



**Before the  
Member and Core Settlement Guarantee Fund Committee  
("MCSGFC"/"Committee")  
of  
National Stock Exchange of India Limited  
Exchange Plaza, Bandra-Kurla Complex, Bandra East, Mumbai – 400051  
held on August 24, 2022**

**In the matter of the Trading Member M/s. HDFC Securities Limited**

**CORAM:**

Ms Mona Bhide	- Chairperson
Ms Anuradha Rao	- Committee Member
Mr Ranganayakulu Jagarlamudi	- Committee Member
Mr Ashishkumar Chauhan	- Committee Member

**ALSO PRESENT:**

Ms Priya Subbaraman	- Chief Regulatory Officer
Mr Suresh Nair	- Vice President – Enforcement
Ms Renu Bhandari	- Vice President – Inspection

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**BACKGROUND**

1. M/s.HDFC Securities Limited ("**HDFC Securities**") is a Trading Member registered with the National Stock Exchange of India Limited ("**NSEIL**"/"**Exchange**") and enabled for trading in the Capital Market ("**CM**") segment since September 2000, Futures & Options ("**F&O**") segment since May 2001 and Currency Derivatives ("**CD**") segment since August 2008.
2. The Exchange conducted a limited purpose inspection of the HDFC Securities's books and records on April 21, 2022, and April 27, 2022, covering the period from October 01, 2021, to March 31, 2022, to verify whether HDFC Securities had collected penalties for short/non-collection of upfront margins from the clients, directly or indirectly.

3. Post-inspection, the Exchange issued a Letter of Observation bearing reference No.NSE/INSP/LPI//22-23/LO/11094 dated May 26, 2022 ("**LO**") to HDFC Securities for the observed non-compliance of regulatory provisions with respect to passing of penalty on short reporting of margins to its clients. HDFC Securities, vide email dated July 12, 2022, replied to the SCN.

### **INSPECTION OBSERVATIONS/ALLEGED VIOLATIONS**

4. The observations/alleged violation mentioned in the LO are summarized hereunder:
  - 4.1 Passing on penalty for short/non-collection of upfront margins to clients in 26 instances of 26 clients involving Rs.95,68,063/- in the F&O segment, and 8 instances of 8 clients involving Rs.1,839/- in the CD segment, out of 90 clients selected for sample scrutiny across CM, F&O and CD segments.

### **REGULATORY PROVISIONS**

5. At the outset, it is appropriate to refer to the relevant regulatory provisions alleged to have been violated by HDFC Securities, extracts whereof are reproduced below:
  - 5.1 Exchange Circular NSE/INSP/45191 dated July 31, 2020

Question no. 15 in Annexure A

*In case of short reporting of margin/margin on consolidated crystallized obligation/MTM, Can Member pass on the penalty to the clients?*

*In case of failure (cheque not cleared or margin\* requirement not met by the client) on part of the client resulting which penalty is levied by the Clearing Corporation on the Member for short reporting of client upfront margins/ margin on consolidated crystallized obligation/MTM losses, Member may pass on the actual penalty to the client, provided he has evidences to demonstrate the failure on part of the client .Wherever penalty for short reporting of upfront margin/ margin on consolidated crystallized obligation/ MTM losses is being passed on to the client relevant supporting documents for the same should be provided to the client.*

*\*Member cannot pass on the penalty w.r.t. short collection of upfront margins to client.*

## 5.2 Exchange Circular NSE/INSP/49929 dated October 12, 2021

*In view of the above, it is reiterated that members are not permitted to pass on the penalty levied by clearing corporations on account of “short/non-collection of upfront margins” to clients under any circumstances.*

*Further, clarification to Question no. 15 in Annexure A of the Exchange Circular NSE/INSP/45191 dated July 31, 2020, has been partially modified as below:*

*15. In case of short reporting of margin/margin on consolidated crystallized obligation/MTM, Can member pass on the penalty to the clients?*

*Member shall not pass on the penalty w.r.t short collection of upfront margins to clients under any circumstances. In case of failure (requirement not met by the client) on part of the client resulting which penalty is levied by the Clearing Corporation on the member for short reporting of margins other than “upfront margins” such as consolidated crystallized obligation, Delivery margins, other margins (Mark-to-market & additional margins), member may pass on the actual penalty to the client, provided he has evidence to demonstrate the failure on part of the client. Wherever penalty for short reporting of margins other than “upfront margins” is being passed on to the client relevant supporting documents for the same should be provided to the client.*

## **PREVIOUS MCSGFC REFERENCE**

6. HDFC Securities was given an opportunity for personal representation before the Committee vide email dated July 6, 2022. HDFC Securities vide email dated July 12, 2022, requested an adjournment.

## **PRESENT PROCEEDINGS BEFORE MCSGFC**

7. The Exchange, vide email dated August 18, 2022, provided HDFC Securities with an opportunity for a personal hearing before the Committee. On behalf of HDFC Securities, Mr.Murli Karkera, Compliance Officer and Mr.Yatin Sawant, Vice

President, attended the personal hearing and made the following oral submissions:

- a. HDFC Securities provides online platform to its clients and its risk management systems are automated to ensure that no orders are executed without collecting upfront margin in advance of the trade in compliance with the provisions of SEBI Circulars dated November 19, 2019, and July 20, 2020.
- b. Thereafter, SEBI had come up with a framework on collection of peak margins. There were some practical difficulties in implementing the same. For e.g., there was increase in the margins during the day due to market movement/volatility. In such cases, it was practically difficult for brokers to predict the margin requirements during the day or at the end of the day.
- c. Based on the representations received from the brokers, SEBI vide circular dated May 10, 2022, had revised the modalities wherein SEBI prescribed the computations of peak margins will be based on beginning of the day ("BOD") risk parameters. The said circular is applicable with effect from August 1, 2022.
- d. In the backdrop of the above, with respect to the observation on passing on penalty for short/non-collection of upfront margins to clients HDFC Securities submits that there was no fault on the part of HDFC Securities since it had ensured that upfront margins are collected from clients in advance of the trade in compliance with the SEBI Circulars. It had stopped the clients from placing further orders in case of non-availability of upfront margins, as a prudent broker.
- e. For the margin increase during the day post the trade execution due to market volatility etc., HDFC Securities had attempted to inform its clients to bring in funds, but there were margin shortfalls.
- f. A penalty of approx. Rs.8 crores of approx. 10000 clients was levied on HDFC Securities for margin short collection from October 2021 onwards.

## **CONSIDERATION & FINDINGS**

8. The observations/alleged violation, HDFC Securities's reply, and the findings of the Committee are as under:

## 8.1 Passing on penalty for short/non-collection of upfront margins to clients

- a. Upon verification of the client ledgers and PNL01 files containing the penalty details for short/ non-reporting of margins, it was observed that HDFC Securities has passed on short reporting penalty to its clients for the period from October 1, 2021, to March 31, 2022, in 26 instances of 26 clients involving Rs.95,68,063/- in the F&O segment and 8 instances of 8 clients involving Rs.1,839/- in the CD segment out of 90 clients selected for sample scrutiny across CM, F&O and CD segments. The total instances
- b. In reply to the LO, HDFC Securities submitted as under-
- i. HDFC Securities has not passed on the penalty levied by Clearing Corporation on account of "Short collection/non-collection of upfront margins" to the clients in accordance with the Exchange circulars No. NSE/INSP/45191 dated July 31, 2020, and NSE/INSP/49929 dated October 12, 2021.
  - ii. HDFC Securities has collected upfront margins in advance of trades.
  - iii. Further appropriate haircut % (in the range of 35% - 40%) is applied on the securities accepted as collateral by way of margin pledge. It is to be noted that the haircut applied on the collateral is much higher than Exchange VaR. This ensures that there is some cushion/buffer amount to account for any increase in the margins due to volatility.
  - iv. For example, client code 2961590, a penalty of Rs.4.44 lakhs were levied for March 25, 2022. The said client had open positions created on February 16, 23, 24 and March 4, 2021. HDFC Securities confirms that the margins required for the above positions were sufficient and reported to the Exchange. Further, due to volatility during the day on March 25, 2022, while there was no new transaction entered by the client, there was an increase in margin in the snapshot of the Exchange. Accordingly, fund hold for additional margin of Rs. 75.33 Lacs was initiated from the client's linked bank account. However, due to insufficient additional margins, there was shortfall in the account and the same was reported to the Exchange.
  - v. This shortfall penalty as received from the Exchange for additional margin post execution of trade due to increase in volatility and non-fulfilment from the client was passed on the client.

c. The Committee finds as under:

- i. HDFC Securities has claimed that it has passed on the penalty as received from the Exchange for additional margin post execution of trade due to increase in volatility and non-fulfilment from the client.
- ii. In this regard, it was observed that SEBI has issued the circulars on Collection and Reporting of Margins by Trading Member (TM) / Clearing Member (CM) in Cash Segment from time to time. SEBI Circular no. CIR/HO/MIRSD/DOP/CIR/P/2019/139 dated November 19, 2019, and SEBI/HO/MIRSD/DOP/CIR/P/2020/146 dated July 31, 2020, prescribes the collection and reporting of margin. SEBI has further clarified the same with respect to other penalties by its circular no. SEBI/HO/MIRSD/DOP/CIR/P/2020/173 dated September 15, 2020. Accordingly, the Exchange has issued the circular providing guidelines/clarifications on margin collection and reporting from time to time.
- iii. The conjoint reading of all three circulars clearly brings to the fore that the upfront margin has to be collected as stipulated by the Stock Exchanges. However, the SEBI has also considered the representation of the various stakeholders and has also prescribed the situations/conditions when the penalty would not be applicable.
- iv. SEBI has issued Master Circulars from time to time for Stock Exchange and Clearing Corporation wherein the importance of comprehensive risk management has also been explained. In this context, SEBI Master Circular no. SEBI/HO/MRD2/MRD2\_DCAP/P/CIR/2021/0000000591 dated July 5, 2021, vide provisions under clause 1.1.19 under Chapter 4 under the heading "Margin from Clients" has stressed the importance of having a prudent system of risk management. The relevant provisions are quoted below:

#### ***1.1.19. Margins from the Client***

*Members should have a prudent system of risk management to protect themselves from client default. Margins are likely to be an important element of such a system. The same shall be well*

*documented and be made accessible to the clients and the Stock Exchanges. However, the quantum of these margins and the form and mode of collection are left to the discretion of the members.*

- v. On verification of margin files as per Exchange records, for 5 sample clients involving penalty of Rs.52.82 Lakhs which was passed on to the clients, the Exchange observed that, in 4 instances involving Rs.47.89 Lakhs, the margin shortfall was on account of short collection of peak margins, and in 1 instance, the penalty was pertaining to delivery margin.
- vi. From the above Circulars, it is evident that the prescription of margin and the onus of collecting them in the manner prescribed is in the interest of the investors and Trading Members. The quantum of these margins, the form and the mode of the collection are left to the Trading Members' discretion. As such, the trading members must put in place an appropriate risk management system to ensure that the compliances with respect to margin are met.
- vii. Therefore, in 4 instances, HDFC Securities's contention that the margin shortfall was on account of short collection of peak margins is not acceptable, in absence of any evidence to demonstrate the failure on part of the clients to pay margins.
- viii. For the remaining 1 instance, the penalty that was passed on to the client was on MTM margins. Exchange circular no.NSE/INSP/45191 dated July 31, 2020, allows the Member to pass on the actual penalty to the client, on MTM losses/margins. Hence HDFC Securities's claim for transfer of penalty to the client is acceptable.
- ix. The revised total irregularity persists for 33 instances involving Rs.95.79 Lakhs in the F&O and CD segments.
- x. HDFC Securities, by passing on the upfront margin penalty to its clients, has violated the provisions of the Exchange Circular NSE/INSP/45191 dated July 31, 2020, and Exchange circular no. NSE/INSP/49929 dated October 12, 2021.

## DECISION

9. In view of the above, the Committee directed HDFC Securities to return any penalty collected from the clients on account of short collection of upfront margins to the respective clients. Further, HDFC Securities is warned to ensure non-recurrence of the observed violation.

Sd/-  
Mona Bhide  
(Chairperson)

Sd/-  
Anuradha Rao  
(Committee Member)

Sd/-  
Ranganayakulu Jagarlamudi  
(Committee Member)

Sd/-  
Ashishkumar Chauhan  
(Committee Member)

Date: September 16, 2022