



CIRCULAR

SEBI/HO/MRD/MRD-PoD-3/P/CIR/2022/173

December 16, 2022

To

All Recognized Clearing Corporations

All Recognized Stock Exchanges

All Registered Clearing Members through Clearing Corporations

Dear Sir/Madam,

Subject: Framework for Orderly Winding Down of Critical Operations and Services of a Clearing Corporation

- A. In order to enable the Clearing Corporations (CCs) to have a framework for orderly winding down of critical operations and services, Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2018 (SECC Regulations, 2018) have been amended vide Gazette Notification No. SEBI/LAD-NRO/GN/2022/104 dated November 15, 2022.
- B. In this regard, it has been decided that the CCs shall have a policy framework for orderly winding down of their critical operations and services, which shall at least contain the following provisions:

1. **Identification of Potential Scenarios**

The scenarios which may potentially prevent a CC from being able to provide its critical operations and services as a going concern and may lead to wind down of its critical operations and services, shall be identified. Some of the reasons for winding down of CC can be:

- 1.1. Voluntary: The CC is solvent and is able to meet all its obligations towards Clearing Members (CMs) as well as other creditors; however, wishes to wind down its critical operations and services and exit as a strategic or business decision.
- 1.2. Involuntary: The winding down of critical operations and services on involuntary basis may be due to various factors including but not limited to the following:
- 1.2.1. Losses due to default by CM(s): The default management resources maintained by the CC may get exhausted due to default by CM(s), and,



consequently, the CC fails to fulfil its obligations towards CM(s) and/or its constituents.

1.2.2. Losses due to other factors: There is no CM default and the settlements have been happening in a timely manner; however, the solvency of a CC may get adversely affected as a result of some large operational expenses, legal expenses, business or investment losses, etc. thereby rendering a CC unable in fulfilling its obligations to CM(s), its constituents and/ or other creditors.

1.2.3. Regulatory Actions: Directions to a CC to wind down its critical operations and services by SEBI or any other statutory authority under applicable laws. SEBI may direct a CC to wind down its critical operations and services including but not limited to the following scenarios:

i. A CC shall be required to continuously meet the annual clearing turnover, aggregated across segments, including by way of interoperability, of at least INR 1,000 Cr. per annum or any other amount as may be specified by SEBI from time to time. In case the CC fails to meet the aforesaid requirement for two consecutive years, it shall be liable to exit and accordingly, apply for orderly winding down of its critical operations and services.

Provided that the above threshold condition shall not be applicable to a CC for a period of 5 years from the date of grant of recognition.

In case where the CC does not apply for voluntary winding down of critical operations and services, pursuant to breaching the minimum turnover threshold as mentioned above, SEBI may proceed with compulsory de-recognition of such CC under applicable laws.

ii. SEBI may also direct a CC to wind down its critical operations and services in case of non-compliance of either the conditions of grant of recognition or renewal, wherever applicable; or any other condition under the applicable laws.

2. Identification of Critical Operations and Services of CCs

2.1. To identify the operations and services which may be classified as critical, CCs shall, *inter alia*, consider their risk profile, operations, organizational structure,



financial resources, business practices, interconnectedness and interdependencies, and any other relevant factor as deemed appropriate. As timely clearing and settlement of trades is a core function of CCs, the operations and services such as collateral management, risk management, clearing and settlement, etc. shall be deemed to be critical.

2.2. Further, the contractual obligations of CCs with CMs, Stock Exchanges, Depositories and other CCs, arising out of clearing and settlement of trades, shall necessarily be classified as critical or essential.

3. **Standard Operating Procedure (SOP)**

3.1. The policy framework of CCs shall contain a Standard Operating Procedure (SOP) duly approved by their governing board, *inter alia*, outlining the manner in which the critical operations and services of the CCs shall be carried out in an orderly manner so as to not cause any disruption to the financial system, upon triggering of any of the scenarios as mentioned at paragraphs 1.1 and 1.2 above. A notice or intimation regarding winding down of critical operations and services shall be issued by the CC as and when the scenarios get triggered, with prior approval of SEBI.

3.2. The SOP shall, *inter alia*, include details of infrastructure and premises, technological systems including back-up, outsourcing activities/ vendors/ service providers, etc. which would need to be retained or continued for orderly winding down of critical operations and services. The SOP shall also contain details of key employees or staff members, along with their roles and obligations, etc., who shall be retained and responsible for development, review, and ongoing monitoring etc. of the critical operations and services, once the process of orderly winding down of critical operations and services is initiated.

3.3. The CCs shall include the operational modalities relating to transfer or close-out of positions, collateral, etc. in detail considering interoperable or non-interoperable scenarios as applicable, while framing their policy for orderly winding down of critical operations and services. Broad guidelines in this regard are as under:

3.3.1. Voluntary Winding Down – Voluntary winding down of a CC shall be approved by the governing board, its shareholders and SEBI. The CC shall inform the members and the market regarding its decision to wind down voluntarily and shall also mention a sufficient notice period (at least six months) for such winding down, after prior approval of SEBI, so as not to



have a significant impact in financial system. Since the CC shall be solvent, it shall have the choice of continuing full range of operations or providing only critical services during the notice period. However, the CC shall continue to provide at least the critical services during the notice period. Once the winding down process is initiated, any open positions of the CMs and/ or its constituents at the exiting CC shall have to be transferred to the new CC where the CMs become member within the notice period. Any open positions within the notice period that could not be transferred shall be closed-out at the daily settlement price and in terms of the provisions of the Rules, Bye-laws and Regulations of the exiting CC.

3.3.2. Involuntary Winding down (due to default by CM(s) or due to other factors) - The procedure for winding down shall be as follows:

- i. The CC shall announce a termination date, with prior approval of SEBI.
- ii. The CMs who have open positions may change their designated CC, or close-out their open positions.
- iii. All open positions, if any, shall expire at the daily settlement prices of the termination date.

3.3.3. Involuntary Winding down due to regulatory action - In this case, SEBI on case to case basis may issue appropriate directions for winding down.

4. The provisions of SECC Regulations, 2018 and various circulars and guidelines issued thereunder, shall continue to apply during the entire period of winding down of critical operations and services of CCs. This shall be mentioned in the policy framework of CCs. The framework shall be (i) periodically reviewed, at least on an annual basis, and (ii) published or disclosed on the website of the CC (excluding any confidential details).

5. Return of Assets

5.1. The exiting CC shall be permitted to distribute its assets subject to conditions as laid down in its framework, guidelines issued by SEBI from time to time, or any other direction issued by SEBI or any other statutory authority.

5.2. For the purpose of valuation of the assets of the CC, a valuation agency may be appointed by SEBI.



5.3. The quantum of assets available for distribution shall be arrived at after payment of statutory dues, including applicable taxes; contribution to SEBI as specified in para 5.4 and 5.5 below, return of refundable collateral and membership deposits of CMs, return of deposits to warehouse service providers, if any, and the unutilized Core SGF contributions of CMs and Stock Exchanges, as the case may be, depending upon the scenario triggering winding down of critical operations and services.

5.4. Subsequent to exit, the CC shall also be required to contribute upto 20% of its assets (after applicable taxes) towards SEBI Investor Protection and Education Fund (IPEF) in order to provide for settlement of any claims pertaining to pending arbitration cases, unresolved complaints or grievances lying with the CC, etc. The contribution percentage may be decided by SEBI taking into account relevant factors such as the governance standards of the CC, estimation of future liabilities, etc.

5.5. The CC shall pay following dues to SEBI:

- i. The dues outstanding to SEBI;
- ii. The outstanding fees of CMs of such exiting CC till the date of such exit:

In this regard, the CC shall recover the dues of the CMs to SEBI out of the CMs' own deposits/ capital/ share of sale proceeds/ winding down proceeds of CC, etc. available with the CC. The CC shall be liable to make good any shortfall in collection of dues of CMs to SEBI.

5.6. Penalties collected from CM(s), issuer(s) contribution in case of Limited Purpose Clearing Corporation (LPCC), and interest on these components, forming part of Core SGF shall be used by the CC in a manner as specified by SEBI from time to time.

5.7. An exiting CC shall not alienate any assets without taking prior approval of SEBI.

6. **Financial Resources**

6.1. Regulation 14(3)(b) of SECC Regulations, 2018 stipulates that every CC shall hold additional capital to cover costs required for orderly winding down or recovery of operations. Further, SEBI vide circular dated April 10, 2019 has, *inter alia*, stipulated that while computing the capital requirements for winding down, a CC shall consider a minimum time span of six months for ensuring an orderly winding



down or restructuring of its activities and thus, hold liquid net assets equal to at least six months of gross operational expenses.

6.2. As the instant policy proposal is intended to serve the purpose as envisaged under the above mentioned regulatory provisions, the said capital requirements for CCs shall be required to be maintained at all times, and shall be used for carrying out critical operations and services of the CCs, once the process of orderly winding down of critical operations and services is initiated.

7. Oversight

The Regulatory Oversight Committee (ROC) of the CC shall oversee the implementation of steps or processes involved in orderly winding down of critical operations and services of the CC and shall submit a report to SEBI after approval from the governing board, in a manner as may be specified by SEBI, upon completion of necessary steps or processes.

8. Directions to be issued by SEBI

Appropriate directions by SEBI shall be issued to CCs for orderly winding down of their critical operations and services.

C. Obligations of Exchange(s) and Clearing Member(s)

1. For non-interoperable segments, if the exchange (whose trades are cleared by the exiting CC) intends to continue to offer trading in the concerned segment(s), then it shall engage with another clearing corporation within the notice period.
2. For both non-interoperable and interoperable segments, the CMs of exiting CC shall have to become members of new or another CC within the notice period. Alternatively, such CMs may close-out their open positions within the notice period.

D. Modification to SEBI circular on Core-SGF dated August 27, 2014

1. With regard to paragraph 6.1 above, it may be noted that the existing regulatory provision in SEBI circular No. SEBI/HO/MRD/DRMNP/CIR/P/2019/55 dated April 10, 2019, stipulates that while computing the capital requirements for winding down, a CC shall consider a minimum time span of six months for ensuring an orderly winding down or restructuring of its activities and thus, hold liquid net assets equal to at least six months of gross operational expenses.



2. Since the abovementioned capital requirement for carrying out winding down in an orderly manner shall be maintained by CCs at all times, clause V of paragraph 16 of SEBI circular No.CIR/MRD/DRMNP/25/2014 dated August 27, 2014 read with SEBI circular No.SEBI/HO/MRD2/DCAP/CIR/P/2020/01 dated January 03, 2020, on “Default Waterfall” of CCs has been modified as follows:

“Default waterfall

16. The default waterfall of CC for any segment shall generally follow the following order:

I.....

....

....

*V. Proportion of remaining CC resources (excluding CC contribution to core SGFs of other segments and higher of INR 100 Crore or the capital requirement towards orderly winding down of critical operations and services) equal to ratio of segment MRC to sum of MRCs of all segments. *”*

3. Similarly, clause VI of paragraph 16A of SEBI circular No. CIR/MRD/DRMNP/25/2014 dated August 27, 2014, read with SEBI circulars bearing No. SEBI/HO/MRD2/DCAP/CIR/P/2020/01 dated January 03, 2020 and No. SEBI/HO/MRD2/DCAP/CIR/P/2020/245 dated December 21, 2020, pertaining to “Default Waterfall of LPCC” has been modified as follows:

“Default waterfall of LPCC

16A) The default waterfall of CC shall generally follow the following order –

I....

...

....

*VI. Remaining LPCC resources (excluding higher of INR 100 Crore or the capital requirement towards orderly winding down of critical operations and services). *”*

E. Applicability:

The CCs shall have the policy framework containing the SOP duly approved by their governing boards and make it available on their websites within 90 days from the date of issuance of this circular.



भारतीय प्रतिभूति और विनिमय बोर्ड
Securities and Exchange Board of India

- F.** While the clearing members are advised to ensure compliance with the relevant provisions of this circular, Stock Exchanges and Clearing Corporations are directed to take necessary steps to put in place proper systems and procedures, including necessary amendments to the relevant bye-laws, rules and regulations.
- G.** This circular is issued in exercise of the powers conferred under Section 11(1) of the Securities and Exchange Board of India Act 1992, read with Section 10 of the Securities Contracts (Regulation) Act, 1956 to protect the interest of investors in securities and to promote the development of, and to regulate the securities market.
- H.** This circular is available on SEBI website at www.sebi.gov.in at “Legal Framework - Circulars.”

Yours faithfully,

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