

Annexure 1

Guidelines to Clearing Members for effective oversight over trading members cleared by Clearing Members

The model CM-TM agreement provides rights to the Clearing Members to call for information from and inspect the trading members. The following guidelines are issued to CMs for effective oversight over TMs cleared by CM:

a. Monitoring payin timelines by the TMs

CM should monitor the payin timelines by the TM and regular delayed receipt of payins/ repeated instances of shortfalls be dealt with in accordance with the Risk Management Policy of the Clearing Member

b. Monitoring penalties levied to clients of the Trading Members:

The CM should analyse the data of the Trading Members such as repeated instances of penalties being levied to the clients of TM for client margin reporting.

c. Seeking data of debit balances of Trading Member's clients

CM should seek data with respect to debit balances of clients from Trading Member and review the exposure allowed by the TM and direct the TM to restrict / reduce exposure for such clients.

d. Monitoring misuse of client collaterals by TM for proprietary trading

The CM should ensure that the TM does not commingle client collateral with the proprietary collateral and that it provides separate collaterals for proprietary positions out of own funds only and not from the client collaterals. The inspection of TM should cover this aspect

e. Correctness of data submitted by TMs to CM

TMs submit various data to the CM, which may be submitted by the CM to Exchange/CC. The CM should assess the correctness of the data submitted by the TMs to CM.

f. Inspection of TMs

It is recommended that the CM carry out inspections of Trading Members, covering atleast 1/3rd of the TMs cleared by it each year in order to cover all TMs over a period of 3 years. Additionally, CM may also conduct surprise inspection based on any rumours / adverse news in the media about the TM or any other concern/ alerts as arising out of the above points by the CM during the course of business.

g. Formation of Risk Management Committee / Board Approved Committee for monitoring the risks

The CMs should be required to form a Risk Management Committee / Board Approved Committee to monitor the various risks in the business. A periodic report (monthly or atleast quarterly) for the TMs for which it has undertaken the clearing activity should be submitted to such Committee.

h. Reporting of alerts by Clearing Members: Clearing Members should be reporting the concerns identified by them during the oversight over Trading Members to the concerned Clearing Corporation, which in turn would report the same to the concerned Exchange for further action.

i. Internal Audit of Clearing Members: NCL has along with other Clearing Corporations (ICCL and MCCIL) introduced a requirement for Clearing Members to adopt a Risk Management Policy duly approved by the Board / Board Approved Committee in July 2020. It has been mandated that the Risk Management Policy of Clearing Members should cover mandatorily the following points:

- i. Internal escalation matrix with respect to non-compliances / defaults by TMs/CPs
- ii. Performance evaluation process of TMs/CPs registered with the CMs including its periodicity
- iii. Seeking data information from TMs/CPs in the event of repeated cases of shortfall in margins / margins on Consolidated Crystallised Obligation or governance issues
- iv. Procedures for segregation of TM proprietary and Client collaterals
- v. Inspection of TMs
- vi. Upper Cap for acceptance of securities from a member and / or across all members in absolute terms and / or on an overall basis to avoid concentration risk
- vii. List of banks from which FDRs and BGs shall be accepted
- viii. List of securities that shall be accepted as collaterals
- ix. Components of cash collateral and non-cash collateral
- x. Ratio of Cash and Non-cash component of collateral
- xi. Haircut percentage for all types of collaterals other than Cash, FDRs and BGs.
- xii. Securities subject to a minimum of VAR and other collateral shall be subject to minimum haircut of 10%
- xiii. Timelines and threshold limits beyond which action such as square off of positions shall be undertaken by CM for non-payment of margins on Consolidated Crystallised Obligation by the TMs/CPs.

The Clearing Members shall submit an internal audit report, providing compliance to on all the above points (a to i). Additionally, the internal audit report should cover the following points:

- i. Confirmation on reporting of TM/CP level fund shortfall beyond Rs 5 lacs to CC as per the timelines prescribed by CC
- ii. Invocation of pledged securities by the Clearing Member was carried out only in respect of debit balance clients

The Internal Audit shall be conducted only by independent qualified Chartered Accountants or Company Secretaries or Cost & Management Accountants who are in practice and do not have any interest in or relation with the Member other than the Internal Audit assignment. The report shall be submitted on half yearly basis for April to September and October to March, within 2 months from the end of the half year. The points referred herein above can be clubbed with the half yearly internal audit report submitted by the Members.