a Trading Member or shareholder of an associate and agent of a Trading Member or;
  - c. hold any position concurrently in the subsidiary of a recognized stock exchange or in any other entity associated with a recognized stock exchange;
- v. the managing director shall be liable for removal or termination of services by the governing board of a recognised stock exchange with the prior approval of SEBI for failure to give effect to the directions, guidelines and other orders issued by SEBI, or the rules, the articles of association, bye-laws and regulations of a recognized stock exchange;
- vi. SEBI may *suo motu* remove or terminate the appointment of the managing director if deemed fit in the interest of securities market.

Presently, the Board of Directors of BSE has 9 members, out of which 4 members are public interest directors. The list of members of the Board of Directors, as on April 18, 2018, has been annexed hereto as **Annexure 14**. The members of the Board of BSE are selected with due regard to integrity, reputation and competence. The Board of Directors of BSE does not include any Trading Member or any associate or agent of a Trading Member. In selecting the members of the Board, BSE has complied with the requirements laid down under Regulations 24 and 25 of the SECC Regulations and the ‘fit and proper’ criteria as laid down under Regulation 20 of the SECC Regulations, which includes, *inter alia*, a requirement that the person must not have been convicted by a court for any offence involving moral turpitude or any economic offences or any offence under securities laws.

BSE, in compliance with the corporate governance norms and provisions under the Companies Act, 2013,<sup>11</sup> has an Audit Committee, Nomination and Remuneration/ Compensation

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<sup>11</sup> Available at <http://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf>

Committee, Stakeholder Relationship/ Share Allotment Committee, Independent Directors/ Public Interest Directors Committee and Corporate Social Responsibility Committee. [The relevant provisions of the Companies Act, 2013 have been annexed hereto as **Annexure 15.**]

#### *Audit Committee*

This committee has been constituted in line with the provisions of Section 177 of the Companies Act, 2013, Regulation 35 of SECC Regulations and corporate governance norms.

The terms of reference of the Audit Committee are as follows:-

- a. oversight of the company's financial reporting process and the disclosure of its financial information to ensure that the financial statement is correct, sufficient and credible;
- b. recommendation for appointment, remuneration and terms of appointment of auditors of the company;
- c. approval of payment to statutory auditors for any other services rendered by the statutory auditors;
- d. review and monitor the auditor's independence and performance, and effectiveness of audit process;
- e. reviewing, with the management, the annual financial statements and the auditors' report thereon, before submission to the Board for approval, with particular reference to-
  - i. matters required to be included in the Director's Responsibility Statement to be included in the Board's report in terms of clause (c) of sub-section 3 of section 134 of the Companies Act, 2013;
  - ii. changes, if any, in accounting policies and practices and reasons for the same;
  - iii. major accounting entries involving estimates based on the exercise of judgment by management;

- iv. significant adjustments made in the financial statements arising out of audit findings;
  - v. compliance with listing and other legal requirements relating to financial statements;
  - vi. disclosure of any related party transactions;
  - vii. qualifications in the draft audit report;
- f. reviewing, with the management, the quarterly, financial statements before submission to the board for approval;
  - g. reviewing the financial statements, in particular, the investments made by the unlisted subsidiary company;
  - h. reviewing, with the management, the statement of uses/ application of funds raised through an issue (public issue, rights issue, preferential issue, etc.), the statement of funds utilized for purposes other than those stated in the offer document/ prospectus/ notice and the report submitted by the monitoring agency monitoring the utilisation of proceeds of a public or rights issue, and making appropriate recommendations to the Board to take up steps in this matter;
  - i. to formulate the scope, functioning, periodicity and methodology for conducting the internal audit in consultation with the internal auditor;
  - j. reviewing, with the management, performance of statutory and internal auditors, and adequacy of the internal control systems;
  - k. reviewing the adequacy of internal audit function, if any, including the structure of the internal audit department, staffing and seniority of the official heading the department, reporting structure coverage and frequency of internal audit;
  - l. discussion with internal auditors any significant findings and follow up there on;
  - m. reviewing the findings of any internal investigations by the internal auditors into matters where there is suspected fraud or irregularity or a failure of internal control systems of a material nature and reporting the matter to the Board;

- n. discussion with statutory auditors before the audit commences, about the nature and scope of audit as well as post-audit discussion to ascertain any area of concern;
- o. to look into the reasons for substantial defaults in the payment to the depositors, debenture holders, shareholders (in case of non-payment of declared dividends) and creditors;
- p. to review the functioning of the Whistle Blower mechanism;
- q. approval of appointment of CFO (i.e., the Whole-Time Finance Director or any other person heading the finance function or discharging that function) after assessing the qualifications, experience and background, etc. of the candidate;
- r. valuation of undertakings or assets of the Company, wherever it is necessary;
- s. scrutiny of inter-corporate loans and investments;
- t. evaluation of internal financial controls and risk management systems;
- u. approval or any subsequent modification of transactions of the company with related parties;
- v. to appoint a person having such qualifications and experience and registered as a valuer in such manner, on such terms and conditions as may be prescribed and appointed by the audit committee for valuation, if required to be made, in respect of any property, stocks, shares, debentures, securities or goodwill or any other assets or net- worth of a company or its liabilities;
- w. to ensure proper system for storage, retrieval, display or printout of the electronic records as deemed appropriate and such records shall not be disposed of or rendered unusable, unless permitted by law provided that the back-up of the books of account and other books and papers of the company maintained in electronic mode, including at a place outside India, if any, shall be kept in servers physically located in India on a periodic basis;
- x. carrying out any other function as is mentioned in the terms of reference of the Audit Committee.

The list of members of the Audit Committee is annexed hereto as **Annexure 16**.

*Nomination and Remuneration/ Compensation Committee*

This committee is vested with all the necessary powers and authority to identify persons who are qualified to become directors and who may be appointed in senior management in accordance with the prescribed criteria, recommend to the Board their appointment and remove and evaluate every director's performance. The terms of reference of the committee are as follows:-

- a. formulate the criteria for determining qualifications, positive attributes and independence of a director and recommend to the Board a policy, relating to the remuneration for the directors, key managerial personnel under Companies Act 2013 and other employees;
- b. devising a policy on Board diversity;
- c. formulation of criteria for evaluation of independent directors and the Board;
- d. decide on the compensation policy of the Company;
- e. determine the duration of appointment and compensation payable to BSE's Managing Director, Whole Time Directors;
- f. decide on the policy relating to duration of appointment and policy relating to compensation payable to Key Management Personnel under SECC Regulations and Companies Act, 2013 other than Managing Director and decide on policy relating to evaluation of their performance. Section 178(4) of Companies Act, 2013 states that the Nomination and Remuneration Committee shall, while formulating the policy under subsection (3) ensure that:
  - i. the level and composition of remuneration is reasonable and sufficient to attract, retain and motivate directors of the quality required to run the company successfully;
  - ii. relationship of remuneration to performance is clear and meets appropriate performance benchmarks;
  - iii. remuneration to directors, key managerial personnel and senior management involves a balance between fixed and incentive pay reflecting

short and long-term performance objectives appropriate to the working of the company and its goals.

The list of members of the Nomination and Remuneration/Compensation Committee is annexed hereto as **Annexure 17**.

*Stakeholder Relationship/ Share Allotment Committee*

This committee has been constituted for allotment of shares of BSE issued/to be issued, from time to time and to look into the redressal of shareholder and investors complaints. It is also in line with the prevailing guidelines on corporate governance. The terms and reference of the committee are as follows:-

- a. to allot shares/securities from time to time;
- b. to consider all matters pertaining to securities, including but not limited to – offer of securities, allotment of securities, issue of securities, crediting of securities in depository system, listing/ de-listing of securities on/ from stock exchange(s) in India or abroad, transfer of securities, transmission of securities, demat of securities, remat of securities, issue of duplicate securities certificate, consolidation of securities certificates, split of securities certificate and to do all acts required to be done under the applicable rules, regulations and guidelines, from time to time and to consider matters incidental thereto;
- c. to monitor the shareholding pattern and related reports on securities;
- d. to approve the opening, operations and closure of bank accounts for payment of interest, dividend and issue / redemption of securities and to authorize officials to open, operate and close the said accounts from time to time;
- e. to appoint/change and fix the fees and other charges payable to the Registrar and Transfer Agents (RTA) for handling the work relating to securities and to delegate powers to the RTA as may be deemed fit and to monitor all activities of the RTA;
- f. to consider and resolve the matters/grievances of shareholders/ investors in regard to the following:-
  - i. transfer of shares

- ii. non-receipt of dividends
- iii. non-receipt of shares in demat account
- iv. non-receipt of annual report
- v. any other matter of shareholder / investor grievance
- vi. to delegate any of the aforesaid matters to Director(s)/official(s) and/or the officials of the RTA, as the Committee may deem fit.

The list of members of the Stakeholder Relationship/ Share Allotment Committee is annexed hereto as **Annexure 18**.

*Independent Directors/ Public Interest Directors Committee*

The role of the Independent Directors/ Public Interest Directors Committee is as stated below:-

- a. *SECC Regulations*: During the meeting, the public interest directors shall review the following:-
  - i. status of compliance with SEBI letters/ circulars;
  - ii. review the functioning of regulatory departments including the adequacy of resources dedicated to regulatory functions;
  - iii. the public interest directors shall prepare a report on the working of the other committees where they are also the members. The report shall be circulated to the other public interest directors;
  - iv. a consolidated report shall then be submitted to the governing board of the stock exchange;
  - v. the public interest directors shall identify important issues which may involve conflict of interest for the stock exchange or may have significant impact on the market and report the same to SEBI;
- b. *Companies Act, 2013*
  - i. review the performance of non-independent directors and the Board as a whole;

- ii. review the performance of the Chairperson of the company, taking into account the views of executive directors and non-executive directors;
- iii. assess the quality, quantity and timeliness of flow of information between the company management and the Board that is necessary for the Board to effectively and reasonably perform their duties.

The list of members of the Independent Directors/ Public Interest Directors Committee is annexed hereto as **Annexure 19**.

*Corporate Social Responsibility Committee*

The Board of Directors at their meeting held on March 11, 2014, constituted the Corporate Social Responsibility Committee to comply with the requirements of Section 135 of the Companies Act, 2013. The role of Corporate Social Responsibility Committee is as follows:-

- a. formulate and recommend to the Board, a Corporate Social Responsibility Policy which shall indicate the activities to be undertaken by the company as specified in Schedule VII of the Companies Act, 2013;
- b. recommend the amount of expenditure to be incurred on the activities referred to in clause (i); and
- c. monitor the Corporate Social Responsibility Policy of the Company from time to time.

The list of members of the Corporate Social Responsibility Committee is annexed hereto as **Annexure 20**.

BSE has undertaken various CSR activities in areas such as Social Welfare, Community Development, Education and Environment. Some notable activities include funding charitable causes for the elderly and the physically challenged, supporting the rehabilitation and restoration efforts in earthquake-hit communities of Gujarat and contributing Rs. One Crore (Ten million) to the Prime Minister's Fund for Tsunami Relief. Further, BSE and the Indian Institute of Corporate Affairs (IICA), established by the Ministry of Corporate Affairs, Government of India, have signed a Memorandum of Understanding on September 23, 2013 to work collaboratively in the domains of business sustainability, CSR, investor education and other allied areas. Besides, BSE has been awarded the Golden Peacock Global

CSR Award for its initiatives in Corporate Social Responsibility by the World Council of Corporate Governance. The CSR Vision & Policy Statement aims:

- i. To promote activities that have a high social impact in a manner which is aligned with BSE's tradition of creating health and wealth in the community and create a framework to identify the beneficiaries, causes to work and the appropriate projects.
- ii. To encourage employees at all levels to participate and increase commitment to give back to the society.
- iii. To identify thrust areas for CSR that currently include Education, Health and Wealth Creation and the Environment.
- iv. To utilise the resources of the Company and its people to give back to the society and affect positive changes in the lives of Indian citizens.

BSE will invest its CSR resources that help build the nation and the economy in important areas such as education including basic education and skills, investor education, capital formation, job creation, entrepreneurship, etc. This policy aims to create a unified approach to the CSR activities to enhance commitment across all levels in the organisation and its stakeholders.

#### *Statutory Committees*

SEBI, in order to ensure effective oversight of the functioning of stock exchanges, through various circulars has mandated the formation of various committees by stock exchanges. Hence, in addition to the aforementioned committees, BSE has various statutory committees as prescribed by SEBI and the SECC Regulations, such as the Membership Selection Committee, Disciplinary Action Committee, Investor Grievance Redressal Committee, Defaulters' Committee, Standing Committee on Technology, Investor Services Committee, Arbitration Committee, Ethics Committee, Oversight Committee (Member Regulation), Oversight Committee (Listing Function), Oversight Committee (Trading and Surveillance Function), Advisory Committee and Sub-Committee for monitoring compliance of suggestions given in SEBI Inspection Report. BSE has also formed committees, viz., Listing Committee and Risk Management Committee for its efficient functioning.

Stock exchanges are required to constitute the aforesaid committees in accordance with the composition and terms of reference prescribed for the respective committee. Stock exchanges are empowered to lay down the policy for frequency of meetings, quorum etc. for the statutory committees.

SEBI's circular dated December 13, 2012 (annexed hereto as **Annexure 13**) requires independent external persons to be appointed to some of these committees. Such persons are required to be appointed from amongst persons of integrity, having a sound reputation and not having any conflicts of interest. Further, the said persons shall be specialists in the field of work assigned to the committee. The circular requires stock exchanges to frame guidelines regarding appointment, tenure, code of conduct, etc., of independent external persons. Extension of the tenure may be granted at the expiry of the tenure pursuant to a review of the contribution, record of attendance at meetings, etc.

A copy of the organizational chart of BSE is annexed hereto as **Annexure 21** for ease of reference. As on March 31, 2018, the total number of employees in BSE is 513, including 395 officers and 118 staff.

***Provisions to minimize conflicts of interest with respect to membership on the governing board and committees of BSE***

*SECC Regulations and Companies Act, 2013*

The SECC Regulations have put in place stringent requirements for controlling conflict of interest, such as the number of public interest directors shall not be less than the number of shareholder directors in a recognized stock exchange, the chairperson shall be elected from amongst the public interest directors, at least one public interest director must be present in the meetings of the governing board to constitute the quorum and no trading member or its associates and agents or foreign institutional investor shall be on the governing board of a recognized stock exchange.

Over and above complying with the provisions under the SECC Regulations, BSE, as a public limited company, has to comply with corporate governance norms under the Companies Act, 2013, such as those pertaining to related party transactions, disclosure of aggregate value of related party transactions entered into during the financial year, whistle blower policy, policy on material subsidiaries, etc.

### *Code of Ethics*

Regulation 26(2) of the SECC Regulations states that every director and key management personnel of a recognized stock exchange shall abide by the code of ethics specified therein. Rule 170(aa) of the BSE Rules states that the members of the Governing Board and functionaries of BSE shall follow and observe the Code of Ethics applicable to the members of the Governing Board, committee members and the functionaries of BSE. The Policy on Ethical Code and Conduct for Functionaries of BSE is annexed hereto as **Annexure 22**.

The Ethics Committee of BSE is responsible for the implementation of the Code of Ethics. It is based on the following fundamental principles:-

- a. fairness and transparency in dealing with matters relating to the stock exchange or and the investors;
- b. compliance with all laws/rules/regulations laid down by regulatory agencies/stock exchange;
- c. exercising due diligence in the performance of duties;
- d. avoidance of conflict of interest between self-interest of directors/ key management personnel and interests of a stock exchange and investors.

The Code of Ethics requires all the directors and functionaries of BSE to declare any conflicts of interest at the point of becoming engaged by BSE and, subsequently, throughout the entire course of engagement to ensure that there are prompt disclosures of any conflict of interest. Paragraph 6 of the Code of Ethics states that all directors and employees shall disclose to the Board of Directors/ Compliance Officer/ Ethics Committee, upon assuming office and during their tenure in office, whenever the following arises:-

- a. any fiduciary relationship of self and family members and directorship/partnership of self and family members in any trading member or clearing member;
- b. shareholding, in cases where the shareholding of the director, directly or through his family exceeds 5% in any listed company or in other entities related to the securities markets;
- c. any other business interest.

Paragraph 9 of the Code of Ethics states that, directors/ committee members of a stock exchange should not use their position to obtain business or any pecuniary benefit in the organization for themselves or family members. Furthermore, the Code of Ethics requires individuals having conflict of interest to be excluded from the process of taking decisions in which that conflict of interest would be relevant. Where an individual has declared his/ her conflict of interest, he or she will be removed from the decision making process. Paragraph 5 of the Code of Ethics states that no director of the Board of Directors or member of any committee of BSE shall participate in any decision making/ adjudication in respect of any person/ matter in which he is in any way, directly or indirectly, concerned or interested.

### *SEBI Circulars*

The norms prescribed by SEBI's circular dated December 13, 2012, on Procedural norms on Recognitions, Ownership and Governance for Stock Exchanges and Clearing Corporations (annexed hereto as **Annexure 13**), requires stock exchanges to have an internal manual covering the management of conflicts between commercial and regulatory functions of the recognized stock exchange. The recognized stock exchange is required to put in place a policy for comprehensive training and awareness of its employees on the various conflicts of interests involved in the functioning of its regulatory departments. Further, the entire conflict management framework shall periodically be reviewed and be strengthened based on the observations of such review. Further, the circular requires public interest directors to identify important issues which may involve conflict of interest for the recognized stock exchange, may have significant impact on the functioning of the recognized stock exchange and may not be in the interest of market. The public interest directors are required to report the same to SEBI.

Further, SEBI issued a circular on August 27, 2013, prescribing general guidelines for dealing with conflicts of interest of intermediaries, recognised stock exchanges, recognised clearing corporations, depositories and their associated persons in securities market<sup>12</sup> [annexed hereto as **Annexure 23**]. The circular provided broad guidelines to minimize the effect of the conflict of interest and required the said entities to put in place systems and policies for implementation

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<sup>12</sup> Circular bearing reference number CIR/MIRSD/5/2013, dated August 27, 2013, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1377662180567.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1377662180567.pdf)

of the said circular and provide necessary guidance enabling identification, elimination or management of conflict of interest situations.

### ***Listing on BSE***

#### *Requirement of Listing*

The listing of equity shares and convertible securities is governed by the SEBI (Issue of Capital & Disclosure Requirements) Regulations, 2009 (“**ICDR Regulations**”), while the listing of debt securities<sup>13</sup> is governed under the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 (“**ILDS Regulations**”). Regulation 4(2) of the ICDR Regulations states that an issuer shall not make a public issue or rights issue of equity shares or convertible securities unless it has made an application to at least one recognized stock exchange having nationwide trading terminals for listing of securities on such stock exchange. In case the exchange does not give permission to the company for listing of securities, the company cannot proceed with the allotment of shares. [ICDR Regulations and ILDS Regulations have been annexed hereto as **Annexure 24** and **Annexure 25** respectively.]

#### *Procedure and Requirements for Listing*

A company, desirous of listing its securities on a stock exchange, is required to file an application, in the prescribed form, with the stock exchange before issue of prospectus by the company, where the securities are issued by way of a prospectus. For the process of listing, a company has to comply with the applicable provisions under the SCRA, the Securities Contracts (Regulation) Rules 1957 (“**SCRR**”), the Companies Act, 2013, SEBI guidelines, Bye-laws and Regulations of the Exchange and other relevant stock exchange guidelines. Section 21 of the SCRA states that where securities are listed on the application of any person on a recognized stock exchange, such person shall abide by the conditions of the listing agreement with that stock exchange. [SCRR has been annexed hereto as **Annexure 26**.]

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<sup>13</sup> Regulation 2(e) ILDS Regulations- “debt securities” means a non-convertible debt securities which create or acknowledge indebtedness, and include debenture, bonds and such other securities of a body corporate or any statutory body constituted by virtue of a legislation, whether constituting a charge on the assets of the body corporate or not, but excludes bonds issued by Government or such other bodies as may be specified by the Board, security receipts and securitized debt instruments;

Further, Regulation 19 of the SCRR deals with the requirements with respect to listing of securities on a recognized stock exchange. It enumerates certain documents to be submitted by the company desirous of getting its securities listed. These include:-

- Memorandum and articles of association and, in case of a debenture issue, a copy of the trust deed;
- Copies of all prospectuses or statements in lieu of prospectuses issued by the company at any time;
- Copies of offers for sale and circulars or advertisements offering any securities for subscription or sale during the last five years;
- Copies of balance sheets and audited accounts for the last five years, or in the case of new companies, for such shorter period for which accounts have been made up;
- Certified copies of agreements or other documents relating to arrangements with or between, for instance, vendors and/or promoters, underwriters and sub-underwriters, brokers and sub-brokers;
- A statement containing particulars of the dates of, and parties to all material contracts, agreements (including agreements for technical advice and collaboration), concessions and similar other documents (except those entered into in the ordinary course of business carried on or intended to be carried on by the company) together with a brief description of the terms, subject-matter and general nature of the documents;
- Particulars of shares and debentures issued (i) for consideration other than cash, whether in whole or part, (ii) at a premium or discount, or (iii) in pursuance of an option.

Vis-à-vis the designated stock exchange, an issuer has the following role:-

- filing of offer document
- filing of due diligence certificate of merchant banker
- filing of underwriting agreement
- filing basis of allotment

- obtaining listing and trading permission.

In addition to these rules and regulations, every stock exchange has its own set of guidelines for the companies to be listed on it. For instance, they may provide for the minimum issue size, financial worthiness such as net-worth requirement, profit for specified period and market capitalization of the company. Companies are also required to pay to the exchange some listing fee as prescribed by the exchange every financial year. A company not complying with these requirements is not granted listing.

BSE through its notice dated March 11, 2016 issued the consolidated master checklist for listing of securities on BSE. The link to the said notice contained the master checklist is <http://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20160311-33> which has been amended from time to time resting with Master circular dated February 28, 2018 and link of the same is <https://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20180228-34>.

#### *Listing Department of BSE*

BSE has a dedicated Listing team divided into two departments namely, Listing Operations department and Listing Compliance department. Listing application is processed by the Listing Operations department in accordance with the provisions of the SCRA, the SCRR, the Companies Act, 2013, the Companies Act, 1956 (wherever applicable), guidelines issued by SEBI and Rules, Bye-laws and Regulations of BSE. Listing Compliance department deals with applicability and interpretation issues relating to listing rules and norms and interaction with regulators and monitoring of the compliance of various requirements. The said bifurcation is on account of requirement of the SECC Regulations, requiring segregation of regulatory and non-regulatory functions.

#### *Listing Requirements prescribed by BSE*

The securities may be of any public limited company, Central or State Government, quasi-governmental and other financial institutions/ corporations, municipalities, etc. BSE has prescribed various guidelines and forms that need to be adhered to and submitted by the companies. These assist companies to expedite the fulfillment of various formalities and disclosure requirements that are required at different stages in case of public issues- Initial

Public Offerings (“**IPOs**”), Follow-on Public Offerings (“**FPOs**”), preferential issues, Indian Depository Receipts, amalgamation and Qualified Institutional Placements (“**QIP**”). Some of the listing requirements prescribed by BSE are as follows:-

- Eligibility criteria for listing of companies through IPOs and FPOs

Minimum post-issue paid-up capital	Rs.100 million for IPOs Rs. 30 million for FPOs
Minimum issue size	Rs. 100 million
Minimum market capitalization	Rs. 250 million

Further, in respect of the requirement of paid-up capital and market capitalization, the issuers need to include in the disclaimer clause forming a part of the offer document that in the event of the market capitalization (product of issue price and the post issue number of shares) requirement of BSE not being met, the securities of the issuer would not be listed on BSE. The above eligibility criteria would be in addition to the conditions prescribed under the ICDR Regulations. The applicant, promoters and/or group companies, shall not be in default in compliance of the Listing Agreement.

- Permission to Use the Name of BSE in an Issuer Company’s Prospectus

Companies desiring to list their securities offered through a public issue are required to obtain prior permission of BSE to use the name of BSE in their prospectus or offer for sale documents before filing the same with the concerned office of the Registrar of Companies. BSE’s Listing Committee, comprising senior officials of BSE, decides upon the matter of granting permission to companies to use the name of BSE in their prospectus/ offer documents. The Listing Committee evaluates the promoters, company, project, financials, risk factors and several other aspects before taking a decision in this regard.

- Minimum Requirements for Companies Delisted by BSE seeking Relisting on BSE

Companies delisted by BSE and seeking relisting at BSE are required to make a fresh public offer and comply with the existing guidelines of SEBI and BSE regarding IPOs.

### *Listing Agreement*

Companies desirous of getting their securities listed on BSE are required to enter into an agreement with BSE called the listing agreement, under which they are required to make certain disclosures and perform certain acts, failing which the company may face disciplinary action, including levy of penalty/suspension in trading of securities/ delisting of securities. As such, the listing agreement is of great importance and is executed under the common seal of a company.

Until recently, the provisions of the listing agreement for different kinds of securities were different and emanated from the particular set of regulations applicable to the kind of security being listed. However, SEBI, on September 02, 2015 notified the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“**Listing Regulations, 2015**”), which became effective from December 01, 2015,<sup>14</sup> whereby it seeks to align the existing listing agreement with the Companies Act, 2013, and consolidate and streamline the scattered requirements under existing listing agreements for different securities under a single piece of regulation. [Listing Regulations, 2015 has been annexed hereto as **Annexure 27**.]

SEBI issued a circular on October 13, 2015 prescribing a simplified listing agreement which is uniform across all types of securities/listed entities (“**Revised Listing Agreement**”). Company specific information is required to be submitted along with the Revised Listing Agreement in the required format. SEBI, in the circular dated October 13, 2015 requires a listed entity which has previously entered into agreement(s) with the stock exchange to list its securities, to execute a fresh listing agreement with the stock exchange within six months from September 2, 2015. [The old listing agreement for equity shares and the Revised Listing Agreement are annexed hereto as **Annexure 28** and **Annexure 29** respectively.]

The conversion of the old listing agreement including Clause 49 and about 128 allied SEBI circulars into the Listing Regulations, 2015 is significant from the point of view of enforcement. The listing agreement was a contract between a stock exchange and the issuer entity, whereas, the Listing Regulations, 2015 as an instrument of law that has been tabled for

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<sup>14</sup> However, two provisions of the Listing Regulations 2015, which are facilitating in nature, had become applicable with immediate effect. These pertain to (i) passing of ordinary resolution instead of special resolution in case of all material related party transactions subject to related parties abstaining from voting on such resolutions, in line with the provisions of the Companies Act, 2013, and (ii) re-classification of promoters as public shareholders under various circumstances.

30 days in each House of the Indian Parliament and hence, is more binding in nature. Further, the Listing Regulations, 2015 prescribe stringent disclosures for companies post listing, which will help improve the quality of secondary market disclosures in the country. It is pertinent to note that the Listing Regulations, 2015 contain the post-listing requirements. Pre-listing requirements continue to be incorporated in respective regulations viz., ICDR Regulations, ILDS Regulations, etc. These provisions for instance, pertain to allotment of securities, refund and payment of interest, 1 % security deposit (in case of public issuance).

Under the Revised Listing Agreement, the issuer undertakes certain covenants such as, to comply with the extant provisions of all the applicable statutory enactments governing the issuance, listing and continued listing of securities; to pay listing and such other fees as may be specified by the concerned stock exchange in a timely manner; to intimate the stock exchange regarding any change in information/details of the issuer entity. The Listing Regulations, 2015 lays down the obligations which entities which have listed their securities on an exchange need to comply with, such as those relating to corporate governance, appointment of compliance officer and share transfer agents, timely filing of shareholding pattern and financial results. Non-compliance with the provisions of the Listing Regulations, 2015, would, in addition to attracting liability under the applicable securities laws, be liable for certain actions (such as imposition of fines, suspension of trading) by the stock exchange. An overview of the important provisions under the Listing Regulations, 2015 has been provided hereafter.

BSE monitors the compliance by companies with regard to the provisions of the Listing Regulations, 2015, especially with regard to timely payment of annual listing fees, submission of results, shareholding patterns and corporate governance reports on a quarterly basis. Penal action is taken against the defaulting companies in terms of SEBI circular dated November 30, 2015, which deals with non-compliance with certain provisions of Listing Regulations, 2015 and Standard Operating Procedure for suspension and revocation of trading of specified securities<sup>15</sup> [annexed hereto as **Annexure 30**].

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<sup>15</sup> Circular bearing reference number CIR/CFD/CMD/12/2015, dated November 30, 2015, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1448885765200.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1448885765200.pdf)

### *Other Requirements for Listing*

Certain other significant requirements for listing are as follows:-

- Submission of Letter of Application

As per Section 40 of the Companies Act, 2013, a company seeking listing of its securities on BSE is required to submit a Letter of Application to all the stock exchanges where it proposes to have its securities listed before filing the prospectus with the Registrar of Companies.

- Allotment of Securities and Trading Permission

As per SEBI's circular dated November 10, 2015,<sup>16</sup> (annexed hereto as **Annexure 31**) an issuer is required to complete listing, allotment of securities and trading process within six working days after the closure of issue.

- Requirement of 1% Security

Companies making public/rights issues are required to deposit 1% of the issue amount with the designated stock exchange before the issue opens. This amount is liable to be forfeited in the event the company does not resolve the complaints of investors regarding delay in sending refund orders/share certificates, non-payment of commission to underwriters, brokers, etc.

### *Public Issue and Private Placement of Debt Instruments*

Listing of public issue of bonds on BSE is simple, fast and cost effective. BSE is the exchange of choice as a 'Designated Stock Exchange' for issuers listing their public issue of debentures/bonds. The exchange platform 'IBBS' is a market leader in terms of garnering online bids for the issuers. Listing of publicly issued debt comprises three main stages:-

- Obtaining In-principle approval (Within seven working days of uploading the draft red herring prospectus on the BSE website, subject to no public comments received)
- Basis of Allotment

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<sup>16</sup> Circular bearing reference number CIR/CFD/POLICYCELL/11/2015 on Streamlining the Process of Public Issue of Equity Shares and Convertibles, dated November 10, 2015, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1447148033366.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1447148033366.pdf)

- Listing and Trading Approval

BSE is the first exchange in the country to list securitized debt instruments. A large number of corporates, banks and institutions tap the market through private placement of debt instruments. Currently, 5469 companies are listed on BSE and 2719 companies are available for trading as on April 20, 2018. Further, out of above referred 5469 companies, number of companies with Listed Equity Capital is 5041 and number of companies with only Debt Capital Listed is 405.

#### *Direct Listing*

BSE provides for direct listing of equity shares of companies which are listed with **other** recognized stock exchanges. The norms for direct listing of shares of such companies which are listed on stock exchanges having average daily turnover on equity segment trading platform greater than or equal to Rs. 5 billion in the previous financial year (as applicable from March 01, 2016) and those having turnover less than Rs. 5 billion in the previous financial year (as applicable from March 01, 2016) are annexed hereto as **Annexure 32**.

#### *Dissemination Board*

The mechanism of Dissemination Board of nationwide stock exchanges displaying the securities of unlisted companies on account de-recognition of stock exchanges is also provided by BSE as mandated by SEBI and a note on the Dissemination Board has been annexed hereto as **Annexure 33**.

#### ***BSE SME Platform – Great opportunity For Small and Medium enterprises***

##### *About BSE SME Platform*

BSE SME Platform provides a great opportunity to entrepreneurs to raise equity capital for the growth and expansion of their companies. It helps bring visibility, corporate governance into the company which further enhances the credibility of company. It will help unleash the valuation of the company and in the process create wealth for all the stakeholders including investors, and facility to exit at any point of time. It also provides immense opportunity to investors to identify and invest in good companies at early stage.

BSE understands the importance of SME to Indian economy and therefore has taken various steps for creating awareness among the entrepreneurs, intermediaries and Investors about the SME Platform. BSE conducts seminars with the Federation of Indian Chambers of Commerce

& Industry (FICCI), Confederation of Indian Industry (CII), Indian Merchant Chamber (IMC), Dun & Bradstreet (D&B), Institute of Chartered Accountants of India (ICAI) and Institute of Company Secretaries of India (ICSI) and many other chambers of commerce and associations at state and central level.

*Origin of BSE SME Platform:*

The path for the BSE SME Platform was paved with the guidelines issued by SEBI on May 18, 2010<sup>17</sup> (annexed hereto as **Annexure 34**), pursuant to which BSE became the first exchange to launch its SME Platform on March 13, 2012. Accordingly the guidelines have been made simpler to help SME companies in getting listed. Currently, the requirements are as follows:-

1. Issuer with post issue face value capital up to Rs.100 million shall be compulsory listed under the SME Platform, Issuer with post issue face value capital between Rs.100 – 250 million may get listed on SME Platform and Issuer with post issue face value capital above Rs.250 million has to necessarily listed on the main board of the exchanges.
2. Net Tangible assets of at least Rs. 30 million as per the latest audited financial results.
3. Net worth (excluding revaluation reserves) of at least Rs. 30 million as per the latest audited financial results.
4. Track record of distributable profits in terms of Section 205 of the Companies Act, 1956 for at least two years out of immediately preceding three financial years and each financial year has to be a period of at least twelve months. Extraordinary income will not be considered for the purpose of calculating distributable profits. Otherwise, the net worth shall be at least Rs 50 million.
5. The post-issue paid up capital of the company shall be at least Rs. 30 million.
6. The company has not been referred to the Board for Industrial and Financial Reconstruction (BIFR).
7. There is no winding up petition against the company that has been accepted by a court.
8. There should have been no change in the promoters of the company in the one year preceding the date of filing application to BSE for listing on SME segment.

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<sup>17</sup> Circular bearing reference number CIR/MRD/DSA/17/2010 on Setting up of a Stock exchange/ a trading platform by a Recognized Stock Exchange having Nationwide Trading Terminals for SME, dated May 18, 2010, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1288155570736.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1288155570736.pdf)

*Benefits of SME Platform:*

- Provides SMEs with equity financing opportunities to grow their business – from expansion to acquisition.
- Equity financing lowers the debt burden leading to lower financing cost and healthier balance sheet.
- Expands the investor base, which in turn helps in getting secondary equity financing, including private placement.
- Enhances company’s visibility. Media coverage provides SME with greater profile and credibility leading to increase in the value of its shares.
- Greater incentive for the employees as they can participate in the ownership of the company and benefit from being its shareholders.
- SME sector will grow better on two pillars of the financial system i.e., banking and capital market.

*Procedure for listing on BSE SME Platform*

There are provisions in place for migration to/ from Main Board from/ to SME Exchange. Further, BSE provides a checklist on preparation for IPO/ documents to be submitted by an SME desirous of getting its securities listed on the SME Exchange. Once the issuer company appoints the merchant banker/s in an advisory capacity, the merchant banker conducts due diligence regarding the company and prepares the documentation. These documents are filed with BSE and SEBI. BSE verifies the documents and processes the same. A visit to the company’s site is undertaken by BSE officials. The promoters are called for an interview with the Listing Advisory Committee (LAC). On recommendation of LAC, the matter is considered by the Internal Listing Committee. BSE issues an in-principle approval on the recommendation of the Internal Listing Committee, provided all the requirements are complied with. The merchant banker then files the prospectus with the Registrar of Companies and once approval is received from the Registrar of Companies, BSE is intimated regarding the opening dates of the issue. After the closure of IPO, the company submits the documents as per the checklist to BSE for finalization of the basis of allotment. BSE finalizes the basis of allotment and issues the notice regarding listing and trading.

*Size of BSE SME Platform*

BSE SME Exchange has provided a fairly vibrant trading platform for SMEs. As on April 16, 2018, 240 companies have been listed on BSE SME platform. During Financial Year 2016-17, the SME platform continued to be a front-runner with a market share of over 65%. 60 companies raised Rs. 7.00 billion from the market. The number of companies listed on the BSE SME platform is the highest amongst all the three national level exchanges in India. On October 5, 2017, BSE celebrated the listing of its 200<sup>th</sup> company on the SME platform. The BSE SME platform has 240 companies listed with a total market capitalization of Rs. 218 billion (as on April 16, 2018). The total value of funds raised by these 240 companies from the capital market through BSE SME platform is Rs. 21.80 billion. Further, there are 111 market makers registered with BSE SME (as on April 16, 2018). Other significant statistics related to the BSE SME platform are as follows:-

- Number of SME companies migrated to Main Board- 46
- Number of companies where approval has been given – 27; Number of companies where draft prospectuses have been filed and awaiting approval – 14.
- Market making has been very successful on this platform and they have been able to provide quotes for more than 90% of the time as per the SEBI guidelines.
- SME IPO index launched on December 14, 2012 with 100 as base (Value as on April 13, 2018 –1950.60).

The list of SME scrips listed on BSE along with the funds raised and industry sectors along with market capitalization and the migrated companies, which has been annexed hereto as **Annexure 35**, indicates that the SME companies that have raised capital and are listed, are from a number of industries and are spread across a wide spectrum of the economy.

### Fees

All companies listed on BSE are required to pay to BSE the Annual Listing Fees by April 30<sup>th</sup> of every financial year as per the Schedule of Listing Fees prescribed from time to time. The schedule of Listing Fees for the Financial Year 2016 – 17 is provided hereunder:-

#### Annual/ Further Listing Fee- Equity Segment<sup>18</sup>

Particulars	Millions (Rs)
Initial Listing Fee	0.02
Listed Capital	
(In Rs. Millions)	
Up to 1500	0.2
Above 1500 to 2000	0.23625
Above 2000 to 3000	0.30375
Above 3000 to 4000	0.3675
Above 4000 to 5000	0.4875
Above 5000 to 10000	Rs.0.4875 million and an additional listing fees of Rs. 0.003188/- for every increase of Rs. 50 million or part thereof in the paid up share capital
Above 10000	Rs.0.80625 million and an additional listing fees of Rs. 0.03469 million for every increase of Rs. 50 million or part thereof in the paid up share capital

\*Plus Applicable Service Taxes

<sup>18</sup> The capital to be considered for the above schedule would include equity shares, preference shares, Indian depository receipts, fully convertible debentures, partly convertible debentures and any other security convertible into equity shares. In case of debenture capital (not convertible into equity shares), the fees will be 75% of the above fees. Further, fees are applicable for the full year.

### Fees for Privately Placed Debt Securities

Particulars	Millions (Rs)
Initial Listing fee	0.002
Listing Processing Fees ( <i>applicable only to Private Companies</i> )	0.0045
Annual Listing Fee (Chargeable Per ISIN):	
Issue size upto Rs.50 million	0.0025
Above Rs.50 million and upto Rs.100 million.	0.00375
Above Rs. 100 million. and upto Rs. 200 million	0.0075
Above Rs. 200 million	Additional fee of Rs. 0.0002 million for every increase of Rs. 10 million or part thereof above Rs. 200 million. Subject to a maximum of Rs. 0.03 million per instrument.

Cap on the annual listing fee of debt instruments per issuer is Rs. 0.5 million per annum

#### Fees for SME Segment

The Annual Fees is Rs. 250,000/- or 0.01% of full market capitalization, whichever is higher. The basis of calculation of market capitalization is the closing price as on March 31st or the last day of trading in the financial year.

#### Fees for Mutual Fund Segment<sup>19</sup>

Particulars	In Millions (Rs)
Initial Listing Fee	NIL
Annual Listing Fee for tenure of the scheme	Payable per 'month or part thereof'
Issue size up to Rs. 500 million.	0.001
Above Rs.500 million. and upto Rs.1000 million.	0.0013
Above Rs.1000 million and upto Rs.3000 million	0.0028
Above Rs.3000 million and upto Rs.5000 million	0.0053

<sup>19</sup> For tenure beyond one month, fees are payable for one month or any part thereof.

Above Rs.5000 million and upto Rs.10000 million	0.0093
Above Rs.10000 million.	0.0148
Processing Fees Per Single Scheme Information Document (SID)	0.01

***Listing Obligations and Disclosure Requirements***

The Listing Regulations, 2015 applies to a listed entity which has listed any of the following securities on recognized stock exchange(s):-<sup>20</sup>

- a) specified securities listed on main board or SME exchange or institutional trading platform;
- b) non-convertible debt securities, non-convertible redeemable preference shares, perpetual debt instrument, perpetual non-cumulative preference shares;
- c) Indian depository receipts;
- d) securitised debt instruments;
- e) units issued by mutual funds; and
- f) any other securities as may be specified by SEBI.

Chapter II of the Listing Regulations, 2015 lays down general principles governing disclosures and obligations of listed entities. Regulation 4(1) therein states that the listed entity shall make disclosures and abide by its obligations under the regulations, in accordance with certain principles, such as preparing and disclosing information in accordance with applicable standards of accounting and financial disclosure, refraining from misrepresentation and ensuring that the information provided to recognized stock exchanges and investors is adequate, timely and is not misleading, ensuring that channels for disseminating of information provide for equal, timely and cost efficient access to relevant information by investors. Regulation 4(2) states that the listed entity shall comply with the corporate governance provisions as specified in Chapter IV which shall be implemented to achieve the objectives of

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<sup>20</sup> Regulation 3, Listing Regulations 2015.

the principles such as, the rights of the shareholders are protected and facilitated by the listed entity, shareholders are given equitable treatment and there is disclosure and transparency.<sup>21</sup>

Chapter III of the Listing Regulations, 2015 provides common obligations which are applicable to all listed entities. The promoters, directors or key managerial personnel of the listed entity should comply with the responsibilities assigned to them under the Listing Regulations, 2015.<sup>22</sup> Regulation 6 defines the responsibility of compliance officer, who should be a qualified company secretary coordinating with SEBI, stock exchanges and depositories for compliance with the rules and regulations of the Listing Regulations, 2015. The listed entity can appoint a share transfer agent or can manage the share transfer facility in-house. As per Regulation 7(3), the listed entity has to submit a compliance certificate to the stock exchange which is duly signed by the compliance officer and the authorized representative of the share transfer agent, if applicable, within one month of end of each half of the financial year, certifying the compliance of Regulation 7(2) ensuring the facility maintained for physical and electronic share transfer either in house or by the registrar to an issue and share transfer agent registered with SEBI. In case of any change or appointment of a share transfer agent, the listed entity has to intimate to the stock exchanges within seven days of entering into the agreement with the share transfer agent.

Under Regulation 12, the listed entity has to use electronic mode of payment, as approved by the RBI for dividends, interests, redemption or repayment of amounts. Under Regulation 13, the listed entity has to file with the recognised stock exchanges on a quarterly basis, within twenty-one days from the end of quarter, a statement giving the number of investor complaints pending at the beginning of the quarter, those received during the quarter, disposed of during the quarter and those remaining unresolved at the end of the quarter.

Chapter IV of the Listing Regulations 2015 details out the obligations which are applicable to the listed entities whose specified securities are listed on any recognised stock exchange(s).<sup>23</sup> The corporate governance regulations as specified from Regulation 17 to Regulation 27, Regulations 46(2)(b) to 46(2)(i) and Paragraphs C, D and E of Schedule V shall not apply to i) the listed entity having paid up equity share capital not exceeding Rs. 100 million and net-

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<sup>21</sup> Please refer to Regulation 4 of the Listing Regulations 2015 for the detailed principles.

<sup>22</sup> Regulation 5, Listing Regulations, 2015.

<sup>23</sup> Regulation 15, Listing Regulations, 2015.

worth not exceeding Rs. 250 million, as on the last day of the previous financial year. Once the regulation becomes applicable to a listed entity at a later date, such listed entity shall comply with the requirements of the regulations within six months from the date on which the provisions became applicable to the listed entity. ii) The listed entity other than body corporate whose specified securities are listed on SME Exchange.<sup>24</sup> SEBI is in the process of publishing some of the formats as applicable under the Listing Regulations 2015.

Under Chapters X and XI, stock exchanges have been given the responsibility to monitor compliance or adequacy/accuracy of compliance with the provisions of the Listing Regulations, 2015 and to take action for non-compliance.

Some of the important provisions under the Listing Regulations 2015 are as follows:-

- Board of Directors (Regulation 17)<sup>25</sup>: The chief executive officer and chief financial officer are required to submit the compliance certificate to the board of directors as specified in Part B of Schedule II. The minimum information which requires to be placed before the board of directors is mentioned in Part A of Schedule II.<sup>26</sup>
- Audit Committee (Regulation 18)<sup>27</sup>: The Audit Committee should meet at least four times in a year with not more than 120 days elapsing between two meetings.
- Related Party Transactions (Regulation 23)<sup>28</sup>: An ordinary resolution will suffice the purpose of approval from shareholders instead of special resolution as required under the listing agreement. The related parties need to abstain from voting on such resolutions, whether they are related party to that particular transaction or not.
- Corporate governance requirements with respect to subsidiary of listed entity are provided in Regulation 24.<sup>29</sup>

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<sup>24</sup> This regulation is in similar lines with the SEBI Circular No. CIR/CFD/POLICY CELL/7/2014 dated 15.09.2014 in terms of amendments to Clause 49 of the equity listing agreement.

<sup>25</sup> Corresponds to Clause 49II of the listing agreement.

<sup>26</sup> Same as Annexure – X of the listing agreement.

<sup>27</sup> Corresponds to Clause 49III of the listing agreement.

<sup>28</sup> Corresponds to Clause 49VI of the listing agreement.

<sup>29</sup> Corresponds to Clause 49V of the listing agreement.

- Other corporate governance requirements (Regulation 27)<sup>30</sup>: As per this, the listed entity may comply with other non-mandatory requirements as mentioned in Part E of Schedule II. The listed entity is required to provide the details of all material transactions with related parties along with the quarterly compliance report on corporate governance as per format specified by SEBI within fifteen days from the close of the quarter.<sup>31</sup>
- In-principle approval of recognized stock exchange(s) (Regulation 28): Listed entity before issuing the securities, should obtain in-principle approval from the recognised stock exchange(s). This requirement is not applicable for the securities issued pursuant to a court approved scheme of arrangement for which the listed entity has already obtained No Objection Letter from recognised stock exchange(s) under Regulation 37.
- Disclosure of events or information (Regulation 30)<sup>32</sup>: Listed companies are required to make disclosures of such events or information which are considered to be ‘material’ by the board of directors of the listed entity. However, the board of directors also has an authority to authorize one or more key managerial personnel for determining the materiality of an event or information. The criteria for determining the materiality of the event or information has been specified under Regulation 30(4). Listed entities are required to frame a policy for determination of materiality duly approved by the board of directors.
- Holding of specified securities and shareholding pattern (Regulation 31)<sup>33</sup>: SEBI has tried to ensure that hundred per cent of shareholding of promoter(s) and promoter group is in dematerialized form to have a proper watch on it.
- Annual Report (Regulation 34): The listed entity is required to send the Annual Report to the stock exchange(s) within twenty-one working days of its adoption by the

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<sup>30</sup> Corresponds to Clause 49X of the listing agreement.

<sup>31</sup> SEBI through Circular No. CIR/CFD/CMD/5/2015 dated 24.09.2015, has provided the formats for Compliance Report on Corporate Governance. There are three reports, Annexure – I which need to be submit on quarterly basis, Annexure – II which need to be submit at the end of the financial year (for the whole of financial year) and Annexure – III which need to be submit within six months from end of financial year i.e. along with second quarter report.

<sup>32</sup> Corresponds to Clause 36 of the listing agreement.

<sup>33</sup> Corresponds to Clause 35 of the listing agreement.

members at the Annual General Meeting. Schedule V of the Listing Regulations, 2015 describes the disclosures requirement in the Annual Report.

- Annual Information Memorandum (Regulation 35): The listed entity is required to submit to the stock exchange(s) an Annual Information Memorandum as specified by the SEBI from time to time.
- Regulation 39 (Issuance of Certificates or Receipts/Letters/Advices for securities and dealing with unclaimed securities): The listed entity shall submit the information regarding the loss of share certificate and issue of the duplicate certificates, to the stock exchange(s) within two days of its getting information. The procedural requirements for dealing with securities issued pursuant to the public issue or any other issues which remain unclaimed or are lying in the escrow account, are specified in the Schedule VI of the Listing Regulations, 2015.

### ***International Listing Cooperation***

BSE has entered into a cooperation agreement with Deutsche Borse which aims at internationalization of the listing businesses of both the exchanges, to benefit all the participants including exchanges, issuers and investors. This cooperation combines the expertise and brand recognition of each partner exchange to achieve global reach and attention. It offers worldwide visibility and investors' awareness through joint marketing initiatives and a common online portal to promote listings and data dissemination. There is also an option of cross listings opportunities. Indian issuers can meet the Europe-based local and global investors, individually or in groups, like the German Equity Forum or at international road shows hosted by Deutsche Borse.

### ***Trading on BSE***

#### *Categories of Securities and Segments for Trading*

The two broad categories of securities that are traded on BSE are:-

- i. Listed Securities: The securities of companies, which have signed the Listing Agreement with BSE, are traded as Listed Securities. Almost all securities traded in the equity segment fall in this category.

- ii. Permitted Securities: To enable market participants to trade in securities of companies, which are actively traded on other stock exchanges but are not listed on BSE, trading in such securities is facilitated as Permitted Securities, provided they meet the relevant norms specified by BSE.

Further, the securities trades on BSE have been classified into various groups, for the guidance and benefit of the investors. In the equity segment, the securities have been classified into “A”, “B”, “T” and “Z” groups on certain qualitative and quantitative parameters. The “F” Group and “T” Group represent the Fixed Income securities and securities which are settled on a trade-to-trade basis as a surveillance measure, respectively. Trading in Government Securities by the retail investors is done under the “G” group. BSE introduced the “Z” group in July 1999, which includes companies which have failed to comply with its listing requirements and/or have failed to resolve investor complaints and/or have not made the required arrangements with both the depositories, viz., CDSL and National Securities Depository Ltd. (NSDL) for dematerialization of their securities. BSE classifies equity securities of companies that are exclusively listed at BSE and satisfy certain parameters into separate sub-segments called “XC”, “XD” and “XT” from surveillance perspective, through its notice number 20160128-35 dated January 28, 2016 (annexed hereto as **Annexure 36**). Further, BSE allows market participants for on-line trading of odd-lot securities in physical form in “A”, “B”, “T”, “XC”, “XD”, “XT”, “F” and “Z” groups and in rights renunciations in all groups of securities in the equity segment. With effect from December 31, 2001, trading in all securities listed in the equity segment takes place in one market segment, viz., Compulsory Rolling Settlement System (CRS).

*Eligibility Criteria for Trading*

Some of the requirements for trading on BSE are as follows:-

<p><b>Lot Size</b></p>	<p>Securities of companies which are in demat can be traded in market lot of one while those still in the physical form are traded in the market lot of generally either fifty or hundred. Investors having quantities of securities less than the market lot are required to sell them as “Odd Lots”, so that they can consolidate their securities into market lots. This facility of selling physical shares in compulsory demat securities is called an Exit Route Scheme. This facility can also be used by small investors for selling up to 500 shares in physical form in respect of Securities of companies where trades are required to be compulsorily settled by all investors in demat mode.</p>
<p><b>Tick Size</b></p>	<p>The minimum difference in rates between two orders on the same side i.e., buy or sell, entered in the system for a particular security, is five paise. However, in order to increase the liquidity and enable the market participants to put orders at finer rates, BSE has reduced the tick size from five paise to one paisa in case of units of mutual funds, securities traded in “F” group and equity shares having closing price up to Rs. 15 on the last trading day of the calendar month.</p>
<p><b>Computation of Closing Price of Securities</b></p>	<p>It is computed on the basis of weighted average price of all trades executed during the last thirty minutes of a continuous trading session. However, if there is no trade recorded during the previous thirty minutes, then the last traded price of security in the continuous trading session is taken as the official closing price.</p>

*Trading Mechanism and Capacity*

BSE provides an efficient, anonymous, and transparent market for trading in equities, debt instruments and various derivatives products on its new generation trading platform – BOLT Plus trading system. This provides flexibility to trading members to trade on a single platform efficiently and at reduced overhead costs.

BSE uses an automated screen-based trading platform named BSE On-Line Trading System (“**BOLT**”). BOLT took its genesis in the year 1994, as part of the four-phase computerization program to create an automated trading environment. The aim was to convert the previous open outcry system of trading to an automated screen-based trading system. BSE embarked on the said project in the year 1991 and seamlessly completed the project in the year 1995 and on March 14, 1995, BSE switched to an electronic trading and order execution system.

Further, in order to provide a seamless and more transparent automated order matching system, BSE launched BOLT Plus on April 07, 2014. BOLT PLUS is based on T7, the global trading architecture of Deutsche Borse AG. BOLT Plus has a capacity of over 13,050 million orders per day. BSE is the first stock exchange in the world to introduce centralized internet trading system (BSEWEBx.co.in), allowing investors from all over the world to trade on the BSE platform. The high-speed BOLT Plus system was already the fastest trading platform in India with a response time of six micro seconds for trade executed on it. In October 2015, BSE became the fastest exchange in the world with a median response time of six micro seconds.<sup>34</sup>

Trading members can connect to BSE’s trading system using exchange-provided front-end trading terminal or API (Application Programming Interface) based trading terminal developed by exchange empaneled software vendors or developed in-house by trading member.

BSE’s trading system has nation-wide reach with a presence in several cities and towns of India whereby members can connect using any of the various types of network connectivity.

The trading members place orders anonymously on BSE’s trading system whereby order matching takes place, after order acceptance in which each order is assigned a unique order no and order time stamp. Matching of orders takes place on the basis of price-time priority of orders entered in a security/contract. Using this logic, system searches for an opposite matching order. If a match is found, a trade is generated, and a trade number and a trade timestamp is assigned to each trade. Based on ongoing order and trade activity in the system, BSE disseminates real-time market data to all trading members giving current order and trade related

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<sup>34</sup> “BSE becomes world’s fastest exchange”, October 13, 2015, available at <http://timesofindia.indiatimes.com/business/india-business/BSE-becomes-worlds-fastest-exchange/articleshow/49341850.cms>

data and statistics for each security/contract and also shares this data with various entities through the data-feed arrangement with Deutsche Bourse AG.

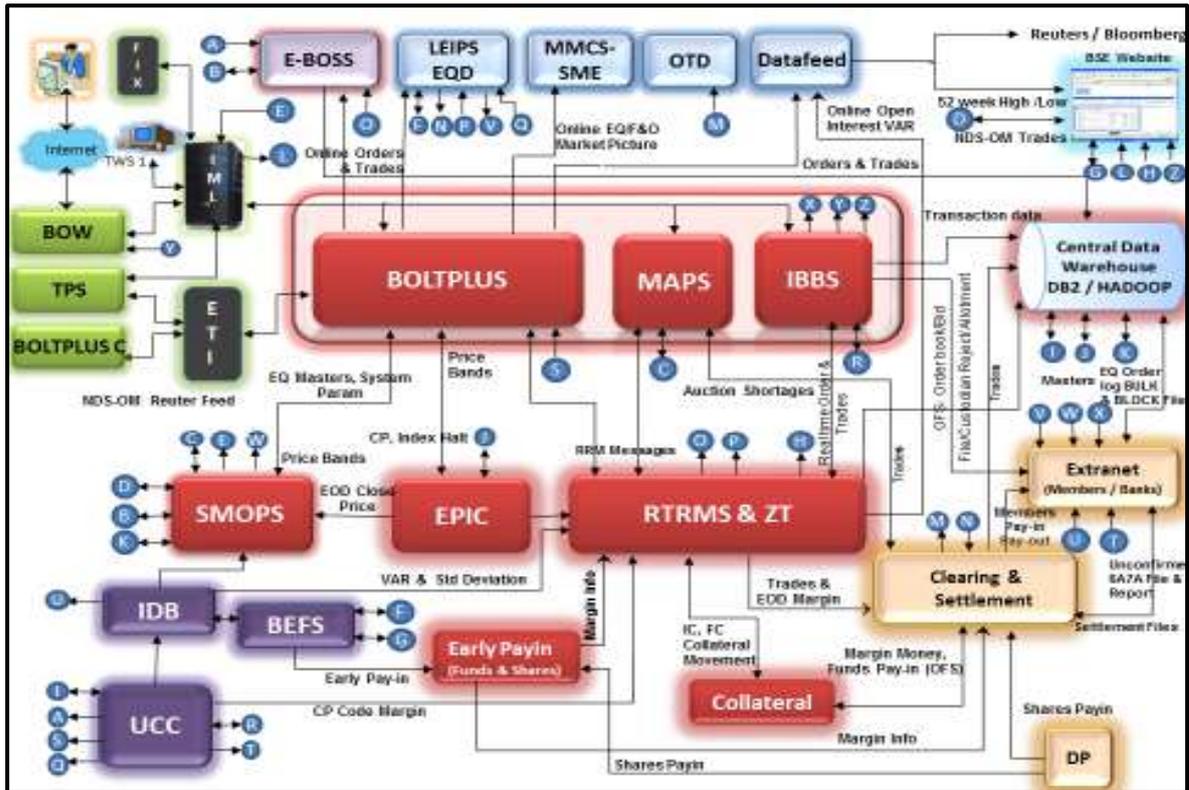
The systems and processes are designed to safeguard market integrity and enhance transparency in operations. Trading participants are assured of complete anonymity in case of matching of orders. Anonymity is maintained by ensuring that counter-party data is not part of the API and market participants, in no way, have a method to ascertain the counter-party for an order.

The trading system architecture is designed to meet scalability, robustness and maintains consistent performance even during load condition. It is further strengthened by hardware and process level fail back mechanism to achieve hardware and software fault tolerance.

High speed or algorithmic trading refers to orders on BSE that are generated using high-frequency and automated execution logic. Further, it has a through put capacity of 0.5 million orders per second. BOLT Plus is accessed by more than 900 member-brokers with more than 0.1 million branches. By extension, millions of users have been able to experience the new trading system and its improved efficiency in the execution of orders. As on April 20, 2018, there are 1,419 members registered with BSE out of which approximately 28 members are banks and as on April 20, 2018, there are approximately 3,86,34,083 registered investors on BSE.

Since the inception of BOLT Plus, the average daily volume and subsequently the market share of BSE have increased. In the first four months of 2018, the combined average daily volume in equity derivatives and currency derivatives exceeded 4.55 million (45,59,493) contracts. Since the launch of BOLT Plus, the cumulative volume of BSE's derivatives markets has surpassed the mark of 1 billion traded contracts.

New partnerships in the technology sphere have allowed BSE to quickly achieve the highest global standards for speed, reliability, order-handling capacity and risk management. The partnership has brought to BSE state-of-the art levels of capacity and latency which were already in place at the International Securities Exchange and the Eurex Exchange. The following diagram provides a description of BSE's technology architecture:-



	Source - Destination	From Source	From Destination
(A)	UCC → EBOSS	UCC Data	---
(B)	SMOPS ↔ EBOSS	Intra day and EOD price bands	---
(C)	SMOPS ↔ MAPS	Intra day and EOD price bands	EOD Close price
(D)	SMOPS ↔ BSE India	NDS OM Real time trades	52 Week High-Low
(E)	SMOPS → IML	NDS OM/Router/News/RBI reference Rate Feed	---
(F)	BEFS ↔ LEIPS-EQD	Member Data	LEIPS Payout (Daily, IO, MM, Retail, Monthly), ERP Monthly File, Service Tax Refund, Dealer Incentive Payout
(G)	BEFS ↔ BSE India	Member Data	---
(H)	RTRMS → BSE India	OI	---
(I)	UCC → DWH	MASTERS	---
(J)	EPIC → DWH	MASTERS; Trades	---
(K)	SMOPS → DWH	MASTERS	---
(L)	IML → BSE India	Stock Price, Feeds	---
(M)	CLASS → OTD	Trades data	---
(N)	CLASS → LEIPS-EQD	Settlement Position	---
(O)	RTRMS → EBOSS	OI	---
(P)	RTRMS → LEIPS-EQD	Member Position	---
(Q)	UCC → LEIPS	UCC Info	---
(R)	UCC ↔ IBBS	WB File(Output Debarrd client)	Real Time UCC Data Through Replication

	Source	Destination	From Source	From Destination
(S)	UCC	BOLTPLUS	WB File(Output Debarred client)	---
(T)	UCC	Extranet	List of clients debarred by SEBI	---
(U)	IDB	Extranet	Corporate Action File, ND file, XD Files, Settlement Calendar Files, VAR files(1...5), EOD VAR Files, Unregistered Location File(EQ/EQD/CDX)	---
(V)	LEIPS	Extranet	Prov. Unreg. Location ID file 1,2,3,4 for Equity	---
(W)	SMOPS	Extranet	Scrp Master file	---
(X)	IBBS	Extranet	OPPS (Order Book, Bid File, Custodian Rejection, Allotment File)	---
(Y)	IBBS	BOW	Real Time Data Communication	---
(Z)	IBBS	Bseindia	Real Time Bid Details of all segments	---

APPLICATION NAME	DETAILS	APPLICATION NAME	DETAILS
BOLTPLUS	Trading engine for Equity, Equity Derivatives & Currency	TPS	Third Party Trading Platform
MAPS	Trading engine for SLB & debt instruments	SMOPS	Market Operations
IBBS	IPO & Book Building Engine	DB2/HADOOP	Central Data Warehouse
RTRMS	Risk Management System	IDB	Reference Master Database
RTRMS-ZT	Members Admin Control for managing Trader's Risk	BEFS	Compliance Reporting System For Members
EPIC	Price & Index Computation System	UCC	Unique Client Code Registration System
EBOSS	Surveillance Monitoring System	COLLATERAL	Collateral Management System
LEIPS	Incentive Calculation System	EPN	Early Payin System
DATAFEED	Online Trade Feed System	CLASS	Clearing & Settlement System
BOW	Exchange Web-Based Trading Platform	BSEINDIA	Exchange Official Website
BOLTPLUS C	Exchange Online Trading Platform Client		

*Trading Sessions*

BSE’s normal trading sessions are on all days of the week except Saturday, Sundays and holidays declared by BSE in advance. Trading on the BOLT System is conducted from Monday to Friday between 9:15 A.M. and 3:30 P.M. normally. The following table indicates the hours of operation of BSE (in terms of Indian Standard Time):-

Session	Timing
Pre-open Trading Session	09:00 – 09:15
Trading Session	09:15 – 15:30

Position Transfer Session	15:40 – 16:00
Closing Session	15:40 – 16:00
Option Exercise Session	17:07

### Trading Halts

Based on SEBI’s circular dated June 28, 2001,<sup>35</sup> (annexed hereto as **Annexure 37**). BSE implemented index-based market-wide circuit breakers with effect from July 02, 2001. SEBI through its circular dated September 03, 2013,<sup>36</sup> (annexed hereto as **Annexure 38**) partially modified the provisions of the aforementioned circular and introduced daily calculation of circuit breaker limits for 10%, 15% and 20% based on the previous day’s closing level of the index. Additionally, a fifteen minutes pre-opening session post each trading halt has been introduced.

Based on the said circular, BSE on a daily basis disseminates the 10%, 15% and 20% circuit breaker limits on the closing value of S&P BSE SENSEX for the next trading day. The index-based market-wide circuit breaker system applies at three stages of the index movement, either way viz. at 10%, 15% and 20%. These circuit breakers when triggered bring about a coordinated trading halt in all equity and equity derivative markets nationwide. The market-wide circuit breakers are triggered by movement of either the S&P BSE SENSEX or the NSE CNX Nifty, whichever is breached earlier.

The trigger limits and the respective halt duration are given below:-

Trigger Limit	Trigger Time	Halt duration	Pre Opening Session duration post each halt
10%	Before 1 P.M.	45 minutes	15 minutes
	At or After 1 P.M. to 2.30 P.M.	15 minutes	15 minutes

<sup>35</sup> Circular bearing reference number SMDRPD/Policy/Cir-37/2001, on Index Based Market Wide Circuit Breaker in Compulsory Rolling Statement dated June 28, 2001, available at <http://www.sebi.gov.in/sebiweb/home/list/1/7/0/0/Circulars>

<sup>36</sup> Circular bearing reference number CIR/MRD/DP/25/2013, on Index Based Market-Wide Circuit Breaker Mechanism, dated September 03, 2013, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1378198702862.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1378198702862.pdf)

	At or after 2.30 P.M.	No Halt	-
15%	Before 1 P.M.	1 hour 45 minutes	15 minutes
	At or after 1 P.M. before 2 P.M.	45 minutes	15 minutes
	On or after 2 P.M.	Trading halt for the remainder of the day	-
20%	Any time of the day	Trading halt for the remainder of the day	-

Further, there are individual security circuit filters. Circuit filter of 20% is applicable on all securities except the securities on which derivative products are available (being the most liquid) and are part of indices on which derivative products are available. However, BSE imposes dummy circuit filter on these securities to avoid freak trades due to punching errors.

The following trading disruptions have happened on BSE. On April 07, 2014, i.e., the first day of the new trading system, market information broadcast stopped during the call auction session, and therefore there was trading disruption. Necessary measures were taken immediately which resulted into resumption of trading within five minutes. On April 9, 2014, i.e., second day of the new trading system, matching could not take place in call auction module of the software, and hence there was trading disruption on the second day of new trading system. On June 11, 2014, the peripheral system, designed for computation of indices was not functioning properly and hence dissemination of indices was delayed and there was a trading disruption. On July 03, 2014, on account of the outage in the network, the primary connections were less than 2,000 as against normal day primary connections of over 8,000 connections and new connections were not being established, resulting in a trading halt. In all the aforesaid incidents, BSE took requisite steps for immediate resumption of trading and has further enhanced and strengthened the policy and process to avoid such inadvertent incidents.

*Trade Annulment*

SEBI issued a circular dated July 16, 2015 prescribing a policy for annulment of trades undertaken on stock exchanges<sup>37</sup> (annexed hereto as **Annexure 39**). As per the circular, stock exchanges can consider annulment of trades on their own or on a member broker's request. The circular requires a member broker to submit the request to the exchange within thirty minutes of the execution of the particular trade and the exchange is under an obligation to inform the details of the said request to all its member brokers in a time bound manner. As per the said policy, stock exchange are required to consider the potential effect of such annulment on the trades of other member brokers and the investors across all segments and decide upon the request before the start of next trading day. The policy provides an alternate mechanism whereby exchanges can reset the price of the trade, if price reset is less disruptive than annulment of the trade. The exchange needs to convey its reasoned decision to all counter parties. Further, the said circular allows exchanges to annul trades resulting from wilful misrepresentation, manipulation or fraud, as provided in their extant bye laws.

Based on the aforesaid circular, BSE has adopted a trade annulment policy (annexed hereto as **Annexure 40**).<sup>38</sup> According to the policy, the value of trade(s) for which annulment is requested should be at least Rs. 2 million (*where a trade refers to a single transaction of Rs. 2 million and above or series of transactions emanating out of a single order with aggregate value of Rs. 2 million and above*). Further, the policy states that trade annulment requests accepted based on the transaction value, should be accepted for further processing and examination with respect to the following conditions for further decision. Any request which does not qualify the below mentioned conditions should be rejected. In case, where the trade annulment request qualifies in terms of the conditions mentioned below, BSE should undertake price reset for such trade in question:-

- a. Minimum twenty trades in the security excluding the trades in question; and

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<sup>37</sup> Circular bearing reference number CIR/MRD/DP/15/2015, dated July 16, 2015, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1437033678905.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1437033678905.pdf)

<sup>38</sup> Trade Annulment Policy for Equity Segment of BSE, available at <http://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20150814-26>  
Trade Annulment Policy for Derivatives Segment of BSE, available at <http://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20150814-27>;  
Trade Annulment Policy for Currency Derivatives Segment of BSE, available at <http://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20150814-28>

- b. Future Contracts - variation of the trade(s) being requested for annulment vis-a-vis its immediate preceding trade is at least equivalent to the applicable price band of the respective future contract. In case of option contracts, variation of the trade(s) being requested for annulment vis-a-vis its immediate preceding trade is at least equivalent to “X%” of difference between the upper and lower price band value of the respective option contract; and
- c. Counterparty/ies agrees for price reset. For cases where a trade annulment request relates to multiple trades arising out of single orders with multiple counterparties, only those trades where the counterparty agrees for trade annulment/ price reset should be considered for the price reset. The counterparty/ies shall confirm the acceptance or rejection in writing to BSE within thirty minutes from the intimation with reasons thereof. No confirmation within the stipulated time is considered as rejection by the counterparty/ies.

BSE is required to expeditiously, not later than start of next trading day, examine and decide upon such requests. While examining such requests, BSE is required to consider the potential effect of such annulment on trades across the market. As per the said policy, BSE should undertake annulment or price reset only in exceptional cases in the interest of the investors, market integrity, and maintaining sanctity of price discovery mechanism.

### *Margins*

- Kinds of margin

In order to contain the risk arising out of transactions entered into by members in various securities either on their own account or on behalf of their clients, BSE has a well-designed risk-management system which *inter-alia*, includes collection of base minimum capital (“**BMC**”, described in detail later), additional capital, etc. In addition to the aforesaid deposits, members who are clearing members of ICCL are required to deposit margins for clearing and settlement of trades. Various kinds of margins are imposed on the members based on their outstanding positions in the market.

The following table indicates the margining system:-

Kind of Margin	Description	Collection and Release	Dissemination of Information
<b>Value at Risk (VaR) Margin</b>	As mandated by SEBI, the VaR margining system, which is internationally accepted as the best margining system, is applicable on the outstanding positions of the members in all securities. The margin seeks to cover the largest loss that can be encountered on 99 per cent of the days (99 per cent VaR). For liquid stocks, the margin covers one-day losses while for illiquid stocks, it covers three-day losses so as to allow BSE to liquidate the position over three days. For liquid stocks, the VaR margins are based only on the volatility of the stock while for other stocks, the volatility of the market index is also used in the computation.	It is collected on an upfront basis by adjusting against the total liquid assets of the member at the time of trade. It is collected on the gross open position of a member, which is the gross of all net positions across all the clients of the member including his proprietary position. There would be no netting of positions across different settlements for this purpose.	The VaR amount applicable in respect of the securities is disseminated on the BSE website on a daily basis.
<b>Extreme Loss Margin</b>	It covers the expected loss in situations that go beyond those envisaged in the 99 per cent VaR estimates used in the VaR margin. The ELM for any stock is higher of 5	It is collected/ adjusted against the total liquid assets of the member on a real time basis and on the gross open position of the member. For this	The ELM amount applicable in respect of securities is disseminated on the BSE website.

	per cent, and 1.5 times the standard deviation of daily logarithmic returns of the stock price in the last 6 months. This computation is done at the end of each month by taking the price data on a rolling basis for the past 6 months and the resulting value is applicable for the next month.	purpose, there is no netting of positions across different settlements. The ELM so collected is released along with the pay-in.	
<b>Special Margin</b>	It may be imposed by BSE from time to time on certain securities as a surveillance measure and informed to the members through notices.	This is collected along with MTM from the members, first, by adjusting the same from the available liquid assets and the balance Special Margin in form of cash from the members through their clearing banks on the same day.	-
<b>Mark-to-Market Margin (MTM)</b>	The MTM is computed after trading hours on T day on the basis of closing price, of that day. In case the security has not been traded on a particular day, the latest available closing price is considered as the closing price. MTM margins is also recomputed in respect of all the pending	Such MTM is collected from the members in the evening on the T day itself, first by adjusting the same from the available cash and cash equivalent component of the liquid assets and the balance MTM in form of cash from the members	<sup>39</sup>

<sup>39</sup> On account of the methodology adopted for computation of the MTM, no fixed amount can be ascertained.

	<p>settlements on the basis of closing prices of T day and the difference due to increase/decrease in MTM margins on account of such re-computation is adjusted in the MTM obligation of the member for the day.</p>	<p>through their clearing banks on the same day. The MTM margin is collected on the gross open position of the member. The gross open position for this purpose would mean the gross of all net positions across all the clients of a member including his proprietary position. For this purpose, the position of a client is netted across his various securities and the positions of all the clients of a member are grossed. Further, there is no netting across two different settlements. There is no netting off the positions and setoff against MTM profits across two rolling settlements i.e. T day and T-1 day. However, for computation of MTM profits/losses for the day, netting or setoff against MTM profits is permitted.</p>	
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For securities that have been listed for less than six months, the trading frequency and the impact cost is computed using the entire trading history of the securities. All statements

pertaining to daily margins viz., VaR, MTM, ELM and Special Margin on the outstanding positions of the members are available for downloading by them in their back-offices at the end of the day. The above-referred margins are released on completion of pay-in of the settlement.

Cases where there are insufficient balances in bank accounts of the members at the time of debit of margin amounts payable in cash on the relevant day, are treated as margin defaults. In case of non-fulfillment of Base Minimum Capital, the trading facilities is deactivated. In case of non-fulfillment of margin obligations to ICCL, such members are restrained from undertaking fresh business and they can undertake fresh business after fulfillment of the margin obligation.

- Exemptions from payment of Margins

The following trades executed in equity and debt securities on the BOLT are exempted from payment of margins on Trade Day. However, the same are margined to the custodians/members on T+1 day in case of acceptance/ rejection of the 6A/7A entry.<sup>40</sup>

- Institutional business. For this purpose, institutional investors include:
  - Foreign Institutional Investors registered with SEBI
  - Mutual funds registered with SEBI
  - Public Financial Institutions as defined under Section 4A of the Companies Act, 1956
  - Banks, i.e., a banking company as defined under Section 5(1)(c) of the Banking Regulations Act, 1949
  - Insurance companies registered with the Insurance Regulatory and Development Authority of India

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<sup>40</sup> 6A/7A entry is a mechanism whereby the obligations of settling the transactions executed by a member-broker on behalf of a client is passed on to a registered custodian based on confirmation of the latter. If a custodian takes up the delivery/payment in respect of a transaction done by a member-broker, he has to confirm the trade done by the member-broker on the BOLT System through 6A-7A entry. For this purpose, custodians have been given access to the BOLT System and have also been admitted as clearing members in the clearing house.

➤ Pension Funds

- In cases where early pay-in of securities is made, the outstanding position of the client to the extent of early pay-in.

The early pay-in of securities done upto 3.45 p.m. on a day are considered for on-line release of blocked liquid assets on account of margins on that day. The benefits of early pay-in done after 3.45 p.m. on a day are available on the next trading day. Members are also able to do early pay-in of securities before execution of the trade on T day to avail benefit of margin exemption.

*Trading Volumes and Figures*

BSE operates through various segments which, *inter-alia*, include the equity cash segment, equity derivatives segment, currency derivatives segment, interest rate derivatives segment, debt market segment, and provides a platform for buying and selling units of mutual funds. The turnover of these segments as on March 31, 2018 (FY 2017-18) is as follows:-

Sr. No.	Segment	Turnover [Rs. in billion]
1.	Cash Segment	10829.68
2.	Derivatives Segment	32.62
3.	Currency Derivatives	46603.11
4.	Debt Market	5635.25
5.	Mutual Funds	150.83

The S&P BSE SENSEX is India’s most widely tracked stock market benchmark index and is traded internationally on the EUREX as well as on other leading exchanges of the BRCS nations (Brazil, Russia, China and South Africa). More than 5400 companies are listed on BSE making it the world’s number one exchange in terms of listed companies. The companies listed on BSE command a total market capitalization of Rs.149.92 trillion as on April 18, 2018. BSE is also one of the world’s leading exchanges (5th largest in March 2015) for index options

trading.<sup>41</sup> As India’s biggest bourse in terms of listed companies and market capitalisation, almost every leading corporate in India has sourced the services of BSE in raising capital and is listed with BSE. The following table indicates the volume of shares traded on BSE in the year 2017-18.

<b>Quantity of Contracts/Shares Traded (Millions) in Financial Year 2017 18</b>	
<i>Equity Derivatives</i>	
Stock Index Futures	0.0441
Stock Index Options	0.0001
Stock Futures	0.0004
Stock Options	0.0000
<i>Currency Derivatives</i>	
Currency Futures	307.66
Currency Options	382.58
<i>Interest Rate Derivatives</i>	
Futures	11.35
<i>Equity</i>	
Equity Shares	77160.33

<sup>41</sup> Source – World Federation of Exchanges.

The following table indicates the trading highlights as on April 17, 2018:-

	Traded	Rolling (Groups)																
		A	B	E	IF	IT	P	SS	ST	T	W	X	XT	Z	ZP	F/FC	G/GC	M/MT
No. of Securities	2,965	393	1,083	12	1	-	8	5	3	143	-	705	361	31	-	141	9	64
No. of Trades	11,30,540	6,46,749	4,06,182	843	2	-	24	46	5	10672	-	54961	8673	964	-	934	61	424
Total No. of Shares (Cr.)	25.44	13.44	6.17	0.07	-	-	-	-	-	2.62	-	1.84	0.55	0.11	-	0.38	0.02	0.21
Total Turnover (Rs, Cr.)	3,531.45	2,609.21	692.50	69.83	0.09	-	-	0.01	0.01	13.75	-	93.65	15.10	0.66	-	23.27	2.04	11.29
% of Total Turnover	-	73.88	19.61	1.98	-	-	-	-	-	0.39	-	2.65	0.43	0.02	-	0.66	0.06	0.32
Average Daily Turnover (Rs. Cr.)	3,490.48	2,552.61	739.95	41.61	2.32	-	17.06	0.07	0.21	13.95	-	94.79	12.64	0.65	-	13.37	1.22	17.06

### ***Integrity of Systems and Safety of Markets***

A major objective of BSE is to promote and inculcate honourable and just practices of trade in securities transactions and discourage malpractices. BSE systems and processes are designed to safeguard market integrity, drive the growth of the Indian capital market and stimulate innovation and competition across all market segments. BSE was the first exchange in India and second in the world to obtain an ISO 9001:2000 Certification for its surveillance function. Further, BSE was the first exchange in the country and second in the world to receive Information Security Management System Standard BS 7799-2-2002 Certification for its on-line trading system i.e. BOLT. BSE monitors equity, equity derivatives, indices derivatives contracts, currency derivatives and interest rate futures. The main objective of the surveillance function is to promote market integrity,

- i. by monitoring price and volume movements (volatility) and detecting potential market abuses (fictitious/ artificial transactions, circular trading, false or misleading impressions, insider trading, etc.) at a nascent stage, with a view to minimizing the ability of the market participants to influence the price of any security in the absence of any meaningful information.

### ***Surveillance Department of BSE***

BSE has a dedicated Surveillance Department to keep a close and daily watch on the price movement of securities, detect market manipulations like price rigging, etc. The Surveillance Department is headed by a Senior General Manager. The head of the Surveillance Department at BSE receives various surveillance and market trend/ monitoring reports, which are then shared with the senior management of BSE. Further, case specific reports are also shared with the regulator either *suo-motu* or on its request. The surveillance and market monitoring at BSE is conducted real-time on a daily basis. The surveillance function at BSE is bifurcated as Online Surveillance and Offline Surveillance.

- Online Surveillance

Online Surveillance carries out price and position monitoring. Price monitoring is mainly related to price movement/ abnormal fluctuation in the prices or volumes of any security, and is conducted to detect potential market abuses at a nascent stage to reduce the ability of market

participants to unduly influence the price of securities traded at BSE. In relation to price monitoring, Surveillance may take the following actions:-

- a. Reduction of Circuit Filters: The circuit filters are reduced in case of illiquid securities or as a price containment measure. The circuit filters are reduced to 10% or 5% or 2% as the case may be, based on the criteria decided by Surveillance. No circuit filters are applicable on securities on which derivative products are available securities. However, BSE imposes 10% dynamic circuit filter on these securities to avoid punching errors, if any. The circuit filter of 20% is applicable on other securities which are not included in the above-mentioned category.
- b. Transferring Securities on a Trade-to-Trade Basis: As a part of the surveillance measure, Surveillance may transfer various securities for trading and settlement to the trade-trade category, i.e., selling/ buying of shares in that security results into giving/ taking delivery of shares at the gross level and no intra-day netting off/ squaring off facility is permitted. The said action is reviewed at periodic intervals.
- c. Rumour Verification: Surveillance liaises with the compliance officers of the listed companies to obtain their comments on various price-sensitive corporate news items appearing in the media. The comments received from the companies are disseminated to the market by way of BSE's Online Trading System's ticker and/or through the notices on the BSE website. If the company denies the news/ information, a letter is sent to the company asking them to take up the matter with the concerned media.
- d. Imposition of Periodic Price Band: With an objective to restrict excessive price movement in the securities of listed companies, SEBI had introduced daily price bands upto 20% on the securities not having derivatives products. Surveillance as surveillance measure, reduces these price bands from 20% to 10%, 10% to 5% and 5% to 2% based on the pre-decided joint criteria. Further, in order to enhance the market integrity and prevent excessive price movement in the securities listed on its trading platform, BSE as a pre-emptive surveillance measure has an additional framework of periodic price

bands apart from the aforesaid daily price band framework. These additional periodic price bands are applicable to securities exclusively listed and traded on BSE equity trading platform, including securities listed on SME platform and SME Institutional Trading platform. The periodicity of these price band are weekly, monthly, quarterly and yearly.

- e. Market-wide Circuit Breakers: In order to contain huge price movements of index securities, SEBI has mandated that Market Wide Circuit Breakers at 10%, 15% and 20% of the movements in the index. The intention of the circuit break is to provide a cooling period to the market participants and to assimilate and react to the market movements. At present Market-wide Circuit Breakers are calculated on a daily basis by BSE. Resumption of Trading happens after the halt opens with a pre-open call auction session.

Position monitoring requires Surveillance to closely monitor the position of trading members in Derivatives Segments vis-à-vis permissible limits. For this purpose, it has developed various market monitoring reports. The reports are scrutinized to ascertain whether there is excessive purchase or sale position build up compared to the normal business of the member or if the applicable limits have been breached.

- Offline Surveillance

The offline surveillance cell conducts the following types of analysis of suspected market irregularities in a systematic and logical manner and takes appropriate and timely actions.

- a. Snap Investigations: Potential cases of market irregularities are taken up for further analysis. A preliminary analysis of the trading pattern and corporate developments in the security is done to ascertain whether the price or volume variation observed requires further detailed analysis.
- b. Preliminary Analysis: It is a more detailed form of preliminary analysis as compared to snap investigation and report is prepared based on the available trading data and various other information available in the public domain. These analyses are conducted usually on receiving a reference from SEBI or any other department of BSE or are based on an investor complaint.

- c. Investigation: These are detailed investigations wherein complete analysis is conducted in a systematic and logical manner based on the information available with BSE and information sought/ received from members, companies, depositories and various other sources. These investigations are conducted to ascertain manipulation, if any, that was suspected in the preliminary analysis.

#### *Surveillance Mechanism*

BSE has an On-line Real Time (OLRT) Surveillance System, which has been in operation since July 15, 1999. Under this system, alerts are generated on-line, in real time during the trading hours, based on certain preset parameters like the price and volume variation in securities, a member taking unduly large positions not commensurate with its financial position or having concentrated positions in one or more securities. This system integrates several databases like company profiles, members' profiles and historical data of turnover and price movement in securities, members' turnovers, their pay-in obligations, etc.

The securities which reach new high or new low and companies which have high trading volumes are watched closely and special emphasis is laid on the newly listed securities. In case certain abnormalities are noticed, the circuit filters are reduced to make it difficult for the price manipulators to increase or push down the prices of a security within a short period of time. BSE imposes special margins in securities where it suspects an attempt to ramp up the prices by creating artificial volumes. As stated above, BSE may also transfer the securities for trading and settlement to the trade-to-trade category. If abnormal movements continue despite the aforesaid measures, BSE suspends trading in the security. Detailed investigations are conducted in cases where price manipulation is suspected and disciplinary action is taken against the concerned members.

#### *Disciplinary action by BSE*

The disciplinary powers of BSE have been provided in the BSE Rules, Bye-laws and Regulations for the cash segment and derivatives segments. These powers are exercised by the Disciplinary Action Committee as constituted by the Board of Directors of BSE from time to time. The composition of the Disciplinary Action Committee of BSE is in compliance with the requirements prescribed by SEBI. The Disciplinary Action Committee consists of public

interest directors (who form a majority). The Managing Director and Chief Executive Officer of BSE is also a member of the Disciplinary Action Committee.

### **Good Conduct and Corporate Governance**

Regulation 35 of the SECC Regulations states that the disclosure requirements and corporate governance norms as specified for listed companies shall *mutatis mutandis* apply to a recognized stock exchange. Therefore, to assist the Board of Directors of BSE in the discharge of its oversight function and for the compliance of corporate governance norms, various Board committees, namely the Audit Committee, Nomination and Remuneration/ Compensation Committee, Stakeholder Relationship/ Share Allotment Committee, Independent Director/ Public Interest Directors Committee and Corporate Social Responsibility Committee have been constituted with terms of reference.

The most fundamental requirement of good corporate governance is an effective and robust board of directors. To foster such a board of directors and to ensure that the public interest directors are well informed of BSE's business and governance practices, BSE conducts a comprehensive orientation programme which is presented by the Executive Management Committee. During every Board meeting, every Executive Management Committee member makes a presentation to the Board of Directors with respect to all new developments that have taken place since the last Board meeting. Some of the areas covered therein are technological initiatives, business, regulatory overview including changes in regulatory framework and finance and accounts. Many of the public interest directors of BSE are also part of one or more of the committees prescribed by SEBI under the SECC Regulations, corporate governance norms or under the Companies Act, 2013. The members of the said committees are also provided with a detailed functioning of the related area of operation that is governed by the respective committee.

Further, Corporate Social Responsibility (CSR) in BSE is aligned with its tradition of creating wealth in the community with a three pronged focus on education, health and the environment.

## **II. ATTRIBUTES LISTED IN RULE 902(B)**

Rule 902(b)(2) identifies seven attributes that will be considered by the SEC in determining whether to designate a non-U.S. securities market as a DOSM. When adopting Regulation S, the SEC stated that the attributes set forth in Rule 902(b)(2) were not the exclusive factors

considered by the SEC in designating foreign markets. The SEC further stated that no single attribute is required and that designations were to be made through the interpretive letter process, based upon consideration of all the facts pertaining to a particular market.<sup>42</sup> The general information provided above serves to broadly define the facts needed for analyzing the factors that are specified under Rule 902(b)(2).

Specifically, BSE seeks a determination as a non-U.S. securities exchange or market designated by the SEC based upon its consideration of, among other things, the attributes specified in Rule 902(b)(2). As discussed below, BSE has the attributes listed in Rule 902(b)(2) of Regulation S.

#### *A. Organization Under Foreign Law*

This section discusses how BSE came into existence and the provisions in accordance with which BSE was granted recognition as a stock exchange in India. It further discusses the manner in which, BSE became a corporatized entity and the provisions governing its operation as a recognized stock exchange.

#### **Establishment and Recognition of BSE as a stock exchange**

BSE was initially established in 1875 as the “Native Share & Brokers’ Association”. In order to obtain the license as a recognized stock exchange, BSE had to meet the criteria prescribed by law. Section 3 of the SCRA states that any stock exchange, which is desirous of being recognised for the purposes of the SCRA, may make an application to the Central Government. The said application has to be accompanied by a copy of the bye-laws of the stock exchange for regulation and control of contracts and a copy of rules relating to the general constitution of the stock exchange, particularly relating to the governing body, constitution and powers of management, manner in which the business is transacted, admission into stock exchange, qualification of membership, expulsion, suspension and re-admission of members etc.

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<sup>42</sup> See SEC Release No. 33-6863 (April 24, 1990).

Section 4 of the SCRA deals with the grant of recognition to stock exchange. It states that if the Central Government is satisfied, after making an inquiry and after obtaining information, if any, as it may require:-

- a. that the rules and bye-laws of a stock exchange applying for registration are in conformity with such conditions as may be prescribed with a view to ensure fair dealing and to protect investors;
- b. that the stock exchange is willing to comply with any other conditions (including conditions as to the number of members) which the Central Government, after consultation with the governing body of the stock exchange and having regard to the area served by the stock exchange and its standing and the nature of the securities dealt with by it, may impose for the purpose of carrying out the objects of SCRA; and
- c. that it would be in the interest of the trade and also in the public interest to grant recognition to the stock exchange;

the Central Government may grant recognition to the stock exchange and may impose certain conditions. The conditions may include, *inter alia*, conditions relating to:-

- i. the qualifications for membership of stock exchanges;
- ii. the manner in which contracts shall be entered into and enforced as between members;
- iii. the representation of the Central Government on each of the stock exchange by such number of persons not exceeding three as the Central Government may nominate in this behalf; and
- iv. the maintenance of accounts of members and their audit by chartered accountants whenever such audit is required by the Central Government.

The Central Government after considering the application for recognition made under Section 3 of the SCRA by BSE, and on being satisfied that it would be in the interest of the trade and also in public interest, granted permanent recognition to BSE under Section 4 of the SCRA on

August 31, 1957. The Central Government apart from granting recognition imposed certain conditions on BSE. BSE has complied with those conditions within the specified time period.

Section 4(3) of the SCRA requires the publication of the grant of recognition to a stock exchange in the Gazette of India and also in the Official Gazette of the State in which the principal office of the stock exchange is situated. It further states that the recognition shall have effect as from the date of its publication in the Official Gazette. The grant of recognition to BSE was published in the Gazette of India. A copy of the publication is annexed hereto as **Annexure 5**.

### **Corporatisation and Demutualisation of BSE**

BSE was initially a mutualized entity which was set up as an association of persons. However, pursuant to the amendments to the provisions under the SCRA in the year 2004, every stock exchange in India was required to be a demutualized and a corporate entity. The amended provisions under the SCRA required every recognised stock exchange to submit a scheme for corporatisation and demutualisation to SEBI for its approval. Accordingly, BSE on March 09, 2005 submitted its corporatisation and demutualisation scheme, i.e., BSE (Corporatisation and Demutualisation) Scheme, 2005, to SEBI for its approval. After deliberating upon the said scheme, SEBI gave its approval on May 20, 2005. A copy of the scheme is annexed hereto as **Annexure 8**.

Further, pursuant to the said scheme, BSE was incorporated as a public limited company under the provisions of the Companies Act, 1956 on August 08, 2005. The Corporate Identity Number of BSE Limited is U67120MH2005PLC155188. BSE Limited filed its duly verified documents with the Registrar of Companies in Mumbai, Maharashtra, India. In 2007, BSE became a demutualised entity. Presently, BSE is a demutualized and a corporate entity which has a broad shareholder base. BSE completed its IPO and got listed on February 3, 2017. The shareholding pattern of BSE as on March 31, 2018 is annexed hereto as **Annexure 41**. The ownership, trading rights and management are segregated as a matter of law and also under the BSE (Corporatisation and Demutualisation) Scheme, 2005.

### **Deemed Recognition under, and Compliance with SECC Regulations**

Regulation 3 of the SECC Regulations, which was enacted in 2012 to regulate recognition, ownership and governance in stock exchanges and clearing corporations, states that stock

exchanges which have been granted recognition under SCRA as on the date of commencement of the SECC Regulations shall be deemed to have been recognised under the SECC Regulations and all the provisions of the SECC Regulations as they apply to a recognized stock exchange shall apply to such exchange. According to the provisions under the SECC Regulations, no person in India can conduct, organise or assist in organising any stock exchange unless he has obtained recognition from SEBI in accordance with the provisions under the SCRA, SCRR and SECC Regulations.

According to Regulation 7 of the SECC Regulations, which deals with the consideration of grant of recognition, an applicant, *inter alia*:- has to be a company limited by shares and demutualized, the applicant, its directors and its shareholders who hold or intend to hold shares, are fit and proper persons, applicant satisfies requirements relating to ownership and governance structure, net-worth specified in these regulations, applicant has to have an online screen-based trading system and the necessary infrastructure for orderly execution of trades, the applicant has to have an online surveillance capability which monitors positions, prices and volumes in real time so as to ensure market integrity and so on.

Regulation 7 of the SECC Regulations states that SEBI may, on being satisfied with the capability of the applicant to comply with the conditions, grant an in-principle approval to the applicant which shall be valid for a period of one year: Further, Regulation 8 of the SECC Regulations states that SEBI may, before granting recognition to a stock exchange, make inquiries and require such further information or document to be furnished, as it may deem necessary. Regulation 9 of the SECC Regulations states that the SEBI may, after considering the application and on being satisfied that the applicant has complied with the conditions laid down in Regulation 7 and is eligible to act as a recognised stock exchange, grant recognition to the applicant in terms of Section 4 of the SCRA, in the interest of the securities market.

BSE's functioning and scope of activities is governed by the provisions of the Companies Act, 2013 and Companies Act, 1956 (wherever applicable), the SEBI Act, the SCRA and the rules and regulations made thereunder. BSE's articles of incorporation, Rules, Bye-laws and Regulations govern its constitution and working.

***B. Association with a Generally Recognized Community of Brokers, Dealers, Banks or Other Professional Intermediaries with an Established Operating History***

This section discusses the kinds of membership in BSE and the scope of activities and responsibilities for each category of membership. The requirements for becoming a member-educational qualifications, financial criteria etc. under SEBI Rules and Regulations and BSE Rules, Bye-laws and Regulations have been discussed. The section also throws light on the procedure adopted by BSE to select its members and the manner in which BSE seeks to ensure compliance with the various requirements for membership. Further, the manner in which member-brokers are regulated has been dealt with. In this context, the obligations on member brokers (who are registered intermediaries) under the SEBI (Intermediaries) Regulations, 2008 (“**Intermediaries Regulations**”) and various provisions of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992 (“**Brokers Regulations**”) have been highlighted. [The Intermediaries Regulations and the Brokers Regulations are annexed hereto as **Annexure 42** and **Annexure 43** respectively.]

The norms on dealing with clients’ funds and maintaining of records by brokers have been discussed in detail. The mechanism for inspection of brokers by SEBI as provided under the Brokers Regulations has been discussed, along with the inspection and monitoring undertaken by BSE. Further, this part also indicates the action SEBI is empowered to undertake in case of default by any member-broker. Audit, as done by the members and by BSE has been discussed. Furthermore, this section discusses the revocation and renewal of membership by BSE and also the risk management system maintained by BSE in relation to its members. The section also throws light on the dispute resolution mechanism resorted to in case of disputes between members of BSE and between members and clients.

**Kinds of Membership and Scope of Activities**

In India, there are two types of members i.e., Trading Member (Stock broker and Member of the exchange) and Clearing Member (member of the clearing corporation).

Regulation 2(1)(gb) of the Brokers Regulations defines ‘stock broker’ as a person having trading rights in any recognized stock exchange and includes a Trading Member. On account of historical perspective, the term “Stock Broker” is used in context of an entity who has become a member of equity segment while the term “Trading Member” is used in context of an entity who has become a member of derivatives segment. However, at present, the two terms

are synonymous and are used interchangeably unless the context suggests otherwise. Regulation 2(1)(ae) of the Brokers Regulations defines ‘clearing member’ to mean a person having clearing and settlement rights in any recognized clearing corporation and includes any person having clearing and settlement rights on a commodities derivatives exchange. Both BSE and its clearing corporation ICCL<sup>43</sup>, respectively, offer trading and clearing memberships for various segments. Further, Clearing Member can be of various types such as Professional Clearing Member (“**PCM**”), Trading cum Clearing Member (“**TCM**”) and Self-Clearing Member (“**SCM**”).

A Trading Member is a person who has only trading rights in BSE. This category of membership allows the members to execute trades on his own account and on the account of its clients, however clearing and settlement of trades executed by the Trading Member would have to be done through a Clearing Member or a Trading cum Clearing Member (“**TCM**”) or a Professional Clearing Member (“**PCM**”). A Clearing Member is a person having clearing and settlement rights in ICCL. A TCM is person who has trading rights in BSE and clearing and settlement rights in ICCL. A TCM membership allows a member to execute trades and to clear and settle the trades executed on his own account as well as on the accounts of its client and to clear and settle trades executed by other Trading Members who choose to use his clearing services. A PCM membership allows a member to clear and settle trades of such members of BSE who choose to clear and settle their trades through this member. A Self-Clearing Member (“**SCM**”) is a clearing member who is also a Trading Member and clears and settle trades on its own account and on account of its clients but cannot clear and settle trades of other Trading Members.

Regulation 2(1)(fa) of the Brokers Regulations defines ‘self-clearing member’ as a member of a clearing corporation who is also a stock broker and clears and settles trades on its own account or on account of its clients only and includes any person having clearing and settlement rights on a commodity derivatives exchange; Provided that such person who clears and settles trades in commodity derivatives, should be required to become a member of an authorized clearing corporation, from such date as may be specified by SEBI. The only difference between PCM and TCM is that a PCM does not have any trading rights. PCM only has the right to clear the

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<sup>43</sup> ICCL is a wholly owned subsidiary of BSE.

trades whereas a TCM can clear his trades as well as trades of other Trading Members. With respect to an SCM, PCM is allowed to clear the trades of any member whereas an SCM has trading rights and can only clear his own trades and on its clients' account but cannot clear and settle trades of other Trading Members.

While BSE was a mutualized exchange, it had an additional category of membership called Limited Trading Member (“LTM”) in the derivatives segment/currency derivative segment. An LTM is a member of BSE in all respects and for all purposes and has all the rights, privileges, obligations and liabilities of a member of BSE, and shall have the right to carry on business as an intermediary. However, pursuant to BSE (Corporatisation and Demutualisation) Scheme, 2005, there is only one class of Trading Members i.e., deposit based membership having same rights/obligations as explained herein below. The following table shows the kinds of membership maintained by BSE, segment wise.

Types of Membership	Cash Segment	Derivatives Segment	Currency Derivatives Segment
Trading Member	✓	✓	✓
Self-Clearing Member	✓	✓	✓
Trading cum Clearing Member		✓	✓
Professional Clearing Member		✓	✓

### Eligibility Criteria and Qualifications for Membership

BSE operates through different segments which, *inter alia*, include the cash segment, equity derivatives segment and currency derivatives segment as indicated above. In order to become a Trading Member of BSE or a Clearing Member of ICCL, a person is required to fulfil various requirements. These requirements are prescribed by different circulars issued by SEBI and the Ministry of Finance, Rules, Bye laws and Regulations of BSE and ICCL, SECC Regulations, Broker Regulations and the SCRR.

On account of regulatory changes i.e., the enactment of the SECC Regulations, the clearing and settlement activities of BSE were transferred to ICCL through a Court approved Scheme

of Arrangement. Pursuant to the transfer, all Clearing Members of BSE automatically became Clearing Members of ICCL with all rights and obligations attached to their membership of BSE. Therefore, the process of admission of different categories of Clearing Members is governed by ICCL and its Rules, Bye-laws and Regulations. The Rules, Bye-laws and Regulations of ICCL have been annexed hereto as **Annexure 44**.

The following is the description of various requirements which a person is required to comply with to be eligible for becoming a Trading Member of BSE and Clearing Member of ICCL.

*1. Requirements for becoming a Trading Member*

- Educational Qualification

The Ministry of Finance issued a circular dated November 9, 1989 prescribing minimum educational qualification and experience requirements for being admitted as a broker. The circular is annexed hereto as **Annexure 45**. The circular states that the minimum educational qualification for authorization as a broker could be fixed as matriculation and reasonable familiarity with English. In the interest of increasing the professional competence levels of brokers, however higher educational qualifications of an applicant should be given weightage in the admission process.

Rule 17(iiA) of the BSE Rules for cash segment prescribes educational qualification which are necessary for becoming a Trading Member of BSE. Rule 17(iiA) states that a person eligible for admission as a member should have a minimum educational qualification of either matriculation or the 10 plus 2 years' qualification of the 10 plus 2 plus 3 years' educational system or such other educational qualification as may be prescribed by the Governing Board from time to time. Rule 17 also empowers the Governing Board to relax the condition of minimum educational qualification in exceptional cases subject to the prior approval of the Central Government. Similarly, in order to be eligible to become a Trading Member of the derivatives segment and/or currency derivatives segment, it is essential to have certain minimum educational qualification and experience.

- Experience

In relation to the requirement of experience, the aforesaid circular dated November 09, 1989 states that a minimum of three years' experience would be required for authorization as a broker. For this purpose, experience would be broadly defined to include all activities which

have relation to securities markets. This criterion is to ensure that persons of certain capabilities and maturity enter the market as brokers. In case of applicants with higher educational qualifications, their experience in activities relating to securities market would be treated as experience.

BSE Rules prescribe professional qualifications which are necessary for becoming a member of BSE. Rule 18 of the BSE Rules for cash segment states that no person eligible for admission as a member shall be admitted as a member unless:

- a. he has worked for not less than two years as partner with or as an authorized clerk or remisier or apprentice to a member of BSE; or
- b. he agrees to work for a minimum period of two years as a partner or to work for such period as a representative member with another member and enter into bargains on the trading system of BSE not in his own name but in the name of such other member of BSE; or
- c. he has, in the opinion of the Governing Board, not less than two years of experience in connection with various activities relating to the securities market.

- Qualifications under SCRR

Rule 8 of the SCRR deals with the qualification for membership of an authorised stock exchange. It states that rules relating to admission of members of a stock exchange seeking recognition should, *inter alia*, provide that: no person should be eligible to be elected as a member if he is less than twenty-one years of age; is not a citizen of India, has been at any time expelled or declared a defaulter by any other stock exchange. Further, it states that no person who is a member at the time of application for recognition or subsequently admitted as a member should continue as such if, *inter alia*, he ceases to be a citizen of India; is adjudged bankrupt or a receiving order in bankruptcy is made against him or he is proved to be insolvent; is convicted of an offence involving fraud or dishonesty.

Further, it states that a company would be eligible to be elected as a member of a stock exchange if, *inter alia*, such company is formed in compliance with the provisions of Section 322 of the Companies Act, 1956; a majority of the directors of such company are shareholders of such company and also members of that stock exchange; and the directors of such company,

who are members of that stock exchange, have ultimate liability in such company. Further, a company as defined in the Companies Act, 1956 would also be eligible to be elected as a member of a stock exchange if, *inter alia*, such company is formed in compliance with the provisions of section 12 of the Companies Act, 1956; such company undertakes to comply with such financial requirements and norms as may be specified by SEBI for the registration of such company under Section 12(1) of the SEBI Act; not less than two directors of the company are persons who possess a minimum two years' experience in dealing in securities or as portfolio managers or as investment consultants.

*Note: References made to the now repealed Companies Act, 1956 would automatically refer to the equivalent sections under the Companies Act, 2013.*

Similarly a limited liability partnership as defined in the Limited Liability Partnership Act, 2008, would also be eligible to be elected as a member of a stock exchange if, *inter alia*, such limited liability partnership undertakes to comply with such financial requirements and norms as may be provided by SEBI for registration of such limited liability partnerships under Section 12(1) of the SEBI Act; the designate partners of the 'limited liability partnership' are not disqualified from being members of a stock exchange; and the designated partners of the limited liability partnership' had not held the offices of directors in any company or body corporate or partner in any firm or 'limited liability partnership', which had been a member of the stock exchange and had been declared defaulter or expelled by the stock exchange. Further, any provident fund represented by its trustees, of an exempted establishment under the Employees' Provident Funds and Miscellaneous Provisions Act, 1952, would also be eligible to be elected as a member of a stock exchange.

In addition to the professional qualifications required to be a member, BSE Rules, Bye-laws and Regulations for the cash segment also provide the eligibility criteria and the procedure for admission of a candidate as a member of BSE. The following are various requirements for becoming a member of BSE as mentioned in BSE Rules for cash segment:-

- a. Eligibility Criteria: Rule 17 of the BSE Rules *inter alia* states that no person shall be eligible to be a member of BSE if :-
  - i. he is less than twenty one years of age;
  - ii. he is not a citizen of India;

- iii. he has been adjudged bankrupt or a receiving order in bankruptcy has been made against him or he has been proved to be insolvent even though he has obtained his final discharge;
  - iv. he has been convicted of an offence involving fraud or dishonesty;
  - v. he is engaged as principal or employee in any business other than that of securities except as a broker or agent not involving any personal financial liability unless he undertakes on admission to sever his connection his connection with such business;
  - vi. he is associated with or is a member of or a subscriber to or a shareholder or debenture holder in or is connected through a partner or employee of a member of or is a member or director of or debenture-holder in a company which is a member of or debenture holder in any other organization, institution, association, company or corporation where forward business of any kind whether in goods or commodities or otherwise is carried on unless he undertakes on admission to sever such association or connection;
  - vii. he has been at any time expelled or declared a defaulter by any other stock exchange. He has been previously refused admission to membership unless a period of one year has elapsed since the date of such rejection.
- b. Eligible Corporate Structure: According to BSE Rules for cash segment, corporate structures such as companies, firms, limited liability partnership etc. are eligible to be the members of BSE. The following are certain condition imposed by the BSE Rules for cash segment:-
- Rule 19A(a) of the BSE Rules states that a company defined in the Companies Act, 1956 shall be eligible to be a member of BSE if,
- i. such company is formed in compliance with the provisions of Section 322 of the Companies Act, 1956;

- ii. a majority of the directors of such company are shareholders of such company and also members of BSE; and
- iii. the directors of such company, who are members of BSE, have unlimited liability in such company.

In case the Central Government makes a recommendation, the Governing Board of BSE shall in relaxation of the abovementioned requirements, admit the following companies, corporations and institutions as member of BSE:-

- i. The Industrial Finance Corporation established under the Industrial Financial Corporation Act, 1948;
- ii. The Industrial Development Bank of India established under the Industrial Development Bank of India Act, 1964; The Life Insurance Corporation of India established under the Life Insurance Corporation Act, 1956;
- iii. The General Insurance Corporation of India constituted under the General Insurance Corporation (Nationalization) Act, 1972;
- iv. The Unit Trust of India, established under the Unit Trust of India Act, 1963;
- v. The Industrial Credit and Investment Corporation of India Ltd., a company registered under the Companies Act, 1956;
- vi. The subsidiaries of any of the corporations or companies specified above and any subsidiary of the State Bank of India or any Nationalized Bank set up for providing merchant banking services, buying and selling securities and other similar activities.

Rule 19A(b) of the BSE Rules states that a company as defined under the Companies Act, 1956 shall also be eligible to be elected as a member of BSE if,

- i. such company is formed in compliance with the provisions of Section 12 of the Companies Act, 1956;
- ii. undertakes to comply with such financial requirements and norms as may be specified by SEBI for the registration of such company under Section 12(1) of the SEBI Act;
- iii. the directors of the said company should not be disqualified for being members of a stock exchange under Rule 8 of the SCRR and the directors of the company should not have held the office of the directors in any company which had been a member of the stock exchange and had been declared defaulter or expelled by the stock exchange;
- iv. the said company has not less than 2 directors who possess a minimum of 2 years of experience in dealing in securities or as portfolio managers or an investment consultants.

Rule 19A(c) of the BSE Rules states that a limited liability partnership, formed and registered under the Limited Liability Partnership Act, 2008 shall be eligible to be elected as a member of the Exchange, subject to such terms and conditions as may be specified by SEBI and/or BSE from time to time;

Rule 19(a) of the BSE Rules states a partnership firm is eligible for trading membership of BSE. Rule 179A of the BSE Rules states that a partnership firm, if registered under the Indian Partnership Act, 1932, is eligible to be a member of BSE subject to the fulfillment of the following conditions:

- i. such partnership firms shall also register with the Income Tax authorities and with the Registrar of Firms and shall produce a proof of such registration to BSE;
- ii. the partners of the firm shall do business only on account of the firm and jointly in the name of the partnership firm;

- iii. partnership firm that includes minor partner shall not be eligible to be a member of BSE;
- iv. atleast two designated partners of the partnership firm are qualified to become a member of BSE as per the Rules, Bye-laws and Regulations of BSE;
- v. atleast two partners shall be termed as designated partners who are responsible for day to day affairs of the firm as a member of BSE;
- vi. atleast 2 designated partners together should have atleast 40% shares in the partnership firm;
- vii. partnership firm qualify eligibility norms as may be provided under the Rules, Bye-laws and Regulations of BSE;
- viii. an application for designated partners by a partnership firm shall be in the form as prescribed shall be signed by at least two designated partner of such partnership firm.

Rules, Bye-Laws and Regulations of BSE (cash segment) are attached hereto as **Annexure 11**.

- Eligibility Criteria under BSE Rules for the Derivatives Segment

In addition to the abovementioned qualifications, BSE Rules of the derivatives segment provide various conditions for the registration as a Trading Member of the derivatives segment/currency derivatives segment of BSE. The following are various requirements for becoming a member of BSE as mentioned in BSE Rules for derivatives segment:-

- a. Eligibility Criteria: Rule 2.9 of the BSE Rules deals with the registration of members of BSE. Rule 2.9 states that no person shall be eligible to be registered as a Trading Member, unless, *inter alia*,

- i. it is a Member of the Exchange (member of the cash segment of BSE);<sup>44</sup>
- ii. he is an individual or a body corporate;
- iii. if he has been previously refused registration as a trading member of the derivatives segment, unless a period of three months has elapsed since the date of such refusal;
- iv. unless he and/or such number of his partners (in a partnership firm which has been approved by the Governing Board and which is carrying on business on BSE) and/or designated directors (in the event of such person being a body corporate) and/or employees, as the Governing Council may prescribe, qualify/ies in a SEBI approved certification programme;
- v. unless such person submits to the derivatives segment the written consent of a clearing member to clear all of such person's trades;
- vi. unless he has a minimum net worth, possesses a minimum working capital of cash and/or marketable securities, and possesses assets of such nature and value as the Governing Council may from time to time in its opinion determine and consider acceptable;
- vii. unless such person undertakes to comply with such requirements and norms as may be specified by SEBI for registration with SEBI as a member of the derivatives segment; and
- viii. unless such person fulfils such other requirements as the Governing Council may from time to time specify. The Governing Council may waive compliance with the said requirements, if the person seeking registration is in respect of means, position, integrity, knowledge and experience of business

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<sup>44</sup> For Qualification, Eligibility Criteria and the Process of Admission of a member in the cash segment of BSE, refer to Rule 17 – to Rule 35B of the BSE Rules for cash segment which are attached as **Annexure 11**.

in securities considered by the Governing Council to be otherwise qualified for registration as a Trading Member

*(This is a discretionary power of the Board of Directors of BSE which allows it to specify any other requirements as it may deem fit).*

An LTM is also required to fulfil the aforementioned qualifications in order to become a member of the derivatives segment and/or currency derivatives segment.

- b. Eligible Corporate Structure: A partnership firm as such is not eligible to be registered as a member of the derivatives segment of BSE. As per the BSE Rules for the derivatives segment, only an individual or a body corporate may be registered as a member.

Rules, Bye-Laws and Regulations of BSE (derivatives segment) are attached hereto as **Annexure 12**.

## *2. Requirements for becoming a Clearing Member*

Rule 17 of the ICCL provides for the eligibility criteria for becoming a Clearing Member. It states that the following people are eligible to become Clearing Members of ICCL:-

- (a) individuals;
- (b) firms registered under the Indian Partnership Act, 1932;
- (c) a public financial institution as defined in Section 4A of the Companies Act, 1956;
- (d) a bank included for the time being in the Second Schedule to the Reserve Bank of India Act, 1934;
- (e) a foreign bank operating in India with the approval of the Reserve Bank of India;
- (f) a state financial corporation established under the provisions of Section 3 of the State Financial Corporations Act, 1951;

- (g) an institution engaged in providing financial services, promoted by any of the institutions mentioned in sub clause I to (f) jointly or severally;
- (h) a custodian of securities who has been granted a certificate of registration by SEBI under sub- section (1A) of Section 12 of the SEBI Act;
- (i) stock broker who has been granted a certificate of registration by SEBI under sub-section (1) of Section 12 of the SEBI Act;
- (j) a company as defined under the Companies Act, 1956 or in any statutory modification or re-enactment thereof;
- (k) a registrar to an issue or share transfer agent and who has been granted a certificate of registration by SEBI under sub – section (1) of Section 12 of the SEBI Act;
- (l) a limited liability partnership formed and registered under the Limited Liability Partnership Act, 2008, or any statutory modification or re-enactment thereof.
- (m) any other entity permitted by the Clearing Corporation and/or SEBI.

Rule 18 of the ICCL Rules provides for conditions precedent for admission. It states that ICCL may admit a person as a Clearing Member of ICCL, if such person:

- (a) is not disqualified under the Securities Laws from becoming a clearing member of a clearing corporation;
- (b) fulfils the requirements prescribed under the securities laws;

Provided however, the following persons should not be entitled to become Clearing Member of ICCL; if he/it:

- (a) is an individual who has not completed 21 years of age;
- (b) has been adjudged bankrupt or a receiving order in bankruptcy has been made against the person or the person has been proved to be insolvent even though he has obtained his final discharge;
- (c) has compounded with his creditors for less than full discharge of debts;

- (d) has been convicted of an offence involving a fraud or dishonesty;
- (e) is a body corporate which has committed any act which renders it liable to be wound up under the provisions of the law;
- (f) is a body corporate in respect of which a provisional liquidator or receiver or official liquidator has been appointed;
- (g) has been at any time expelled or declared a defaulter by any stock exchange, depository or other clearing corporation, or;
- (h) has been previously refused admission to Clearing Membership of ICCL unless the period of one year has elapsed since the date of rejection;
- (i) is not a fit and proper person as prescribed by SEBI from time to time.

In addition to the above, ICCL may impose additional requirements. Rule 19 of the ICCL Rules states that the Relevant Authority may, in addition to the above, prescribe from time to time, for different classes of Clearing Members and clearing segments, further and other criteria for eligibility for admission to, or retention of Clearing Membership. No person should be eligible to be admitted to the Clearing Membership of ICCL unless the person also satisfies such additional eligibility criteria. However the Relevant Authority may waive compliance with any or all of the admission conditions and at its discretion waive the requirements set out as above, if it is of the opinion that the person seeking admission is considered by the Relevant Authority to be otherwise qualified to be admitted as a Clearing Member by reason of his means, position, integrity, knowledge and experience of business in securities.

### *III. Minimum Financial Requirements*

The aforesaid Ministry of Finance circular dated November 9, 1989 prescribed a broad framework for authorization criteria for brokers which the stock exchanges were required to adopt. The circular states that the authorisation criteria for brokers should ensure minimum standards of competence, integrity and financial solvency. Further, the provisions under the SCRR lay down the requirement of financial soundness. Rule 8 of the SCRR provides that person applying for membership should not be adjudged as insolvent or wound up and should comply with the financial requirements as prescribed by time to time.

Further, the BSE Rules, Bye-laws and Regulations for both the cash segment and the derivatives segment require a person to be financially sound to become eligible for the membership of BSE. According to Rule 2.9(iv) of the BSE Rules of the derivatives segment, a candidate does not become eligible for BSE membership unless he has a minimum net-worth, possesses a minimum working capital of cash and/or marketable securities and possess assets of such nature and value which the Board of Directors of BSE may from time to time in its opinion determine and consider acceptable. Further, Rule 18 of the ICCL Rules states that a person should not be entitled to become a Clearing Member if it has been adjudged bankrupt or a receiving order in bankruptcy has been made against the person or the person has been proved to be insolvent even though it has obtained its final discharge.

- Base Minimum Capital

As a part of the liquid assets which form the core of the risk management system, BSE requires the Trading Member to maintain a minimum paid-up capital requirement of Rs. 3 million and deposit the Base Minimum Capital (“**BMC**”). BMC is the deposit given by the member of the exchange against which no exposure for trades is allowed. SEBI issued a circular dated December 19, 2012<sup>45</sup> (annexed hereto as **Annexure 46**) and prescribed the requirement of BMC for stock broker and Trading Member. BMC requirement was prescribed to be commensurate with the risks, other than market risk, that the broker may bring to the system. The Trading Members are required to deposit fifty per cent cash/ cash equivalent (minimum Rs. 0.125 million in cash is mandatory) and fifty per cent cash or non-cash equivalent as per SEBI circular dated December 19, 2012.

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<sup>45</sup> Circular bearing reference number CIR/MRD/DRMNP/ 36 /2012, on Requirement of Base Minimum Capital for Stock Broker and Trading Member, dated December 19, 2012, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1355915021615.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1355915021615.pdf)

The details of the BMC and other details in relation to membership in the cash segment are mentioned in the table below:-

Particulars	For Corporate & Individual		
	Cash Market and Futures & Options Trading	Refundable / Non Refundable	Exposure for trading margin
Deposit for DBM Membership (Cash Segment)	Rs. 1 million	Refundable	Yes
Base Minimum Capital	Base Minimum Capital- (50% Cash/Cash equivalent (minimum Rs.0.125 million in cash is mandatory) and 50% cash or non-cash equivalent) as per SEBI, vide circular no. CIR/ MRD/ DRMNP/ 36/ 2012 dated December 19, 2012. The revised requirement of BMC to be maintained by Stock Broker and Trading Member, according to their profiles as given below, which is effective from April 01, 2013.	Refundable	No

Categories	BMC Deposit		
a) Only Proprietary trading without Algorithmic trading (Algo)	Rs. 1 million		
b) Trading only on behalf of Client without proprietary trading and without Algorithmic Trading	Rs. 1.5 million		
c) Proprietary trading and trading on behalf of Client without	Rs. 2.5 million		

	Algorithmic Trading			
	d) All Trading Members/ Brokers with Algorithmic Trading	Rs. 5 million		
Admission Fees (Cash) *	Rs. 0.005 million	Non Refundable	No	
Annual Subscription(Cash) * Annual Subscription Fees Rs. 50,000/- payable by all members including LTMs. Link to the Exchange Notice No. 20160511-14 dated May 11, 2016 is:- <a href="http://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20160511-14">http://www.bseindia.com/markets/MarketInfo/DispNewNoticesCirculars.aspx?page=20160511-14</a>	Rs. 0.025 million	Non Refundable	No	

**Note:** Admission Fees will be Rs. 0.005 million if member applies in both Equity and Equity Derivatives Segment, and if member applies in only Equity segment Admission fees will be Rs. 0.25 million.

- Net-worth Requirements

SEBI appointed a committee under the chairmanship of Dr. L. C. Gupta<sup>46</sup> in November 1996 to “develop appropriate regulatory framework for derivatives trading in India”, which submitted its report in March 1998. The Board of SEBI in its meeting dated May 11, 1998 accepted the recommendations of the committee and approved the suggestive bye laws recommended by the committee. Further, SEBI issued a circular dated June 16, 1998<sup>47</sup> (annexed hereto as **Annexure 47**) enforcing the recommendations of the L. C. Gupta Committee. The L. C. Gupta Committee Report prescribed a net-worth requirement and also the method of computation of such net-worth. Presently, the net-worth formula prescribed by Dr. L. C. Gupta Committee has been adopted under Schedule VI of the Brokers Regulations as prescribed by Regulations 5(h) and 9(g) of the Brokers Regulations. Based on the aforesaid regulatory framework, BSE has prescribed a net-worth criteria for Trading Members (cash and equity derivatives segment).

The details of the net-worth criteria, minimum security deposit and other details are as follows:-

- a. **PCM:** The details are given in the table below:

<b>* Net worth</b>	Rs. 30 million
<b>*Minimum security Deposit</b>	Rs. 5 million – (whole of Rs. 5 million can be given in the form Bank Guarantee/FDR/cash) (This amount is payable after SEBI registration is received and at the time of commencement of business in Derivatives Segment)
<b>* SEBI Annual Charges</b>	Demand Draft of Rs. 0.05 million drawn in favor of SEBI

<sup>46</sup> Report on the Committee of Derivatives, available at <http://www.sebi.gov.in/commreport/lcgupta.html>

<sup>47</sup> Circular bearing reference number FITTC/DC/CIR-1/98 on Derivatives Trading in India dated June 16, 1998, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1364459484666.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1364459484666.pdf)

b. **TCM/SCM:** The details of TCM and SCM are given below:

<b>Net worth</b>	Rs. 30 million for TCM  Rs 10 million for SCM
<b>* Minimum security Deposit</b>	Rs. 5 million – (whole of Rs.5 million can be given in the form Bank Guarantee/ FDR/cash) (This amount is payable after SEBI registration is received and at the time of commencement of business in Derivatives Segment)
<b>* SEBI Annual Charges</b>	Demand Draft of Rs. 0.05 million drawn in favor of SEBI.

c. **Trading Member:** The details of the Trading Member are given below:

<b>* Net worth</b>	Rs. 2.5 million
<b>Minimum security Deposit</b>	Nil

### Compliance with Requirements for Membership

BSE provides a booklet which describes the applicable Rules, Bye Laws and Regulations for the specific category of membership, contains a checklist of documents to be submitted by different applicants such as, partnership firms or individuals for membership. Further, BSE provides the format for making applications for membership and also takes a number of undertakings from entities applying for membership. Compliance with various requirements for membership as stated above are confirmed by BSE/ ICCL through an initial application process, in which the applicant is required to fill such forms, provide undertakings, certifications, furnish documents as required under the checklist specified by BSE/ ICCL. On being satisfied that all the terms, conditions and eligibility requirements for membership have been complied with, BSE/ ICCL may admit the applicant as a Trading Member/ Clearing

Member. In this manner, it helps ensure that only applicants meeting the prescribed criteria become members and thereby ensures compliance with the same. The procedure of admission has been discussed in detail below.

### **Procedure for Admission of a Member**

Initially BSE was setup as a mutualized entity and the persons who were elected as members were entitled to hold a membership card, which was a personal permission and hence not alienable. Pursuant to the BSE (Corporation and Demutualisation) Scheme, 2005, BSE was corporatized and it became a demutualized entity. In accordance with the Scheme, there was segregation of membership rights into ownership rights and trading rights. In light of the same, a person who complies with the eligibility criteria as provided under the SCRR, Brokers Regulations, Intermediaries Regulations, Rules, Bye-laws and Regulations of BSE, relevant circulars issued by SEBI/ BSE would be entitled to be admitted as members of BSE. There was a structural change in the process of admission of members. The concept of card-based membership was replaced with deposit-based membership and the procedure of election became redundant and infructuous over a period of time.

#### *Single Registration*

SEBI issued a circular dated October 13, 2014<sup>48</sup> (annexed hereto as **Annexure 48**) in relation to single registration for Trading Members and Clearing Members. The circular states that the existing requirement of obtaining registration as a stock broker/ clearing member for each stock exchange/ clearing corporation has been done away with and replaced with a single registration with any stock exchange/ clearing corporation. The circular sets out the following guidelines for the purposes of implementing the revised registration requirements:-

- a. If a new entity desires to register as a stock broker or Clearing Member with any stock exchange or clearing corporation, as the case may be, then the entity should apply to SEBI through the respective stock exchange or clearing corporation in the manner prescribed in the Broker Regulations. The entity should be issued one certificate of registration, irrespective of the stock exchange(s)/ clearing corporation(s) or number of segment(s);

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<sup>48</sup> Circular bearing reference number CIR/ MIRSD/ 4/ 2014, dated October 13, 2014, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1413189318458.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1413189318458.pdf)

- b. If the entity is already registered with SEBI as a stock broker with any stock exchange, then for operating on any other stock exchange(s) or any clearing corporation, the entity can directly apply for approval to the concerned stock exchange or clearing corporation, as per the procedure prescribed in the Broker Regulations for registration. The stock exchange/ clearing corporation are required to report to SEBI about such grant of approval;
- c. Similarly, if any entity is already registered with SEBI as a Clearing Member in any clearing corporation, then for operating in any other clearing corporation(s) or any stock exchange, the entity is required to follow the procedure as prescribed above;
- d. Fees should be applicable for all the stock brokers, SCM and Clearing Members as per Schedule V of the Broker Regulations. As per the current requirement, the entity should continue to be liable to pay fees for each segment approved by the stock exchange or clearing corporation as per the Schedule to the Brokers Regulations.

Further, the said circular states that the stock exchange or clearing corporation should grant approval for operating in any segment(s) or additional segment(s) to the SEBI registered stock broker, SCM or Clearing Member, as the case may be, after exercising due diligence and on being satisfied about the compliance of all relevant eligibility requirements, and should also, *inter alia*, ensure:-

- a. The applicant, its directors, proprietor, partners and associates satisfy the “fit and proper criteria” as defined in the Intermediaries Regulations;
- b. The applicant has taken satisfactory corrective steps to rectify the deficiencies or irregularities observed in the past in actions initiated/taken by SEBI/stock exchanges(s) or other regulators. The stock exchange or clearing corporation may also seek details whether the board of the applicant is satisfied about the steps taken. They may also carry out inspection, wherever considered appropriate; and
- c. Recovery of all pending fees/ dues payable to SEBI, stock exchange and clearing corporation.

### *Procedure for Admission as Members*

- Step-wise Admission Procedure

The admission procedure followed by BSE for the admission of Trading Member in cash segment is as follows:-

Step I: To apply for membership of BSE, the interested applicants are required to send in their applications in writing in a sealed envelope addressed to the Chief General Manager, Member/Institutional Sales Department of BSE. The application form in the prescribed format has to be accompanied by a demand draft/ pay order for Rs. 0.1 million drawn in favour of “BSE Limited” towards earnest money deposit on which no interest is payable. The applications for admission as Trading Member in cash and derivatives segment are attached hereto as **Annexure 49**.

Step II: If BSE accepts the offer of an applicant, an offer acceptance letter is sent to the applicant. The applicants whose offer is accepted by BSE is required to provide all the documents as required by the checklist in the prescribed application form.

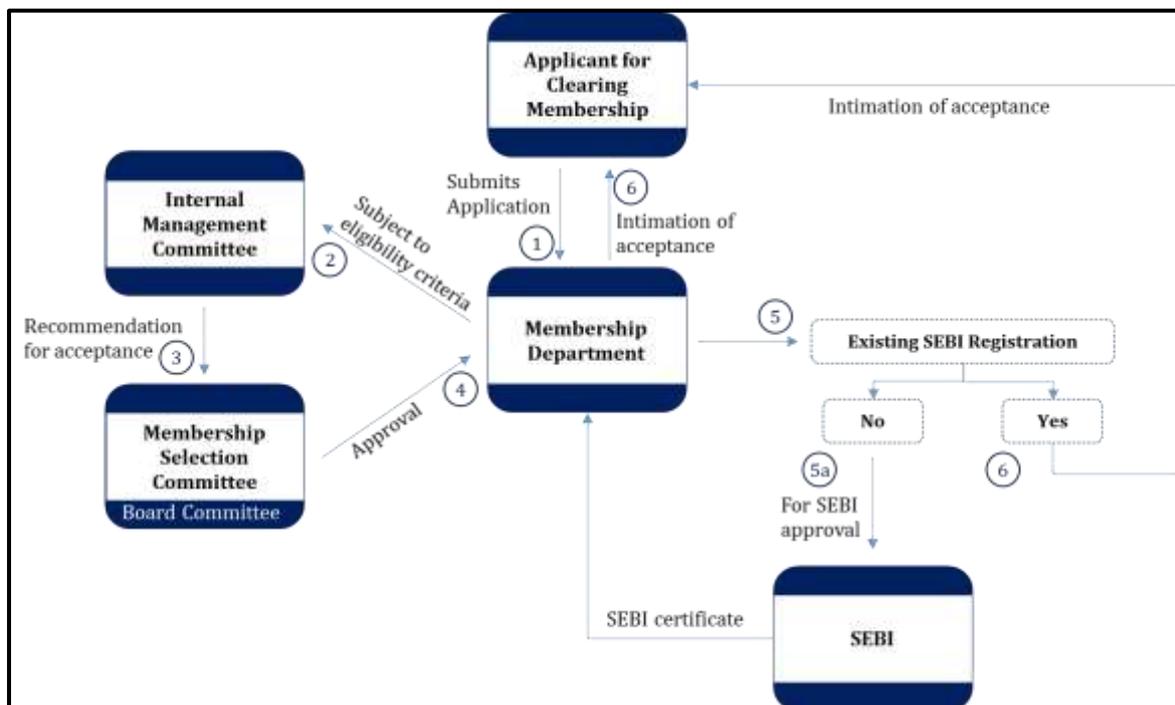
Step III: After the applicant submits the documents required for admission of a member as per the checklist, the application is placed before the Membership Selection Committee (“**MSC**”) (which is a committee mandated by SEBI) for its approval. After approval of MSC and on receipt of remaining documents the application is placed before Membership Approval Committee (“**MAC**”) (which is an internal Committee of BSE) for its approval. Once the MAC approves the application, the admission letter is issued to the applicant and the application is forwarded to SEBI for SEBI registration. All approvals by MAC are ratified by MSC. In case, the member is already a member on another stock exchange and is registered with SEBI, then the application is not required to be sent to SEBI for registration.

Step IV: After the application is sent to SEBI, the member is required to simultaneously start working on the commencement formalities. The applicant has to pay the balance amount after it receives the SEBI registration certificate but before the commencement of business.

The following process flow chart provides a description of the admission procedure undertaken by BSE to admit new members:-



The following process flow chart provides a description of the admission procedure undertaken by ICCL to admit Clearing Members:-



Further, in case of the derivatives segment, the applicant is not required to deposit the aforesaid Rs. 0.1 million towards earnest money deposit. If BSE accepts the offer of an applicant, an offer acceptance letter is sent to the applicant and the applicants has to provide all documents

as required by the checklist in the prescribed application form. The remaining steps to be followed are the same.

- Discretion of BSE

BSE has discretion to reject any application for admission. The Board of Directors may expel a member if in its opinion the member has, at the time of his application for admission to membership or during the course of the inquiry made by the Board of Directors preceding his admission, made any wilful misrepresentation or suppressed any material information required of him as to his character and antecedents; or has directly or indirectly given false particulars or information or made a false declaration.

Furthermore, BSE follows the 'fit and proper person' standards as prescribed by SEBI for market participants in Schedule II of the Intermediaries Regulations. As per the said standard, all background information regarding the registration and disciplinary history is checked before the admission of a candidate as a member. Schedule II states that for the purpose of determining as to whether an applicant or the intermediary is a 'fit and proper person', SEBI may take account of any consideration as it deems fit, including but not limited to the following criteria in relation to the applicant or the intermediary, the principal officer and the key management persons by whatever name called:-

- a. integrity, reputation and character;
- b. absence of convictions and restraint orders;
- c. competence including financial solvency and net-worth.

The members of BSE are required to provide undertakings with respect to them and their directors being "fit and proper". BSE scrutinizes all the documents provided by the candidates in order to ensure that the candidates comply with the 'fit and proper' criteria. Further, BSE takes appropriate regulatory actions against its members and its directors in case of any disciplinary action taken by SEBI or any other statutory or regulatory body.

### **Regulation of Stock-Brokers**

Stock-brokers and sub-brokers are regulated by SEBI under the Brokers Regulations and Intermediaries Regulations. Intermediaries Regulations was enacted in order to consolidate the common requirements which apply to all the intermediaries and to put in place a

comprehensive regulation. The Intermediaries Regulations provides for requirements such as grant of registration, general obligations, common code of conduct, common procedure for action in case of default and miscellaneous provisions etc. which are common to all the intermediaries. The Intermediaries Regulations forms the umbrella regulatory scheme for all intermediaries, however the specifics of a particular type of intermediary entity are governed by the respective supplementary regulation, for instance, stock-brokers are governed by the Brokers Regulations.

### *Brokers Regulations*

Brokers Regulations specifically deals with the registration, conduct, supervision of brokers and oversight of brokers' on-going compliance. The Brokers Regulations empower SEBI to take disciplinary actions against these market participants under the provisions of the SEBI Act, in case of non-compliance and misconduct. Some of the significant obligations on brokers as provided under the Brokers Regulations are stated herein. Regulation 3 of the Brokers Regulations states that no person shall act as a stock-broker, unless he obtains a certificate of registration from SEBI.

Before the issuance of certificate of registration, SEBI has to take into account various factors relating to trading, settling or dealing in securities. Further, the Brokers Regulations requires brokers to comply with certain general obligations such as, appointment of Compliance Officer as per Regulation 18A, prohibition on dealing with unregistered sub-broker as per Regulation 18B, restriction on brokers carrying on the activity of buying, selling or dealing in securities, other than commodity derivatives, from undertaking the activity of buying, selling or dealing in commodity derivatives, unless permitted by SEBI, as per Regulation 18C. The member-brokers of the BSE are required to maintain the books of accounts and records (such as register of transactions, clients ledger, general ledger, journals, margin deposit book) as per Rule 15 of the SCRR and Regulation 17 of the Brokers Regulations, which are to be preserved for a minimum period of 5 years as per Regulation 18 of the Brokers Regulations.

The Brokers Regulations also prescribe a code of conduct for brokers. Regulation 15 of the Broker Regulations provides for the general obligations of the brokers and requires a broker to abide by the code of conduct as specified in the Schedule II of the Broker Regulations. The code of conduct *inter alia* obligates a broker to act with due skill, care and diligence in the conduct of all his business; to not to indulge in manipulative, fraudulent or deceptive

transactions or schemes or spread rumours with a view to distort market equilibrium or make personal gains.

*Norms relating to dealing with Client funds*

- Segregation of Funds

The rules and regulations of SEBI and the Rules, Bye-laws and Regulations of BSE and ICCL require the members to segregate their proprietary accounts and the account of the client so that there is no intermingling of proprietary and client funds and funds of various clients *inter se*. SEBI issued a circular dated November 18, 1993<sup>49</sup> (annexed hereto as **Annexure 50**) in relation to regulation of transactions between clients and brokers.

The rules and regulations of SEBI and BSE/ ICCL regarding dealings with clients require all transactions relating to clients to be routed through the client bank account. Further, there are certain restrictions on withdrawal from the client's account. The member cannot withdraw money other than money in respect of which there is a liability to the member, provided that the money so drawn should not exceed the total of the money so held for the time being for each such client. Members are restricted from using clients' bank account for making any other financial transaction, including payment for, office expenses such as, salary, telephone bills, tax payments, purchase of office equipment, etc.

- Separate Accounts

Further, as per the aforesaid November 18, 1993 circular, it is compulsory for all member brokers to keep separate accounts for clients' securities and to keep such books of accounts, as may be necessary, to distinguish its securities from those of the clients' securities. Member broker is under an obligation to ensure payment of money/ delivery of securities to the clients within one working day of the declaration of pay out by the exchange in respect of the concerned settlement. Also, the member broker is under an obligation to pass on the corporate benefits such as interest, dividend and bonus/ right shares received on behalf of the clients to the clients immediately.

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<sup>49</sup> Circular bearing reference number SMD/SED/CIR/93/23321, dated November 18, 1993, available at [http://www.sebi.gov.in/cms/sebi\\_data/pdf/files/20231\\_t.pdf](http://www.sebi.gov.in/cms/sebi_data/pdf/files/20231_t.pdf)

- Restriction on accepting cash

Pursuant to provisions contained in SEBI's circular dated August 27, 2003<sup>50</sup> (annexed hereto as **Annexure 51**), members are restricted from accepting cash from clients whether against obligations or as margin for purchase of securities and/or give cash to the clients against sale of securities. The circular requires that all payments should be strictly received/ made by the members from/ to the clients strictly by account payee crossed cheque/ demand drafts or by way of direct credit into the bank accounts of the clients concerned.

- Restriction on trading via other members

SEBI in order to increase transparency and prevent excessive speculation, banned member brokers from routing proprietary or other trades through other brokers on the same exchange. The rules and regulation of SEBI restrict member brokers from trading via other member brokers. SEBI issued a circular dated January 13, 2004<sup>51</sup> (annexed hereto as **Annexure 52**) regarding the review of norms on trading by members-brokers. The circular states that a stock broker/ sub-broker of an exchange cannot deal with brokers/ sub-brokers of the same exchange either for proprietary trading or for trading on behalf of clients, except with the prior permission of the exchange. The stock exchange while giving such permission, is required to consider the reasons stated by the brokers/ sub-brokers for dealing with brokers/ sub-brokers of the same exchange and after carrying out due diligence, allow such brokers/ sub-brokers to deal with only one stock broker/ sub-broker of the same exchange.

- Record of Collateral

The member brokers are required to maintain proper records of client collateral. SEBI, in order to prevent misuse of client collateral, issued a circular dated April 17, 2008<sup>52</sup> (annexed hereto as **Annexure 53**). The circular requires member brokers to have adequate systems and procedures in place to ensure that client collateral is not used for any purposes other than meeting the respective client's margin requirements/ pay-ins. The member brokers are required

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<sup>50</sup> Circular bearing reference number SEBI/MRD/SE/Cir- 33/2003/27/08, on Mode of Payment and Delivery, dated August 27, 2003, available at [http://www.sebi.gov.in/cms/sebi\\_data/pdffiles/16600\\_t.pdf](http://www.sebi.gov.in/cms/sebi_data/pdffiles/16600_t.pdf)

<sup>51</sup> Circular bearing reference number SEBI/MIRSD//Cir-06/2004 dated January 13, 2004, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1292904894614.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1292904894614.pdf)

<sup>52</sup> Circular bearing reference number MRD/DoP/SE/Cir- 11/2008 on Collateral Deposited by Clients with Brokers, dated April 17, 2008, available at [http://www.sebi.gov.in/cms/sebi\\_data/pdffiles/7159\\_t.pdf](http://www.sebi.gov.in/cms/sebi_data/pdffiles/7159_t.pdf)

to maintain records to ensure proper audit trail of use of client collateral. Further, the circular required member brokers to issue daily statement of collateral utilization to their clients which should include, *inter alia*, details of collateral deposited, collateral utilized and collateral status (available balance/due from client) with break up in terms of cash, fixed deposit receipts, bank guarantee and securities.

- Uniform Documentation

SEBI through its circular dated August 22, 2011<sup>53</sup> (annexed hereto as **Annexure 54**) issued guidelines for the simplification and rationalisation of trading account opening process. The circular prescribed a uniform documentation which all member brokers are required to follow while opening a trading account. Member brokers are required to provide documents such as account opening form (including Know Your Client form), rights and obligations document, risk disclosure, document, guidance note, policies and procedures and tariff sheets. The arrangement between a broker and its client is governed by the rights and obligations documents as prescribed by the circular. The member broker, *inter alia*, is under an obligation to provide order/ trade confirmation details to its customer. Further the member broker is required to provide various other documents/ information such as, contract notes and daily margin statement, to its clients in relation to the execution and settlement of the order submitted by it on behalf of its clients.

- Shortfall

The member is under an obligation to notify BSE in the event the amount of funds segregated or set aside for clients is below the amount required under the Bye-laws of BSE. BSE can initiate disciplinary action against the member in the event that the amount of funds or assets segregated or set aside for clients is less than the amount required to be segregated or set aside under the Rules and Bye laws of BSE.

### *Record keeping and Reporting*

Member brokers of BSE are required to maintain the books of accounts and records as prescribed under BSE Bye-laws. For instance, Bye-law 10.3 of the BSE Bye-laws of the

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<sup>53</sup> Circular bearing reference number CIR/MIRSD/16/2011, dated August 22, 2011, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1314013806825.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1314013806825.pdf)

derivatives segment mandates member brokers to keep certain records such as trade confirmation slips or summary of trade confirmation slips as obtained from the system and order book in respect of Trading Member's own orders. Bye-law 10.7 of the BSE Bye-laws of the derivatives segment requires every Trading Member to maintain for a period of five years after the closure of the account or termination of the agreement documents such as copies of agreements executed with its clients and with each of the settling agencies or banks, originals of all communications received and copies of all communications sent by such Trading Member relating to its business as such. Similarly, Chapter 21 of the ICCL Regulations requires Clearing Members to adhere to various requirements with regards maintenance of records and annual accounts. Regulation 21.1.3 of the ICCL Regulations states that every Clearing Member of ICCL should maintain certain records relating to its business for a period of five years, such as statements of fund and securities obligations received from the clearing(s).

Furthermore, the Brokers Regulations provides for mechanism for inspection of the member-brokers with a view to ascertain whether the member-brokers registered are carrying on the business in terms of the provisions of the Brokers Regulations and also whether the conduct of the member-brokers is in the overall interest of the capital market and investors.

#### *Inspection of Brokers by SEBI*

The brokers are subject to on-going examination and supervision of SEBI. SEBI is empowered to undertake the inspection of the books of account, other records and documents of the brokers to ensure that they are being maintained in the manner required and that the provisions of SEBI Act, rules, regulations and the provisions of SCRA and the rules made thereunder are being complied with. Chapter V of the Brokers Regulations provides for the procedure for inspection of the brokers.

Regulation 19 of the Brokers Regulations states that where it appears to SEBI, it may appoint one or more persons as inspecting authority to undertake inspection of the books of account, other records and documents of the brokers. Regulation 21 of the Brokers Regulations provides for the obligations of stock brokers on inspection by SEBI. It states that every director, proprietor, partner, officer and employee of the stock-broker, who is being inspected, is under an obligation to produce to the inspecting authority such books, accounts and other documents in its custody or control and furnish him with the statements and information relating to the transactions in securities market within such time as the said officer may require. Further, it

states that the stock broker should allow the inspecting authority to have reasonable access to the premises occupied by such stock-broker or by any other person on its behalf and also extend reasonable facility for examining any books, records, documents and computer data in the possession of the stock-broker or any other person and also provide copies of documents or other materials which, in the opinion of the inspecting authority are relevant.

*Action in case of Default*

SEBI has the power to revoke, suspend the certificate of registration of the brokers and also has the power to impose monetary penalty on brokers. Chapter VI of the Broker Regulations provides for the procedure for action in case of default. Regulation 25 of the Broker Regulations states that a stock broker who contravenes any of the provisions of the SEBI Act, rules or regulations framed thereunder should be liable for any one or more of the following actions:-

- i. Monetary penalty under Chapter VIA of the SEBI Act;
- ii. Penalties as specified under Chapter V of the Intermediaries Regulations including suspension or cancellation of certificate of registration as a stock broker;
- iii. Prosecution under Section 24 of the SEBI Act.

As per Regulation 26 of the Broker Regulations, SEBI may impose monetary penalty in respect of certain violations, such as, failure to file any return or report with SEBI, failure to furnish any information, books or other documents within fifteen days of issue of notice by SEBI, failure to redress the grievances of investors within thirty days of receipts of notice from SEBI, failure to deliver any security or make payment of the amount due to the investor within forty eight hours of the settlement of trade unless the client has agreed in writing otherwise, charging of brokerage which is in excess of brokerage specified in the regulations or the bye-laws of the stock exchange, dealing in securities of a body corporate listed on any stock exchange on his own behalf or on behalf of any other person on the basis of any unpublished price sensitive information, indulging in fraudulent and unfair trade practices relating to securities and failure to obtain prior approval of SEBI in case of change in control of the stock broker.

As per Regulation 27 of the Brokers Regulations states that a stock broker should be liable for any action as specified in Chapter V of the Intermediaries Regulations including suspension or cancellation of its certificate of registration as a stock broker, as the case may be, if it, *inter alia*, ceases to be a member of a stock exchange, has been declared defaulter by a stock

exchange and not re-admitted as a member within a period of six months, has been found to be not a fit and proper person by SEBI, fails to pay fee as per Schedule III of Brokers Regulations, fails to comply with the rules, regulations and bye laws of the stock exchange of which it is a member; fails to co-operate with the inspecting or investigating authority, indulges in market manipulation of securities or of the index.

Further, Regulation 28 of the Brokers Regulations states that a stock broker would be liable for prosecution under Section 24 of the SEBI Act for, *inter alia*, the following violations:- dealing in securities without obtaining certificate of registration from SEBI as a stock broker, dealing in securities or providing trading floor or assisting in trading outside the recognized stock exchange in violation of provisions of the SCRA or rules made or notifications issued thereunder, failure to pay penalty imposed by the adjudicating officer or failure to comply with any of his directions or orders, violating SEBI (Prohibition of Fraudulent and Unfair Trade Practices relating to Securities Market) Regulations, 2003 (annexed hereto as **Annexure 55**).

Further, as per SEBI guidelines, each member needs to take broker indemnity insurance policy (without error and omissions or with error and omissions) with a minimum sum insured of Rs. 0.5 million and to submit the proof of the same to the exchange.

#### *Inspection by BSE*

- BSE's Obligation to Inspect

Stock exchanges are the entities which are primarily responsible for ensuring orderly conduct and compliance with applicable regulations by their member-brokers. Stock exchanges and clearing corporations have the power of inspection with respect to its members and typically impose fine for violations of their rules and bye laws. In addition, stock exchanges and clearing corporations may take more severe action like suspension or expulsion which is discussed in detail below. Where a member is suspected of more serious statutory offenses like manipulation, the investigation is initiated by SEBI which has a broader set of powers to enforce against such a member.

SEBI by its master circular dated March 17, 2010<sup>54</sup> and circular December 7, 2012<sup>55</sup> directed stock exchanges and clearing corporations to inspect members who posed risks to the investors and the market at large on account of the activities conduct by them. The nature and scope of the inspection is to ensure that:-

- a. proper books of accounts, records and documents have been maintained by a member-broker in the manner specified in Rule 15 of the SCRR and Regulation 17(1) of the Brokers Regulations;
- b. the member has complied with the Rules, Bye laws and Regulations of stock exchange/ clearing corporation;
- c. the member has complied with the provisions of the SCRA, the SCRR, the SEBI Act and the rules and regulations made thereunder and Brokers Regulations;
- d. to ensure that various provisions contained in the Rules, Bye laws and Regulations of the derivatives segment of BSE/ ICCL and any Business Requirement Specifications for the Derivatives Trading and Settlement System, notices, circulars, orders, resolutions, directions or instructions issued thereunder or pursuant thereto by SEBI and stock exchange/ clearing corporation are being complied with;
- e. to investigate into the complaints received from the clients/ investors, other members of stock exchange/ clearing corporation or any other person on any matter having a bearing on the activities of the members;
- f. to comply with any of the directions issued in this behalf by any regulatory authority including the Government of India;

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<sup>54</sup> Circular bearing reference number SEBI/MIRSD/Master Cir-04/2010, on Oversight of Members (Stock Brokers/Trading Members/Clearing Members of any Segment of Stock Exchanges and Clearing Corporations), dated March 17, 2010 available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1288263327681.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1288263327681.pdf)

<sup>55</sup> Circular bearing reference number CIR/MIRSD/13/2012 on Oversight of Members (Stock Brokers/Trading Members/Clearing Members of any segment of Stock Exchanges/Clearing Corporations), dated December 7, 2012, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1354880858992.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1354880858992.pdf)

- g. to check whether the member has complied with all the trading and clearing restrictions, if any, imposed by the stock exchange/ clearing corporation from time to time;
- h. to check whether the conduct of the member is in overall interest of the capital market and the member is fair in dealing with its client;

[SEBI's master circular dated March 17, 2010 and circular dated December 7, 2012 are annexed hereto as **Annexure 56** and **Annexure 57** respectively.]

SEBI's circular dated December 7, 2012 prescribes a policy of annual inspection of members of the stock exchange/clearing corporation. The circular provides for various parameters which a stock exchange and a clearing corporation is required to take into consideration while shortlisting the members it wants to inspect. The parameters are as follows:-

- a. Members servicing investors, having disabled on account of shortage of funds for more than three times in a month;
- b. Members servicing investors, having overnight disablement on account of margin shortage for more than two days;
- c. Top twenty five members paying high and recurring penalties for short reporting of margin, client code modification and trading terminal mismatch;
- d. Top twenty five members in terms of pending investor complaints and arbitration cases filled by investors;
- e. Members having adverse observations in the internal audit report on high risk issues such as incorrect reporting of margins, transfer of trades, pledging of client securities, dealing with unregistered intermediaries etc.;
- f. Subsidiaries of the regional stock exchanges are required to be inspected every year;
- g. Members penalized for more than five times during the last six months in relation to high algorithmic order to trade ratio in equity derivatives segment;
- h. Twenty-five members are randomly selected;

The members who do not fall under any of the aforesaid parameters would be inspected by BSE/ ICCL once in three years.

- Procedure of Inspection by BSE

Through its inspection mechanism and internal audit, BSE seeks to ensure that the members comply with the Brokers Regulations, SCRA, SEBI Act, BSE Rules, Bye-laws and Regulations etc. The Department of Brokers' Supervision which was earlier part of Department of Surveillance & Supervision ("DOSS") of BSE is entrusted with the responsibility to carry out inspection of the books of accounts, records and other documents maintained by its member-brokers including their branches. As on date, the department consists of about forty to fifty personnel approximately. Based on the assessment, BSE provides hands-on training, improvement of soft-skills to its personnel from time to time.

BSE and ICCL conduct inspection of all members of different segments of BSE and ICCL, respectively. BSE issues letters to the member-brokers informing them about the scheduled date of inspection and advising them to send the Inspection Questionnaire (containing basic information about background and operations of the member) before the commencement of inspection.

The inspecting team inspects the books and records on a sample basis and prepares an inspection report based on the findings of inspection. Non-compliances, if any observed during the course of inspection are forwarded to the member-broker concerned for their explanation. The member-broker is required to submit its reply along with documentary evidence within the stipulated time. The reply given by the member-broker is then vetted and action against the member-broker for the non-compliances observed during the inspection, is initiated as per the norms laid down in this regard by the Disciplinary Action Committee constituted by the BSE. The final action initiated is communicated to the member-broker and the member-broker is also advised to take necessary steps to ensure that such non-compliances do not recur in future.

Based on the findings during the course of inspections, BSE has reviewed and regrouped the penalty norms relating to the inspection of members. BSE has issued a list which contains commonly observed violations and penalties and actions which BSE may take. The list is indicative in nature and the violations are dealt with on a case to case basis depending on the seriousness and gravity of such violations. Further, based on the violation detected during the course of surveillance and investigation function, action is initiated against the Trading Members on the basis of history of such violations.

- Special Purpose Inspection by BSE

Further, BSE conducts special purpose/ limited inspections on the basis of triggers, for instance, patterns found during investor complaint resolution/ arbitration, complaints on specific malpractices of a broker and reference from various authorities such as SEBI/ Income Tax Department etc. Under the regulatory framework and the powers vested with the regulatory authorities, as and when directions are provided to BSE to effect inspection, BSE conducts such inspection.

#### *Monitoring by BSE*

As discussed, BSE through its Surveillance Department closely monitors the outstanding positions of the members on a daily basis. For this purpose, it has developed various market monitoring reports based on certain pre-set parameters. These reports are scrutinized by officials of the Surveillance Department to ascertain whether a member has built up excessive purchase or sale positions compared to his normal level of business. Further, it is examined whether purchases or sales are concentrated in one or more securities, whether the margin cover is adequate and whether transactions have been entered into on behalf of institutional clients. Even the quality of securities, i.e., liquid or illiquid, is looked into in order to assess the quality of exposure. Based on an analysis of these factors, the margins already paid and the total capital deposited by the member, an advance pay-in is taken from the concerned member.

Trading restrictions are placed on financially weak members as and when deemed fit. BSE/ICCL also scrutinizes the pay-in position of the members and such members who have larger funds pay-in positions are, at the discretion of BSE/ICCL, asked to make advance pay-in on the T+1 day instead of on the T+2 day. The BOLT TWSs of a member are deactivated for non-payment/ late payment of margins or settlement dues or on apprehension of financial difficulties or on detection of serious irregularities or for frequent violations of trading restrictions. Such decisions are taken on a case-to-case basis. The overall objective in resorting to this ultimate step is to ensure that questionable trading behavior of a member does not compromise the safety of the market or jeopardize the integrity of the market.

#### **Audit Requirements**

The members of BSE/ ICCL are required to carry out internal audits on a half-yearly basis. In addition to the internal audits, the members of BSE are required to carry out system audit on

annual basis and half-yearly basis, depending on the facilities they use. The members are required to submit the internal audit report and the system audit report highlighting any material inadequacy in their systems. BSE/ ICCL, on the basis of the said reports, may impose penalties on the members for the violation of different norms prescribed by SEBI and BSE/ ICCL and may direct the members to take corrective measures.

#### *Internal Audit by Members*

SEBI issued a circular dated August 22, 2008<sup>56</sup> [annexed hereto as **Annexure 58**] regarding the internal audit of the Trading Members/ Clearing Members of a stock exchange/ clearing corporation. Through the said circular, SEBI advised stock exchanges to make necessary amendments to the relevant bye laws, rules and regulations for implementation of the internal audit mechanism immediately, bring the provisions of the circular to the notice of the Trading Member/ Clearing Members of the stock exchange/ clearing corporation and also to disseminate the same on its website, and communicate to SEBI, the status of the implementation of the provisions of the circular in the monthly development report.

Further, SEBI through a letter dated March 23, 2009 (annexed hereto as **Annexure 59**) provided the scope/guidelines of internal audit, format of audit report, audit certificate and the time limit for submission of internal audit report by the member brokers of the stock exchange. Annexure-1 of the said letter provides for applicability, scope/purpose of the audit and who can conduct the said audit etc.; Annexure-2 of the said letter provides for the areas to be covered in the internal audit and the areas on which comments needs to be incorporated in the audit report and Annexure-3 of the said letter provides a format for the certificate for internal audit.

All the members are required to carry out complete internal audit on a half yearly basis by chartered accountants, company secretaries or cost and management accountants who are in practice and who do not have any conflict of interest. The internal auditor is required to submit the audit report to the proprietor/ partners/ board of respective member. Members are required to submit the internal audit report and internal audit certificate along with management comments on negative observations, if any with the BSE within three months from the end of the relevant half yearly period. The internal audit report is required to be submitted to the BSE

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<sup>56</sup>Circular bearing reference number MIRSD/ DPSIII/ Cir-26/ 08 on Internal Audit for Stock Brokers/Clearing Members, dated August 22, 2008, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1291175570372.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1291175570372.pdf)

in electronic form through BSE Electronic Filing System (“BEFS”) as per the format prescribed by BSE.

The minimum sample size required to be verified for the internal audit is prescribed by BSE. Further, the quality of internal audit reports received from members is monitored and appropriate steps are taken if the reports do not meet minimum expected quality levels. In case where internal audit report submitted is incomplete and not as per the guidelines, it is treated as non-submission of internal audit report. Further, BSE takes strict actions and imposes penalties on the members in cases of violations and non-compliance. Non-submission of internal audit report as per guidelines is treated as non-compliance and charges of i) Rs.100 per day for first three months after the due date of submission, ii) Rs. 1000 per day for next three months and iii) In case of non-submission of the report by the end of 6<sup>th</sup> month, all the trading terminals of the member are deactivated.

#### *System Audit*

SEBI’s master circular for stock exchange and clearing corporation dated May 26, 2015<sup>57</sup> (annexed hereto as **Annexure 60**) requires member brokers to conduct annual system audit. Chapter 2,<sup>58</sup> paragraph 8.2 of the master circular states that stock exchanges should ensure that system audit of stock brokers/ trading members are conducted in accordance with the prescribed guidelines. It further states that stock exchanges are advised to keep track of findings of system audits of all member brokers on a quarterly basis and ensure that all major audit findings, specifically in critical areas, are rectified/ complied in a time bound manner failing which, follow up inspection of such member brokers may be taken up for necessary corrective steps/ actions thereafter, if any. Paragraph 8.2, requires stock exchanges to report all major non-compliances/ observations of system auditors, broker wise, on a quarterly basis to SEBI. It also provides for a stock broker system audit framework dealing with aspects such as periodicity of audits, norms and terms of reference of the audit, norms for selection of auditors by stock brokers.

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<sup>57</sup> Master Circular bearing reference number CIR/MRD/DP/9/2015 dated May 26,2015, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1432638310942.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1432638310942.pdf)

<sup>58</sup> Master Circular dated May 26, 2015, Chapter 2 – Trading Software and Technology, available at [http://www.sebi.gov.in/cms/sebi\\_data/commondocs/chapter2trading\\_p.pdf](http://www.sebi.gov.in/cms/sebi_data/commondocs/chapter2trading_p.pdf)

The following table provides a description of the yearly compliance, half yearly compliance, monthly compliance and daily compliance which the member brokers are required to undertake as prescribed by BSE:-

Sr. No	Compliance related to	Description	Charges Leviable
<b>Yearly Compliance</b>			
1.	System Audit report	Trading Members who has availed the Intermediate Messaging Layer (“IML”) /Internet Trading facility from BSE are required to submit the System Audit Report and Secured Socket Layer certificate for the year ended March 31.	<p>The charges levied for late or non-submission of the report are as follows:-</p> <ol style="list-style-type: none"> <li>1. Charges of Rs 100/- per working day are levied for non-submission of annual System Audit Report and related documents for one month after the due date (after taking into consideration any extensions permitted by BSE).</li> <li>2. Further, on completion of one month (1<sup>st</sup> working day of 2<sup>nd</sup> month), BSE withdraw IML facility for non-submission of annual System Audit Report.</li> </ol>

<b>Half-Yearly Compliance</b>			
1.	Internal Audit report	Members are required to carry out complete internal audit on half yearly basis and submit the report for the same in the format prescribed by BSE in the relevant notice for the particular half year.	<p>The charges levied for late or non-submission of the report are as follows:-</p> <ol style="list-style-type: none"> <li>1. Rs 100 per day for first three months after the due date of submission;</li> <li>2. Rs 1000 per day for next three months;</li> <li>3. In case of non-submission of the report by the end of the 6<sup>th</sup> month, all the trading terminals of the member are deactivated.</li> </ol>
2.	Margin Trading Compliance certificate	Members are required to carry our audit of books of accounts maintained by them, with regard to margin trading facility offered by them. Further members are required to submit certificate certifying the extent of compliance with the conditions of Margin Trading Facility.	-
3.	System Audit Requirements for Algorithmic Trading	All members having approved algorithmic trading facility are required to undertake Algorithmic System's Audit every six months through BSE	<p>The charges levied for late or non-submission of the report are as follows:-</p> <ol style="list-style-type: none"> <li>1. Charges of Rs 100/- per day are levied for non-submission of</li> </ol>

		empanelled system auditors and submit the report to BSE.	<p>Algorithmic System Audit Report and related documents for one (1) month after the due date (after taking into consideration any extensions permitted by BSE).</p> <p>2. Further, on completion of 1 month (1<sup>st</sup> working day of 2<sup>nd</sup> month) Exchange will withdraw IML facility for non-submission of Algorithmic System Audit report.</p>
<b><i>Quarterly Compliance</i></b>			
1.	Execution of Orders	All the members are required to review and define the requirement of placement of orders. Further, Compliance Officer of the member is required to submit a certificate on the same to BSE on a quarterly basis.	-
<b><i>Monthly Compliance</i></b>			
1.	Client Funding	Members required to provide disclosure of their net exposure towards their clients on a particular day, should be maximum/peak exposure of funding by the Trading Members	<p>The charges levied for non-compliance are as follows:-</p> <p>1. Charges of Rs. 1000 is levied for not reporting</p>

		for their clients. The disclosure shall include the temporary funding of the Trading Member for their clients towards margin (retail clients), settlement obligations (both institutional and retail clients) and margin trading as also the total (i.e. the maximum/peak exposure of funding by the Trading Member for their clients).	the client funding data by due date.  2. Charges of Rs 1,500 are levied for consecutive defaults in reporting the data of client funding data for subsequent months.
2.	Client code modification	Modification of client codes are allowed during the entire day from 9:00 am to 4:00 pm.	All cases of modification of client codes of non-institutional trades executed on BSE and not transferred to broker error account are liable for a penalty of 1% of value of non-institutional trades modified if value of non-institutional trades modified as a percentage of total value of non-institutional trades executed is less than or equal to 5% and penalty of 2% if modification exceeds 5%, in a segment during a month.
3.	High order to trade ratio in Algorithmic Trading in Equity	In case of a high daily order to trade ratio through Algorithmic Trading in Equity Derivatives Segment, charges should be levied for algorithmic orders	Charges of Rs. 0.02 or Rs. 0.1 per order for order to trade ratio of fifty or more. Cooling off action for fifteen

	Derivatives Segment	having high order to trade ratio with effect from July 02, 2012. The said charges, computed daily, should be collected on a monthly basis, after reckoning all algorithmic orders and trades pertaining to all user ids of the member	minutes if order to trade ratio is five hundred or more. Additional penalty of suspension off proprietary trading rights for one hour, for more than ten occasions of above referred penalty in last thirty trading days.
<b>Daily Compliance</b>			
2.	Unregistered Unique Client Code (“UCC”) /UCC without Permanent Account Number (“PAN”)	Members have to register the unique client code as "OWN" in BSE database before commencing the OWN/proprietary trading on BSE platform.	Charges of Rs.10,000/- per day per client code would be levied for execution of trade before registration of client code along with PAN till the date of registration of such code including PAN details in the UCC database of BSE.
3.	Reason for Client code modifications	The members are required to inform BSE, on a daily basis by end of day, the reasons for modification of client codes of non-institutional trades based on the objective criteria. The member has to select any one of mentioned objective criteria for each of the modified trade.	-
4.	Location code mismatch	Cumulative file containing information regarding locations which are not registered or are incorrectly registered and orders	Charges of Rs 100 per day per terminal are levied.

		are being punched from that location.	
5.	PAN mismatch file	<p>The file will consist of details of those clients whose details have been uploaded incorrectly in UCC database of BSE due to any of the following reasons:-</p> <ol style="list-style-type: none"> <li>a. Invalid/wrong PAN details entered in UCC module;</li> <li>b. Client name wrongly entered in the UCC module;</li> <li>c. First name/middle name/last name left blank in UCC module.</li> </ol> <p>The report gives information related to the name and PAN details of the clients as uploaded in UCC database and as per income tax records. Members are required to update the name in UCC database exactly in the manner as is appearing as per Income Tax records in the PAN mismatch report.</p>	-
6.	Reporting of Bulk/Block deal	Bulk/Block deal reporting is fully automated. BSE provides an indicative report of bulk/block deals to the members on a daily basis after market hours. Further, the members are required to	-

		<p>verify each and every record in the file so downloaded.</p> <p>In case of any mismatch, members are required to fax the entire bulk/block deal(s) details to BSE with the corrections within thirty minutes from the time the indicative bulk/ block deal report is downloaded in the prescribed format.</p>	
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**Revocation of Membership on BSE**

*Trading Member*

The provisions under the BSE Bye-laws state that a member is liable to expulsion or suspension or withdrawal of all or any of its membership rights and/or to payment of a fine and/or to be censured, reprimanded or warned for any misconduct, unbusinesslike conduct or unprofessional conduct. For instance, the Bye laws 7.20, 7.21, 7.22, of the BSE Bye-laws of the derivatives segment state the description of misconduct (such as committing fraud, not complying with resolution, order, notice, direction, decision or ruling of the Governing Council or Chairman or of any committee, refusing to submit to arbitration), unbusinesslike conduct (such as transacting in fictitious names, engaging in reckless or unwarrantable dealings in the market) and unprofessional conduct (such as entering into bargains in securities that are not permitted, carrying on business with any member who has been suspended, expelled or declared a defaulter) respectively.

Further, Rule 14.1 of the BSE Rules for derivatives segment states that the Governing Council has the power to cancel or suspend the registration of and/or fine and/or censure and/or warn and/or withdraw the membership rights of a member if it is guilty of contravention, non-compliance, disobedience, disregard or evasion of Rules, Bye-laws and Regulations of BSE, or any resolutions, orders, notices, directions, decisions or ruling thereunder of BSE or the

Governing Council or the Chairman<sup>59</sup> or any committee or any officer of BSE, or of any conduct, proceeding or method of business which the Governing Council in its absolute discretion deems dishonourable, disgraceful or unbecoming a member of the derivatives segment or inconsistent with just and equitable principles of trade or detrimental to the interest, good name or welfare of BSE or prejudicial or subversive to its objects and purposes.

Similarly, Bye-law 355 of cash segment of BSE deals with the penalty for breach of Bye-laws and Regulations. It states that every member shall be liable to expulsion or suspension or withdrawal of all or any membership rights and/or to payment of fine and/or to be censured, reprimanded or warned for contravening, disobeying, disregarding or wilfully evading any of the Bye-laws and Regulations of BSE or any resolutions, orders, notices, directions, decisions or ruling thereunder of BSE or the Board of Directors or the Managing Director and Chief Executive Officer or any Committee or any officer of BSE or for any disreputable or fraudulent transactions or dealings with any person whether a member or not or for any conduct, proceeding or method of business which the Board of Directors in its absolute discretion deems unbecoming a member of BSE or inconsistent with just and equitable principles of trade.

#### *Clearing Member*

Rule 30 of the ICCL Rules deals with the disciplinary jurisdiction of ICCL. It states that ICCL may expel or suspend or censure or warn or reprimand any Clearing Member or impose fine or penalty on any Clearing Member, or withdraw or restrict all or any of its clearing membership rights or facilities, if it is found guilty of contravention, non-compliance, disobedience, disregard or evasion of any of the Rules, Bye Laws and Regulations of ICCL or circulars, orders, notices, directions, decisions or rulings of the Relevant Authority or ICCL or of any conduct, proceeding or method of business which ICCL in its discretion deems dishonourable, disgraceful or unbecoming of a Clearing Member of the Clearing Corporation or inconsistent with just and equitable principles of trade or detrimental to the interests, good name or welfare of ICCL or prejudicial or subversive to its objects and purposes.

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<sup>59</sup> Chairman of the Governing Council

## **Renewal and Readmission of Membership of Participants**

### *Trading Member*

The membership offered by BSE is perpetual in nature, hence there is no question of renewal. As per the provisions under the Rules, Bye-laws and Regulations of BSE, in cases of expulsion, the member cannot be re-admitted as a member of BSE. However, in cases where member is suspended, the suspension is revoked on compliance with certain requirements as specified by BSE. Further, in case of defaulter member, the said person may be re-admitted on BSE, if it makes an application for re-admission as prescribed by BSE under the Rules, Bye-laws and Regulations and complies with the relevant provisions of the Rules, Bye-laws and Regulations.

Chapter IV of the BSE Rules of the derivatives segment deals with termination of trading membership, for instance termination of the membership on account of death of an individual, member being a company is wound up, declaration of a defaulter, resignation of the member, cancellation of his registration with SEBI as per Broker Regulations, expulsion from membership, member being a bank and license granted by the Reserve Bank of India is cancelled etc. Explanation (ii) to Rule 4.1 of the BSE Rules of the derivatives segment states a Trading Member who is declared a defaulter and is readmitted to the membership of the BSE/ other stock exchange, should not, upon readmission to the membership of BSE/ other stock exchange, be registered as a Trading Member by reason that he was registered as a Trading Member at the time of or prior to his declaration of default. However, such readmitted member may apply to be registered as a Trading Member in accordance with these Rules, Bye laws and Regulations of BSE.

Rule 14.12(v) of the BSE Rules of the derivatives segment states that no member of BSE should transact business for or with a suspended Trading Member for one year from the date of suspension or share brokerage with a suspended Trading Member during the term of its suspension except with the previous permission of the Governing Council. Further, Rule 14.12(vi) of the BSE Rules of the derivatives segment states that registration/ membership of all segments of BSE should also be suspended during the period of suspension of its registration as a Trading Member.

Further, Bye-law 71 of the BSE Bye-laws deals with the measures to meet emergencies. It states that if in the opinion of the Board of Directors an emergency exists or has arisen or is likely to occur or if in its opinion, the conditions are such as to make free trading in securities

extremely difficult the Board of Directors may by a special resolution take such action as it deems fit for stabilising the market.

*Clearing Member*

Rule 29 of the ICCL Rules deals with re-admission of Clearing Members. It states that ICCL may at its discretion re-admit, a Clearing Member declared as a defaulter or a person whose clearing membership has been compulsorily terminated, as a Clearing Member subject to such terms and conditions as may be specified by ICCL. However, ICCL is restricted from re-admitting a Clearing Member expelled due to disciplinary action taken against him. Further the provision states that ICCL may, at its discretion, re-admit only such defaulter or such person, whose clearing membership has been compulsorily terminated and who, in the opinion of ICCL:-

- (i) has paid up all the dues, crystallized or admitted, to SEBI and ICCL;
- (ii) has paid up all the dues, crystallized or admitted, to other Clearing Members, clients and such other persons as may be specified by ICCL;
- (iii) has no insolvency or dissolution or winding up proceedings pending against him or it;
- (iv) has defaulted owing to the default of clients whom it might have reasonably expected to be good for their commitments;
- (v) has not been guilty of material breach of the Rules, Bye laws and Regulations of ICCL;
- (vi) has been irreproachable in its general conduct;
- (vii) meets all the eligibility criteria for admission as a Clearing Member.

### **Expulsion from all Stock Exchanges/ Clearing Corporations**

SEBI issued a master circular dated March 17, 2010 (annexed hereto as **Annexure 56**) which, *inter alia*, deals with multiple memberships in stock exchanges/ clearing corporations. It states that whenever a member of any segment is declared a defaulter, the concerned stock exchange/ clearing corporation should immediately declare it a defaulter in all its segments. It should also immediately inform all other stock exchanges/ clearing corporations the details of the defaulter member such as name of the member, the names of the proprietors/ partners/ promoters/ dominant shareholders, as applicable. Further, according to the circular issued by the Ministry of Finance dated August 12, 1991, if a member is expelled from one stock exchange it would automatically stand expelled from all other stock exchanges where it is a member.

### **Investor Protection Fund**

BSE set up an Investor Protection Fund (“**IPF**”) on July 10, 1986 to compensate the clients who suffer financial loss due to a member broker being declared as a defaulter, in accordance with the guidelines issued by the Ministry of Finance, Government of India. The IPF is managed by the trustees appointed by BSE. The corpus of IPF is created by contributions by the member brokers and BSE. Bye-law 16.3 of the BSE Bye-laws of the derivatives segment provides for the circumstances under which the IPF can be utilized to compensate the clients.

At present, the amount of compensation paid by BSE is to the extent of the award amount or Rs. 1.5 million, whichever is lower (*this amount has been progressively raised by BSE from Rs.10,000/- in 1988 to the present level*). The arbitration award obtained by the client against a defaulter is scrutinized by the Defaulters Committee of BSE, which may recommend to the trustees of the IPF to release of payment to the clients of the defaulters. After the approval of the trustees, the amount is disbursed to the clients from IPF.

Further, IPF is creating Investor Awareness and imparting financial literacy by spearheading Investor awareness programs across India. IPF is also supporting Investor Education and promotion of research activities in the field of Capital Market.

### **Dispute Resolution Mechanism**

With a view to ensuring speedy and effective resolution of claims, differences and disputes between non-trading members and Trading Members and the disputes among the Trading Members, *inter se*, BSE has laid down an arbitration mechanism. This mechanism is duly

embodied in the Rules, Bye-laws and Regulations of BSE, and duly approved by the Government of India/ SEBI, under the provisions of SCRA. BSE has opened Regional Investor Service Centres at various places including Ahmedabad, Bengaluru, Chennai, New Delhi, Hyderabad, Indore, Jaipur, Kanpur, Kolkata, Lucknow, Mumbai, Patna, Pune and Vadodara to provide investor grievance redressal and arbitration mechanism to the investors. The provisions relating to Arbitration Committee which deals with arbitration between non-trading members and Trading Members are laid down in the Bye-laws 248 to 281 of the BSE Bye-laws. The period for filing the claim in arbitration is governed by the law of limitation as prescribed under the Limitation Act, 1963. Every arbitration application is subject to the Rules, Bye-laws and Regulations of BSE and is deemed to be wholly made, entered into and to be performed in the city of Mumbai and the parties to such dealings, transactions, contracts and agreements are deemed to have submitted to the jurisdiction of the Courts in Mumbai for the purpose of giving effect to the provisions of the Rules, Bye-laws and Regulations of BSE.

#### **Audit Trail maintained by BSE/ ICCL**

BSE/ICCL maintains complete audit trail in relation to the execution of trades on its electronic platform, settlement of trades and the risk management facilities. Every trade which takes place on the electronic order matching platform of BSE is time-stamped. The extent of the audit trail maintained is such that BSE could rebuild the market based on the audit trail, if required.

In relation to the flow of information within the organisation, Regulation 28 of SECC Regulations requires that recognized stock exchange and recognized clearing corporation should segregate its regulatory departments from other departments in the manner specified in Part C of Schedule – II of the SECC Regulations. Part C states that in order to ensure the segregation of regulatory departments, every recognized stock exchange and recognized clearing corporation, should adopt a “Chinese Wall” policy which separates the regulatory departments of the recognized stock exchange or recognized clearing corporation from the other departments. The employees in the regulatory department should not communicate any information concerning regulatory activity to any one in other departments. The employees in regulatory areas may be physically segregated from employees in other departments including with respect to access controls. In exceptional circumstances employees from other departments may be given confidential information on “need to know” basis, under intimation to the Compliance Officer. BSE complies with the said requirement and provides for physical

segregation of the regulatory department from other departments. Further, Code of Ethics prescribed in SECC Regulations prescribes that flow of information from one department to another department of BSE must be through proper channels and puts an obligation on BSE to maintain an audit trail of the same.

Apart from the stock exchanges, even member brokers are required to maintain audit trail. Paragraph 1.2(iii) of Chapter 2 of the master circular issued by SEBI on May 26, 2015<sup>60</sup> (annexed hereto as **Annexure 60**) states that member brokers should maintain all activities/alerts log with audit trail facility. Further, member broker is under an obligation to send electronic contract notes, statement of accounts and daily margin report to their clients.

An electronic contract note is a contract document issued by the member brokers to their client showing the detailed log of transactions done on any given day in the stock exchange. It is a document through which a contractual obligation is established between the member broker and its clients. This is a prime document on the basis of which all the disputes between the member broker and its clients are settled. Bye-law 1.40(i) of the BSE Bye-laws of the derivatives segments requires every member broker to issue contract note to its clients for all trades executed for or with the client. The contract note should be in such format, contain all such details, and be issued in such manner and within such time as may be specified by the derivatives segment of BSE. Further, in case of multiple trades resulting from single order, the member broker is required to ensure that all the details of trades such as contract number, order number, order time, trade number, trade time, traded quantity etc. are attached to the contract note.

Further, the member broker is required to send a complete 'statement of accounts' for both funds and securities in respect of each of its clients in such periodicity and format within such time, as may be prescribed by BSE from time to time. This requirement emanates from SEBI circular dated December 03, 2009<sup>61</sup> (annexed hereto as **Annexure 61**) which requires member brokers to send 'statement of accounts' to their clients containing extract from the client ledger for funds and an extract from the register of securities displaying all receipts/ deliveries of

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<sup>60</sup> SEBI master circular dated May 26, 2015, Chapter 2 - Trading Software and Technology, available at [http://www.sebi.gov.in/cms/sebi\\_data/commondocs/chapter2trading\\_p.pdf](http://www.sebi.gov.in/cms/sebi_data/commondocs/chapter2trading_p.pdf)

<sup>61</sup> Circular bearing reference number MIRSD/ SE /Cir-19/2009 on Dealings between a client and a stock broker (trading members included), dated December 03, 2009, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1289365664189.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1289365664189.pdf)

funds/ securities. The statement should also explain the retention of funds/ securities and the details of the pledge, if any. The member brokers are also required to send a daily margin statement to the clients

The member brokers are also required to maintain an audit trail of the funds received through electronic fund transfers to ensure that the funds are received from their clients only. SEBI, in order to restrict the flow of third party funds/ unidentified money, issued a circular dated June 9, 2011<sup>62</sup> (annexed hereto as **Annexure 62**) requiring the member brokers to accept the instruments only if the same are drawn by their clients and issue cheques in favour of the clients only, for their transactions. However, in exceptional circumstances the member-broker may receive the amount in cash, to the extent permitted by the Income Tax Department/ authorities from time to time.

In addition to the above, the member brokers are required to display all the information/documents in relation to client's position, margin, statement of accounts and other related information on their website and allow secured access to their clients by way of client specific username and password. Further, the member brokers are required to ensure that the receipt/ delivery of securities in demat mode should be directly made to/ from the demat account of the respective client except in case of delivery of securities to a recognised entity such as approved intermediaries under the approved scheme of the stock exchange and/or SEBI.

### **Risk Management System**

As per SEBI Regulations and the Rules, Bye-laws and Regulations of BSE, a member broker is required to adopt a risk management policy for meeting the requirements laid down by SEBI and the stock exchanges on risk containment and for setting its own operational guidelines with proper parameters to combat various risk related issues.

Further, SEBI through its master circular dated May 26, 2015 (annexed hereto as **Annexure 60**) prescribes a comprehensive framework on the risk management system<sup>63</sup>. Paragraph 1.1.13

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<sup>62</sup> Circular bearing reference number CIR/MIRSD/03/2011 on Pre-funded instruments/ Electronic Fund Transfers dated June 9, 2011, available at

[http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1308551991898.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1308551991898.pdf)

<sup>63</sup> SEBI master circular dated May 26, 2015, Chapter 4 - Comprehensive Risk Management, available at

[http://www.sebi.gov.in/cms/sebi\\_data/commondocs/chapter4\\_p.pdf](http://www.sebi.gov.in/cms/sebi_data/commondocs/chapter4_p.pdf)

of the master circular deals with shortfall of margins/ pay-in of funds. In relation to margin shortfall, the circular states that in any shortfall in margin, the terminals of the broker should be immediately deactivated. Further, in relation to pay-in shortfall, the circular states as follows:-

- i. In cases where the amount of shortage in a settlement for a Trading Member is in excess of the base minimum capital prescribed, the trading facility of the member should be withdrawn and the securities pay-out due to the member should be withheld;
- ii. In cases where the amount of shortage exceeds twenty per cent. of the base minimum capital but less than the base minimum capital on six occasions within a period of three months, then also the trading facility of the member should be withdrawn and the securities pay-out due to the member should be withheld;
- iii. Upon recovery of the complete shortages, the member should be permitted to trade subject to its providing a deposit equivalent to its cumulative funds shortage as the 'funds shortage collateral'. Such deposit should be kept with the exchange for a period of ten rolling settlements and should be released thereafter. Such deposit should not be available for adjustment against margin liabilities and also not earn any interest. The deposit may be by way of cash, fixed deposit receipts or bank guarantee;
- iv. The exchange may levy a penal interest of not less than 0.07% per day on the pay-in shortage of the member.

#### *Additional Margins*

The aforesaid circular empowers the stock exchanges/ clearing corporations to impose additional margins in order to contain the risk. Paragraph 1.1.16 of the said circular deals with additional margin. It states that stock exchanges/ clearing corporations have the right to impose additional risk containment measures over and above the risk containment system mandated by SEBI. However, the stock exchanges/clearing corporations should keep the following three factors in mind while taking such action:

- i. Additional risk management measures (like ad-hoc margins) would normally be required only to deal with circumstances that cannot be anticipated or were not

anticipated while designing the risk management system. If ad-hoc margins are imposed with any degree of regularity, exchanges should examine whether the circumstances that give rise to such margins can be reasonably anticipated and can therefore be incorporated into the risk management system mandated by SEBI. Exchanges are encouraged to analyse these situations and bring the matter to the attention of SEBI for further action;

- ii. Any additional margins that the exchanges may impose should be based on objective criteria and should not discriminate between members on the basis of subjective criteria;
- iii. Transparency is an important regulatory goal and therefore every effort must be made to make the risk management systems fully transparent by disclosing their details to the public.

In relation to the above, it is pertinent to note that both BSE and ICCL have incorporated the said mechanisms. Bye law 8.3 of the ICCL Bye laws deals with quantum of margin. It states that the Clearing Member depositing margins, in the form of securities should always maintain the value thereof so that the same does not go below the quantum of margin required to be deposited by such member. In the event the value of such securities goes below the level of margin, then such member is required to provide further security to the satisfaction of the Relevant Authority. The Relevant Authority alone is entitled to determine the value of the additional security provided by such member.

Further, the capital position of member broker is treated as per the risk management norms prescribed by SEBI. Only unencumbered assets are accepted as collateral and in case of assets which cannot be readily converted or realized within a short time frame, the said asset suffers a much higher haircut and the collateral amount deemed to be deposited, of the said broker is accordingly reduced.

Furthermore, the risk management systems of BSE/ ICCL are very robust and neither has had to resort to imposing ad-hoc margins in the last ten years, including during the financial crisis of 2008. The members of BSE are under an obligation to notify and give an early warning to BSE in case its customer defaults in making payment or in case of failure of risk management system of the member. Further, the member broker is under an obligation to notify BSE if it is declared insolvent or winding-up proceedings are ensued.

### ***C. Oversight by a Governmental or Self-Regulatory Body***

This section highlights the powers of SEBI as the securities market regulator in India. The authority and autonomy of SEBI are discussed, followed by the organizational structure at SEBI. The section discusses the range of functions SEBI is supposed to perform under the SEBI Act and the scope of powers given to SEBI to undertake measures to protect the interests of the securities market. The powers of SEBI to regulate the organization and functioning of stock exchanges has been discussed thereafter.

#### **Constitution, Authority and Autonomy of SEBI**

BSE is subject to the regulatory oversight of SEBI. SEBI has been established as a body corporate having a separate legal identity, under Section 3 of the SEBI Act. SEBI is the statutory regulatory agency charged with the administration of securities laws and laws on commodity trading and regulation of securities markets and commodity futures markets in India. SEBI has been given financial autonomy by way of establishment of separate fund under Section 14 of the SEBI Act. This fund comprises all grants, fees and charges received and levied by SEBI. As an autonomous regulator, SEBI has independent legislative, executive and quasi-judicial powers. SEBI functions in an autonomous manner except wherein the Central Government may issue directions on the questions of policy as provided under Section 16 of the SEBI Act.

The autonomy of SEBI is not unbridled. Apart from the mechanism provided for appealing against the quasi-judicial orders passed by SEBI before SAT, SEBI is statutorily required to furnish a report every year to the Central Government under Section 18 of the SEBI Act, giving an account of its activities and policies. Sections 29 and 30 of the SEBI Act empower SEBI to make rules and regulations, respectively. The rules and regulations framed by SEBI are required to be laid before the Parliament under Section 31 of the SEBI Act and are subject to modification by the Parliament. Further, the accounts of SEBI are subject to audit by the Comptroller and Audit General of India under Section 15 of the SEBI Act. Also under Section 17 of the SEBI Act, the Central Government has been empowered to supersede SEBI in specified cases including grave emergency where SEBI is unable to discharge its functions and duties. Section 20A of the SEBI Act bars the jurisdiction of civil courts in matters where SEBI could take action. Further, Section 26 of the SEBI Act states that no court shall take cognizance of any offence punishable under the SEBI Act or any rules and regulation made thereunder,

except on a complaint made by SEBI. For ease of reference, please refer to the SEBI Act annexed hereto as **Annexure 2**.

### **Organisational Structure**

SEBI is managed by 8 members including a Chairman, 1 member from amongst the officials of the Ministry of the Central Government dealing with Finance, 1 member from Ministry of Corporate Affairs, 1 member from amongst the officials of the RBI and 4 other members to be appointed by the Central Government, out of which at least 3 shall be appointed as Whole-Time Members. These persons are required to have special knowledge of different aspects of securities market. The general superintendence, direction and management of the affairs of SEBI is vested with the board members of SEBI and these members are empowered to exercise all powers and do all acts and things which may be exercised or done by SEBI.

### **Functions and Scope of Authority of SEBI**

Section 11 of the SEBI Act deals with the functions of SEBI. Under Section 11, it is the duty of SEBI to protect the interest of investors in securities market and to promote the development of, and to regulate the securities market, by such measures as it thinks fit. Further, Section 11 states that the measures referred to therein may provide for:

- a) regulating the business in stock exchanges and any other securities markets;
- b) registering and regulating the working of stock brokers, sub-brokers, share transfer agents, bankers to an issue, trustees of trust deeds, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers and such other intermediaries who may be associated with securities markets in any manner;
- c) registering and regulating the working of the depositories, participants, custodians of securities, foreign institutional investors, credit rating agencies and such other intermediaries as SEBI may, by notification, specify in this behalf;
- d) registering and regulating the working of venture capital funds and collective investment schemes, including mutual funds;
- e) promoting and regulating self-regulatory organisations

- f) prohibiting fraudulent and unfair trade practices relating to securities markets;
- g) promoting investors' education and training of intermediaries of securities markets;
- h) prohibiting insider trading in securities;
- i) regulating substantial acquisition of shares and takeover of companies;
- j) calling for information from, undertaking inspection, conducting inquiries and audits of the stock exchanges, mutual funds, other persons associated with the securities market, intermediaries and self-regulatory organisations in the securities market;
- k) calling for information and records from any person including any bank or any other authority or board or corporation established or constituted by or under any Central or State Act which, in the opinion of SEBI, shall be relevant to any investigation or inquiry by SEBI in respect of any transaction in securities;
- l) calling for information from, or furnishing information to, other authorities, whether in India or outside India, having functions similar to those of SEBI, in the matters relating to the prevention or detection of violations in respect of securities laws, subject to the provisions of other laws for the time being in force in this regard;
- m) performing such functions and exercising such powers under the provisions of SCRA, as may be delegated to it by the Central Government;
- n) levying fees or other charges for carrying out the purposes under Section 11;
- o) calling from or furnishing to any such agencies, as may be specified by SEBI, such information as may be considered necessary by it for the efficient discharge of its functions;
- p) performing such other functions as may be prescribed.

Further, Section 11(4) states as follows:-

(4) Without prejudice to the provisions contained in sub-sections (1), (2), (2A) and (3) and section 11B, the Board may, by an order, for reasons to be recorded in writing, in the interests of investors or securities market, take any of the following measures, either pending investigation or inquiry or on completion of such investigation or inquiry, namely:-

- (a) suspend the trading of any security in a recognised stock exchange;
- (b) restrain persons from accessing the securities market and prohibit any person associated with securities market to buy, sell or deal in securities;
- (c) suspend any office-bearer of any stock exchange or self-regulatory organisation from holding such position;
- (d) impound and retain the proceeds or securities in respect of any transaction which is under investigation;
- (e) attach, after passing of an order on an application made for approval by the Judicial Magistrate of the first class having jurisdiction, for a period not exceeding one month, one or more bank account or accounts of any intermediary or any person associated with the securities market in any manner involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder : Provided that only the bank account or accounts or any transaction entered therein, so far as it relates to the proceeds actually involved in violation of any of the provisions of this Act, or the rules or the regulations made thereunder shall be allowed to be attached;
- (f) direct any intermediary or any person associated with the securities market in any manner not to dispose of or alienate an asset forming part of any transaction which is under investigation:

Provided that the Board may, without prejudice to the provisions contained in sub-section (2) or sub-section (2A), take any of the measures specified in clause (d) or clause (e) or clause (f), in respect of any listed public company or a public

company (not being intermediaries referred to in section 12) which intends to get its securities listed on any recognised stock exchange where the Board has reasonable grounds to believe that such company has been indulging in insider trading or fraudulent and unfair trade practices relating to securities market:

Provided further that the Board shall, either before or after passing such orders, give an opportunity of hearing to such intermediaries or persons concerned.

Hence, SEBI has been empowered to take appropriate measures under Section 11 of the SEBI Act for the purposes of discharging its functions and duties. Under Section 11B of the SEBI Act, SEBI is empowered to issue directions, after making an enquiry, to protect the interest of the investors or orderly development of securities market, to prevent the affairs of any intermediary conducted in a manner detrimental to the interests of the investors or securities market etc. SEBI has been vested with investigation powers under Section 11C of the SEBI Act. SEBI grants registration to various classes of market participants in accordance with the provision of Section 12. The quasi-judicial powers of SEBI emanate from Section 11(4), Section 11B, Section 11D, Section 12(3) and Chapter VIA of the SEBI Act. Under Chapter VIA of the SEBI Act, SEBI can impose monetary penalties through the process of adjudication. All quasi-judicial actions of SEBI can be appealed under Section 15T of the SEBI Act before SAT.

### **SEBI's Power and Authority to Regulate Stock Exchanges**

BSE is subject to a comprehensive regulatory regime. The SCRA empowers the Central Government to provide recognition to stock exchanges. The provisions under SCRA deal with application of recognition of stock exchanges, grant of recognition of stock exchanges, withdrawal of recognition, power of the recognized stock exchange to make bye-laws, power of SEBI to make or amend the bye-laws of the recognized stock exchanges, recognition of clearing corporation, power of the Central Government to supersede governing body of a recognized stock exchange. The procedural norms for the same are provided in the SCRR.

SCRA was subjected to legislative amendments at various stages particularly in light of the regulatory powers which were imposed upon SEBI upon the enactment of the SEBI Act in 1992. SEBI was constituted as an expert authority and was vested with statutory functions and duties in relation to the securities market. Section 12A was introduced into the SCRA by the Parliamentary amendment so as to empower SEBI to issue directions to stock exchanges as

well as to companies whose securities were listed or proposed to be listed in a recognized stock exchange, in the interest of investors and of the securities market, if SEBI is satisfied that it is necessary (a) in the interest of investors or orderly development of the securities market; (b) to prevent the affairs of a recognized stock exchange being conducted in a manner detrimental to the interests of investors or the securities market; or (c) to secure the proper management of a stock exchange. Further, Section 29A was introduced into the SCRA by the Parliamentary amendment to enable the Central Government to delegate its powers under the SCRA (except for the rule making power) to SEBI or to the RBI.

In exercise of the powers which were conferred by Section 29A of the SCRA, the Central Government issued a notification on July 30, 1992 directing that the powers exercisable by it under Section 4(5), Section 7 (annual reports to be furnished to Central Government by stock exchanges), Section 8 (power of the Central Government to direct rules to be made or to make rules), Section 11 (power of Central Government to supersede governing body of a recognized stock exchange), Section 12 (power to suspend business of recognised stock exchange) and Section 16 (power to prohibit contracts in certain cases) were delegated concurrently to SEBI. Further, in exercise of powers conferred by Section 29A of the SCRA, the Central Government issued a notification on September 13, 1994 directing that the powers exercisable by it under Section 3 (application for recognition of stock exchange), Section 4 (grant of recognition to stock exchanges), Section 5 (withdrawal of recognition), Section 7A(2), Section 13, Section 18(2), Section in the exercise of 22 and Section 28(2) were also to be delegated to SEBI.

### **Process of Recognition of Stock Exchanges**

SEBI, in exercise of its powers under the SEBI Act and the SCRA, enacted the SECC Regulations in 2012 to regulate recognition, ownership and governance in stock exchanges and clearing corporations. Regulation 3 of the SECC Regulations states that, stock exchanges which have been granted recognition under SCRA as on the date of commencement of the SECC Regulations shall be deemed to have been recognised under the SECC Regulations and all the provisions of the SECC Regulations as they apply to a recognized stock exchange shall apply to such exchange. In Chapter II of the SECC Regulations, SEBI has prescribed conditions for recognition of stock exchanges. Chapter III of the SECC Regulations deals with the net-worth requirements, Chapter IV prescribes requirements in relation to ownership of stock exchanges and Chapter V stipulates norms for governance of stock exchanges.

The following is the description of procedure undertaken by SEBI in order to grant recognition to a stock exchange in India.

Authority of SEBI to Grant Recognition: Regulation 3 of the SECC Regulations provides that no person in India can conduct, organise or assist in organising any stock exchange unless it has obtained recognition from SEBI in accordance with the provisions under the SCRA, SCRR and SECC Regulations.

Procedure for Grant of Recognition: Regulation 6 of the SECC Regulations states that for the grant of recognition, an application in a prescribed manner has to be submitted to SEBI. The application is required to be accompanied by copies of memorandum of association, articles of association and bye laws. Regulation 7 of the SECC Regulations requires the applicant seeking recognition as a stock exchange to comply with the following conditions:-

- a. the applicant must be a company limited by shares;
- b. the applicant must be demutualised;
- c. the applicant, its directors and its shareholders who hold or intend to hold shares, must be fit and proper persons as described in Regulation 20 of SECC Regulations;
- d. the applicant must satisfy the requirements relating to ownership and governance structure specified under the SECC Regulations;
- e. the applicant must satisfy the networth requirements specified under the SECC Regulations;
- f. the applicant must have financial capacity, functional expertise and infrastructure to operate as a stock exchange.

In addition to the abovementioned conditions, the applicant seeking recognition as a stock exchange is required to comply with the following conditions: -

- a. the applicant must have the necessary infrastructure for orderly execution of trades;
- b. the applicant must have an online screen-based trading system;

- c. the applicant must have an online surveillance capability which monitors positions, prices and volumes in real time so as to ensure market integrity;
- d. the applicant must have adequate infrastructure to list securities for trading on its platform, wherever applicable;
- e. the applicant has necessary capability to have a nationwide network of trading members and has adequate facility to admit and regulate its members;
- f. the applicant is required to make necessary arrangements to establish connectivity with its trading members and clearing corporation;
- g. the applicant must have an adequate Investor Protection Fund and Investor Services Fund;
- h. the applicant has put in place adequate investor grievances redressal mechanisms and arbitration mechanism to resolve disputes arising out of trades and its settlement;
- i. the applicant must have the facility to disseminate information about trades, quantities and quotes in real time to at least two (2) information vending networks which are accessible to investors in the country;
- j. the applicant must have adequate systems' capacity supported by a business continuity plan including a disaster recovery site;
- k. the applicant must have sufficient employees having adequate professional and other relevant experience;
- l. the business feasibility plan of the applicant has been appraised by a reputed agency having expertise in securities market.

SEBI may, on being satisfied with the capability of the applicant to comply with the abovementioned conditions, grant an in-principle approval to the applicant which is valid for a period of one year. Further, SEBI may, before granting recognition to a stock exchange, make inquiries and require such further information or document to be furnished, as it may deem necessary.

Grant of Recognition: Regulation 9 of the SECC Regulations empowers SEBI to grant recognition to a stock exchange. It states that SEBI may, after considering the application and on being satisfied that the applicant has complied with the conditions and is eligible to act as a recognised stock exchange, grant recognition to the applicant in terms of Section 4 of the SCRA, in the interest of the securities market. Regulation 10 of the SECC Regulations states that the period of recognition granted to a stock exchange should be as per Rule 6 of the SCRR. Rule 6 of the SCRR states that that the recognition unless granted on a permanent basis, should be for such period not less than one (1) year as may be specified in the recognition.

### **Other Powers of SEBI for Regulating Stock Exchanges**

Section 11 of the SCRA empowers SEBI to supersede the governing body of a recognised stock exchange. Section 11 states that where Central Government is of opinion that the governing body of any recognised stock exchange should be superseded, then the Central Government may serve on the governing body a written notice that the Central Government is considering the supersession of the governing body for the reasons specified in the notice and after giving an opportunity to the governing body to be heard in the matter, it may, by notification in the Official Gazette, declare the governing body of such stock exchange to be superseded, and may appoint any person or persons to exercise and perform all the powers and duties of the governing body, and, where more persons than one are appointed, may appoint one of such persons to be the chairman and another to be the vice-chairman thereof. The powers given to the Central Government under the said provision are exercised by SEBI.

Further, Section 12 of the SCRA provides SEBI the power to suspend business of recognised stock exchanges. Section 12 states that if in the opinion of the Central Government an emergency has arisen and for the purpose of meeting the emergency the Central Government considers it expedient so to do, it may, by notification in the Official Gazette, for reasons to be set out therein, direct a recognised stock exchange to suspend such of its business for such period not exceeding 7 days and subject to such conditions as may be specified in the notification, and, if, in the opinion of the Central Government, the interest of the trade or the public interest requires that the period should be extended, may, by like notification extend the said period from time to time.

## **Inspection, Monitoring and Investigation by SEBI**

Supervision of intermediaries, stock exchanges, clearing corporations and depositories through on-site and off-site inspections, enquiries and adjudications in case of violation of rules and regulations and administrative and statutory actions are essential features of effective enforcement by SEBI. Risk based and special purpose i.e., theme based inspections of registered intermediaries like brokers are conducted on the basis of investor complaints, surveillance reports, specific concerns, etc. These inspections are carried out throughout the year in order to ensure and verify the compliance levels of intermediaries, stock exchanges, clearing corporations and depositories.

SEBI, to monitor the securities market and its participants, uses both human resources and technological tools available at its disposal. The Integrated Surveillance Department at SEBI monitors market activity through its market alert systems and is in charge of overall market surveillance. SEBI is equipped with Integrated Market Surveillance System (“**IMSS**”) and Data Warehousing and Business Intelligence System (“**DWBIS**”) facilities to carry out market surveillance. The IMSS keeps track of market aberrations and generates alerts on a daily basis by analysing data across all stock exchanges, clearing corporations and depositories. The alerts are analysed periodically to identify any potential fraud, manipulation or insider trading being carried out in the market. The DWBIS comprises data warehouse, data mining and business intelligence tools. DWBIS allows SEBI to exploit the power of modern technology in terms of computation and speed of data analysis. This system is installed to monitor the trade and order data received by SEBI, in order to identify networked clients who possibly collectively indulge in violations of securities laws.

In addition to the efficient surveillance mechanism, SEBI is equipped with broad investigative powers to seek information. Section 11(3) of the SEBI Act states that SEBI will have same powers of that of a civil court in respect of matters such as, the discovery and production of books of account and other documents, summoning and enforcing the attendance of persons and examining them on oath. Section 11(3) reads as follows:-

“Notwithstanding anything contained in any other law for the time being in force while exercising the powers under 23[clause (i) or clause (ia) of sub-section (2) or sub-section (2A)], the Board shall have the same powers as are

vested in a civil court under the Code of Civil Procedure, 1908 (5 of 1908), while trying a suit, in respect of the following matters, namely:-

- (i) the discovery and production of books of account and other documents, at such place and such time as may be specified by the Board;
- (ii) summoning and enforcing the attendance of persons and examining them on oath;
- (iii) inspection of any books, registers and other documents of any person referred to in section 12, at any place;
- (iv) inspection of any book, or register, or other document or record of the company referred to in sub-section (2A);
- (v) issuing commissions for the examination of witnesses or documents.”

SEBI’s investigation powers under the SEBI Act were expanded by the Securities Laws (Amendment) Act, 2014 (“**SEBI Amendment Act**”). [Securities Laws (Amendment) Act, 2014 is annexed hereto as **Annexure 63**.] Pursuant to the SEBI Amendment Act, SEBI is empowered, *inter alia*, to call for information and records from any person, including any bank or any other authority established by or under any Central or State Act which, in SEBI’s opinion shall be relevant to any investigation or inquiry in respect of any transaction in securities,<sup>64</sup> and to call for information from, or furnish information to, other authorities, whether in India or outside India, having functions similar to those SEBI, in matters relating to the prevention or detection of violations in respect of securities laws.

Further, SEBI, for the purpose of furnishing any information to any authority outside India, may enter into an arrangement or agreement or understanding with such authority with the prior approval of the Central Government.<sup>65</sup> Such expanded powers of SEBI are designed to enhance its ability to engage in information sharing with other regulators and improve securities legislation in line with international best practices. Further, the broad categories of measures which can be undertaken by SEBI are cease and desist order, suspension or debarment of person registered as intermediary, imposition of administrative penalty and remedial directions to

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<sup>64</sup> Section 11(2)(ia), with .retrospective effect from. 18-07-2013.

<sup>65</sup> Section 11(2)(ib), with .retrospective effect from. 06-03-1998.

protect the interest of the investor. However the broad process for enforcement by remedial, penal and disciplinary actions is common because all must satisfy the requirements of natural justice.

### **Standards for New Products**

Further, SEBI sets the standards which recognized stock exchanges have to follow for approving products for trading. In India, the general standards followed by the recognised stock exchanges for the purposes of introducing a product for trading are as follows:

- i. The parameters based on which a product can be introduced by a recognised stock exchange are prescribed by SEBI through circulars, guidelines etc. So essentially, SEBI provides for a basic framework which the recognised stock exchanges are expected to keep in mind while designing a product. Further, SEBI has the power to change these parameters or specify additional conditions as it deems fit;
- ii. Based on such parameters, the recognised stock exchange prepares a proposal with various details such as nature of products, contract specifications, trading rules, economic rationale for introducing such product, benefits associated with such products etc. Before introducing a product, the recognised stock exchange is required to submit the said proposal to SEBI for its approval.
- iii. The recognised stock exchange will only introduce the said products if it obtains SEBI's approval. Further, the recognised stock exchanges do not allow any third party product to be traded on its platform.

Accordingly, BSE has to comply with said general standard and seek prior approval before introducing any new product for trading.

#### ***D. Oversight Standards Set by an Existing Body of Law***

This section discusses the broad and comprehensive regulatory regime that BSE, as an incorporated entity and a recognised stock exchange, is subject to. The section discusses certain general obligations which BSE is mandated to perform. The manner in which BSE's constitution and operation as a stock exchange is subject to the requirements prescribed under the SCRA, SECC Regulations etc. have been discussed. For instance, BSE has to maintain a

minimum net worth at all points in time and it cannot undertake activities unrelated to its functioning as a stock exchange, except in the manner prescribed under the applicable law.

The SCRA provides that any stock exchange desirous of being recognized for the purposes of the SCRA needs to make an application to the Central Government, which if satisfied based on certain factors, will grant such recognition to the stock exchange. The SCRA requires the applicant to submit copy of its bye-laws for the regulation of contracts, a copy of the rules relating to the admission of various classes of members into the stock exchange. As indicated above, the Central Government granted recognition to BSE on being satisfied about the relevant factors. BSE, as a recognized stock exchange regulates the operations and the standards of practice and business conduct of its members in accordance with its Bye-laws, Rules, Regulations, policies and procedures.

The SEBI Act was passed to establish SEBI as the Indian capital markets regulator, in order to protect interests of investors in securities, to promote the development of and to regulate the securities market. The SEBI Act and the relevant regulations made thereunder set out the oversight standards for the stock markets, stock exchanges, clearing houses, market participants and intermediaries such as stock brokers. They *inter alia* deal with registration, investment vehicles, insider trading, anti-fraud provisions and other specific norms, that are in line with the best legal practices adopted in established international jurisdictions and contain high standards designed to protect investors and regulate the capital markets. SEBI is subject to the oversight standards set forth in the SEBI Act.

### **Obligations on BSE under SCRA and SECC Regulations**

BSE is subject to a comprehensive regulatory regime which emanates from the SEBI Act, the SCRA, SCRR and the SECC Regulations. Further, BSE is governed by its Rules, Bye-laws and Regulations and approved by Central Government/SEBI under the provisions of SCRA. SEBI has issued a number of rules, regulations, guidelines and circulars for the regulation and supervision of stock exchanges in India. SEBI is responsible for the on-going supervision and oversight of BSE.

#### *General obligations on BSE*

Chapter VI of the SECC Regulations deals with the general obligations of the recognised stock exchange. In meeting its general obligations, BSE is accountable to SEBI. The general obligations are as follows:

- a. a recognised stock exchange shall use the services of recognised clearing corporation(s) for clearing and settlement of its trades;
- b. a recognised stock exchange shall avail the service of a recognised clearing corporation pursuant to an agreement in writing between them stipulating their rights and obligations, the conditions for admission of securities for clearing and settlement, risk management measures, charges for clearing and settlement and other incidental and consequential matters. Further, the recognised stock exchange shall extend its arbitration mechanism for settlement of disputes or claims arising out of clearing and settlement of trades executed on such stock exchange;
- c. a recognised stock exchange shall not engage in activities that are unrelated or not incidental to its activity as a stock exchange, except through a separate legal entity and as permitted by SEBI;
- d. a recognised stock exchange shall maintain and preserve the books of account and documents as per Rule 14 of the SCRR;
- e. a recognised stock exchange shall furnish to the SEBI its annual financial statements and returns as per Rule 17 and 17A of the SCRR.

Rule 17 of the SCRR requires every stock exchange to submit, before the 31<sup>st</sup> day of January, each year or within such extended time as SEBI may from time to time allow, a report about its activities during the preceding calendar year to SEBI, which should, *inter alia*, contain detailed information about the following matters:-

- a. changes in rules and bye laws, if any;
- b. changes in the composition of the governing body;
- c. any new sub-committees set up and changes in the composition of existing ones;

- d. admissions, re-admissions, deaths or resignations of members; (e) disciplinary action against members;
- e. arbitration of disputes (nature and number) between members and non-members;
- f. defaults;
- g. action taken to combat any emergency in trade;
- h. securities listed and de-listed; and
- i. securities brought on or removed from the forward list.

Further, Rule 17 also requires every stock exchange to submit, within one month from the date of the holding of its annual general meeting, a copy of its audited balance sheet and profit and loss account for its preceding financial year.

Rule 17A of the SCRR requires every stock exchange to submit periodical returns to SEBI relating to the following:-

- a. the official rates for the securities enlisted thereon;
- b. the number of shares delivered through the clearing house;
- c. the making-up prices;
- d. the clearing house programmes;
- e. the number of securities listed and de-listed during the previous three (3) months;
- f. the number of securities brought on or removed from the forward list during the previous three (3) months; and
- g. any other matter as may be specified by SEBI.

#### *SEBI's Power to Issue Directions*

Further, SEBI may from time to time call for any information, documents or records from the recognised stock exchange or the recognized clearing corporation or their governing board or

any shareholder thereof.<sup>66</sup> Furthermore, SEBI may, either *suo motu* or on receipt of any information or during pendency of any inspection, inquiry or investigation or on completion thereof, in the interest of public or trade or investors or the securities market, issue such directions as it deems fit, including but not limited to any or all of the following:-<sup>67</sup>

- a. directing a person holding equity shares or rights over equity shares in a recognised stock exchange in contravention of SECC Regulations to divest his holding, in such manner as may be specified in the direction;
- b. directing transfer of any proceeds or securities to the Investor Protection Fund of a recognised stock exchange;
- c. debarring any recognised stock exchange, any shareholder of such recognised stock exchange, or any associate and agent of such shareholder, or any transferee of shares from such shareholder, directors and key management personnel of recognised stock exchange from accessing the securities market or dealing in securities for such period as may be determined by SEBI.

#### *Other Significant Obligations on BSE*

Certain other obligations on stock exchanges under the SECC Regulations are as follows:-

- a. the recognised stock exchanges are required to maintain the minimum net-worth requirement at all times. The minimum net-worth requirement for a recognised stock exchange is Rs 100 million. The recognised stock exchange is required to submit audited net-worth certificate from the statutory auditor on a yearly basis to SEBI;
- b. the recognised stock exchanges are required to ensure that the shareholding or voting rights of any persons should not exceed the limits prescribed under the SECC Regulations. Further, the recognised stock exchanges are required to disclose to SEBI their shareholding pattern on a quarterly basis. Also, the recognised stock exchanges are required to maintain and preserve all the

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<sup>66</sup> Regulation 47 of the SECC Regulations.

<sup>67</sup> Regulation 49 of the SECC Regulations.

- books, registers, other documents and records relating to issue or transfer of its securities for a period of not less than 10 years;
- c. the recognised stock exchanges are required to ensure that their directors and key management personnel are fit and proper;
  - d. the recognised stock exchanges are required to segregate their regulatory departments from other departments in the manner;
  - e. the recognised stock exchanges are required to appoint a compliance officer who shall be responsible for monitoring the compliance of SCRA, Companies Act, 2013, SEBI Act, rules, regulations or directions issued thereunder and for the redressal of investors' grievances;
  - f. the recognised stock exchanges are required to credit the penalties levied by them to their investor protection fund;
  - g. the recognised stock exchanges are required to ensure equal, unrestricted, transparent and fair access to all persons without any bias towards their associates and related entities;
  - h. the recognised stock exchanges should not engage in activities that are unrelated or not incidental to their activity as a stock exchange or clearing corporation, as the case may be, except through a separate legal entity and as permitted by SEBI;
  - i. the recognised stock exchanges are required to maintain and preserve the books of account and documents as prescribed under the SCRR;
  - j. the recognised stock exchanges are required to furnish to SEBI their annual financial statements and returns as prescribed under SCRR;
  - k. the recognised stock exchanges are required to make bye-laws for the regulation of contracts and clearing and settlement, as the case may be, with the previous approval of SEBI.

*BSE's Obligation during Inspection by SEBI*

Regulation 48 of the SECC Regulations equips SEBI to undertake inspection, conduct inquiries and audit of any recognised stock exchange or recognised clearing corporation, any associate of such exchange or clearing corporation, any shareholder of such stock exchange or clearing corporation or any associate and agent of such shareholder. Further, where an inspection is undertaken by SEBI, such recognised stock exchange or recognised clearing corporation or shareholder or associate and every manager, director, managing director, chairperson or officer and other employee of such recognised stock exchange, recognised clearing corporation, shareholder or associate shall co-operate with SEBI.

*BSE Directors' Appointment Subject to SEBI*

Regulation 24 of the SECC Regulations requires the recognised stock exchange to seek approval of SEBI for the appointment and re-appointment of all shareholder directors on the governing board. Further, SEBI has the power to nominate the public interest directors on the governing board of the recognised stock exchange. Regulation 25 of the SECC Regulations requires stock exchange to seek approval of SEBI for the appointment, renewal of appointment and termination of service of the managing director of a recognised stock exchange.

Further, Regulation 25 of the SECC Regulations enables SEBI to remove or terminate the appointment of the managing director if deemed fit in the interest of the securities market. Also, SEBI may, for any failure by the directors to abide by SECC Regulations or the Code of Conduct or Code of Ethics or in case of any conflict of interest, either upon a reference from the recognised stock exchange or *suo motu*, take appropriate action including removal or termination of the appointment of any director, after providing him a reasonable opportunity of being heard. Further, SEBI in the interest of public is empowered to revoke the recognition of a stock exchange. Further, the chairman of board of directors of a stock exchange has to be appointed only with the approval of SEBI.

*BSE's Rules and Bye-laws subject to SEBI*

Furthermore, as per the provisions under SCRA and SECC Regulations, BSE is required to institute operating rules to govern its activities and the activities of its members and the market participants. SEBI's prior approval is required for the enforcement of these rules. SEBI may order an exchange to amend the rules/ bye-laws to conform to the provisions of SCRA. Every

draft pertaining to the constitutional documents, bye-laws and rules of BSE requires prior approval of SEBI. Regulation 44 of the SECC Regulations states that a recognised stock exchange shall, with the previous approval of SEBI, make bye-laws for the regulation of contracts, as per Section 9 of the SCRA and the SECC Regulations. Section 9(2) of the SCRA provides for broad principles which a recognised exchange is required to incorporate in its bye-laws. It states that such bye-laws may provide for:-

- a. the opening and closing of markets and the regulation of the hours of trade;
- b. a clearing house for the periodical settlement of contracts and differences thereunder, the delivery of and payment for securities, the passing on of delivery orders and the regulation and maintenance of such clearing house;
- c. the submission to the SEBI by the clearing house as soon as may be after each periodical settlement of all or any of the following particulars as SEBI may, from time to time, require, namely:-
  - i. the total number of each category of security carried over from one settlement period to another;
  - ii. the total number of each category of security, contracts in respect of which have been squared up during the course of each settlement period;
  - iii. the total number of each category of security actually delivered at each clearing;
- d. the publication by the clearing house of all or any of the particulars submitted to SEBI under clause (c) subject to the directions, if any, issued by the SEBI in this behalf;
- e. the regulation or prohibition of blank transfers;
- f. the number and classes of contracts in respect of which settlements shall be made or differences paid through the clearing house;

- g. the regulation, or prohibition of *budlas* or carry-over facilities;
- h. the fixing, altering or postponing of days for settlements;
- i. the determination and declaration of market rates, including the opening, closing highest and lowest rates for securities;
- j. the terms, conditions and incidents of contracts, including the prescription of margin requirements, if any, and conditions relating thereto, and the forms of contracts in writing;
- k. the regulation of the entering into, making, performance, rescission and termination, of contracts, including contracts between members or between a member and his constituent or between a member and a person who is not a member, and the consequences of default or insolvency on the part of a seller or buyer or intermediary, the consequences of a breach or omission by a seller or buyer, and the responsibility of members who are not parties to such contracts;
- l. the regulation of *taravani* business including the placing of limitations thereon;
- m. the listing of securities on the stock exchange, the inclusion of any security for the purpose of dealings and the suspension or withdrawal of any such securities, and the suspension or prohibition of trading in any specified securities;
- n. the method and procedure for the settlement of claims or disputes, including settlement by arbitration;
- o. the levy and recovery of fees, fines and penalties;
- p. the regulation of the course of business between parties to contracts in any capacity;
- q. the fixing of a scale of brokerage and other charges;
- r. the making, comparing, settling and closing of bargains;

- s. the emergencies in trade which may arise, whether as a result of pool or syndicated operations or cornering or otherwise, and the exercise of powers in such emergencies, including the power to fix maximum and minimum prices for securities;
- t. the regulation of dealings by members for their own account;
- u. the separation of the functions of jobbers and brokers;
- v. the limitations on the volume of trade done by any individual member in exceptional circumstances;
- w. the obligation of members to supply such information or explanation and to produce such documents relating to the business as the governing body may require.

Also, Section 9(3) states that the Bye-laws made under this Section may:-

- a. specify the bye-laws the contravention of which shall make a contract entered into otherwise than in accordance with the bye-laws void;
- b. provide that the contravention of any of the bye-laws shall render the member concerned liable to one or more of the following punishments, namely:-
  - i. Fine,
  - ii. Expulsion from membership,
  - iii. Suspension from membership for a specified period of time,
  - iv. Any other penalty of a like nature not involving the payment of money.

Section 9(4) of the SCRA states that the Bye-law of the recognised stock exchange, when approved by SEBI, should be published in the Gazette of India and also in the Official Gazette of the State in which the principal office of the recognised stock exchange is situate, and shall have effect as from the date of its publication in the Gazette of India. For governing its activities

and the activities of its members, BSE has formulated Rules, Bye-laws and Regulations for both cash and derivatives segments (annexed hereto as **Annexure 11** and **Annexure 12**).

#### *Disclosure Obligations on BSE*

As mentioned above, BSE has a number of disclosure obligations. It must periodically make disclosures regarding its shareholding pattern and it is required to submit its audit reports and financials to SEBI. Further, BSE is under an obligation to communicate to SEBI any information relating to its activities that may be useful to SEBI in exercising its functions and powers. In all such respects, and wherever possible, BSE assists SEBI as may be required for the proper administration of the SCRA, SCRR, SECC Regulations and SEBI Act.

#### *SEBI Circular on Governance in Stock Exchanges*

BSE is compliant with the requirements laid down under the SECC Regulations, which was primarily enacted to regulate recognition, ownership and governance in stock exchanges. SEBI, for the effective implementation of the SECC Regulations, issued a circular dated December 13, 2012 prescribing procedural norms on recognitions, ownership and governance for stock exchanges. Some of the requirements under the circular are discussed herein.

- **Furnishing of Information**

The circular requires all persons to submit details regarding educational qualifications, details of employment/ occupation, details of other directorship, declaration regarding fulfilment of 'fit and proper' criteria, a declaration in respect of non-association with Trading Members, details of regulatory actions taken by any statutory authority in India, disclosures of the names of his dependents associated with the securities market as a Trading Member, sub-broker, authorized person or holding any SEBI registration and details regarding pending/ completed criminal cases pending before any authority in India or abroad, if any in relation to the shareholders of BSE or a person intending to become a shareholder of BSE. For the purpose of appointment of Directors/ Managing Director & CEO, the recognized stock exchange is required to forward these details to SEBI while recommending the names of the persons along with the minutes of the governing board meeting where the names were approved, copy of the shareholders' resolution (wherever applicable), a confirmation by the recognized stock exchange that they are fit and proper persons in terms of their 'fit and proper' criteria and are not associated with any Trading Member.

- Appointment of CEO/ Managing Director

For the appointment of managing director/ executive director, the aforesaid circular dated December 13, 2012 states that a recognized stock exchange shall constitute a committee for the selection of CEO/ managing director/ executive director, as the case may be. The circular states that the managing director shall be selected through open advertisement in all editions of at least one national daily from amongst persons qualified in the fields of capital market/finance/management and possessing sufficient experience. In case of re-appointment, or extension, the recognized stock exchanges shall apply to SEBI two months before the last working day of such managing director.

- Appointment of Public Interest Directors

For the appointment of public interest directors, the circular states that the names of the public interest directors shall be forwarded to SEBI after the approval of the board of directors of the recognized stock exchange. The shareholders' approval shall not be necessary. The recognized stock exchange shall select public interest directors from diverse fields of work. The circular states that for the appointment of public interest directors, the recognized stock exchange shall take into account the following factors:

- i. qualification in the area of law, finance, accounting, economics, management, administration or any other area relevant to the financial markets;
- ii. atleast one person may be inducted having experience and background in finance/accounts who may preferably be inducted in the audit committee;
- iii. persons currently holding positions of trust and responsibility in reputed organisations or person who have retired from such positions;
- iv. persons, who are likely to have interested positions in commercial contracts and financial affairs of stock exchanges, may be excluded. Also, persons who are regular traders/speculators in the market or are director in the board of the promoter entity of the stock exchange shall be excluded.

In case of extension of the term of the public interest director or appointment of a new public interest director, the recognized stock exchange shall apply to SEBI two months before the expiry of the term. Further, the application for extension of term of the public interest director

shall be accompanied with his attendance details on meetings of various mandatory committees and on the board of directors of the recognized stock exchange, reasons for waiver of the cooling off period etc.

- Appointment of Shareholder Directors

For the appointment of the shareholder directors, the circular states that the manner of election, appointment, tenure, resignation, vacation, etc. of shareholder directors shall be governed by the Companies Act, 1956 save as otherwise specifically provided under the SECC Regulations or in accordance with the SCRA. Further, the circular states that the names of persons to be appointed as shareholder directors shall be first approved by the board of directors of the recognized stock exchange, followed by shareholders' approval before submitting the same to SEBI for approval.

- Other Requirements under the Circular dated December 13, 2012 and SECC Regulations

The recognized stock exchange is required to complete the appointment process within thirty days from SEBI's nomination/ approval for directors and submit a compliance report within one week from the date of appointment. In case any other official of the recognized stock exchange is appointed on the governing board in addition to the managing director, the same shall be subject to the approval of shareholders and SEBI, in that order.

Regulation 23(7) the SECC Regulations requires that no Trading Member or their associates and agents shall be on the board of directors of the recognized stock exchange. The circular provides more clarity on who would be considered as an associate or agent of a Trading Member for the purposes of Regulation 23(7) of the SECC Regulations. It states that a person who is a director in an entity, that itself is a Trading Member or has associate(s) as Trading Members, he/ she will be deemed to be a Trading Member. However, a person who is an independent director on the board of a bank or financial institution, which is in public sector or which either has no identifiable ultimate promoter or the ultimate promoter is in public sector or such banks or financial institutions has well diversified shareholding, and it/its associate is a Trading Member, the applicant will not be deemed to be Trading Member or their associate for the purpose of SECC Regulations. However, the appointment shall be subject to fulfilment of other requirements and satisfaction of SEBI.

Further, a person who is an independent director on the board of the public limited company whose other independent director(s) are also independent directors in an entity, which is a Trading Member, the person will not be deemed to be associate of Trading Member subject to that public limited company not having any other association with the Trading Member. The circular further states that the recognized stock exchange shall monitor and ensure the compliance of Regulation 23(7) SECC Regulations on a continuous basis, to ensure that directors appointed, on their board of directors will not get associated with a Trading Member after approval and appointment.

The SECC Regulations and the circular mandate a recognized stock exchange to appoint or employ fit and proper person as its chairman, CEO, directors and key management officers. Pursuant to Regulation 20 of the SECC Regulations, the criteria for considering whether a relevant person is fit and proper include but are not limited to the following:-

- i. Financial integrity;
- ii. Good reputation and character; and
- iii. Honesty.

Further, Regulation 20 states that such person should not have incurred the following disqualifications:-

- i. the person, or any of its whole time directors or managing partners, has been convicted by a court for any offence involving moral turpitude or any economic offence or any offence against the securities laws;
- ii. an order for winding up has been passed against the person;
- iii. the person, or any of its whole time directors or managing partners, has been declared insolvent and has not been discharged;
- iv. an order, restraining, prohibiting or debarring the person, or any of its whole time directors or managing partners, from dealing in securities or from accessing the securities market, has been passed by the SEBI or any other regulatory authority, and a period of three years from the date of the expiry of the period specified in the order has not elapsed;

- v. any other order against the person, or any of its whole time directors or managing partners, which has a bearing on the securities market, has been passed by SEBI or any other regulatory authority, and a period of three years from the date of the order has not elapsed;
- vi. the person has been found to be of unsound mind by a court of competent jurisdiction and the finding is in force; and
- vii. the person is financially not sound.

#### *Compliance by BSE with Circular dated December 13, 2012 and SECC Regulations*

BSE adopts a comprehensive and detailed process in the selection of its directors. BSE has complied with the requirements under the SECC Regulations and the circular for the appointment of its Board of Directors. BSE ensures that a person is independent, fit and proper, and the appointment of such person will not result in the violation of the SECC Regulations and the circular dated December 13, 2012. Presently, the majority of the current Board of Directors is independent according to the requirements set out under the SECC Regulations and the circular. There are eleven members on the Board of Directors of BSE, five of whom are public interest directors.

#### *Other Standards of Oversight*

SEBI has issued various circulars for the regulation of electronic trading including internet trading, direct market access and algorithmic trading. SEBI pursuant to these circulars allowed BSE to provide its members access to internet trading, direct market access and algorithmic trading facilities subject to fulfilment of certain criteria. Further, SEBI has issued various regulations governing the regulating entities, registration of the intermediaries, registration of stock brokers, sub-brokers, clearing members etc. In addition, SEBI periodically publishes circulars regarding various regulatory actions.<sup>68</sup> Further, as discussed, SEBI regulations and the Rules, Bye-laws and Regulations of BSE put an obligation on the members of BSE to

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<sup>68</sup> Master Circular for Stock Exchanges and Clearing Corporation, available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1432638310942.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1432638310942.pdf)  
Also see Master Circular on Oversight of Members (Stock Brokers/Trading Members/Clearing Members of any Segment of Stock Exchanges and Clearing Corporations), available at [http://www.sebi.gov.in/cms/sebi\\_data/attachdocs/1288263327681.pdf](http://www.sebi.gov.in/cms/sebi_data/attachdocs/1288263327681.pdf)

segregate clients' property from their property and maintain separate accounting records in order to provide protection to client's funds.

Therefore, the Rules and Bye-laws of both BSE and the ICCL are approved by SEBI in terms of the provisions under SCRA and SECC Regulations discussed above. Pursuant to powers vested under the Rules, both BSE and ICCL have the power to make/ amend their Regulations. Further, the Articles of Association of BSE and ICCL, which deal with management of BSE and ICCL, require SEBI's approval in terms of the provisions under the SCRA and the SECC Regulations. The broad principles governing the arrangement between BSE and ICCL for clearing and settlement of trades is provided in the SECC Regulations. Therefore, BSE is subject to a comprehensive regulatory oversight in its functioning as a recognized stock exchange in India.

***E. Reporting of Securities Transactions on a Regular Basis to a Governmental Body or Self-Regulatory Body***

SEBI being the securities market regulator, has an online integrated surveillance system to report securities market transactions. As mentioned above, BSE has a number of disclosure obligations. BSE is required to make periodic disclosures regarding its shareholding pattern and submit its audit reports and financials to SEBI. Further, BSE is under an obligation to communicate to SEBI any information relating to its activities that may be useful to SEBI in exercising its functions and powers.

The information regarding securities transactions submitted by BSE to SEBI can be broadly classified as follows:

1. Order and trade details regarding various products
2. Various other information is also provided to SEBI, as detailed below:-
  - a. Trading frequency in equity segment of BSE and NSE
  - b. Settlement statistics for equity segment of BSE and NSE
  - c. Open interest of equity derivatives segment at BSE/NSE
  - d. Equity derivatives trading at BSE/NSE during the month

- e. Open interest of equity derivatives trading at BSE/NSE during the month
- f. Settlement statistics in equity derivatives segment at BSE and NSE
- g. Trading in the corporate debt market
- h. Trading statistics of currency derivatives at BSE
- i. Daily trends of currency futures and options trading at BSE during the month
- j. Settlement statistics of currency derivatives segment at BSE
- k. Trading statistics of interest rate futures segment at BSE
- l. Daily trends of interest rate futures trading at BSE during the month
- m. Settlement statistics in interest rate futures segment at BSE
- n. Instrument wise turnover in index derivatives
- o. Maturity wise turnover in equity derivative segment of BSE
- p. Category wise share of turnover in cash segment of BSE
- q. Category wise share of turnover & open interest in equity derivative segment of BSE
- r. Category wise share of turnover & open interest in currency derivative segment of BSE
- s. Instrument wise turnover and open interest in currency derivatives
- t. Maturity wise turnover in currency derivative segment of BSE.

In addition to the aforesaid, BSE also shares a host of other reports pertaining to raising of capital and listing of securities such private placement of corporate debt, capital raised by various companies, turnover and market capitalization of companies, etc, with SEBI.

The aforesaid information also reflects in the monthly bulletin issued by SEBI and a link for the same is as follows:

<https://www.sebi.gov.in/sebiweb/home/HomeAction.do?doListing=yes&sid=4&ssid=30&smid=0>

3. Further, BSE shares various reports at different frequencies relating to surveillance such as information on open, high, low, close prices of securities traded on the platform of BSE, settlement data, action initiated under surveillance, if any, etc.

Further, various details with regards to transactions in currency derivatives segment is shared with the Reserve Bank of India, a co-regulator in the field of currency derivatives segment.

#### ***F. A System for Exchange of Price Quotations through Common Communication Media***

Regulation 7 of the SECC Regulations, while laying down the conditions for grant of recognition as a stock exchange, states that the applicant has to have the facility to disseminate information about trades, quantities and quotes in real time to at least two information vending networks which are accessible to investors in the country.<sup>69</sup> BSE disseminates information on market data on stocks and its major indices. The market data is disseminated through BSE provided trader work stations/ BOLT Plus, trading applications which connects to BSE via APIs (IML/ETI/MDI/EOBI), BSE website (market watch/ streamer) and data feed applications for data feed vendors.

Marketplace Technologies Pvt. Ltd., a hundred per cent subsidiary of BSE, developed FASTRADE™/ BOLT+ On Web, a terminal based and internet-based market access solution which allows the user to get live market quotes from multiple exchanges and execute orders in multiple markets simultaneously.

BSE provides support and activities with respect to various modes of BSE networks for a prescribed fee, such as VSAT, leased line, MPLS, campus LAN for Trader Work Station (TWS) connectivity. BSE requires members to apply for connectivity post receiving the letter of admission from BSE and before obtaining the registration certificate from SEBI.

In addition, market data including price quotations is disseminated to both domestic and international registered data vendors/customers who have executed agreements for data-feed

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<sup>69</sup> Regulation 7(3)(i) of the SECC Regulations.

subscription. For broadening the marketing and distribution of the BSE market data both in India and worldwide, BSE has entered into a partnership with Deutsche Bourse AG (“DBAG”). Under the said partnership arrangement, the marketing, sales, licensing, and other administrative services for the BSE market data is provided by DBAG to international data vendors (*viz.* Bloomberg, Thomson Reuters, MorningStar, Facset, etc.). BSE provides the same to domestic data vendors.

The data delivery of a wide range of BSE market data, to both domestic and international customers, is provided by BSE on a real time, delayed, and historical basis. Access to real time streaming data is available via established lease line connectivity through all major network service providers within India and access for delayed products and EOD products is available through a HTTPs website.

The real time BSE market data-feed subscribers includes Bloomberg, Thomson Reuters, Interactive Data, Six Telekurs, MorningStar, Cogencies Information Services, Reliable Software, Tickerplant, Spider Software, Facset, etc. The delayed BSE market data-feed subscribers include C-Mots Infotech, Accord Fintech, Dion Global Solutions, etc.

Further, the price quotation of a security is also disseminated on the website of BSE for the benefit of the investing public.

### ***G. An Organized Clearance and Settlement System***

This section discusses the background of ICCL and the scope of its responsibilities. Various Rules, Bye-laws and Regulations of ICCL are highlighted. The manner in which ICCL carries out the clearing and settlement functions for various segments of BSE are discussed. The section indicates how ICCL is well-capitalised and has undertaken various measures to ensure the safety of investors, such as maintaining a Core Settlement Guarantee Fund (“**Core SGF**”), subscribing to an insurance cover, etc. The section also throws light on the recognition gained by ICCL at various levels for its role as a Central Counter Party, and its compliance with standards for financial market infrastructure. The organizational structure of ICCL is discussed, along with its various committees. The kinds of membership available at ICCL are also discussed in this part. The mechanism and technology used by ICCL to perform its functions as a Central Counter Party are also stated herein.

## **Establishment of ICCL**

ICCL, located in Phiroze Jeejeebhoy Towers, Dalal Street, Mumbai, is a wholly owned subsidiary of BSE and was incorporated on April 26, 2007 under the provisions of the Companies Act, 1956. The Corporate Identity Number of ICCL is U67120MH2007PLC170358. ICCL is a public limited company, the securities of which are not listed on any stock exchange. ICCL is recognized as a clearing corporation in terms of provisions of SECC Regulations and is regulated by SEBI under the SEBI Act, SCRA, SECC Regulations and rules and regulations made thereunder. [The Certificate of Incorporation of ICCL is annexed hereto as **Annexure 64**. The Memorandum of Association and Articles of Association of ICCL are annexed hereto as **Annexure 65**.]

## **Rules, Bye-laws and Regulations of ICCL**

The key documents containing the rules of ICCL are the Rules, Bye-laws and Regulations (annexed hereto as **Annexure 44**). The Bye-laws of ICCL contain the bulk of governing norms such as dealing by the clearing members, margins, rights, duties and liabilities of the clearing members and clients, arbitration mechanism; the Rules contain basic corporate information along with some governing norm, such as conduct of board meetings, composition and powers of the board of directors, constitution of committees, membership, disciplinary proceedings and penalties; and the Regulations contain the operational details such as kind of deals, types of settlement, modes of delivery, clearing time frame for various contracts, delivery and payment details, procedure for settlement of cleared deals, details relating to closing out of contracts, requirement of maintenance of records, annual accounts and audit and inspection proceedings.

## **Scope of Activities of ICCL**

ICCL carries out the functions of clearing, settlement, collateral management and risk management for various segments of BSE. ICCL gained importance in the year 2012 as BSE's internal clearinghouse operations were shifted to ICCL. ICCL also became the the only Central Counterparty in India to clear trades for two stock exchanges, BSE and United Stock Exchange of India Limited ("USE"). ICCL provides post-trade clearing and settlement services for all trades on BSE. ICCL acts as a central counterparty through the process of novation, in essence, ICCL splits the original contract between the initiating counterparties into two new contracts; one each between ICCL and the initiating counterparties. The initiating parties are only

exposed to ICCL and no longer face the other initiating party's credit risk. In order to guarantee the settlement of each and every trade, ICCL has set up a Core SGF. It operates like a self-insurance mechanism where various contributions, including those from BSE, the CCP and clearing members are pooled in and are utilised, in case of failure of a Clearing Member to honour its settlement obligations, to the extent required for successful completion of the settlement. [Core SGF is discussed in detail below.]

## **Products**

ICCL settles trades reported on the Indian Corporate Debt Segment and the Mutual Fund ('StAR MF') Segment of BSE and clears and settles trades executed on all the other segments of BSE, including Equity Cash, Equity Derivatives, BSE SME, Offer for Sale, Securities Lending & Borrowing, Debt Segment, Interest Rate Futures, the Currency Derivatives Segment and Sovereign Gold Bond.

## **Clearing and Settlement Process**

All contracts which are traded on BSE are centrally cleared by the Central Counterparty which is ICCL. All such contracts are Marked-to-Market ("MTM") on a daily, end of the day, basis. The MTM margin is collected on the gross open position of the member. The gross open position in this context means the gross of all net positions across all the clients of a member including its proprietary position. For this purpose, the position of a customer is netted across its various securities and the positions of all the customers of a member broker are grossed. ICCL margins its members on 1 day Margin Period of Risk (MPOR) on Gross basis at client level. For illiquid securities in cash market, ICCL margins on three day MPOR on Gross basis.

Further, there is no netting across two different settlements. There is no netting off the positions and set-off against MTM profits across two rolling settlements i.e. T day and T-1 day. However, for computation of MTM profits/ loses for the day, netting or set-off against MTM profits is permitted. ICCL has a different settlement schedule and settlement process for different segments. It is responsible for clearing and settlement of trades in Equity Cash Segment, Equity Derivatives (F&O) Segment, Currency Derivatives Segment and Indian Corporate Debt Market Segment. The description of the settlement process and schedule in different segments has been provided in **Annexure 66**.

## ICCL's Ratings and Recognition

ICCL is the only clearing corporation in India to have been granted "AAA" rating by two rating agencies, namely, India Ratings Limited (Indian arm of Fitch Ratings) and Care Ratings Limited. In June 2017, India Rating & Research reaffirmed ICCL a Long-Term Issuer Rating of 'IND AAA' with Stable Outlook. Further in April 2018, CARE Ratings also reaffirmed 'CARE AAA (IS)' rating to ICCL. The rationale for assigning the said rating was ICCL's strong parentage (ICCL being wholly-owned subsidiary of BSE), zero gearing, good corporate governance and risk management framework, strong regulatory supervision, continued profitability and a dedicated default fund (i.e., the Core SGF).

On January 3, 2014, SEBI granted the Qualified Central Counterparty ("QCCP") status<sup>70</sup> to ICCL. A copy of the press release is annexed hereto as **Annexure 67**. A QCCP member is subjected to lower capital requirements/ charges under the Basel III Framework introduced by the Basel Committee on Banking Supervision. The capital requirements for banks and primary dealers in India, for a QCCP like ICCL are subject to the Capital Adequacy Standards and Risk Management Guidelines for Standalone Primary Dealers as prescribed by the RBI. SEBI granted renewal of recognition to ICCL to act as a clearing corporation in India with effect from October 3, 2017. A copy of the notification published in the Gazette of India is annexed hereto as Annexure 68.

ICCL as a QCCP is also subjected, on an on-going basis, to the rules and regulations that are consistent with the Principles for Financial Market Infrastructures ("PFMI") issued by the Committee on Payments and Market Infrastructures ("CPMI") and International Organization of Securities Commissions ("IOSCO"). These rules and regulations focus on limiting systemic risk and on enhancing transparency and stability in the financial market. A clearing member registered with a QCCP like ICCL will be a beneficiary of the enhanced risk management framework of ICCL and will also benefit in the form of lower capital costs. ICCL has published its self-assessment detailing its compliance of the CPMI-IOSCO's PFMI on its website. The said disclosure addresses each of the 23 principles of the PFMI. The disclosure is available at

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<sup>70</sup> A QCCP member is subjected to lower capital requirements/charges under the Basel III Framework introduced by the Basel Committee on Banking Supervision. The capital requirements for Banks and Primary Dealers in India, for a QCCP like ICCL is subject to the Capital Adequacy Standards and Risk Management Guidelines for Standalone Primary Dealers as prescribed RBI.

[http://www.icclindia.com/downloads/ICCL\\_Qualitative\\_Disclosure\\_CPMI\\_IOSCO\\_PFMI\\_May2015.pdf](http://www.icclindia.com/downloads/ICCL_Qualitative_Disclosure_CPMI_IOSCO_PFMI_May2015.pdf)

On September 10, 2013, ICCL had applied to the European Securities and Market Authority (“ESMA”) for recognition as a Third-Country Central Counterparties (“TC-CCP”) under European Market Infrastructure Regulation (“EMIR”) which was, inter-alia, contingent upon India being rated “Equivalent” by the European Commission. On December 15, 2016, the European Commission determined that India has an equivalent regulatory regime for central counterparties to the European Union, and that the legal and supervisory arrangements of India ensure that CCPs authorised therein comply with legally binding requirements which are equivalent to those laid down in Title IV of EMIR, providing effective supervision and enforcement on an ongoing basis. As per Article 25, on the basis of the information provided by ICCL, ESMA concluded that, ICCL is authorised in India and is subject to effective supervision and enforcement ensuring full compliance with the prudential requirements applicable in the country. Furthermore, conditions in Article 25 are met as cooperation arrangements pursuant to Article 25 have been established between SEBI and ESMA on June 21, 2017. After having assessed the application and concluding that the conditions for recognition of ICCL under Article 25 of EMIR are met, on September 27, 2017 ESMA concluded that ICCL is recognised as a TC-CCP under Chapter 4 of Title III of EMIR.

On November 18, 2014 the ICCL became the first company in India to apply for, and receive Pre-Legal Entity Identifier (“LEI”) from Clearing Corporation of India Limited (CCIL).

### Trading Volume

The following table shows the volume of contracts/ shares traded in the financial year 2018:-

Quantity of Contracts/Shares Traded (Rs. in millions)	
<i>Equity Derivatives</i>	
Futures and options	0.04
<i>Currency Derivatives</i>	
Currency Futures	306.49
Currency Options	382.50
<i>Interest Rate Derivatives</i>	

Futures	11.35
<i>Equity</i>	
Equity Shares	76250.20

### **ICCL’s Net-worth, Insurance and Safety of Investors**

As on December 31, 2017, the net-worth of ICCL is Rs. 5.30 billion. ICCL, with its net-worth of over Rs. 5.30 billion, which is nearly two times its default fund requirements, is well-capitalized and instils a high level of confidence in its members and investors of the ability to handle extreme loss situations. ICCL is committed to the safety of investors and Clearing Members and to further add to this security, ICCL has subscribed to a unique insurance policy for Rs. 3.90 billion. The objective of the said policy is to protect ICCL against counterparty defaults and to add a capital cushion to the ICCL net-worth, making the resources of the non-defaulting Clearing Members even safer.

The additional capital cushion of Rs. 3.90 billion, provided by the Insurance cover, along with the net-worth covers nearly five times the default fund requirement of ICCL and further increases the safety for domestic and international participants alike.

### **Organisational and Governance Structure of ICCL**

ICCL is governed by its Board of Directors, the composition of which is regulated by the SECC Regulations. Regulation 23 of the SECC Regulations deals with the composition of the board of directors of a recognised clearing corporation. It states that the number of public interest directors should not be less than two-third, and shareholder directors should not exceed one-third, of its governing board. The managing director will be an ex-officio director on the board of directors and should not be included in either the category of public interest directors or shareholder directors. The chairperson of the board is required to be elected by the board of directors from amongst the public interest directors, subject to the prior approval of SEBI.

The Board of Directors of ICCL has six members; the Managing Director & CEO, four are public interest directors (independent directors) and two shareholder directors<sup>71</sup>. As on April

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<sup>71</sup> Regulation 2(n) of the SECC Regulations defines ‘public interest directors’. It states that public interest director means an independent director, representing the interests of investors in securities market and who is not having any association, directly or indirectly, which in the opinion of SEBI, is in conflict with his role;

2018, the members of the Board of Directors of ICCL are Mr. M. S Sudareshan (Chairman, Public Interest Director), Ms. Devika Shahr (Managing Director & CEO), Mr. Ramabhadran S. Thirumalai (Public Interest Director), Mr. Prasad Dahapute (Public Interest Director), Mr. Nehal Vora (Shareholder Director) and Mr. Neeraj Kulshreshtha (Shareholder Director).

ICCL has various statutory committees in compliance with the provisions of the Companies Act, 2013, such as Audit Committee, Corporate Social Responsibility Committee, Investment Committee, Nomination and Remuneration Committee and Stakeholders Relationship Committee. In addition to the aforementioned committees, ICCL has constituted various statutory committees as prescribed by SEBI through the SECC Regulations, such as, Membership Selection Committee, Disciplinary Action Committee, Grievance Redressal Committee, Defaulters' Committee/ SGF Utilisation Committee, Compensation Committee, Selection Committee, Standing Committee on Technology, Sub-Committee for Monitoring Compliance of Suggestions given in SEBI Inspection Report, Investor Services Committee, Public Interest Directors' Committee, Ethics Committee, Independent Oversight Committee (Member Regulation), Risk Management Committee, Advisory Committee. ICCL also has its own dedicated regulatory departments. ICCL has completely segregated its Business function from its Regulatory function and the information flow across departments is on a strict need-to-know basis.

### **Risk Management Committee (RMC)**

ICCL has an elaborate Risk Management procedure, which is based on three pillars: Business Risk Assessment, Operational Controls Assessment and Policy Compliance processes. Major risks identified by the businesses and functions are systematically addressed through mitigating actions on a continuing basis. These are discussed with the RMC.

ICCL has an independent risk function, headed by the Chief Risk Officer and a RMC comprising of Independent Directors and outside experts. ICCL has constituted a RMC to continuously review and monitor the risk management policy and its implementation. The Chief Risk Officer is responsible for implementation of the risk management policy and reports independently to the MD & CEO and the Risk Management Committee ("**RMC**"). The Chief Risk Officer has a dual reporting – to the MD&CEO as well as the RMC. The RMC reviews the entire risk management system of ICCL, including the margining framework. The RMC formulates a detailed risk management policy which shall be approved by the governing Board

and monitors implementation of the risk management policy and keeps SEBI and the governing Board informed about its implementation and deviation, if any. The Risk Management Function is separate from Business and Operations functions.

### **Core SGF**

Regulation 39(1) of the SECC Regulations requires every recognised clearing corporation to establish and maintain a fund for each segment, to guarantee the settlement of trades executed in respective segment of a recognised stock exchange. So in order to fulfil its statutory obligations, ICCL has set up segment wise Core SGFs (segregated default funds) for the equity segment, equity derivatives segment, currency derivatives segment and debt segment, to guarantee the settlement of trades executed in the respective segment. The Core SGF is utilised to the extent required for successful completion of the settlement, in the event of a failure of a Clearing Member to honour settlement commitments. The presence of such a mechanism has helped alleviating counter-party risk of trading on BSE.

#### *Corpus of Core SGF*

The corpus of the Core SGF must be adequate to meet out all the contingencies arising on account of failure of any member(s). The risk or liability to the Core SGF depends on various factors such as trade volume, delivery percentage, maximum settlement liability of the members, the history of defaults, capital adequacy of the members, the degree of safety measures employed by ICCL/ BSE, etc. However, in order to assess the fair quantum of the corpus of Core SGF, ICCL considers the following factors:-

- i) Risk management system in force;
- ii) Current and projected volume/turnover to be cleared and settled by ICCL on a guaranteed basis;
- iii) Track record of defaults of clearing members (number of defaults, amount in default).

The Minimum Required Corpus (“MRC”) for each segment of BSE is subject to the following:-

- i) MRC is fixed for a month;

- ii) By 15<sup>th</sup> of every month, ICCL reviews and determines the MRC for next month based on the results of daily stress tests of the preceding month. (For instance, by 15<sup>th</sup> February, ICCL determines MRC for March based on results of various stress tests conducted in January). ICCL also reviews and determines by 15<sup>th</sup> of every month, the adequacy of contributions made by various contributors and any further contributions to the Core SGF required to be made by various contributors for the next month;
- iii) For every day of the preceding month (i.e., January as per example in (ii) above), uncovered loss numbers are estimated by the various stress tests for credit risk conducted by ICCL for the segment and highest of such numbers is taken as the worst case loss number for the day;
- iv) Average of all the daily worst case loss numbers determined in (iii) above is calculated;
- v) The MRC for next month (i.e., March as per the above example) shall be higher of the average arrived in at step (iv) above and the segment MRC as per previous review (i.e., review done on 15<sup>th</sup> January for the month of February).

*Policy for Contribution to Core SGF*

At any point of time, the contributions of various contributors to Core SGF of any segment will be as follows:-

- a. Clearing Corporation contribution: ICCL contributes at least fifty per cent of the MRC to the Core SGF. ICCL is required to make this contribution from its own funds. Its contribution to the Core SGFs is considered as part of its net-worth;
- b. Stock Exchange contribution: BSE contributes at least twenty five per cent of the MRC (can be adjusted against transfer of profit by stock exchange as per Regulation 33 of the SECC Regulations<sup>72</sup>, which may be reviewed in view of these guidelines);

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<sup>72</sup> Regulation 33 of SECC Regulations states that every recognised stock exchange shall credit twenty five per cent. (25%) of its profits every year to the Fund as specified in Regulation 39, of the recognised clearing corporation(s) which clears and settles trades executed on that stock exchange.

- c. Clearing Member primary contribution: If the ICCL wishes, it can seek risk based contribution from clearing Members of the segment (including custodial clearing members) to the Core SGF subject to the following conditions:-
- i) That total contribution from clearing members should not be more than twenty five per cent of the MRC;
  - ii) That no exposure should be available on Core SGF contribution of any clearing member (exposure-free collateral of clearing member available with ICCL can be considered towards Core SGF contribution of clearing member); and
  - iii) That required contributions of individual clearing member should be pro-rata based on the risk they bring to the system.

ICCL has the flexibility to collect Clearing Members' primary contribution either upfront or staggered over a period of time. In case of staggered contribution, the remaining balance is met by ICCL to ensure adequacy of total Core SGF corpus at all times. The contribution made by ICCL on behalf of the Clearing Members is available to ICCL for withdrawal as and when further contributions from Clearing Members are received. Further, any penalties levied by ICCL (as per Regulation 34 of the SECC Regulations<sup>73</sup>) are credited to the Core SGF corpus. Interest on cash contribution to Core SGF also accrues to the Core SGF and is attributed pro-rata to the contributors in proportion to their cash contribution. ICCL is required to adhere to specific guidance which may be issued by SEBI from time to time in relation to Core SGF.

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<sup>73</sup> Regulation 34 of the SECC Regulations states that penalties levied by recognised stock exchange or recognised clearing corporation shall be credited to its Investor Protection Fund or the Fund as specified in Regulation 39, as the case may be

The following table provides information regarding ICCL's Core SGF and the contribution by various contributors:-

April 2018 (In million)					
Segment	ICCL Contribution	BSE Contribution	Members Contribution	Other Contributions (Refer Note)	Total
<b>Equity</b>	1412.80	473.90	0.00	47.30	1934.00
<b>Equity Derivatives</b>	134.10	45.00	0.00	0.70	179.80
<b>Currency Derivatives</b>	610.40	201.90	0.00	47.90	860.20
<b>Debt</b>	13.70	0.00	0.00	0.00	13.70
<b>Additional Contribution*</b>	0.00	573.00	0.00	0.00	573.00
<b>Total</b>	2171.00	1293.80	0.00	95.90	3560.70

Note:

- i) *Other Contributions reflect a one-time upfront contribution which used to be collected by ICCL from Members towards Settlement Guarantee Fund ("SGF") at the time of admission to membership which has been discontinued since December 1, 2014. The SGF was replaced with the new Core SGF guidelines w.e.f. December 1, 2014.*
- ii) *Other Contributions also includes penalties levied by ICCL (as per Regulation 34 of SECC Regulations) till February 28, 2018.*
- iii) *Other Contributions of Currency Derivatives Segment ("CDS") also includes contribution made by the erstwhile United Stock Exchange of India Limited ("USE") towards SGF which has subsequently been merged into Core SGF of CDS of BSE pursuant to the scheme approved by the Hon'ble High Court for merger of USE with BSE.*
- iv) *\*Additional Contribution denotes the quantum of excess resources in Core SGF from BSE towards their compliance with the requirement of 'Transfer of Profits' under Regulation 33 of SECC Regulations*

2012, from the date the SECC Regulations, 2012 came into effect till August 29, 2016, and which has not been allocated to any specific segment.

### *Investment Policy for Core SGF*

ICCL follows prudential norms of Investment policy for Core SGF corpus to ensure that Core SGF corpus is invested in highly liquid financial instruments with minimal market and credit risk and is capable of being liquidated rapidly with minimal adverse price effect.

ICCL broadly invests in the following:

- a) Fixed Deposit with Banks [only those banks which have a net worth of more than Rs. 5 billion and are rated A1 (or A1+) or equivalent];
- b) Central Government Securities; and
- c) Liquid schemes of debt mutual funds.

Investment in liquid scheme of debt mutual funds shall not exceed a limit of 10% of the total investible resources held by ICCL, at any point in time.

ICCL ensures that the financial instruments in which the Core SGF corpus is invested remains sufficiently diversified at all times.

### *Default Waterfall*

ICCL also maintains a dedicated Default Waterfall for each segment i.e. Equity Cash Segment, Equity Derivatives Segment, Currency Derivatives Segment and Debt Segment, effectively ring fencing each segment of ICCL from defaults in other segments. The Default Waterfall outlines the hierarchy along with the quantum of resources available in each layer of the default waterfall and is published on the ICCL website.

## Resources in each layer of Default Waterfall

April 2018 (Rs. Million)						
Sl. No.	Description	Equity Cash Segment	Equity Derivative Segment	Currency Derivative Segment	Debt Segment	
1.	Monies of defaulting member (including defaulting member's primary contribution to Core SGF(s) and excess monies of defaulter in other segments)	As applicable	As applicable	As applicable	As applicable	
2.	Insurance, if any	3900.00				
3.	Clearing Corporation resources (equal to 5% of the segment MRC)	88.30	7.30	37.40	0.00	
4.	i. Penalties ii. Clearing Corporation contribution to the extent of at least 25% of the segment MRC. iii. Remaining Core SGF: Clearing Corporation contribution, Stock Exchange contribution and non-defaulting clearing members' primary contribution to	1934.00	179.80	860.20	13.70	

	Core SGF on pro-rata basis				
5.	Proportion of remaining Clearing Corporation resources (excluding Clearing Corporation contribution to core SGFs of other segments and Rs. 1000 millions) equal to ratio of segment MRC to sum of MRCs of all segments.	1274.30	104.70	540.00	0.00
6.	Clearing Corporation/Stock Exchange contribution to Core SGFs of other segments (after meeting obligations of those segments) and remaining Clearing Corporation resources to that extent as approved by SEBI.	2267.50	5225.70	4127.10	5503.10
7.	Capped additional contribution by non-defaulting clearing members of the segment.	1394.00	133.00	89.00	35.00
8.	Any remaining loss to be covered by way of pro-rata haircut to pay-outs	As applicable	As applicable	As applicable	As applicable

*The quantum of CC resources is based on financial results for the year ended December 31, 2017.*

*\* ICCL limits the additional contribution by non-defaulting members in Layer 7 to Rs 1 million per member, across segments. ICCL has 1421 unique members, hence the maximum additional contribution that can be called from members, across segments is limited to Rs. 1.42 billion.*

## Membership of ICCL

ICCL offers clearing membership for various segments. ‘Clearing Member’ of ICCL is a person having clearing and settlement rights in ICCL. A Clearing Member can be of various types such as Professional Clearing Member (“**PCM**”), Trading cum Clearing Member (“**TCM**”) and Self-Clearing Member (“**SCM**”).

As discussed, a TCM is person who has trading rights in BSE and clearing and settlement rights in ICCL. A TCM membership allows a member to execute trades and to clear and settle the trades executed on its own account as well as on the accounts of its client and to clear and settle trades executed by other Trading Members who choose to use its clearing services. A PCM membership allows a member to clear and settle trades of such Trading Members who choose to clear and settle their trades through this member. An SCM is a Clearing Member who is also a Trading Member and clears and settle trades on its own account and on its clients’ account but cannot clear and settle trades of other Trading Members.

The Clearing Members of ICCL are governed by the Rules, Bye-laws and Regulations of ICCL made pursuant to the SECC Regulations. Rule 18 of ICCL provides for conditions precedent for admission as a member of ICCL. ICCL confirms compliance with these requirements through an initial application process, in which an applicant is required to furnish declarations, confirmations and such other documents or papers as specified by ICCL. On being satisfied that all other terms and conditions and other requirements for the clearing membership have been complied with, ICCL may admit the applicant as a member. The requirements for membership of ICCL have been annexed hereto as **Annexure 69**.

## Collateral and Risk Management Systems

ICCL handles the technical processing and settlement tasks required to be executed for trades conducted on BSE. ICCL plays the role of a Central Counter Party, which involves not only trade management, but also sophisticated risk management process. ICCL uses cutting-edge technology for the clearing and settlement process. It uses the Collateral System (“**CLASS**”) which keeps track of the collateral deposited by the Clearing Members with ICCL on a real-time basis and uses the Real-Time Management System (“**RTRMS**”) which accept trades from the trading engine on a real-time basis.

CLASS maintains the utilised and unutilised collateral for all members; asset-wise and instrument-wise, with valuation done after applying applicable haircut. It is made available to the members on a free-of-cost basis through which they can themselves, add collateral, withdraw excess unutilised collateral or transfer the excess unutilised collateral to other segments.

ICCL employs RTRMS which is a robust real-time risk management system in which the permissible exposure for a Clearing Member is based on the collateral deposited by the member with ICCL. It calculates the margin on a near real-time basis and blocks it in CLASS. It is made available to the members on a free-of-cost basis through which they can monitor their risk profile as well as the risk profile of their trading members and the clients. The RTRMS generates various alerts at different collateral utilization levels (70%, 80% and 90%) and disables the trading terminal of a member when the collateral utilization exceeds 100%.

ICCL ensures that the members are mandatorily put in risk-reduction mode when 90% of the member's collateral available for adjustment against margins gets utilized on account of trades that fall under a margin system. Such risk reduction mode includes the following:-

- a. All unexecuted orders are cancelled once the member breaches 90% collateral utilization level.
- b. Only orders with Immediate or Cancel attribute are permitted in this mode.
- c. All new orders are checked for sufficiency of margins.
- d. Non- margined orders are not accepted from the member in risk reduction mode.
- e. The member is moved back to the normal risk management mode as and when the collateral of the stock broker is lower than 90% utilization level.

ICCL has established a robust risk management framework which utilises a VaR model for margining of Equity Cash Segment and a risk based SPAN (Standard Portfolio Analysis of Risk) model for all its derivatives transactions, namely equity derivatives, currency derivatives and interest rate derivatives. ICCL aims to provide secure, capital-efficient counterparty risk management and post-trade services. Further, about twenty banks have been empanelled as clearing banks for providing clearing and settlement services for trades executed on the BSE platform; the aggregate lines of credit being more than the average daily funds pay-out.

In short, ICCL has multiple shock absorbers in the system to minimize the chance of a default cascading into a systemic issue for the market. Default by a client results in the trading member absorbing the consequences of such default. Default by a trading member is similarly absorbed by the clearing member. In addition, capital and margin requirements along with the cushion of a trade guarantee fund which acts as a counter party to every trader ensures smooth, timely and risk free clearance and settlement. The trade guarantee fund is further bolstered by an insurance policy if it were to be depleted. Finally, the Indian Supreme Court has held the supremacy of the clearing corporation when a default occurs, and even the tax claims are subordinate to the exchange's claims on the assets of a defaulting member.

### ***Conclusion***

Based upon the foregoing, we hereby respectfully request that BSE be designated as a designated offshore securities market within the meaning of Rule 902(b) for the purposes of Regulation S. We submit that BSE's application for designation is deserving on its merits, furthers BSE's goals of fostering competing marketplaces and investor protection by ensuring that investors availing themselves of Rule 904 will receive the best available prices in accordance with Indian trade-through protections. BSE is subject to extensive oversight and regulation in India and follows best practices in line with international marketplaces. BSE has always focused on new business opportunities, product and service innovation, upgrades in technology, increased investor and member protection.

BSE seeks to continually improve and adopt new and better ways of conducting its business and to undertake various initiatives to build on its strong brand, legacy and market position to create value for its stakeholders and the financial system. The designation under Regulation S as a designated offshore securities exchange or market will strengthen its role in that capacity. In light of the greater cross-border trade and cross-market linkages being witnessed due to the globalization of financial markets, recognition as a DOSM will be a significant step in furthering Indo-US understanding and co-operation also.

If you have any questions or require additional information regarding this application, please do not hesitate to contact the undersigned at +91-22-62363181 or [sandeep.parekh@finseclaw.com](mailto:sandeep.parekh@finseclaw.com).

Yours faithfully,

  
Sandeep Parekh