

CHAPTER 2

TRADING MEMBERSHIP

2.1 Stock Brokers

A stock broker is an intermediary who arranges to buy and sell securities on the behalf of clients (the buyer and the seller). According to SEBI (Stock Brokers and Sub-Brokers) Regulations, 1992, a stockbroker is member of a stock exchange and requires to hold a certificate of registration from SEBI in order to buy, sell or deal in securities. SEBI grants a certificate to a stock broker subject to the conditions that the stock broker:

- a) Holds the membership of any stock exchange,
- b) Should abide by the rules, regulations and bye-laws of the stock exchange or stock exchanges of which he is a member,
- c) Should obtain prior permission of SEBI to continue to buy, sell or deal in securities in any stock exchange in case of any change in the status and constitution,
- d) Should pay the amount of fees for registration in the prescribed manner, and
- e) Should take adequate steps for redress of grievances of the investors within one month of the date of the receipt of the complaint and keep SEBI informed about the number, nature and other particulars of the complaints.

While considering the application of an entity for the grant of registration as a stock broker, SEBI checks out if the applicant:

- a) Is eligible to be admitted as a member of a stock exchange,
- b) Has the necessary infrastructure like adequate office space, equipment and manpower to effectively discharge his activities,
- c) Has any past experience in the business of buying, selling or dealing in securities,
- d) Is subjected to any disciplinary proceedings under the rules, regulations and bye-laws of a stock exchange with respect to his business as a stock-broker involving either himself or any of his partners, directors or employees.

2.2 NSE Membership

There are no entry/exit barriers to the membership of NSE. Anybody can become a member by complying with the prescribed eligibility criteria and exit by surrendering membership without any hidden cost.

The members are admitted to different segments of the Exchange subject to the provisions of

the Securities Contracts (Regulation) Act, 1956, the SEBI Act, 1992, the rules, circulars, notifications, guidelines, etc. issued hereunder and the bylaws, rules and regulations of the Exchange. The trading members of NSE have certain benefits, which includes:

- a) Access to a nation-wide trading facility for equities, derivatives, debt and hybrid instruments / products;
- b) Ability to provide a fair, efficient and transparent securities market to the investors;
- c) Use of state-of-the-art electronic trading systems and technology;
- d) Dealing with an organisation which follows strict standards for trading & settlement at par with those available at the top international bourses and constantly strives to move towards a global marketplace in the securities industry.

2.2.1 New Membership

The persons eligible to become trading members of Exchange are:

- a) Individuals,
- b) Partnership firms registered under the Indian Partnership Act, 1932,
- c) Institutions, including subsidiaries of banks engaged in financial services,
- d) Banks for Currency Derivatives Segment,
- e) Body corporates including companies as defined in the Companies Act, 1956. A company is eligible to be admitted as a member if:
 - (i) It is formed in compliance with provisions of Section 12 of the Companies Act 1956 which mentions about the mode of forming incorporated company,
 - (ii) It complies with the financial requirements and norms as may be specified by SEBI,
 - (iii) The directors of the company shouldn't have been disqualified for being members of a stock exchange and should not have held the offices of the directors in any company which had been a member of the stock exchange and had been declared defaulter or expelled by the stock exchange, and
- (f) Such other persons or entities as may be permitted from time to time by RBI/SEBI under the Securities Contracts (Regulations) Rules, 1957.

Membership for Different Segments at NSE

Persons or Institutions desirous of securing admission as members (stock brokers) on the Exchange may apply for membership on any one of the following segment groups:

- a) Wholesale Debt Market (WDM) Segment,

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- b) Capital Market (CM) segment,
 - c) Capital Market (CM) and Wholesale Debt Market (WDM) segment,
 - d) Capital Market (CM) and Futures & Options (F&O) segment,
 - e) Capital Market (CM), Futures & Options (F&O) segment and Wholesale Debt Market (WDM) segment,
 - f) Currency Derivatives (CD) segment with or without the above mentioned segments,
 - g) Clearing Membership of National Securities Clearing Corporation Ltd. (NSCCL) as a Professional Clearing Member (PCM). Professional Clearing Members do not trade but only clear and settle trades executed by other trading members (TMs). Professional clearing membership is only applicable for the F&O and Currency Derivatives segments.

In addition to the trading membership in the F&O segment, the trading member can also take two types of clearing membership in the F&O Segment i.e. as a clearing member and self clearing member. The self clearing members clear and settle the trades executed by them only, either on their account or on account of their clients. Trading members cum clearing members can clear and settle their own trades as well as trades of other trading members.

Trading members registered in F&O segment and CD segment are eligible to trade in interest rate futures market.

2.2.2 Eligibility Criteria for Membership at NSE

The standards for admission of members are laid down by the Exchange in terms of corporate structure (shareholding pattern), capital adequacy (Paid up capital), net worth, Interest Free Security Deposit (IFSD), Collateral Security Deposit (CSD), track record, education, experience etc. This is done to ensure quality broking services so as to build and sustain confidence among investors in the Exchange's operations.

Corporate Structure (Shareholding Pattern)

Securities markets are inherently volatile and risky, and hence risk containment mechanisms are put in place by the stock exchange. One such risk containment tool is the concept of 'Dominant Promoter/Shareholder Group' which is very unique for applicants acquiring membership on the NSE. The shareholders holding the majority of shares have a dominant role in the affairs of the company. In case of any default by the broking entity, the Exchange should be able to identify and take action against the persons who are behind the company. The Exchange, therefore, needs to know the background, financial soundness and integrity of the shareholders holding such controlling interest. Hence, during the admission process (explained in the later section

of the book) the dominant shareholders are called for an interview with the Membership Recommendation Committee (MRC).

Dominant Promoter norms are applicable to all trading members. The norms relating to dominant promoters falls in different categories such as unlisted corporate trading member, listed corporate trading member, corporate shareholders, banks, central or state government owned finance and development institutions and foreign entities, which are given as under:

(i) Unlisted corporate trading member: In case of an unlisted corporate trading member, there are three conditions under which the corporate trading member will be eligible to constitute dominant promoter group. These conditions are given below:

If a person holds 51% of shares in the trading member corporate on his own or together with

- a) His relatives as defined under Companies Act 1956
- b) Person(s) falling within the definition of 'control'³ under the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997.
- c) The support of strategic investors in such corporate trading member. (Strategic investors mean the corporates or individual investors that add value to investments they make through industry and personal ties that can assist companies in raising additional capital including financial investors, venture capitalists and others who invest primarily with the aim of generating a large return on their investment).

(ii) Listed corporate trading member: In case of listed corporate trading members, any person(s) identified as promoter in the offer document or in any document for offer of securities to the public or existing shareholders or in the shareholding pattern disclosed by the corporate trading member under the provisions of the Listing Agreement, whichever is later, would be eligible to constitute dominant promoter group.

(iii) Corporate shareholders to be identified as dominant shareholders: Corporate shareholder is allowed to be identified as dominant shareholders (Dominant Promoter Group - DPG) of a corporate trading member provided that the corporate shareholder identifies any person or persons as their dominant promoter group as per the aforesaid norms applicable to the corporate trading member. In case the dominant promoter group consists of more than one corporate shareholder, the dominant promoter group should be identified separately for each such corporate shareholder.

³ Here 'control' means the right to appoint majority of directors or to control the management or policy decisions by virtue of the shareholding or management rights.

(iv) Banks, central or state government owned finance and/or development institutions: The following entities are allowed to be identified as dominant shareholder(s) provided they have a networth of at least ₹ 50 crores:

- a) Scheduled Banks,
- b) Central or State Government owned Finance and/or Development Institutions.
- c) Any financial institution registered and regulated by any regulatory authority such as RBI, SEBI, IRDA,
- d) Any other entity that is fit to be identified as dominant shareholder in the opinion of relevant authority.

(v) Foreign Entities: Foreign entities are allowed to take trading membership of the Exchange through their Indian subsidiary under the automatic approval route permitted by the government, subject to compliance with the following guidelines of the RBI in this regard.

- (a) The promoting foreign entity or its subsidiary should be either a bank or insurance organisation regulated by the Central Bank or such other appropriate regulatory authority of that country

Or

The promoting foreign entity or its subsidiary should be broking house/ participant in the securities market that is registered or regulated by the relevant regulatory authority of that country and that the relevant authority should be a member of International Organisation of Securities Commission (IOSCO). The entity should have a sound track record.

Or

The promoting foreign entity is one whose domestic arm or subsidiary is registered with SEBI for participation in any domestic venture for custodial or Asset Management services.

- b) The promoting foreign entity shall hold, directly or indirectly not less than 51 % of the controlling stake in the applicant company proposing to take the trading membership of the Exchange.
- c) The net worth of the entity having controlling stake in the applicant company or the promoting foreign entity should be at least ₹ 50 Crores.

A foreign entity is allowed to become part of the dominant promoter group of an existing trading member corporate provided it meets the dominant promoter group norms as applicable to Indian entities, FIPB (Foreign Investment Promotion Board) norms / RBI norms and any other requirements of the Exchange / SEBI as may be applicable from time to time.

Corporate trading members will also be allowed to change their shareholding pattern so long as such change is within the above norms and the existing Dominant Promoter Group (DPG) continues to hold controlling interest and prior approval from the Exchange is obtained. Once a DPG is identified during admission, the same has to be maintained at all points of time. In case of any change in the DPG, the trading member is required to seek fresh approval of the Exchange as it is done at the time of admission of new trading member and rules relating to the same apply. Inter-se transfer of shareholding among the dominant promoters, however will be exempt from the formalities as required in case of new trading membership. Any changes in the shareholding require prior approval from the Exchange, except in case of shareholding changes related to public shareholding in a listed company.

Failure to maintain the required level of shareholding by DPG is treated as a breach of the continuing membership norms and tantamounts to reconstitution of the trading member corporate. This is because the existing DPG would no longer hold controlling interest in the trading member corporate or alternatively a new group would have emerged with controlling stake. In such case the Exchange can initiate disciplinary action including withdrawal of trading facility of such trading members.

Networth and Other Deposit Requirements

The networth of the member is calculated as summation of Capital and free reserves less non allowable assets. Non allowable assets include fixed assets, pledged securities, member's card, non-allowable securities (unlisted securities), bad deliveries, doubtful debts and advances, prepaid expenses, intangible assets and 30% marketable securities.

Deposit requirements are of two types i.e. **Interest Free Security Deposit (IFSD) and Collateral Security Deposit (CSD)**. IFSD has to be in liquid cash while CSD can be in cash or non-cash form. Cash component means cash, bank guarantees, fixed deposit receipts, units of money market mutual fund and gilt funds and any other form of collateral as may be prescribed from time to time. Non-cash component means all other forms of collateral deposits like deposit of approved list of demat securities and units of the other mutual funds and any other form of collateral as may be prescribed from time to time.

The eligibility criteria for corporates, individuals and partnership firms for different segments of the Exchange are explained in Table 2.1 and 2.2 below.

Table 2.1: Eligibility Criteria for Membership-Corporates (Amount in ₹ Lakh)

Particulars/ Segments	CM	CM and F&O	WDM	CM and WDM	CM,WDM and F&O
Minimum Paid-up capital	30	30	30	30	30

Net Worth	100	100	200	200	200
		(Membership in CM segment and Trading/ Trading and self clearing membership in F&O segment)			(Membership in WDM segment, CM segment and Trading/ Trading and Self Clearing membership in F&O segment)
		300 (Membership in CM segment and Trading and Clearing membership in F&O segment)			300 (Membership in WDM segment, CM segment and Trading and Clearing membership in F&O segment)
Interest Free Security Deposit with NSEIL	85	110	150	235	260
Interest Free Security Deposit with NSCCL	15	15 *	NIL	15	15 *
Collateral Security Deposit with NSCCL	25	25**	NIL	25	25**
Annual Subscription	1	1	1	2	2
Advance Minimum Transaction Charges for Futures Segment	NIL	1	NIL	NIL	1
Education	Two directors should be HSC. Dealers	Two directors should be HSC. Dealers should also have passed SEBI approved certification test for Derivatives and	Two directors should be HSC. Dealers	Two directors should be HSC. Dealers	Two directors should be HSC. Dealers should also have passed FIMMDA-NSE

	should also have passed SEBI approved certification test for Capital Market Module of NCFM.	Capital Market Module of NCFM.	should also have passed FIMMDA -NSE Debt Market (Basic Module) of NCFM.	should also have passed FIMMDA-NSE Debt Market (Basic Module) of NCFM & Capital Market Module of NCFM.	Debt Market (Basic Module) of NCFM, Capital Market Module of NCFM & of NCFM & SEBI approved certification test for Derivatives
Experience	———— Two year’s experience in securities market —————				
Track Record	The Directors should not be defaulters on any stock exchange. They must be debarred by SEBI for being associated with capital market as intermediaries. They must be engaged solely in the business of securities sand must not be engaged in any fund-based activity.				

Net worth requirement for Professional Clearing members in F&O segment is ₹ 300 lakhs. Further, a Professional Clearing member needs to bring IFSD of ₹ 25 lakhs with NSCCL and Collateral Security Deposit (CSD) of ₹ 25 lakh with NSCCL as deposits.

**Additional IFSD of ₹ 25 lakhs with NSCCL is required for Trading and Clearing members (TM-CM) and for Trading and Self clearing members (TM/SCM).*

*** Additional Collateral Security Deposit (CSD) of ₹ 25 lakhs with NSCCL is required for Trading and Clearing members (TM-CM) and for Trading and Self clearing members (TM/SCM). In addition, a member clearing for others is required to bring in IFSD of ₹ 2 lakh and CSD of ₹ 8 lakh per trading member he undertakes to clear in the F&O segment.*

Table 2.2: Eligibility Criteria for Membership - Individuals/ Partnership Firms

(Amount in ₹ lakh)

Particulars	CM	CM and F&O	WDM	CM and WDM	CM,WDM and F&O
Net Worth	75	75 (Membership in CM segment and Trading membership in F&O segment)	200	200	200 (Membership in WDM segment, CM segment and trading/ Trading and

		100 (Membership in CM segment and Trading and Self clearing membership in the F&O segment)			Self Clearing membership in F&O segment)
		300 (Membership in CM segment and Trading and Clearing membership in F&O segment)			300 (Membership in WDM segment, CM segment and Trading and clearing membership on F&O segment)
Interest Free Security Deposit (IFSD) with NSEIL	26.5	51.5	150	176.5	201.5
Interest Free Security Deposit (IFSD) with NSCCL	6	6*	NIL	6	6*
Collateral Security Deposit (CSD) with NSCCL	17.5	17.5 **	NIL	17.5	17.5 **
Annual Subscription	0.5	0.5	1	1.5	1.5
Advance Minimum Transaction Charges for Futures Segment	NIL	1	NIL	NIL	1
Track Record	The Partners/Proprietor should not be defaulters on any stock exchange. They must not be debarred by SEBI for being associated with capital market as intermediaries. They must be engaged solely in the business of securities and must not be engaged in any fund-based activity.				

**Additional IFSD of ₹ 25 lakhs with NSCCL is required for Trading and Clearing Members (TM-CM) and for Trading and Self clearing members (TM/SCM).*

*** Additional Collateral Security Deposit (CSD) of ₹ 25 lakh with NSCCL is required for Trading and Clearing members(TM-CM) and for Trading and Self clearing member (TM/SCM).*

In addition to certain eligibility criterion, there are certain professional requirements for clearing membership as described in Table 2.3 below.

Table 2.3: Requirements for Professional Clearing Membership

(Amount in ₹ lakh)

Particulars	CM Segment	F&O Segment
Eligibility	Trading Member of NSE/SEBI Registered Custodians/ Recognized Banks	
Net Worth	300	300
Interest Free Security Deposit (IFSD) *	25	25
Collateral Security Deposit (CSD)	25	25
Annual Subscription	2.5	Nil

**The Professional Clearing Member (PCM) is required to bring in IFSD of ₹2 lakh and CSD of ₹8 lakh per trading member whose trades he undertakes to clear in the F&O segment and IFSD of ₹6 lakh and CSD of ₹17.5 lakh (₹9 lakh and ₹25 lakh respectively for corporate Members) per trading member in the CM segment.*

The following Table 2.4 provides the eligibility criterion for trading membership and clearing membership for currency derivatives.

Table 2.4: Currency Derivatives - Corporates, Individuals and Firms

(Amount in ₹ Lakh)

Particulars	NSE Members		NCDEX Members		New Applicants		Professional Clearing Membership
	Trading Membership	Trading cum Clearing Membership	Trading Membership	Trading cum Clearing Membership	Trading Membership	Trading cum Clearing Membership	
Networth	100	1000	100	1000	100	1000	1000
Interest Free Security Deposit with NSEIL	2	2	2	2	2	2	-
Collateral	8	8	10.5	13	13	18	-

Security Deposit with NSEIL							
Interest Free Security Deposit with NSCCL	-	25	-	25	-	25	25
Collateral Security Deposit with NSCCL	-	25	-	25	-	25	25
Education	Two directors should be HSC. Dealers should also have passed SEBI approved National Institute of Securities Markets (NISM) Series I – Currency Derivatives Certification Examination						
Experience	-----Two year's experience in securities market-----						
Track Record	The Directors/Partners/Proprietor should not be defaulters on any stock exchange. They must not be debarred by SEBI for being associated with capital market as intermediaries. They must be engaged solely in the business of securities and must not be engaged in any fund-based activity.						

In addition to the individuals, corporates and partnership firms, Banks authorized by the Reserve Bank of India under section 10 of the Foreign Exchange Management Act, 1999 as 'AD Category - I bank' are permitted to become trading and clearing members of the currency derivatives market of the recognized stock exchanges, on their own account and on behalf of their clients, subject to minimum prudential requirements of minimum net worth of ₹ 500 crores, minimum CRAR of 10 per cent, net NPA not exceeding 3 per cent and net profit should have been made for last 3 years.

The AD Category - I banks which fulfill the prudential requirements are required to lay down detailed guidelines with the approval of their Boards for trading and clearing of currency derivatives contracts and management of risks. AD Category - I banks which do not meet the above minimum prudential requirements and AD Category - I banks which are Urban Cooperative banks or State Co-operative banks can participate in the currency derivatives market only as clients, subject to approval therefore from the respective regulatory Departments of the Reserve Bank.

2.2.3 Admission Procedure for New Membership

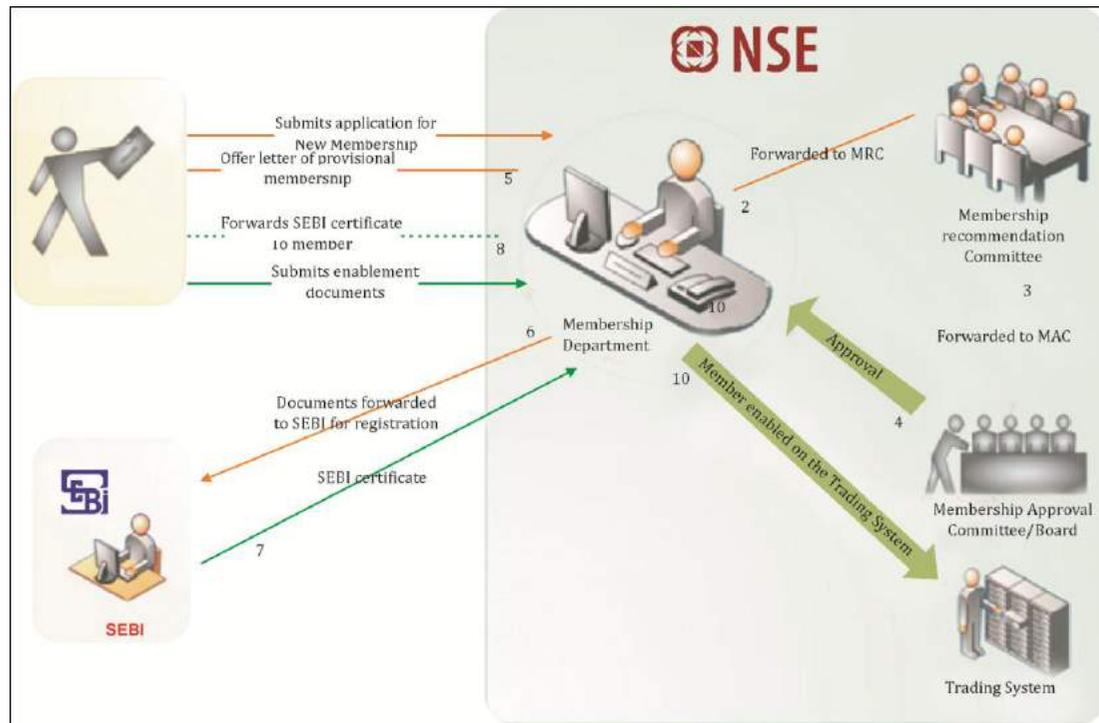


Figure: 2.1 Admission Procedure for New Membership at NSE

Admission is a two-stage process with applicants requiring to go through an examination (a module of NCFM) followed by an interview with the Membership Recommendation Committee. At any point of time the applicant has to ensure that at least the sole proprietor/one of the designated partner/one of the designated director/compliance officer has a valid certificate of Securities Market (Basic) Module or Compliance Officers (Brokers) Module or the relevant module pertaining to the segments wherein membership of the Exchange has been sought i.e.

- Capital Market (Dealers) Module
- Derivatives Market (Dealers) Module
- National Institute of Securities Markets (NISM) Series I – Currency Derivatives Certification Examination

The admission procedure for new membership depicted in figure 2.1 is explained below:

Applicants are required to submit application form, in the prescribed format along with other relevant documents to the Exchange.

The application for new membership is then forwarded to Membership Recommendation Committee. The Membership Recommendation Committee (MRC)



consists of seven persons from various disciplines. The MRC conducts interviews of the applicants for trading membership. In case of corporates, the dominant shareholder and designated directors; in case of individuals, the individual himself and in case of partnership firms – two designated partners have to appear for the interview. The purpose of the interview is to acquire information about their capability & commitment to carry on stock broking activities, financial standing and integrity.

The MRC recommends the names for admission of trading members to the Membership Approval Committee (Sub-committee of board of directors)/Board of directors of the Exchange.

The Board of Directors after taking into consideration the recommendations of the MRC either approves or rejects the applications.

On getting approval from the Board, an admission on a provisional basis is provided to the applicant subject to certain conditions like registration with SEBI, submission of relevant fees/ deposits and documents. The documents of the member are then forwarded to SEBI for registration.

After satisfying itself as to compliance with respect to all the prescribed norms, SEBI grants a Registration Certificate in the name of the applicant.

The applicant then has to remit the prescribed membership deposits (as required by the demand advice attached to the provisional offer letter) within the time frame prescribed in the demand advice attached to the provisional offer letter.

After obtaining SEBI Registration, the trading member has to satisfy the Exchange and NSCCL regarding all the formalities and requirements such as payment of fees/deposits and submission of relevant documents, for enablement. The dealers on CM segment are required to clear the Capital Market (Dealers) Module of NCFM; dealers on Futures & Options Segment are required to clear the Derivatives Market (Dealers) Module or equivalent examination of NCFM and dealers on Currency Derivatives segment are required to clear National Institute of Securities Market (NISM) Series I- Currency Derivatives Certification Examination. This is a pre-requisite without which user-ids are not issued.

After ensuring that all the formalities and requirements with regard to the Exchange and NSCCL are complied, the Trading Member is enabled to trade on the NEAT system.

2.3 Surrender of Trading Membership

Trading members can apply for surrender of their trading membership once admitted to the Exchange. Surrender of trading membership can be permitted by the Exchange after fulfilling certain conditions by the member such as, clearing off all the dues to the Exchange and NSCCL, notifying all other TMs of the approval of surrender, obtaining 'No dues' certificate from SEBI, issuance of a public notification in leading dailies etc. The deposits of the trading

members would be released by the Exchange/NSCCL after a prescribed lock-in period. There is, however, no lock-in period applicable in case of trading member, who is

- a) Not SEBI registered
- b) SEBI registered but not enabled
- c) SEBI registered and enabled but not traded at all

NSE provides a scheme for enabling the trading member to surrender their membership to the Exchange. Details of the norms and procedures related to the surrender of membership to the Exchange are prescribed as below:

- a) A trading member desirous of surrendering its membership of the Exchange is required to send its request in writing in the prescribed format.
- b) Before submission of an application for surrender of membership, the trading member is required to comply with all the pre-requisites for application of surrender in the prescribed format. The following aspects should be covered in the application for surrender of membership from a trading member,
 - (i) Who has been suspended/ disciplinary action taken by the Exchange /SEBI
 - (ii) In respect of whom any investigation/ action consequent to a default has been initiated by the Exchange /SEBI,
 - (iii) Who is falling within the category of 'associates' as defined by SEBI,
 - (iv) Who owes dues to the Exchange/ NSCCL,
 - (v) Against whom claims by investors of value of ₹10 lakh or more are pending or any claim for any amount is pending for a period more than 6 months,
 - (vi) Against whom any other claim /complaint is pending which, in the opinion of the Exchange/ NSCCL, needs to be resolved by the concerned trading member,
 - (vii) Whose turnover fees liability to SEBI is still outstanding,

The Exchange has absolute discretion in dealing with such applications and if it decides to process/accept the surrender application of such trading member, it may impose additional terms and conditions as it may deem fit.

- c) No trading member, who has surrendered its trading membership, their partners (in case of partnership firm) and/ or dominant shareholders (in case of corporates) is eligible to be re-admitted to the trading membership of the Exchange in any form for a period of one year from the date of cessation of trading membership (i.e. from the date of approval of surrender).
- d) The application of surrender of trading membership is subject to fulfillment of certain conditions, such as submission of original SEBI registration certificate(s) on all



segments on which the trading member is registered; submission of sub-broker registration certificate(s) of all the sub-brokers associated with the trading member for onward transmission to the SEBI for cancellation etc.

- e) The trading member should request the Exchange through their surrender application to dismantle and recover all the leased line(s)/ VSAT(s) and other equipments given to them at their dealing offices.
- f) A notice to public by way of a public notification in newspapers should be made by the Exchange and certain time (from the date of public notification) is given to investors, public, etc. to lodge claims against the surrendering trading member.
- g) A letter is also sent to SEBI seeking pending dues, if any, from member.
- h) On the expiry of period for receipt of investor claims and on receipt of intimation of dues amount, if any, from SEBI, the total amount payable by the member should be appropriated against trading member's deposits available with the Exchange / NSCCL and the trading member will be intimated accordingly. In case the amount payable exceeds the deposits, the trading Member would be intimated to bring in the requisite amount within 21 days of intimation. Upon the failure of the member to do so within 21 days of intimation, the case shall be referred to the relevant authority for further action.

2.4 Suspension & Expulsion of Membership

The Exchange may expel or suspend, fine under censure, warn, withdraw any of the membership rights of a trading member if it is guilty of contravention, non-compliance, disobedience, disregard or evasion of any of the bye-laws, rules and regulations of the Exchange or of any resolutions, orders, notices, directions or decisions or rulings of the Exchange or the relevant authority.

2.4.1 Basis of Suspension of Membership

Following are some grounds on basis of which there can be suspension or expulsion of membership:

- (i) **Misconduct:** A trading member is deemed guilty of misconduct for any of the following or similar acts or omissions namely:
 - a) Fraud or fraudulent act or if he is convicted of a criminal offence.
 - b) Violation of the provisions of any statute governing the activities, business and operations of the Exchange.
 - c) Improper conduct.
 - d) Failure to submit to or abide by arbitration.
 - e) Failure to testify or give information sought by the Exchange or any committee or any other person authorized on that behalf.

- f) Failure to submit special returns in such form as the relevant authority may from time to time prescribe.
- g) Failure to submit audited accounts.
- h) Failure to compare or submit accounts with defaulter.
- i) Failure to submit or make any false or misleading returns.
- j) Make vexatious, malicious or frivolous complaints.
- k) Failure to pay subscription fee, arbitration charges etc.

(ii) Un-businesslike conduct: A trading member is deemed guilty of un-businesslike conduct for any of the following or similar acts or omissions namely:

- a) Transaction or business dealings in fictitious names.
- b) Circulation of rumours.
- c) Any unfair dealing in securities which does not reflect the true market values.
- d) Market manipulation and rigging.
- e) Unwarrantable business which effects purchases or sales for its account or any account related to the trading member.
- f) If a trading member accepts less than a full and bonafide money payment in settlement of a debt due by another trading member arising out of a transaction in securities.
- g) Dishonoured cheque.
- h) Failure to carry out transactions with constituents.

(iii) Unprofessional conduct: A trading member is deemed guilty of unprofessional conduct for any of the following or similar acts or omissions namely:

- a) Business in securities in which dealings not permitted
- b) Business for defaulting constituent who failed to carry out engagements relating to securities and is in default to another trading member
- c) Transacts in business with an insolvent without obtaining the consent of the relevant authority even if the individual has obtained his final discharge from an insolvency court
- d) Carrying out his business during his suspension period
- e) Business with suspended, expelled and defaulter trading members
- f) Business for employees of other trading members

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- g) Business for Exchange employees if it makes a speculative transaction in which an employee of the Exchange is directly or indirectly interested
 - h) If it advertises for business purposes or issue regularly circular or other business communications to persons other than its own constituents, trading members of the Exchange, banks and joint stock companies or publishes pamphlets, circular or any other literature or report or information relating to the stock markets with its name attached
 - i) Evasion of margin requirements
 - j) Evasion of brokerage charges
 - k) Dealings with entities prohibited by SEBI to buy or sell or deal in securities market

(iv) Trading member's responsibility for partners, agents and employees: A trading member is fully responsible for the acts and omissions of its partners, authorised officials, attorneys, agents, authorised representatives and employees. If any such act which is against the relevant rules and regulations is committed or omitted by them then the trading member is liable to the same penalty to the same extent as that act or omission would have been done or omitted by itself.

(v) Suspension on failure to provide margin deposit and/or capital adequacy requirements: The Exchange can suspend the business of a trading member when it fails to provide the margin deposit and/or meets capital adequacy norms as provided in the Bye Laws, Rules and Regulations. The trading member shall remain suspended until he furnishes the necessary margin deposit or meet the capital adequacy requirements.

2.4.2 Suspension of Business

The relevant authority may require a trading member to suspend its business in part or in whole under following conditions:

- a) **Prejudicial business:** When the relevant authority finds that the trading member conducts business in a manner prejudicial to the Exchange by making purchases or sales of securities or offers to purchase or sell securities for the purpose of upsetting equilibrium of the market or bringing about a condition of demoralisation in which prices will not fairly reflect market values, or
- b) **Unwarrantable business:** When in the opinion of the relevant authority the trading member engages in unwarrantable business or effects purchases or sales for its constituent's account or for any account in which it is directly or indirectly interested which purchases or sales are excessive in view of its constituent's or its own means and financial resources or in view of the market for such security, or

- c) **Unsatisfactory financial condition:** When the relevant authority finds that the trading member is in a bad financial condition and it cannot be permitted to do business with safety to its creditors or the Exchange.

2.4.3 Removal of Suspension

The suspension of business as above shall continue until the trading member has been allowed by the relevant authority to resume business. It may be done on its paying such deposit or on its doing such act or providing such thing as the relevant authority may require.

2.4.4 Consequences of Suspension

The suspension of a trading member has the following consequences:

- a) **Suspension of membership rights:** The suspended trading member shall during the terms of its suspension be deprived of and excluded from all the rights and privileges of membership. It shall also include the right to attend or vote at any meeting of the general body of trading members of the relevant segment.
- b) **Rights of creditors unimpaired:** The suspension should not affect the rights of the trading members who are creditors of the suspended trading member.
- c) **Fulfillment of contracts:** The suspended trading members are bound to fulfill contracts outstanding at the time of its suspension.
- d) **Further business prohibited:** The suspended trading member should not during the terms of its suspension make any trade or transact any business with or through a trading member. With the permission of the relevant authority, however it can close the transactions outstanding at the time of its suspension.
- e) **Trading members not to deal with suspended trading member:** No trading member is allowed to transact in business with a suspended trading member during the terms of its suspension except with the prior permission of the relevant authority.

2.4.5 Consequences of Expulsion

The expulsion of a trading member has the following consequences:

- a) **Trading membership rights forfeited:** The expelled trading member shall forfeit to the Exchange its right of trading membership and all rights and privileges as a trading member of the Exchange including any right to the use of or any claim upon or any interest in any property or funds of the Exchange but any liability of any such trading member to the Exchange or to any trading member of the Exchange shall continue and remain unaffected by its expulsion.
- b) **Office vacated:** The expulsion would create a vacancy in any office or position held by the expelled trading member.

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- c) Rights of creditors unimpaired: The expulsion does not affect the rights of the trading members who are creditors of the expelled trading member.
 - d) Fulfillment of contracts: The expelled trading members are bound to fulfill transactions outstanding at the time of his expulsion and it may with the permission of the relevant authority close such outstanding transactions with or through a trading member.
 - e) Trading members not to deal with expelled trading member: No trading member is allowed to transact business for or with or share brokerage with the expelled trading member except with the previous permission of the relevant authority.
 - f) Consequences of declaration of defaulter to follow: The provisions of pertaining to default and Protection Fund mentioned in the byelaws become applicable to the trading member expelled from the Exchange as if such trading member has been declared a defaulter.

2.5 Declaration of Defaulter

A trading member may be declared a defaulter by direction/circular/notification of the relevant authority of the trading segment if:

- a) He is unable to fulfill his obligations; or
- b) He admits or discloses his inability to fulfill or discharge his duties, obligations and liabilities; or
- c) He fails or is unable to pay within the specified time the damages and the money difference due on a closing-out effected against him under the bye laws, rules and regulations; or
- d) He fails to pay any sum due to the Exchange or to submit or deliver to the Exchange on the due date, delivery and receive orders, statement of differences and securities, balance sheet and such other clearing forms and other statements as the relevant authority may from time to time prescribe; or
- e) If he fails to pay or deliver to the defaulters' committee all monies, securities and other assets due to a trading member who has been declared a defaulter within such time of the declaration of default of such trading member as the relevant authority may direct; or
- f) If he fails to abide by the arbitration proceedings as laid down under the bye laws, rules and regulations.

Without prejudice to the foregoing, if a trading member is either expelled or declared a defaulter by any other recognised stock exchange on which he is a member or if the registration certificate is cancelled by SEBI, then the said trading member is expelled from the Exchange.

2.6 Authorised Persons

Trading members of the Exchange can appoint authorised persons in the Capital Market, Futures & Options and Currency Derivatives Segments. Authorised Person is “Any person-individual, partnership firm, Limited Liability Partnership (LLP) or body corporate who is appointed as such by a stock broker (including trading member) and who provides access to trading platform of a stock exchange as an agent of the stock broker.” Authorised Person can receive remuneration - fees, charges, commission, salary, etc. for his services only from the stock broker and shall not charge any amount from the clients. Accordingly, stock broker can share brokerage with the Authorised Person but shall not charge any amount directly from the clients

The clients introduced by the authorised person should have a direct relationship with the trading member i.e. the member-constituent agreement, know your client forms, risk disclosure document, etc. are executed between the client and the trading member. This implies that the authorised person is not allowed to have any trading relationship with the clients. The trading member should issue the contract notes and bills directly to the client i.e. the authorized person should not issue contract notes, confirmation memo and/or bills in their name.

The clients introduced by the authorised person are required to deliver securities and make payments directly in the trade name of the trading member (as appearing on the SEBI registration certificate). Similarly, the trading member should deliver securities and make payments directly in the name of the clients.

2.7 Sub-Brokers

Sub broker is an important intermediary between stock broker and client in capital market segment. The trading members of the Exchange may appoint sub-brokers to act as agents of the concerned trading member for assisting the investors in buying, selling or dealing in securities. The sub-brokers are affiliated to the trading members and are required to be registered with SEBI. A sub-broker is allowed to be associated with only one trading member of the Exchange.

Trading members desirous of appointing sub-brokers are required to submit the following documents to the Membership Department of the Exchange:

- a) Copy of sub-broker - broker agreement duly certified by the trading members
- b) Application form for registration as a sub-broker with Securities and Exchange Board of India (Form B)
- c) Recommendation letter to be given by the trading member with whom the sub-broker is affiliated (Form C)



The trading member has to ensure the settlement of all deals entered into by a trading member even if the deals may have originated from its sub-broker.

The sub-broker will be required to adhere to NSE's 'know your clients' requirements. The important documents relating to dealing through a sub-broker are given below:

- a) Individual client registration application form
- b) Non-individual client registration application form
- c) Sub-broker client agreement

2.7.1 Eligibility

A sub-broker may be an individual, a partnership firm or a corporate. In case of corporate or partnership firm, the directors or partners and in the case of an individual sub-broker applicant should comply with the following requirements:

- a) They should not be less than 21 years of age;
- b) They should not have been convicted of any offence involving fraud or dishonesty;
- c) They should have either passed 12th standard equivalent examination from an institution recognized by the Government or 10th standard with 2 years of work experience in securities market.
- d) They should not have been debarred by SEBI

2.7.2 Registration

No sub-broker is allowed to buy, sell or deal in securities, unless he or she holds a certificate of registration granted by SEBI. Sub-brokers are required to obtain certificate of registration from SEBI in accordance with SEBI (Stock Brokers & Sub-brokers) Rules and Regulations, 1992, without which they are not permitted to buy, sell or deal in securities. SEBI may grant a certificate to a sub-broker, subject to the conditions that:

- a) He should pay the fees in the prescribed manner;
- b) He should take adequate steps for redress of grievances of the investors within one month of the date of the receipt of the complaint and keep SEBI informed about the number, nature and other particulars of the complaints received;
- c) In case of any change in the status and constitution, the sub-broker should obtain prior permission of SEBI to continue to buy, sell or deal in securities in any stock exchange; and
- d) He should be authorised in writing, by a stock-broker being a member of a stock exchange for affiliating himself in buying, selling or dealing in securities.

The applicant sub-broker should submit the required documents to the stock exchange with the recommendation of a trading member. After verifying the documents, the stock

exchange may forward the documents of the applicant sub-broker to SEBI for registration. A sub-broker can trade in that capacity after getting himself registered with SEBI. The Exchange may not forward the application of the sub-broker to SEBI for registration if the applicant dealt with fake, forged, stolen, counterfeit etc. shares and securities in the market.

2.7.3 Cancellation of Registration

In case a trading member/sub-broker intends to cancel the registration as a sub-broker, the sub-broker is required to submit the original SEBI Registration certificate through their affiliated trading member. While applying for cancellation of registration, the affiliated trading member needs to give a public notification to this effect.

2.8 Broker-Clients Relations

2.8.1 Client Registration Documents

The trading member (TM) is required to enter into an agreement in the specified format provided by NSE with the client before accepting orders on latter's behalf. The agreement is executed on non-judicial stamp paper of adequate value, duly signed by both the parties on all the pages. Copy of the agreement has to be kept with the TM permanently. The agreement should contain all the clauses mentioned in Uniform Documentary Requirement (UDR). Stock broker may incorporate any additional clauses in these documents provided these are not in conflict with any of the clauses in the model document, and also the rules, regulations, articles, byelaws, circulars, directives and guidelines. There should be segregation of mandatory and voluntary documents/clauses pertaining to client registration in separate docket (compilation of documents). In case of internet trading, in addition to clauses mentioned in UDR, the client has to mention clauses pertaining to internet trading.

Under "Know Your Client (KYC)" requirements, the TM should seek information such as: investor risk profile, financial profile, investor identification details, address details, income, PAN number, employment, age, investments experience, trading preference. The TM has to obtain recent passport size photograph (photographs of partners/whole time directors, individual promoters holding 5% or more, either directly or indirectly, in the shareholding of the company and of persons authorized to deal in securities, and of each of their clients in case of individual clients). The TM should also take proof of identification and address of the client. In-person verification should be done by the trading member's staff, name & signature of the person doing the in-person verification together with the stamp of trading member should be there on the KYC form.

Under Member Constituent Agreement (MCA), trading members are required to make the constituent/clients aware of (a) trading segment to which TM is admitted, (b) particulars of SEBI registration number, (c) the precise nature of the trading member's liability for business to be conducted, (d) basic risks involved in trading on the



Exchange (equity and other instruments) including any limitations on the liability and the capacity in which the trading member acts.

In order to assess the risk involved in trading, TM is required to issue Risk Disclosure Document (RDD)⁴ in such format, as may be prescribed by the Exchange from time to time and should obtain the same from his constituents duly signed.

A stock-broker should not deal knowingly, directly or indirectly, with a client who defaults to another stock-broker. There is no limit on the number of clients for a TM.

Copy of the client registration documents is required to be sent to the clients. Trading member must ensure periodic review of client's financial information & client database.

2.8.2 Unique Client Code (UCC)

SEBI has made it mandatory for all trading members/brokers to use unique client codes for all clients. Brokers are required to collect and maintain the Permanent Account Number (PAN) allotted by Income Tax Department for all their clients.

Brokers should verify the documents with respect to the unique code and retain a copy of the document. They are also required to provide the PAN and UCC of their clients to the stock exchanges/clearing corporations and these details have to be updated before placing orders for the clients. The stock exchanges are also required to maintain a database of client details submitted by brokers.

2.8.3 Margins from the Clients

Members should have a prudent system of risk management to protect themselves from client default. Margins are an important element of such a system. The policy of risk management addressing the margin requirements should be well documented and be made accessible to the clients and the stock exchanges. In capital market segment, however, the quantum of these margins, the form and the mode of collection are left to the discretion of the members⁵. The margin so collected is kept separately in the client bank account/client beneficiary account. In case of default, they are utilized for making payment to the clearing corporation for margin and settlement with respect to that client.

2.8.4 Execution of Orders

Where the constituent requires an order to be placed or any of his order to be modified after the order has entered the system but has not been traded, the trading member may, if it so desires, obtain order placement/modification details in writing from the constituent. The trading member should accordingly provide the constituent with the relevant order confirmation/ modification slip or copy thereof, forthwith, if so required by the constituent.

⁴ The said documents are to be obtained as per Exchange circular NSE/INSP/5387 dt. 27-Aug-04

⁵ SEBI/MRD/DoP/SE/Cir-07/2005 dated February 23, 2005

Where the constituent requires any of his orders to be cancelled after the order has been entered in the system but has not been executed, the trading member may, if it so desires, obtain the order cancellation details in writing from the constituent. The trading member should accordingly provide the constituent with the relevant order cancellation details, forthwith, if so required by the constituent. The trading member may, if it so desires, obtain in writing, the delivery and payment requirement in any instructions of an order that it receives from the constituent.

Where a trading member receives a request for order modification or order cancellation from the constituent, it should duly bring it to their notice that if the total order results in a trade in the meantime, the requests for modification or cancellation cannot be executed.

2.8.5 Contract Note

Contract note is a confirmation of trade(s) done on a particular day for and on behalf of a client. A stock-broker should issue a contract note to his clients for trades (purchase/sale of securities). The contract note should contain name and address (registered office address as well as dealing office address) of the TM, the SEBI registration number of the TM, details of trade viz. order number, trade number, order time, trade time, security name, quantity, trade price, brokerage, settlement number and details of other levies.

As per Regulation 18 of SEBI (Stock-Brokers & Sub-Brokers) Regulations, 1992, the TM should preserve the duplicate copy of the contract notes issued for a minimum of five years. The TM should ensure that:

- a) Contract note is issued to a client within 24 hours and should be signed by the trading member or by an authorized signatory trading member.
- b) Contract notes are in the prescribed format⁶.
- c) Stamp duty is paid,
- d) All statutory levies are shown separately in the contract note

2.8.6 Payments/Delivery of Securities to the Clients

Every TM should make payments to his clients or deliver the securities purchased within one working day of pay-out unless the client has requested otherwise.

2.8.7 Brokerage

The maximum brokerage chargeable by TM in respect of trades effected in the securities admitted to dealing on the CM segment of the Exchange is fixed at 2.5% of the contract

⁶ As per circular NSE/LEGL/7036 dated January 05, 2006 in Cash Market segment



price, exclusive of statutory levies. This maximum brokerage is inclusive of sub-brokerage. The brokerage should be indicated separately from the price, in the contract note. The TM may not share brokerage with a person who is a TM or in employment of another TM.

For example: If a client has sold 10000 shares of a scrip @ ₹ 50, what is the maximum brokerage that the client can be charged?

In this case, the maximum brokerage = brokerage rate*value of the transaction
= 2.5 %*(10000 shares *₹ 50) = ₹ 12,500

2.8.8 Segregation of Bank Accounts

The TM should maintain separate bank accounts for client's funds and own funds. It is compulsory for all TMs to keep the money of the clients in a separate account and their own money in a separate account. Funds should be transferred from the client account to the clearing account for the purpose of funds pay-in obligations on behalf of the clients and vice-versa in case of funds pay-out. No payment for transaction in which the TM is taking position as a principal is allowed to be made from the client's account.

2.8.9 Segregation of Demat (Beneficiary) Accounts

The trading members should keep the dematerialised securities of constituents in a separate beneficiary account distinct from the beneficiary account maintained for holding their own dematerialised securities. No delivery towards the own transactions of the trading members is allowed to be made from the account meant for constituents. For this purpose, every trading member is required to open a beneficiary account in the name of the trading member exclusively for the securities of the constituents (to be referred to as "constituents' beneficiary account"). A trading member may keep one consolidated constituents' beneficiary account for all its constituents or different accounts for each of its constituents as it may deem fit.

2.9 Sub-Broker-Clients Relations

2.9.1 Relationship with clients

A sub-broker is required to enter into a tripartite agreement with its clients and the stock broker specifying the scope of rights and obligations of the sub-broker, the stock broker and such client of the sub-broker as per the format prescribed by SEBI for dealing in securities in cash segment. There should be privacy of contract between the stock broker and the sub-broker's client. A separate agreement has to be executed for each Exchange.

Sub-broker is required to help the client in redress of grievance in respect of transactions executed through its associated broker. Sub-broker is also required to assist and co-operate in ensuring faster settlement of any arbitration proceeding arising

out of the transaction entered through its associated broker and is jointly/severally liable to implement the arbitration award.

A sub-broker should provide assistance to stock broker and clients to reconcile their accounts at the end of each quarter with reference to all the settlements where payouts have been declared during the quarter.

2.9.2 Contract notes

A stock broker should issue contract note as per the format prescribed by the Exchange to client introduced through a sub-broker. A sub-broker should render necessary assistance to its client in obtaining the contract note from the stock broker. Sub-broker should not issue any contract note or confirmation memo to its client.

2.9.3 Securities/ Funds

Transactions in securities executed on behalf of a client introduced through the sub-broker should be settled by delivery/ payment between the stock broker and the client directly, in accordance of the rules, regulations and byelaws of the Exchange and such settlements should not take place through sub-broker. Delivery of securities and payment of funds relating to the transactions of a client introduced by the sub-broker should be directly between the stock broker and the client of the sub broker.

2.10 Investor Service Cell and Arbitration

Investor complaints received against the trading members / companies in respect of claims/ disputes for transactions executed on the Exchange are handled by the Investor Service Cell (ISC). The complaints are forwarded to the trading members for resolution and seeking clarifications. The ISC follows-up with the trading members and makes efforts to resolve the complaint expeditiously. In certain cases, on account of conflicting claims made by the investor and the trading member, when it is not possible to administratively resolve the complaint, investors are advised to take recourse to the arbitration mechanism prescribed by the Exchange.

Arbitration, which is a quasi judicial process, is an alternate dispute resolution mechanism prescribed under the Arbitration and Conciliation Act, 1996. The Exchange bye-laws prescribe the provisions in respect of arbitration and the procedure therein has been prescribed in the regulations. The reference to arbitration should be filed within six months from the date when the dispute arose. The time taken by the ISC is excluded by the arbitrator, while considering the issue of limitation.

2.11 Code of Advertisement

Trading Members of the Exchange while issuing advertisements in the media have to comply with the Code of Advertisement prescribed by the Exchange. In pursuance of that, a copy of an advertisement has to be submitted to the Exchange to get a prior approval before its issue in publication/media. The trading members may apply for approval of advertisement as per the



application format. Trading Members not complying with the Code of Advertisement may have to face disciplinary proceedings.

The code of Advertisement is as follows:

1. The term advertisement as referred in this code means and includes any document, pamphlets, circulars, brochures, notice or any research reports, material published, or designed for use in a newspaper, magazine or other periodical, radio, television, telephone or tape recording, video tape display, signs or bill boards, motion pictures, telephone directories (other than routine listings) or other public media, whether in print or audio visual form.
2. The Trading Member should designate and authorise a person to ensure the correctness of the information given in any advertisement.
3. The Trading Member issuing any such advertisement should inform the name of such authorized person to the Exchange.
4. The advertisement should be related to the nature of services that the Trading Member can offer. If the Trading Member is engaged in any other business then any advertisement if permissible for such business should not indicate the name of the Trading Member as a member of the Exchange.
5. The advertisement should be written in clear language and should not be such which may prejudice interest of the investors in general.
6. The advertisement should not contain any confusing, misleading or offensive information.
7. It should be free from inaccuracies.
8. The advertisement should not contain a recommendation regarding purchase or sale of any particular share or security of any company. It should not make any promise including guaranteeing of any return to the investing public.
9. The material should not contain anything that is otherwise prohibited.
10. The Advertisement shall contain :-
 - a) Name and/or his logo, code of National Stock Exchange membership.
 - b) Registration No. allotted by the Securities and Exchange Board of India.
11. The Advertisement may be issued individually or jointly with other Trading Members provided that the Trading Member shall not allow its name to be advertised or caused to be published in the advertisement of other Trading Members, unless such advertisement is issued by it.
12. In the event of suspension of any Trading Member by the Exchange, the Trading Member so suspended shall not issue any advertisement either singly or jointly with any other Trading Member, during the period of suspension.
13. In the event of any proceeding/action initiated against a Trading Member by a

- regulatory body other than National Stock Exchange, National Stock Exchange reserves the right to direct the Trading Member to refrain from issuing any advertisement for such a period as it may deem fit.
14. National Stock Exchange reserves the right to call for the advertisement and/or such other information/explanation as it may require, after the publication of the said advertisement. National Stock Exchange shall have 'cease and desist' powers in this behalf.
 15. The copy of such advertisement should be retained for a period of three years.
 16. A copy of the advertisement must be submitted to the Exchange within seven days before their issue. If the advertisement is found to violate any provisions of the Rules and Bye-laws of the Exchange or rules framed by the SEBI on this behalf, the Trading Member shall be subject to disciplinary proceedings by the Exchange.
 17. These norms will apply to any other investment/consultancy agencies associated with the Trading Member concerned.
 18. The above norms shall also apply to an advertisement, T.V or Cable T.V. or any other such media of audio/visual nature.
 19. The Trading Members should check with the Exchange in case of any doubt for advice prior to the issue of any such material or advertisement.
 20. The advertisement should not have any adverse reference regarding the reputation of any other Trading Members and also of the Exchange. While preparing any advertisement a Trading Member should keep in mind that any information if found to be incorrect will affect not only the reputation of the particular Trading Member but also the reputation of the Trading Members of the Exchange in general and also on the Exchange itself.
 21. In the event of any Trading Member of the Exchange having any grievance against any other Trading Member, consequent upon the publication of advertisement of the other Trading Member, the Exchange shall be informed of the same in writing, within a period of seven days from the date of such publication for necessary remedial measure from the Exchange.

SEBI has advised the stock exchanges to ensure that their brokers/sub-brokers do not advertise their business, including in their internet sites, by subsidiaries, group companies etc., in prohibition of code of conduct⁷. The code of conduct in the regulations require a stock broker/ sub-broker not to advertise his business publicly unless permitted by the stock exchange and not to resort to unfair means inducing clients from other stock brokers.

⁷ As specified in the Schedule II of the SEBI (Stock Brokers and Sub-brokers) Regulations, 1992 (SEBI circular Ref. No. SMDRP/Policy/Cir-49/2001 Dated October 22, 2001)