

QJA/SS/MRD/MRD-SEC-3/31405/2025-26

SECURITIES AND EXCHANGE BOARD OF INDIA

ORDER

Under Section 12A(2) read with Section 23GA of Securities Contracts (Regulation) Act, 1956 read with Rule 4 of the Securities Contracts (Regulations) (Procedure for Holding Inquiry and Imposing Penalties) Rules, 2005 in the matter of examination of Indian Clearing Corporation Limited.

Name of Noticee	PAN
Indian Clearing Corporation Limited	AABCI7140K

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1. India Clearing Corporation Ltd. ('ICCL') is a clearing corporation ('CCP') recognised and regulated by the Securities and Exchange Board of India (SEBI) and is responsible for clearing, settlement and risk management for the Bombay Stock Exchange Limited (BSE).
 2. SEBI conducted examination in the matter of Inter-CCP collateral to check whether ICCL was ensuring compliance with SEBI norms and the provisions of Interoperability Agreement under the interoperability framework. Pursuant to the examination, a letter dated July 21, 2023 was sent to ICCL informing it regarding the violations observed during the examination and initiation of quasi-judicial proceedings in the matter.
 3. Subsequently, a Show Cause Notice (SCN) dated November 21, 2023 was issued to ICCL which is the subject matter of instant proceedings. In the SCN, following allegations have been made:
 - 3.1. ICCL failed to maintain sufficient Inter CCP collateral from NSE Clearing Ltd (NCL) and ensure adequate risk management mechanism.
 - 3.2. ICCL failed to calculate additional capital applicable to NCL as per BASEL III guidelines required under the Inter CCP Agreement dated June 01, 2019 (hereinafter referred to as the 'Inter CCP Agreement').
 - 3.3. ICCL failed to ensure compliance with provisions of the Inter CCP Agreement with respect to frequency, timelines and determination of threshold amount of Inter CCP collateral.

3.4. ICCL failed to constitute Coordination Committee as per provisions of the Inter CCP Agreement.

4. In view of the above, it was observed that the ICCL failed to comply with the Regulation 7(4) (b) read with 12 (5) of Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2018('SECC Regulations'), para 5.2, 5.3 and 5.9 of the SEBI circular No. CIR/MRD/DRMNP/CIR/P/2018/145 dated November 27, 2018(hereinafter referred to as the 'Inter CCP circular'), Clause 'a' and 'j' of Part III of Schedule 4, Part IV of Schedule 4 and clause 20 of the Inter CCP Agreement dated June 01, 2019 during the period from April 2020 to April 2023 ('Examination Period').
5. Therefore, SEBI issued a show cause notice (SCN) SEBI/HO/MRD/MRD-SEC3/ P/OW/2023/46366/2 dated November 21, 2023 to ICCL calling upon it to show cause as to why an inquiry should not be held against it in the manner prescribed in SEBI (Procedure for Holding Inquiry and Imposing Penalties) Rules, 1995 ('SEBI Adjudication Rules') and SEBI Contracts (Regulations) (Procedure for Holding Inquiry and Imposing Penalties) Rules, 2005 ('SCRA Adjudication Rules') and why penalty should not be imposed under Section 23GA read with Section 12A (2) of the Securities Contracts (Regulation) Act, 1956 ('SCRA'), and Section 15HB read with Section 11B(2) of the of the Securities and Exchange Board of India Act, 1992 ('SEBI Act'), for the aforesaid violations.
6. The SCN was served upon ICCL on November 22, 2023. Thereafter, it proposed to SEBI for settlement of the proceedings under regulation 3(1) of the SEBI (Settlement Proceedings) Regulations, 2018 ('the Settlement Regulations'). In line with regulation 8(2) of the Settlement Regulations, the instant proceedings were kept in abeyance till the said settlement application was disposed. Meanwhile, ICCL requested for inspection of documents, which was provided to it on January 15, 2024. The application for settlement by ICCL was rejected by SEBI on November 11, 2024. Thereafter, ICCL filed its reply to the SCN on February 08, 2025. It also availed the opportunity of hearing on February 10, 2025 when Mr. P.N. Modi, Senior Advocate appeared on behalf of ICCL. Subsequently, the ICCL filed additional written submissions on February 20, 2025.
7. While reiterating all submissions made by ICCL in its written reply, Ld. Senior Advocate presented a written note and based on the same he pithily argued about purpose of Inter CCP collateral and that

interoperability is a new feature that commenced in June 2019. The Ld. Senior Advocate took me through the practical challenges in exchange of margin and collateral between CCPs, both in terms of frequency and manner of computation as envisaged in the Inter CCP Agreement. It was demonstrated that computation of Inter CCP margins and its exchange on a real time basis is impossible because of huge volumes of trading and constant changes in margin obligations and the fact that Inter CCP margins are by way of bank guarantees requiring Board approvals. It was also explained that from time to time, the queries raised by SEBI were duly responded to by ICCL with relevant details. In this regard, attention was drawn to ICCL's email dated January 05, 2023 to SEBI, wherein, ICCL, *inter alia*, stated that "*ICCL is not computing inter-CC collateral requirement based on inter-CC exposure. Currently ICCL is not computing the Risk based collateral as per the methodology as outlined the Credit Value Adjustment using standardized approach in Basel Standard. The same will be put in place shortly.*" Additionally, it was informed that by a joint representation to SEBI on November 01, 2023, the CCPs have made suggestions with respect to modifications required in the SOP for exchange of Inter CCP Collateral and margin and further clarifications to queries raised by SEBI (vide email dated February 20, 2024) and changes required in the SOP have been provided to SEBI by CCPs vide email dated February 22, 2024 and February 29, 2024, respectively. In view of the above, the Ld. Sr. Advocate argued that the matter and policy with respect to interoperability has not achieved finality even till now and this new feature of interoperability is a learning experience for both SEBI and CCPs.

8. Additionally, he reemphasised that certain documents were not furnished to ICCL during inspection, that the SCN was issued after filing of settlement application, that the purpose of inspection is remedial, that Section 23GA of SCRA cannot be applied in this case and that as per Enforcement Manual of SEBI, violations that can be remedied by corrective measures or first time violations (other than the cases where there is no ill-gotten gain or fraudulent and unfair trade practice affecting the market integrity or causing widespread losses to investors) may be dealt through administrative actions. He further submitted that there are no justifiable grounds or basis to conduct an inquiry against the ICCL or impose any penalties against it and the *bona fide* actions taken by it ought to be considered. Presently, the ICCL has in place a robust risk management mechanism which is reinforced by the SOP that outlines the framework for monitoring inter-CCP margins, inter-CCP collateral requirements and exchange of inter-CCP collateral, in line with the SEBI Circular. He pleaded that the proceedings against ICCL be disposed of without any adverse finding or impositions of penalty. He vehemently argued that no loss was caused to the investors and no gain made by the Noticee in relation to the allegations specified in the Notice and such

allegations do not have a market-wide impact nor do they affect the integrity of the market. According to him, the present case, assuming without admitting, that there were irregularities observed, these were not a continuing violation and do not represent a systemic failure on part of ICCL to fulfil its obligation as a CCP. Further, any irregularities observed never posed any real risk to clearing members. Hence, the same can amount to a technical violation at best, distinct from a substantial breach of the Act or Regulations, and as such can be dealt with by administrative/cautionary advice thereby not requiring imposition of any penalty under the SEBI Act. He relied upon judgement of Hon'ble Supreme Court in the matter of *Adjudicating Officer, SEBI vs Bhavesh Pabari*, wherein it has been held that the factors laid down in Section 15J of the SEBI Act are illustrative in nature. Factors other than those can also be considered in mitigating the quantum of penalty sought to be imposed on the Noticee. Further, Hon'ble SAT in the matter of *Jagdish Kumar Arora vs SEBI*, specifically held that when the violations are venial in nature, excessive penalty should not be levied on the entity. It was held as follows:

“The AO in paragraph No.23 found that the violation was venial in nature. But contended that since there was a statutory violation of the regulations and even though no undue profits or gains were made by the appellants, nonetheless, imposed a penalty of Rs.10lac...”

10. The AO itself has found that the violation is venial in nature. Venial means not very serious and the action which is pardonable or forgivable. Thus, imposition of a penalty of Rs.10 lac in the circumstance of the case appears to be too harsh and excessive.”

Further, it is also relevant to note the observations of Hon'ble SAT in *Piramal Enterprise Limited vs SEBI* that: *...SEBI is the watchdog and not a bulldog. If there is an infraction of a rule, remedial measures should be taken in the first instance and not punitive measures. ...”*

9. I have carefully considered the allegation in the SCN and all submission made by and behalf of ICCL. The submissions made by ICCL on each of the allegations in the SCN are considered specifically hereinafter. However, before considering the issues on merit, it would be appropriate to deal with the preliminary objections raised by ICCL.

Non- furnishing of relevant documents-

10. Relying upon the decision of the Hon'ble Supreme Court in the matter of *T. Takano v. SEBI* (Appeal Nos. 487-488 of 2022) and the observation of the Hon'ble Bombay High Court in its order dated March 11, 2024 in the matter of *Mr. Milind Patel v. Union Bank of India & Ors.* (Writ Petition No. 3671 of 2023) ICCL, ICCL has stated that its request for the original examination report and minutes of the NCL governing board meeting dated August 04, 2022 was rejected. Hence, principles of natural justice are violated. In this regard, it is settled position about supply of documents as held by Hon'ble Supreme Court in *T. Takano Vs SEBI* that:

- (a) As the purpose of disclosure of information targets both the outcome (reliability) and the process (fair trial and transparency), it would be insufficient if only the material relied on is disclosed.
- (b) Such a rule of disclosure only holds nexus to the outcome and not the process. Therefore, as a default rule, all relevant material must be disclosed.
- (c) It would be fundamentally contrary to the principles of natural justice if the relevant part of the investigation report which pertains to the appellant is not disclosed.
- (d) The Noticee has to be given a reasonable opportunity of hearing.
- (e) The requirement of a reasonable opportunity would postulate that such material which has been and has to be taken into account under Regulation 10 must be disclosed to the Noticee. If the report of the investigation authority under Regulation 9 has to be considered by the Board before satisfaction is arrived at on a possible violation of the regulations, the principles of natural justice require due disclosure of the report.

11. Further, as subsequently clarified by Hon'ble Supreme Court in *Kavi Arora v. SEBI* (Delivered on 149-2022), principles of natural justice do not require the supply of documents upon which no reliance is proposed to be placed by the authority setting the law into motion. If the documents sought to be relied upon, which are the basis of issuance of SCN, have been supplied to Noticees, then courts cannot compel authorities to supply documents that are not to be considered or relied upon. In this case, as the examination report which has been relied upon has been provided to ICCL, I find that the original examination report or the minutes of the NCL governing board meeting dated August 04, 2022 (which anyway is a third party document falling under the exception to rule prescribed under *T. Takano vs. SEBI*) is not relevant to the current proceedings. Hence, I find that this contention of ICCL is not tenable.

SCN issued after filing of application for settlement by ICCL

12. The SCN, in this case was issued on November 21, 2023, i.e., a day after the ICCL filed application for settlement of the proceedings on November 20, 2023. It has claimed that this is in noncompliance of regulation 8(2) of the Settlement Regulations, which says that no proceedings shall be initiated till the settlement application is rejected or withdrawn. Thus, the SCN is void *ab initio*. There is no dispute that the SCN should not be issued if settlement application filed by the Noticees is yet not disposed of. However, this is a case of just a coincidence and not a deliberate attempt to issue the SCN on November 21, 2023 after ICCL filed an application for settlement on the evening of November 20, 2023. Since different departments are involved, such a close coordination could not be possible to avoid the SCN after the settlement application was filed. After the above facts came on record, the proceedings were kept in abeyance and a reply from ICCL was insisted upon only after its application for settlement was rejected in November 2024. In the meanwhile, the inspection of documents was requested and the opportunity was availed by ICCL on January 15, 2024.

13. I find that the principles of natural justice have been complied with and the technical objection, is not likely to affect the course/conclusion of the current proceeding. Since SEBI had right to issue SCN and demand explanation after rejection of settlement application of ICCL, the restart of proceedings that were kept in abeyance as above after coming to knowledge of filing of settlement application is sufficient compliance of the Regulations.

Purpose of inspection is remedial and not punitive.

14. ICCL has contended that SCN emanates from examination/inspection observations qua ICCL and has relied on the decision of Hon'ble Securities Appellate Tribunal ('SAT') in *UPSE Securities Limited v. SEBI* (Appeal No. 109 of 2011) decision dated July 25, 2011, *Religare Securities Limited v. SEBI* (Appeal no. 23 of 2011 decision dated June 16, 2011), *IDBI Trusteeship Services Limited v. SEBI* (Appeal No. 186 of 2023 decision dated February 22, 2023) and *M/s. DSE Financial Services Ltd. v. SEBI* (Appeal No. 153 of 2012 decision dated September 11, 2012), to contend that the purpose of carrying out inspection is not punitive and not every irregularity or deficiency noticed during the course of inspection calls for initiation of penalty proceedings. In this regard, I note that the Hon'ble SAT in *UPSE Securities Limited* (supra) and *IDBI Trusteeship Services Limited* (supra) observed that for serious lapses, it would always be open to SEBI to take penal action in accordance with law. In the matter of *DSE Financial Services* (supra), the Order of SEBI was set aside because the violations were found to

be technical in nature. Further, in *Religare Securities Limited* (supra), the Hon'ble SAT observed as follows:

“This will, of course, depend on the nature of the irregularity noticed and we hasten to add a caveat that it is not being suggested that if any serious lapse is found during the course of the inspection, the Board should not proceed against the delinquent.”

15. In view of the above observations of Hon'ble SAT, I find that the SCN issued to ICCL cannot be held to be bad in law merely because the allegations arise from an inspection/examination.

Section 23GA does not apply to this case

16. The SCN contemplates imposition of penalty under Section 23GA read with Section 12A (2) of SCRA and Section 15HB read with Section 11B(2) of the SEBI Act. The charging section 23GA of SCRA provides as follows:

“Penalty for failure to conduct business in accordance with rules, etc.

23GA. *Where a stock exchange or a clearing corporation fails to conduct its business with its members or any issuer or its agent or any person associated with the securities markets in accordance with the rules or regulations made by the Securities and Exchange Board of India and the directions issued by it under this Act, the stock exchange or the clearing corporations, as the case may be, shall be liable to penalty which shall not be less than five crore rupees but which may extend to twenty-five crore rupees or three times the amount of gains made out of such failure, whichever is higher.”*

17. Relying on the order of the Hon'ble Supreme Court in the matter of *Maharashtra University of Health Sciences v. Satchikitsa Prasarak Mandal*, (2010) 3 SCC 786 it has been contended that a statutory term is recognised by its associated words and that in section 23GA of SCRA, the words “*any person associated with securities market*” has to be read in the context of intermediaries and cannot mean to include a CCP as the said words are preceded by the words “*its members or any issuer or its agent*”. In this regard, it is pertinent to note that head note of section 23GA reads as ‘*Penalty for failure to conduct business in accordance with rules, etc.*’. The opening words of said section 23GA say that -“*Where a stock exchange or a clearing corporation fails to conduct its business with its members or any issuer or its agent or any person associated with the securities markets in accordance with the rules or regulations made by the Securities and Exchange Board of India and the directions issued by it...*”

(.....emphasis supplied)

18. Thus, if ICCL being a recognised clearing corporation fails to conduct **its business** with “*its members or any issuer or its agent or any person associated with the securities markets*” it is covered in the ambit of said section 23GA. The said section has different and mutually exclusive categories, i.e., members of ICCL, any issuers or its agent or *any person associated with securities market*. The expression ‘*any person associated with securities market*’ is of wide amplitude and is not limited to an intermediary as sought to be contended by ICCL. The expression includes a stock exchange and a CCP also. Thus, if ICCL has failed to conduct its business with NCL in accordance with the rules or regulations made by SEBI and the directions issued by it, it is covered within the ambit of said section 23GA.

No penalty can be imposed invoking wrong provisions

19. The SCN contemplates proceedings under SEBI Adjudication Rules and SCRA Adjudication Rules and penalty under Section 23GA read with Section 12A(2) of the SCRA and Section 15HB read with Section 11B(2) of the SEBI Act. Relying on an order of SEBI’s adjudicating officer in the matter of *IFGL Refractories Limited v. SEBI (Appeal No. 1044 of 2022 decision dated January 06, 2023)*, ICCL has contended that penalty cannot be imposed under a wrong provision. I note that it is settled position of law that the penalty provisions should be strictly interpreted, penalty cannot be imposed under a wrong provision and mitigating factors should be taken while adjudicating the quantum of penalty. In this case, section 15HB of the SEBI Act, provides, as residue provision, penalty for a failure of compliance of the SEBI Act, rules and regulation made thereunder for which no separate penalty has been provided. It is beyond cavil that SECC Regulations have been made under SCRA read with SEBI Act. But, where the activities of a stock exchange are specifically governed pursuant to provisions of SCRA and specific penalty is provided in SCRA for default in that regard, a fanciful approach to invoke section 15HB read with Section 11B(2) also is not appropriate as it does not serve any purpose at all. In my view, this case is limited to the ambit of Section 23GA read with Section 12(2) of the SCRA and proceedings are to be in the manner prescribed in SCRA Adjudication Rules and not the SEBI Adjudication Rules. However, since SCRA Adjudication Rules are analogous to SEBI Adjudication Rules and prescribe identical procedures which has been duly followed in this case, there is no infirmity in these proceedings in that regard.

20. The question that remains for determination is whether ICCL violated the SEBI norms regarding Inter CCP collateral during the Examination Period as alleged in the SCN and if yes, whether such violations deserve penalty. I note that the first three separate allegations as mentioned in para 3.1, 3.2, 3.3 above

are actually interconnected and interwoven so as to find out the main issue as to whether ICCL has failed to maintain sufficient Inter CCP collateral from NCL and failed to ensure adequate risk management mechanism during the Examination Period. And, the fourth one as mentioned in para 3.4 is independent. I proceed to deal with the allegations accordingly. In order to deal with the charge, it is necessary to deal with provisions alleged to have been violated by the ICCL. In this context the charge is that ICCL has violated the provisions of para 5.2 and 5.3 of the Inter CCP circular. Further, it has violated provisions of Reg. 7(4)(b) read with Reg.12(5) of the SECC Regulations. The extracts of the relevant provisions of law in the context of this charge are reproduced as follows:

Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2018

7. (4) An applicant seeking recognition as a clearing corporation shall, in addition to the conditions as specified in sub-regulations (1) and (2), comply with the following conditions, namely:—

(b)the applicant has adequate risk management mechanism;”

12. (5) The recognised stock exchange and recognised clearing corporation shall comply with the applicable conditions specified in sub-regulation (3) and sub-regulation (4) of regulation 7, as the case may be, on a continuous basis.”

SEBI circular No. CIR/MRD/DRMNP/CIR/P/2018/145 dated November 27, 2018 (SEBI interoperability circular)

“5.2. Interoperable links among CCPs

- (1) The recognised clearing corporations shall establish peer-to-peer link for ensuring interoperability. A CCP shall maintain special arrangements with another CCP and shall not be subjected to normal participant (membership) rules. Risk management between the CCPs shall be based on a bilaterally approved framework and shall ensure coverage of inter-CCP exposures. CCPs shall exchange margins and other financial resources on a reciprocal basis based on mutually agreed margining models.*
- (2) However, SEBI, in certain cases, may require a CCP to establish participant link for interoperability. In such cases the CCP concerned shall become participant of another CCP (the host CCP) and shall be subjected to the host CCP’s normal participant rules. Since the*

participant CCP would be posting margins with the host CCP, but would not be collecting margins from the host CCP, it shall be required to hold additional financial resources to protect itself against default of the host CCP.

5.3. Inter CCP Collateral

- (1) To manage the inter-CCP exposure in the peer-to-peer link, CCPs shall maintain sufficient collateral with each other so that any default by one CCP, in an interoperable arrangement, would be covered without financial loss to the other non-defaulting CCP. The inter-CCP collateral shall comprise two components, viz.
 - (a) Margins as per the existing Risk Management Framework (initial margin, extreme loss margin, calendar spread margin, etc.) prescribed by SEBI; and*
 - (b) Additional capital, to be determined by each CCP, based on the credit risk from the linked CCP, on which no exposure shall be granted to the linked CCP.**
- (2) The collateral posted by one CCP with another CCP shall be maintained in a separate account which can be clearly identified in the name of such linked CCP which is providing collateral and shall not be included in the Core SGF of the CCP receiving them.*
- (3) The liquid assets as well as hair-cuts as prescribed vide SEBI Circular MRD/DoP/SE/Cir-07/2005 dated February 23, 2005 on “Comprehensive Risk Management Framework for the cash market” and SEBI Circular CIR/MRD/DRMNP/9/2013 dated March 20, 2013 on “Corporate bonds and Government securities as collateral” shall be applicable for inter-CCP transactions.”*

5.9 Inter-CCP Agreement

- (1) Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2018 prescribes that “...in case a recognised stock exchange enters into an arrangement with more than one recognised Clearing Corporation, it shall enter into a multipartite agreement in writing with such recognised clearing corporations to ensure interoperability among the clearing corporations”.*
- (2) The agreements entered into by the Stock Exchanges/ Clearing Corporations shall, inter alia, include system capability, inter-CCP links and CCP-trading venue link, risk management framework, monitoring of client margin/position limits, obligation system, settlement process,*

surveillance systems, sharing of client data, sharing of product information, default handling process and dispute resolution process.

The relevant clauses of the Interoperability Agreement dated June 01, 2019 among CCPs

“3.2 The CCPs under this Agreement, shall connect to each other through “Peer to Peer” Model as referred by SEBI in its Circular dated November 27, 2018, wherein a CP shall maintain sufficient collateral as set out in Schedule 4 with another Clearing Corporation(s) for margining and clearing of trades executed on the trading platform of the Exchange.

20.1 The Parties agree that with the overall intention of overseeing the smooth functioning of the interoperability Arrangements under this Agreement, it may be expedient for the parties to constitute amongst themselves a Committee which shall act as a recommendatory body without any regulatory mandate with such mandate as mutually agreed upon between the Parties. The Parties further agree keeping in mind the intention to ensure smooth functioning of the interoperability arrangements. The Parties shall adopt and implement the decisions including any recommendations, if any, of the Committee from time to time subject to provisions of Clause 30.4 Settlement of Disputes in case of any disagreements with such decisions.

*20.2 Constitution: For the purpose of supervising and managing the implementation of the Interoperability Arrangement, the parties agree to constitute a committee consisting of 2 (two) nominees of a senior management level as communicated by each of the Parties (“**Coordination Committee**”).*

Schedule 4

III. Provision of Collateral and Utilization:

- a) The collateral requirements shall be calculated on a real-time basis by the CPs. Such requirements shall be exchanged by CCPs with each other with such frequency of update and such timelines as mutually agreed by the CCPs.*
- h) In the event the collateral deposited by the delivering Clearing Corporation is insufficient, the receiving clearing corporation shall not have any recourse against the delivering Clearing Corporation except to the extent of the utilization of collateral and shall seek recourse to its default waterfall in accordance with its Rules, Bye-laws and Regulations of the receiving CCP and circulars/directions issued by SEBI from time to time.*

j) CCPs shall mutually agree on threshold amounts up to which collateral shortfall during trading hours may be permitted. In case of collateral shortfall beyond such amount, the CCP facing shortfall shall have a right to submit an instruction to the Exchanges to refuse to admit all mixed member transaction with such CCP.

IV. Inter-CC Collateral

a) Risk-based capital requirement for Clearing Corporations

The CCPs shall maintain risk-based collateral with each other based on the methodology as given in Annexure of this Schedule 4. Such risk based collateral shall not be considered towards fulfilment of margin or any other obligation of the CCPs.”

Annexure to Schedule 4 states that risk based collateral shall be maintained using the Credit Value Adjustment methodology as outlined in Basel Standard for arriving at the Inter CCP collateral requirement based on credit risk of associated CCP.

21. In terms of regulation 7(4) read with regulation 12(5) of the SECC Regulations, a recognised CCP is under obligation to continuously maintain adequate risk management mechanism. It is also relevant to mention that in terms of regulation 7(4) read with regulation 12(5) of the SECC Regulations, the recognised CCP is also under obligation to comply with conditions specified in regulation 7(3) including other conditions as may be specified by the Board (SEBI). The above mentioned Inter CCP circular specifies conditions for inter-operability among CCPs. In terms of para 5.2 and 5.3 of the Inter CCP circular, to manage the inter CCP exposure, CCPs shall maintain sufficient collateral with each other. Further, such inter CCP collateral shall contain two components viz., (1) Margins as per the existing Risk Management Framework and (2) Additional capital to be determined by each CCP, based on the credit risk from the linked CCP.

22. One of the contentions of ICCL is that Clause 5.2 of the Inter CCP circular stipulates that the risk management shall be based on whatever is ‘*bilaterally approved*’ and the collateral was to be exchanged between the CCPs on a ‘*reciprocal basis based on mutually agreed margining models*’. Therefore, contractual autonomy ‘*inter –party*’ prevails and the allegation of violation of Clause 5.2 of the Inter CCP Circular is denied. I note that the SECC Regulations read with said circular specify some conditions and leaves more specific conditions to be governed by Inter CCP Agreement. The regulatory interoperability framework for CCPs is, thus, predominantly, on the basis of regulation by contract model. Such model, though criticised, yet widely applies particularly to the circumstances of particular

utilities, with more or less financing and investment risk passed to the private bodies. Still the regulator/Government/courts play an important role in enforcing the obligations and upholding the concept of “*financial equilibrium*,” which prevents one party from being unduly affected by a change in circumstances. Since the conditions of Inter-CCP Agreement flow from regulatory requirements and have impact of affecting the system at large, the operation cannot be allowed to be the exclusive domain of the contracting parties, in this case, ICCL and NCL. In case of any mis-management or demeanour impacting the risk management system, the provisions of SECC Regulations and SEBI’s circulars will come into play to ensure that the parties do not deviate from their obligations in the Inter CCP Agreement so as to pose systemic risks in the system.

23. Coming to the scope of Clause 5.2 and 5.3 of the Inter CCP circular and based on the reply of ICCL, for inquiring into the allegations under Rule 4 of the SCRA Adjudication Rules, the overall risk mitigation system that operates pursuant to the Inter CCP circular in the market simultaneously needs to be kept in mind. It is a matter of fact that the three stock exchanges [*i.e. BSE, NSE and MSEI (erstwhile MCX-SX Stock Exchange)*] have established their respective CCPs through the subsidiary route, which clears and settles the trades executed on their parent stock exchanges. It is relevant to mention that in securities markets, interoperability among CCPs is an arrangement that links multiple CCPs, thereby, facilitating market participants to consolidate their clearing and settlement functions at a single CCP, irrespective of the stock exchange on which the trade is executed. For this purpose, India has adopted ‘*peer to peer link model*’ as opposed to ‘*participant link model*’ so as to ensure that all recognised CCPs are on equal footing. Considering suboptimal utilization of margin and capital resources in the securities market, the interoperability amongst the respective CCPs was operationalised pursuant to the Inter CCP circular by linking the CCPs and allowing market participants to consolidate their clearing and settlement function at a single CCP, irrespective of the stock exchange on which the trade is executed. A significant risk that is intended to be mitigated arises out of Inter CCP settlements given the possibility that a CCP may not pay-out to the other CCP after receiving pay-in from the other CCP. It is pertinent to note that in order to manage and mitigate the inter-CCP exposures, the instant framework is intended to ensure that the CCPs to exchange have sufficient collateral so as to provide a high degree of confidence that any default by a CCP, in an interoperability arrangement, would be covered without financial loss to the surviving CCP. In order to address this risk, in the prevalent ‘*peer to peer link model*’, CCPs exchange Inter CCP collateral amongst themselves.

24. This model of trading, clearing and settlement, requires the market participants to take membership of a particular stock exchange and its CCP (or tie-up with a member of that CCP), thereby effectively locking-in the trading, clearing and settlement activities in a closed group of related entities. A market participant was required to take membership of another closed group of related entities to access another trading platform. This model of membership obligated the market participants to make multiple deployments of margin and capital resources separately at the three stock exchanges/CCPs, which leads to suboptimal utilization of these resources, thereby increasing costs for the market participants. The idea behind these requirements is also in the direction of efficient allocation of capital for the market participants, thereby saving on cost as well as providing better execution of trades.
25. The requirements in clause 5.2 of the Inter CCP circular is to draw a framework based on *bilaterally approved framework* and *CCPs are required to exchange margins and other financial resources on a reciprocal basis based on mutually agreed margining models*. However, the requirement in clause 5.3 of the Inter CCP circular cannot be given complete go by in view of these technicalities of bilateral arrangements. The requirement in clause 5.2 shall always be read in conjunction with requirement in Clause 5.3 so as to give intended meaning to the scope of entire interoperability framework as discussed above. It is noted that the prescriptive specifications as listed in the above Regulations/circular/agreement also envisage mitigating two interconnected risks. First, the credit risk (i.e. default by members) faced by the CCPs and the second, the additional risk faced by interoperable CCPs being the inter-CCP credit risk or counterparty credit risk, resulting from exposures between interoperable CCPs. The inter-CCP credit risk is the risk when one CCP which is party to an interoperable arrangement, is unable to honour its obligations to its interoperable counterparty CCP, when due, or at any time in the future. The flow of funds and securities between the interoperable CCPs is, thus, for the purpose of meeting margin requirements or delivery requirements. Failure to honour either of the obligations by an interoperable CCP, thus, puts the counterparty CCP at risk of potential losses. The objective of having sufficient inter CCP collateral as mandated by above Inter CCP circular is to protect one CCP from the risk of default of another CCP. Having sufficient Inter CCP collateral ensures that inter CCP exposures are covered and this is one of the two key risk mitigation measures.
26. Considering that the CCPs would not be contributing to each other's Core Settlement Guarantee Fund, this additional capital without exposure acts as a buffer and aid in the absorption of losses arising due to default by an interoperable CCP. Therefore, the framework in Clause 5.3(1) of the Inter CCP circular

provides for the inter-CCP margins to include above mentioned two components viz. Margins as per the existing Risk Management Framework prescribed by SEBI and, (b) Additional capital, to be determined by each CCP, based on the credit exposure from the linked CCP, on which no exposure is granted. It is clear that the requirement for CCPs to maintain sufficient collateral with each other is independent of requirements regarding margins as per the applicable Risk Management Framework (initial margin, extreme loss margin, calendar spread etc.) prescribed by SEBI. Both components of para 5.3 (1) of the SEBI Inter CCP Circular are mutually exclusive and independent and cannot be mingled with each other as both serve different aspects of counter party risk management. Therefore, it is not permissible to allow the CCPs to not provide additional '*sufficient collateral*' with each other merely because they have sufficient margins. The default in this regard pose systemic risks which the CCPs should cautiously avoid and in case of any difficulties find practical solutions instead of avoiding compliance. Therefore, I am not inclined to accept above contentions of ICCL.

27. In this case, upon examining the sufficiency of the actual Inter CCP collateral received by ICCL from NCL *vis-à-vis* the amount of Inter CCP collateral that should have been received as per the applicable norms, it has been observed that during April 2020 to April 2023, on 615 trading days out of 763 trading days the daily average collateral required as per Inter CCP circular across market was much higher than the actual collateral maintained by ICCL from NCL. The daily shortfall in Inter CCP collateral was in the range of ₹4.61 crore to ₹3,049.57. Further, as per interoperability agreement, Schedule 4 – III- Provision of Collateral and Utilization, clause 'h', in case of collateral by one CCP being insufficient, the recourse available is to fall upon default waterfall and utilize its Core SGF. In the instant case, the shortage of collateral was observed to be much higher than Core SGF of ICCL. It was also observed that the collateral requirement for cash segment data was not matching with margin that has been provided by NCL for cash segment and there was difference in margin data. It was also observed that the practice of monitoring of collateral requirement under Inter-CCP at T+1 by ICCL is not on real time basis. Thus, ICCL failed to ensure real time risk monitoring mechanism under Inter CCP circular.

28. In this case, the facts that are basis of allegation in the SCN have not been disputed. It is a matter of record that CCPs did not maintain sufficient collateral with each other, i.e., the additional capital to be determined by each CCP, based on the credit risk from the linked CCP and it is admitted position that ICCL did not maintain sufficient Inter CCP collateral from NCL as alleged. Therefore, the matter

proceeds under rule 5 of the SCRA Adjudication Rules based on replies, submissions and explanations offered during these proceedings.

29. The Ld. Senior Advocate appearing for ICCL valiantly argued that the ICCL has not deliberately defaulted as alleged. According to him the compliance was difficult, if not impossible, in view of the fact that netting is permitted, margins constantly change and, thus, it is impossible to find out net position on real time basis. Reiterating written reply of ICCL, he attempted to show operational difficulties in implementation of the risk management framework under the interoperability agreement dated June 01, 2019 as follows:

- (a) As per SEBI circulars dated April 17, 2008 and June 20, 2019, clients' funds and securities can only be used for meeting the respective client's margin requirements/pay-ins.
- (b) SEBI, vide its email dated April 25, 2019, provided guidance on some of the issues, including that for the interoperability exposure, stating that the CCP should exchange bank guarantees with each other but each CCP should also continue collecting collaterals from their respective Clearing Members ('CM(s)').
- (c) The Inter-CCP Agreement dated June 1, 2019 had contained various provisions and terms which were subsequently found to be impractical or non-viable.
- (d) Inter-CCP collateral bank guarantees cannot be collected/returned even on a daily basis as providing such bank guarantee is a long and time consuming involving board approval, applying to the banks, waiting for the banks to complete their internal processes, making available the requisite funds for the funded portion of the bank guarantee, etc.
- (e) As per SEBI's circular dated February 25, 2020, there is no provision for pledging/transferring of margin provided by a client/Trading Member ('TM')/CM from one CCP to the other CCP under interoperability or otherwise. Further, as margin obligations of TMs / CMs are constantly changing, such required constant real time monitoring of the margin obligations can only be undertaken by the respective CCP and the same cannot be passed on to the other CCP doing the clearing under interoperability.
- (f) There have been email correspondences dated April 25, 2019, January 05, 2023, February 20, 2024, February 22, 2024, February 23, 2024 and February 29, 2024 between SEBI and ICCL with respect to communication of challenges faced by ICCL in implementing interoperability and copies of these email have been provided by ICCL.

- (g) Further, by a representation to SEBI dated November 01, 2023, with reference to the provisions of the Inter CCP Circular, ICCL, *inter alia*, recorded the problems and issues faced in interoperability and proposed/suggested that the Inter CCP Circular be modified to permit CCPs to enter into mutually agreed arrangements to define the framework for monitoring margins/ credit risk, sharing the requisite information, deciding on margin and additional capital requirement and the permitted shortfall threshold amount, etc.
- (h) ICCL is rated "AAA" by two rating agencies, India Ratings Ltd. (Indian arm of Fitch Ratings) and Care Ratings Ltd. Similarly, NCL is rated "AAA" by CRISIL. AAA is defined to mean highest level of safety and lowest level of risk and ICCL has also subscribed to a unique "*Commercial Perils Counterparty Default Insurance*" policy which, *inter alia*, protects ICCL against defaults. Even assuming that NCL were to ever default in its pay-in obligations to ICCL, considering the available collateral, the insurance policy taken by ICCL, ICCL's core Settlement Guarantee Fund (SGF) and net worth, there was no risk or danger of the ICCL defaulting in the interoperability settlements.
- (i) The bilaterally approved framework and the mutually agreed margining models were as set out in the aforesaid SOPs which were also submitted to SEBI and in respect of which SEBI had not raised any objections contemporaneously. Therefore, while the initial intention in the Inter CCP circular and the Inter CCP Agreement was to undertake the collateral monitoring on a real time basis, it was later realized from experience that the same was not viable and even SEBI has appreciated the same.
- (j) In terms of the SOPs between CCPs, the collateral/margin was and is computed and adequacy of available margin (bank guarantees) is assessed on a monthly basis and collateral calls are to be made in the next succeeding month, and topping up of collateral if any, required is to be in the next month thereafter. Further, as per the SOPs which were also shared with SEBI, the call for additional collateral is to be made only if the deficit is more than the permitted 110% -125%. Therefore, deficit in the Inter-CCP collaterals is in fact permitted and is expected.
- (k) Additional collateral requests by ICCL were collected as of April 2020, August 2020, February 2021, December 2021, January 2022 and May 2022.
- (l) Even considering the equity cash margins based on available data, there was no collateral deficit upon applicability of 110% collateral threshold, considering the Core SGF and net worth of ICCL.

(m) The collateral data given by NCL for cash segment is higher than ICCL's data for cash segment and that it is incorrect to presume that the data provided by NCL will be applicable to ICCL as the computation of collateral required will be different for ICCL and NCL, particularly since the computation is on a net basis per CM.

30. I note that in the beginning of operationalisation of interoperability in June 2019, various problems were faced in implementing interoperability and ICCL and SEBI were actively engaged to find practical solutions. In fact, on April 25, 2019, i.e., before the ICCL could operationalise the inter-operability with NCL in June 2019, SEBI had provided guidance to CCPs on some of the issues, such as mode of exchange of collateral through bank guarantee, interoperability exposure, and it was stated that each CCP should also continue collecting collaterals from their respective Clearing Members. After operationalisation of interoperability among CCPs pursuant to Interoperability Agreement dated June 01, 2019 following other developments took place:-

June 20, 2019	SEBI Circular stipulated that to protect clients' funds and securities, stock-brokers are, <i>inter alia</i> , required to segregate securities of the clients and ensure that they did not use the securities of a client for their own proprietary trading.
February 25, 2020	SEBI circular stated that for providing collateral, the clients shall pledge securities with the Trading Members, the Trading Members may re-pledge the same with the Clearing Members and the Clearing Members in turn can re-pledge the same to the CCP. However, there was no provision for further re-pledging /transferring of securities by CCPs.
September 07, 2021	SEBI issued its Circular on "Introduction of T + 1 rolling settlement on <u>an optional basis</u> ".
October 2022 to February 2023	SEBI started examination regarding compliance of interoperability framework by CCPs.
December 06, 2022	Standard Operating Procedure ('SOP') v1.0 for interoperability was agreed upon in writing.
December 2022 to June 2023	Various correspondences were exchanged between SEBI and ICCL regarding interoperability wherein ICCL provided requisite information to SEBI.
January 04, 2023	ICCL had nominated its officials for the Co-ordination Committee and thereafter the Committee was constituted and has been operational.

July 21, 2023	SEBI vide its letter informed ICCL regarding 6 observations relating to interoperability. The Examination Report was not shared with ICCL but it was informed that quasi-judicial proceedings have been initiated and ICCL shall receive SCN in due course.
November 01, 2023	Pursuant to ongoing discussion between ICCL and NCL, a Joint Proposal was shared with SEBI seeking amendments to Inter CCP circular and SOP.
February 20, 2024	In response to the aforesaid Joint Proposal, SEBI raised certain queries.
February 22, 2024	ICCL and NCL gave joint response to the aforesaid SEBI queries.
February 23, 2024	SEBI requested ICCL and NCL to state the changes required by them to the said Inter CCP Circular and the SOP.
February 29, 2024	The changes proposed jointly by ICCL and NCL to the SOP as well as the Inter CCP Circular were shared with SEBI.

31. After the Inter CCP Agreement came into effect, there were certain policy changes introduced by SEBI which required that client funds and securities to be used only for client margining/pay-ins but CCPs already had clarity (since April 2019) that Inter CCP collateral should be in the form of bank guarantees. However, CCPs did not completely adhere to these requirements in Clause 5.3(1)(a) of the Inter CCP circular as the said Agreement provided that *‘collateral requirements shall be calculated on a real-time basis’* because of the practical difficulties in obtaining bank guarantees on daily basis. Thus, in a strict legal sense this was a non-compliance. But the fact remains that there was effectively double margining and double collateral because the CCPs collect all the requisite margins, etc., in the permitted forms and manner from its clearing members as per all the applicable rules, regulations, circulars etc. These are retained by that CCP only and fully cover the exposure and risk management requirements. In the case of interoperability, one CCP, in turn, also provides its own bank guarantees to the other CCP and *vice versa*, towards risk management and clearing and settlement under the interoperability process. Therefore, there is double margin available and ICCL did not compromise with risk mitigation in the facts and circumstances of this case. It is also pertinent to mention that when in October 2022, SEBI began examining the compliance of interoperability framework by CCPs, ICCL provided information to SEBI in responses to the queries raised by SEBI and also nominated its officials for the Co-ordination Committee in January 2023.

32. I also note that in November 2022, when SEBI pointed out the difference in inter CCP margins in cash segment stating that *‘in cash market, the inter CCP margins shall be same’* to ICCL, it had submitted

that it had reconciled the difference with the other CCP based on Inter CCP obligation. Further, the SOP between CCPs was signed in December 2022, i.e., after SEBI had raised queries regarding compliance with Inter CCP Agreement, and there was no SOP in place before that. It is noted that this SOP mentions that the call for additional collateral is to be made if the deficit is more than 110%. This SOP could be considered the *bilaterally approved framework* emanating from Inter CCP Agreement and SEBI was in know of the same at relevant times. It is also admitted fact that the collateral calls were made and collateral was collected by ICCL during April 2020 to May 2022. Additionally, the high credit rating of CCPs and the fact that all the requisite margins were being collected by both CCPs from CMs, means that the real risk of CCP defaulting, although existent, was rather low.

33. Subsequently, CCPs shared a joint proposal with SEBI on November 01, 2023 seeking amendments to Inter CCP circular and SOP. After initiation of instant quasi-judicial proceedings, SEBI during February 2024 continued engaging with both the CCPs to address their concerns and asking their suggestions for change in the framework for smooth implementation. Thus, on the one hand the concerns raised by CCPs was being examined and considered, on the other hand the instant proceedings were initiated and also advisory was issued to ICCL on July 21, 2023 to take necessary corrective steps. ICCL has submitted that it has complied with such advisory of SEBI. I also note that interoperability was a new feature introduced by SEBI in 2018, implemented in 2019 and the practical difficulties faced in implementing the system required changes compared to what was envisioned in the Inter CCP Agreement. ICCL has been rated AAA by two rating agencies signifying that it has highest level of safety and lowest level of risk.

34. Further, it has also subscribed to a unique “*Commercial Perils Counterparty Default Insurance*” policy which, *inter alia*, protects ICCL against counter party defaults. Additionally, ICCL has informed that corrective measures have already been taken by ICCL by making collateral calls and collecting additional capital from other CCP in terms of agreed SOP. Further, I note that discussions of CCPs with SEBI are ongoing with respect to changes required in SOP in terms of the frequency and manner of exchange of collateral. In this regard, I also note that in similar cases, where strict compliance of other Regulations was not enforced considering the facts and circumstances that the cases were closely meeting the requirements and corresponding with SEBI with regard to alleged noncompliance.¹

¹ SEBI order No. WTM/ASB/IMD/FPI&C/29225/2023-24 dated September 13, 2023 in the matter of The India Debt Opportunities Fund Limited; and Order No. Order/BS/YK/2023-24/29158 dated September 07, 2023 in the matter of Life Insurance Corporation of India (LIC).

Therefore, I am of the view that the deviation from the conditions of the Inter CCP Agreement dated June 01, 2019 is technical in nature in the facts and circumstances as explained by ICCL. Considering these peculiar facts and circumstance, I agree with Ld. Senior Advocate's contention that the default, if any, was not blameworthy enough so as to penalise with penalty prescribed in section 23GA of the SCRA.

35. With regard to the second allegation that ICCL failed to calculate additional capital applicable to NCL as per BASEL III guidelines required under the Inter CCP Agreement, ICCL has contended that as per para 5.3 of the SEBI circular, additional capital was to be determined "*based on the credit risk from the linked CCP*", i.e., NCL, and the question of additional capital was understood to arise if and when there was credit risk in respect of NCL. Further, ICCL has stated that both NCL and ICCL are AAA rated and consequently, none of the CCPs communicated to each other the additional capital computations or demands, which any way was negligible, at less than 1%. I note that as discussed above, in terms of Clause 5.2 of the Inter CCP circular, to manage the inter CCP exposure, ICCL was required to maintain sufficient collateral which shall include additional capital, to be determined by each CCP, *based on the credit risk from the linked CCP*, on which no exposure shall be granted to the linked CCP. The allegation stems from the fact that the Interoperability Agreement between the CCPs provided that additional capital applicable to CCPs should be calculated as per BASEL III guidelines, which was not done by ICCL. However, I note that in addition to the factors such as high credit rating of both the CCPs, requisite margins being collected by both the CCPs and collateral calls being made during April 2020 to May 2022 based on mutual understanding between the CCPs coupled with the fact that ICCL has, upon being informed by SEBI, been computing and collecting additional capital from NCL since January 2023, I find that this deviation is also not blameworthy to penalise ICCL.

36. With regard to allegation that ICCL failed to ensure mutually agreed norms relating to frequency, timelines and determination of threshold amount of shortfall for the collateral requirement, it has stated that clause (a) of the Inter CCP Agreement specifically provides that "*frequency of update and such timelines*" is to be "*mutually agreed*" by the CCPs. In this regard, ICCL has not disputed that collateral was exchanged since inception of the interoperability framework, which proves that ICCL and NCL had such mutually agreed norms. Further, ICCL has stated that ICCL and NCL have always been in touch with each other for various issues in computation and collection of Inter-CCP collateral and SOP in this regard was documented in December 2022. I note that this allegation also stems from the fact that even

though the Interoperability Agreement provided an agreement for frequency, timeline and determination of threshold amount of shortfall for collateral requirement, there were no written mutually agreed norms till SEBI inquired regarding the same. It was after SEBI inquired that an SOP was documented in December 2022 but in view of the fact that collateral was being exchanged between NCL and ICCL even before the SOP was put in place and it may be incorrect to state that such norms never existed, I find that this tantamount to a technical violation.

37. With regard to allegation that ICCL failed to constitute a Coordination Committee and nominate its officials to the said Co-ordination Committee, ICCL has stated that while there was some delay in the technical/official constitution of the Co-ordination Committee, risk management teams were acting as the *de facto* Co-ordination Committee and that ICCL had formally nominated its officials to the Co-ordination Committee on January 04, 2023 and the Committee has been duly constituted. Further, ICCL has stated that the Inter-CCP Circular does not require constitution of any such Co-ordination Committee and the Inter-CCP Agreement in Clause 20.1 states that “*it may be expedient for the Parties to constitute from amongst themselves a Committee...*” meaning that the requirement was not mandatory. From a combined reading of clause 20.1 and 20.2 of the Inter CCP Agreement, I find that the wordings of the Inter CCP Agreement are in the nature of creating soft obligation instead of being definitive to the extent of enforcing the obligation by punishment. Nevertheless, ICCL has formally nominated its officials to the Co-ordination Committee on January 04, 2023 and the Committee has been duly constituted. Hence, I am inclined to drop this charge.

38. Coming to the issue whether ICCL should be penalised by imposing a minimum prescribed in view of the above facts and circumstances of the case, one may argue that in respect of the charges in the SCN against NCL, the SCN has been disposed of on payment of settlement amount of Rs. 27,13,10,000 (Rupees Twenty-Seven Crore Thirteen Lakh and Ten Thousand only) vide order dated October 29, 2024, hence, ICCL should also be penalised by imposing prescribed minimum of Rs. 5 crore. In this regard, it is relevant to mention that though the allegations in and proceedings commenced by a SCN remain the same in settlement proceedings under the Settlement Regulations and also under the quasi-judicial proceedings, both proceedings operate in different and independent dispensations and with different approaches of assessment. The Noticee has choice to opt for settlement of the charge without admitting or denying the guilt on payment of settlement amount under the Settlement Regulations or to contest the allegations in a *quasi-judicial* proceeding. The choice is guided by human hunch and not merely based

on possibility of being punished after trial. Considering strict calculation in the Settlement Regulations, such choice may involve consideration of various significant factors, including the potential costs and time savings, the risk and benefit of going to trial, the impact on reputation, the possibility of a long-term relationship, impact on any ensuing market transaction or business and the desire for a resolution.

39. As opposed to settlement proceedings as per extant Settlement Regulations, which is purely administrative based on mathematical calculations without going into inquiry or determination of the case on merit, in the quasi-judicial proceedings, the allegations are tested and evaluated based on examination and analysis of detailed submissions and assessment of factual matrices and evidences and the decision cannot be based on set mathematical formulae when law prescribed in Section 23I(2) of SCRA gives discretion based on facts and circumstances and applying the principles of reasonability and proportionality. The current proceedings do not entail restorative justice practice as victim restitution. Proportionality demands that a penalty should be proportionate with the mischief it seeks to address and penalties cannot be disproportionate to the magnitude of default. No arithmetical formula can be devised to impose a fixed penalty on each case and if Section 23GA is applied lexicographically it may render provisions of Section 23J of SCRA and Regulation 49 of SECC Regulations otiose. In fact, Section 23J of SCRA and Regulation 49 of SECC Regulations cast duties to consider several other factors. Section 23 J of the SCRA provides as follows:

“Factors to be taken into account while adjudging quantum of penalty.

23J. While adjudging quantum of penalty under section 12A or section 23I , the Securities and Exchange Board of India or the adjudicating officer shall have due regard to the following factors, namely: —

- (a) the amount of disproportionate gain or unfair advantage, wherever quantifiable, made as a result of the default;*
- (b) the amount of loss caused to an investor or group of investors as a result of the default;*
- (c) the repetitive nature of the default.*

Explanation. — For the removal of doubts, it is clarified that the power to adjudge the quantum of penalty under sections 23A to 23C shall be and shall always be deemed to have been exercised under the provisions of this section.”

40. Sections 23I (2) and 23 J of the SCRA are *pari materia* Sections 15I(2) and 15J of the SEBI Act. While dealing with scope of such discretion under section 15I (2) of the SEBI Act with expression “*may impose such penalty as he thinks fit* ” mentioned therein and applicability of inclusive factors in 15J in such situation, Hon’ble Supreme Court in *SEBI v. Bhavesh Pabari (Civil Appeal No.11311 of 2013)* decided on February 28, 2019² held that the charging sections must have to be read along with Section 15J in a manner to avoid any inconsistency or repugnancy. Conflict and head-on-clash in different provisions between the one which gives discretion and the other which prescribes penalty must be avoided and both the provisions must be construed harmoniously. Provision of one section cannot be used to nullify and obtrude another unless it is impossible to reconcile the two provisions. The Explanation to Section 15J of the SEBI Act has clarified and vested in the Adjudicating Officer a discretion under Section 15J on the quantum of penalty to be imposed while adjudicating defaults under. This clarification through the medium of enacting the Explanation to Section 15-J, also states that the Adjudicating Officer shall always have deemed to have exercised and applied the provision. It was held that the provisions of Section 15J were never eclipsed and had continued to apply in terms thereof to the defaults.
41. Regulation 49 of the SECC Regulations lays down guidelines as to when to issue direction and levy penalty. The guiding principles for invoking monetary penalty is provided in proviso to regulation 49(2)(b) as under: -
- (i) a mala fide intent; or
 - (ii) an act of commission or an act of omission; or
 - (iii) negligence, or
 - (iv) repeated instances of genuine decision making that went wrong.
42. In this case, there is no *mala fide* intent of CCPs and the deviation in implementation has happened on account of practical difficulties in implementing the framework with fulfilling nuances with fine precision. There is no apparent or demonstrable misconduct with respect to failure to conduct business. There is technical omission as observed in this case but ICCL has been able to protect the systemic risks by other means. The non-compliances have not affected the interests of the investors or the market or caused any harm or loss to anyone or any benefit or advantage to ICCL and the violations were not repetitive. Nevertheless, the instant case could be a case of repeated instances of genuine decision

² Coram:- [Ranjan Gogoi, CJI, Deepak Gupta and Sanjiv Khanna, JJ.] Authored by SANJIV KHANNA, J.

making in an incorrect approach of implementation. However, this is also not case of wanton negligence but a case subsequently perceived as mis- judgement based on bilateral framework and the mutually agreed margining models adopted by CCPs as set out in the SOPs and also informed to SEBI contemporaneously. The facts and circumstances as discussed hereinabove and summarised below are relevant while adjudicating this case: -

- (a) a totally new feature of interoperability entailing massive change was introduced by SEBI in 2018 and the Inter CCP Agreement was entered into in 2019 requiring CCPs to lay down practical nuances bilaterally through agreement;
- (b) The mechanism, systems and requirements for interoperability required modifications in view of the experience gained of the difficulties faced in implementing what was originally envisioned as compared to the reality faced by the CCPs.
- (c) SEBI started inquiry only in 2022 and in 2023 advised ICCL to take corrective steps.
- (d) ICCL had on January 4, 2023 nominated its officials for the Co-ordination Committee and thereafter the committee was constituted and has been operational.
- (e) CCPs have communicated additional issues in implementing the Inter CCP circular to SEBI in 2024 with suggested changes that are under consideration.
- (f) ICCL has put in place a system of regularly monitoring the Inter-CCP collateral (including for cash market trades) required and on a monthly basis making collateral calls for additional collateral if required, in terms of agreed SOP.
- (g) ICCL has been computing and collecting additional capital from NCL since January 2023.
- (h) Observations recorded in SEBI letter dated July 21, 2023 issued to ICCL after examination of compliance with interoperability framework have been addressed and implemented.

43. Taking into account the facts and circumstances in totality, I am inclined to take a lenient view and do not find this case fit for imposition of a penalty as prescribed in Section 23GA of the SCRA.

44. While parting with this order, I also deem it necessary to mention that the requirements when seen with robust objectives of risk containment not only for the protection of interest of investors but also for that of the CCPs, the prescribed framework cannot be diluted based on hunch or any apprehension of practical difficulties. ICCL being a market infrastructure institution (MII) must strictly follow the prescribed norms. I must hasten to add that it is not appropriate for an MII to not come back to SEBI of its own volition with the issues faced in implementing the Inter CCP circular and Agreement operational since June 2019 but only after an examination of compliance of the interoperability framework is begun

by the Regulator in October 2022. I strongly discourage such attitude on the part of ICCL and encourage it to comply with prescribed norms strictly and raise practical difficulties if any, with possible alternatives to SEBI promptly.

45. The Show Cause Notice dated November 21, 2023 is disposed of accordingly.

Date: May 15, 2025

Place: Mumbai

Santosh Shukla

Quasi-judicial Authority

Securities and Exchange Board of India