

## **Committee on “Strengthening Governance of Market Infrastructure Institutions” SEBI seeks public comments on the Report**

The Committee on Strengthening Governance of Market Infrastructure Institutions submitted its report to SEBI on November 2, 2022. SEBI has sought public comments on the Report.

SEBI had constituted a Committee, in April 2022, under the chairmanship of Shri G. Mahalingam, ex-Whole Time Member, SEBI, to review the existing governance framework and make recommendations for further strengthening of governance norms at MIIs.

The Committee consulted various stakeholders, including Public Interest Directors, Chief Regulatory Officers, representatives of MIIs and other relevant persons. It also took into consideration the past committee reports on governance of MIIs.

The report of the Committee sets out various recommendations on measures for

- a. strengthening the role played by the governing board and committees of MIIs;
- b. reviewing the requirements related to appointment and role & responsibility of directors on the board and key managerial persons (KMPs);
- c. developing effective metrics for monitoring various aspects of the functioning of the MIIs and its KMPs;
- d. enhancing accountability and transparency;
- e. reviewing the policy on safekeeping and sharing of information held by MIIs;
- f. revisiting the code of conduct and code of ethics for directors of the governing board and KMPs;
- g. activities and governance of investee companies of MIIs, etc.

Public comments on the recommendations of the Committee may be sent by email, in the following format:

| Name of the entity/person:       |                                  |                     |           |
|----------------------------------|----------------------------------|---------------------|-----------|
| Contact Number & E-mail Address: |                                  |                     |           |
| Sr. No.                          | Recommendation No. in the report | Suggestion/Comments | Rationale |
|                                  |                                  |                     |           |
|                                  |                                  |                     |           |

The comments may be sent by e-mail to Shri Manish Tekriwal ([manisht@sebi.gov.in](mailto:manisht@sebi.gov.in)) and Shri Dhanush Kumar Reddy ([ghanushs@sebi.gov.in](mailto:ghanushs@sebi.gov.in)) latest by November 30, 2022.



REPORT OF THE COMMITTEE ON  
“STRENGTHENING GOVERNANCE OF  
MARKET INFRASTRUCTURE INSTITUTIONS”



November 02, 2022



## Letter of Transmittal

November 02, 2022

Ms. Madhabi Puri Buch,  
Chairperson,  
Securities and Exchange Board of India  
Mumbai

Madam

### **Report of the Committee on Strengthening Governance of Market Infrastructure Institutions**

We have great pleasure in submitting the Report of the Committee on *“Strengthening Governance of Market Infrastructure Institutions”*.

We sincerely thank you for entrusting us with this task of contemporary relevance.

Yours faithfully,

(G. Mahalingam)  
Chairman

(J. N. Gupta)  
Member

(Ashish Chauhan)  
Member

(Vikram Limaye)  
Member

(Arun Raste)  
Member

(P.S Reddy)  
Member

(Padmaja Chunduru)  
Member

(Nehal Vora)  
Member

(Sandip Bhagat)  
Member

(Aarti Nihalani)  
Member

(Neeraj Kulshreshtha)  
Member

(Uttam Bagri)  
Member

(Amarjeet Singh)  
Member-Secretary

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## Acknowledgements

The Committee wishes to place on record its heartfelt thanks to several stakeholders of the capital market ecosystem who shared their perspectives with the Committee on streamlining the role of Market Infrastructure Institutions (MIIs), which constitute the basic edifice of the system. Special thanks are due to all Public Interest Directors and Share Holder Directors of the MIIs who attended the meetings and provided significant feedback for the Committee to consider and deliberate.

The Committee expresses its gratitude to a number of SEBI officials, particularly Shri V.S. Sundaresan, Executive Director; Shri B. Rajendran, Executive Director; Shri Ali Asgar Mithwani, Chief General Manager; Shri Debashis Bandyopadhyay, Chief General Manager; Shri Amit Kapoor, General Manager; Ms. Richa Goel, General Manager; Shri Vishal Shukla, General Manager; Shri Hruda Ranjan Sahoo, Deputy General Manager; Shri Jainendra Shandilya, Assistant General Manager; Shri Suman Kumar, Assistant General Manager; Ms. Rinkal Sanghavi, Assistant General Manager; Shri Manish Tekriwal, Assistant General Manager; Shri Kumar Rohit, Assistant General Manager; Shri Kennedy Rina, Manager; Shri Dhanush Kumar Reddy, Assistant Manager and Shri R.V. Aditya, Assistant Manager for their useful inputs and support during the course of the meetings and finalization of the report.

The committee would like to specially thank Ms. Jabarati Chandra, Shri Ananya Kumar and Ms. Oshika Nayak from S&R Associates for their strenuous efforts and invaluable assistance in drafting the report.



## Executive Summary

Market Infrastructure Institutions (MIIs) are unique institutions providing vital infrastructure of trading, settlement and record keeping. They are vested with regulatory responsibilities, while pursuing commercial interests like other profit-oriented entities. Because of this conflicting nature of MII's role, the governance standards of MIIs need to be robust to increase market confidence and deter malpractices. In light of the governance lapses observed in some of the MIIs, rapidly changing market dynamics and increasing reliance of MIIs on technology, a Committee headed by Shri G. Mahalingam, former Whole Time Member, SEBI was set up by SEBI to make recommendations for further strengthening the governance norms relating to MIIs.

As a part of its deliberations, the Committee consulted various stakeholders, including Public Interest Directors ("PIDs"), Shareholder Directors ("SHDs"), Chief Regulatory Officers ("CRO"), representatives of MIIs and other relevant persons. It also took into consideration International Principles and past reports on Governance of MIIs.

The Committee considered that MIIs in pursuance of their business objectives, should not lose sight of their regulatory roles vested upon them as a first line regulator. At the same time, the Committee acknowledged that tightening of the norms should not deter innovation or cause unintended consequences for the MIIs. Hence, a rule-based approach for the regulation of MIIs should be balanced with a principle-based approach in order to achieve the intended outcomes.

Key recommendations made by the Committee include the following:

1. The functions of MIIs should be categorized into three verticals viz. Critical Operations; Regulatory, Compliance and Risk Management; and Other functions including Business Development. The KMPs heading the functions under the first two verticals should be at par in hierarchy with the KMPs heading the third vertical.
2. In terms of resource allocation and utilization, the functions under the first two verticals separately should be given higher priority by MIIs over functions under the third vertical. The resources including the human as well as financial and technology resources deployed by MIIs for each of the core functions under different verticals should be quantified and disclosed in the annual report of the MIIs.

3. To ensure greater independence of the Board of the MII, at least two-third members of the Board of the MII shall comprise of PIDs. The roles and responsibilities of all directors should be clearly outlined especially their responsibilities towards regulatory, compliance and risk management functions.
4. The existing process of appointment of PIDs, Non-Independent Directors (“NID”) and Managing Director (“MD”) should be rationalized by mapping certain skill-sets/expertise to PIDs while maintaining an overall balance of expertise required in the Board. Further, provisions in SECC Regulations, 2018 and D&P Regulations 2018 should be incorporated to enable SEBI to appoint PIDs on the Board of the MII.
5. The role of the Board of the MII and its senior management team in upholding a strong culture in the MIIs should be clearly outlined through a set of guiding principles, especially focused on regulatory, compliance, risk and conduct related aspects.
6. The existing Board level Statutory Committees at MIIs should be rationalized with respect to their composition and functioning.
7. In order to enhance transparency, the MIIs should disclose the agenda and minutes of meetings of their Board, keeping in mind their role as a ‘first-level regulator’. To begin with, agendas related to regulatory, compliance & risk management areas may be disclosed on the website of the MII.
8. The Board of the MII or the Chairperson of the Board (without the presence of the MD and any other executive director), on a periodic basis as specified by SEBI, should meet the Chief Regulatory Officer (CRO)/ Compliance Officer, the Chief Risk Officer (CRiO), the Chief Information Security Officer (CISO), the Statutory Auditor of the MII and any other person as determined by the PIDs and NIDs to discuss important issues concerning the MII.
9. The PIDs should continue to meet twice a year and submit to SEBI a periodic report highlighting issues of importance/concern to MIIs.
10. The definition of KMPs should be changed to cover employees based on importance of activities carried out by them and their relative hierarchy within the MII. Further the MII must clearly delineate and segregate the roles and responsibilities of such

identified KMPs within each function (especially their responsibilities towards regulatory, compliance and risk management functions) in order to improve overall accountability.

11. Accountability and objective appraisals of the Board of MIs, Directors and Board level Statutory Committees and KMPs are essential. Video and audio recordings of the meetings of the Board of the MI should be made mandatory. Apart from the usual self-appraisals, an external agency should also be appointed to independently assess the performance of the Board and Statutory Committees of the MI.
12. The regulations should be amended to provide for a minimum (25%) as well as maximum (50%) amount as variable component of the KMPs' compensation. For each KMP, due weightage should be provided to the regulatory, risk management and compliance related aspects including Code of Conduct/Ethics for determining variable pay.
13. If any KMP or Board member becomes/ is aware of any acts of wrongdoing and fails to report the same to the Board of the MI or to SEBI, respectively, then such person should be held accountable.
14. The existing Code of conduct and Code of ethics for the directors and KMPs of the MIs may be rationalized into a single code of conduct to specifically include regulatory, compliance and risk management, good governance and due diligence as important components of operations.
15. The Board of the MI should be responsible for monitoring compliance with the Code of Conduct by the members of the Board of the MI. The Regulatory Oversight Committee should be responsible for monitoring compliance with the Code of Conduct by the KMPs and the other members on the committees of the MIs.
16. A code of conduct for Stock Exchanges and Clearing Corporations similar to the existing code of conduct for Depositories may be introduced.
17. Considering the phenomenal growth in the market capitalisation, trading volumes, investor base and number of market intermediaries linked to MIs, the MIs' net worth

may additionally include a variable component to cover various risks associated with their operations and level of activity of the MIIs.

18. Keeping the interest of investors in mind, the adequacy of Investor Protection Fund and Settlement Guarantee Fund should be periodically reviewed and a specific percentage of profits should be shifted to IPF in consultation with SEBI.
19. There should be continuous supervision by MIIs of all its members by leveraging technology. Information that is material to investors related to members of MIIs should be made public in a consolidated and structured manner on the website of the MII.
20. Use of technology (such as RegTech and SupTech) should be further enhanced by the MIIs to implement a transparent governance framework.
21. The MII's policy should adequately cover all methods of data sharing (including emails and social media) with appropriate delegation of powers for sharing data. The MIIs should develop escalation matrix for sharing confidential and sensitive information for any legitimate purpose.
22. The scope of SEBI's powers under SECC Regulations, 2018 and D&P Regulations 2018 should include levy of penalty and taking other disciplinary action (like suspension, barring to attend meetings etc.) on individuals of MII, including its directors, members of statutory committees, KMPs, employees and other persons associated with the MIIs, for any contravention of regulations.
23. In exceptional cases (including repeated breaches or violations), SEBI may explore the harsher options of debarring MIIs from introduction of new products/ services, restricting MIIs' existing activities, products and services etc. Further, the SCRA, the SEBI Act, and the Depositories Act may be reviewed by SEBI to increase the penalty amount that may be applicable for MII and relevant persons associated with MII.
24. Any activity being carried out by any of MII's investee companies which is in conflict with its role as a first line regulator should be phased out in a time bound manner.

## Chapter 1: Introduction and Background

### **I. Background**

Stock Exchanges (including Commodity Exchanges), Clearing Corporations and Depositories, collectively referred to as Market Infrastructure Institutions (“MIIs”), play a critical role in the securities market. The role of MIIs, which are at the core of a well-functioning securities market, assumes importance due to the following factors

–

- a. They provide the vital infrastructure for trading, clearing & settlement and holding securities.
- b. These institutions are in the nature of public utility infrastructure service providers in the securities market, and hence they constitute the key element in the economic growth of the country.
- c. They are the ‘first-level’ regulators for key participants in the securities market, vested with regulatory responsibilities under various statutes, including supervision of their members, monitoring of listed entities, carrying-out surveillance function, etc.
- d. They are entrusted with responsibilities to protect the interest of investors, redress investors’ grievances and educate them, and ensure that all investors get fair and equitable access to the market infrastructures.

Due to the phenomenal growth in the market capitalisation, trading volumes, investor base and number of market intermediaries linked to such institutions, MIIs have become more vital. Consequently, any failure or mis-governance in such important institutions could result in an adverse impact on the securities market and may affect the overall economy.

MIIs also perform a unique dual role. On the one hand, MIIs are corporate entities wherein attention to bottom line of their business is a natural outcome. On the other hand, as a first-line regulator, MIIs carry out the key regulatory and public utility functions cast upon them under the applicable law. A robust governance framework at MIIs is an important source of strength for securities markets, giving market participants the confidence to participate in such markets.

In light of the above, MIs are expected to be subject to high governance standards. SEBI, over a period of time, has undertaken various exercises in order to safeguard the functioning of such institutions.

In 2002, SEBI constituted a group headed by Justice M.H. Kania, former Chief Justice of India, on the corporatisation and demutualisation of Stock Exchanges in India. The Kania Committee recommended the adoption of a common model for corporatisation and demutualisation of all Stock Exchanges to remove any conflict of interests and to create greater management accountability. Accordingly, the Securities Contracts (Regulation) Act, 1956 was amended in 2004 and the corporatisation and demutualization of all stock exchanges was made mandatory under law. Subsequently, the Securities Contracts (Regulation) (Manner of Increasing and Maintaining Public Shareholding in Recognised Stock Exchanges) Regulations, 2006 (“MIMPS Regulations”) was brought in to broad base the ownership structure of Stock Exchanges and to pave the way for sprucing up the governance mechanisms.

In 2010, SEBI set up a committee under the Chairmanship of Dr. Bimal Jalan, former Governor, Reserve Bank of India (“RBI”), to examine various aspects such as the ownership structure, board composition, listing and governance requirements of Stock Exchanges and Clearing Corporations. In addition, the Bimal Jalan Committee made recommendations on the working of the Depositories. Based on its recommendations, the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 (“SECC Regulations, 2012”) were notified on June 20, 2012 and the amendments to the Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996 (“D&P Regulations, 1996”) were also notified in 2012, which provided similar governance norms for the depositories.

As part of its recommendations, the Bimal Jalan Committee had suggested that the working of the MIs should be reviewed after a period of five years. In view of the above recommendation and the evolving nature of the securities market, SEBI constituted a committee under the Chairmanship of Shri R. Gandhi, former Deputy Governor, RBI, in 2017 to comprehensively review the SECC Regulations, 2012, the D&P Regulations, 1996 and all related circulars.

Accordingly, in 2018, SEBI issued the SECC Regulations, 2018 and the D&P Regulations, 2018 which reflected the recommendations of the Gandhi Committee on various issues, such as the appointment process for Public Interest Directors (“PIDs”), the norms for compensation of Key Management Personnel (“KMPs”), the composition and structure of statutory committees and the functions of the regulatory departments of the MIIs.

To summarize, MIIs are currently regulated under various laws, including among others, the Companies Act, 2013 and the rules and regulations framed thereunder, the Securities and Exchange Board of India Act, 1992 (“SEBI Act”), the Securities Contracts (Regulation) Act, 1956 (“SCRA”), the Securities Contracts (Regulation) Rules, 1957 (“SCRR”), the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2018 (“SECC Regulations, 2018”), the Depositories Act, 1996 (“Depositories Act”), SEBI (Depositories and Participants) Regulations, 2018 (“D&P Regulations, 2018”) and SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“LODR Regulations, 2015”) and various circulars and directions issued thereunder, as amended from time to time.

## **II. Need for review of Governance of MIIs**

While the regulatory framework on governance of MIIs is being periodically reviewed, considering the phenomenal growth of the markets over the years and some instances of governance lapses which came to the fore in the recent past, a need was felt that the governance of MIIs could be further strengthened. Additionally, MIIs increasing reliance on technology and rapidly changing market dynamics, necessitate a regulatory overhaul especially in governance norms.

Revisiting various regulatory provisions applicable to the MIIs requires a review of the functions and accountability structures of the Board of the MII, its Directors and the KMPs, the procedure of appointment of members of the Board of the MIIs and KMPs, composition and role of the Board of the MII and its committees, the role of MIIs in monitoring and regulating their members and empaneled entities and the role of technology in the governance functions of the MII, etc.

In the international context, the Committee on Payment and Market Infrastructures (“CPMI”) and the Technical Committee of the International Organization of Securities Commissions (“IOSCO”) have published the Principles for Financial Market Infrastructures (“PFMI”).<sup>1</sup> The PFMI Principles set out the international standards for Financial Market Infrastructures (“FMIs”), which include the payment systems, central securities depositories, securities settlement systems, central counterparties and trade repositories, and provide a set of key standards for strengthening and preserving financial stability in the markets. In this regard, the PFMI Principle 2 on Governance states that,

*“An FMI should have governance arrangements that are clear and transparent, promote the safety and efficiency of the FMI, and support the stability of the broader financial system, other relevant public interest considerations, and the objectives of relevant stakeholders.”*

Accordingly, the governance arrangements of the FMIs are required to clearly define, among other things, the composition and role of the board of the FMI and its committees, the senior management structure, the design of risk management, the appointment process for the members of the board of the FMI and key management persons and the systems for ensuring accountability in the performance of the roles and responsibilities assigned to such persons. The PFMI principles have acknowledged that differences might arise in the governance arrangements across jurisdictions and therefore, have not prescribed a single set of principles for all FMIs across the world. Each jurisdiction has been recommended to adopt the governance principles depending on the ownership structure and regulatory requirements specific to the FMIs in their countries.

### **III. Composition of the Committee**

The committee on *“Strengthening Governance of Market Infrastructure Institutions”* (“Committee”) was constituted on April 4, 2022 with the following members:

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<sup>1</sup> Committee on Payment and Market Infrastructures (earlier Committee on Payment and Settlement Systems) and the Technical Committee of the International Organization of Securities Commissions, *Principles for financial market infrastructures* (April, 2012) (accessible at: <https://www.bis.org/cpmi/publ/d101a.pdf>).



| S.No. | Member Name          | Organization and Designation                                | Capacity         |
|-------|----------------------|-------------------------------------------------------------|------------------|
| 1.    | Shri G. Mahalingam   | Former WTM, SEBI                                            | Chairman         |
| 2.    | Shri J. N. Gupta     | MD, Stakeholders Empowerment Services                       | Member           |
| 3.    | Shri Ashish Chauhan  | MD & CEO, BSE Limited*                                      | Member           |
| 4.    | Shri Vikram Limaye   | MD & CEO, National Stock Exchange of India Limited**        | Member           |
| 5.    | Shri P.S Reddy       | MD & CEO, Multi Commodity Exchange of India Limited         | Member           |
| 6.    | Shri Arun Raste      | MD & CEO, National Commodity & Derivatives Exchange Limited | Member           |
| 7.    | Ms. Padmaja Chunduru | MD & CEO, National Securities Depository Limited            | Member           |
| 8.    | Shri Nehal Vora      | MD & CEO, Central Depository Services (India) Limited       | Member           |
| 9.    | Shri Sandip Bhagat   | Partner, S&R Associates                                     | Member           |
| 10.   | Ms. Aarti Nihalani   | Partner, Oliver Wyman                                       | Member           |
| 11.   | Shri Uttam Bagri     | Former Chairman, BSE Brokers Forum                          | Member           |
| 12.   | Shri Amarjeet Singh  | Executive Director, SEBI                                    | Member Secretary |

\* Shri Chauhan was appointed as the MD & CEO of NSE with effect from July 26, 2022 and participated in the meetings of the Committee in the said capacity after such appointment. After Shri Chauhan's appointment as MD & CEO of NSE, Shri Neeraj Kulshrestha, CRO, BSE represented BSE in the Committee.

\*\* After the end of his term as MD & CEO, NSE, Shri Limaye had participated in the Committee's meetings as a special invitee.

#### IV. Terms of Reference of the Committee

The terms of reference of the Committee include making recommendations on the following:

- Measures for strengthening the role played by the Board and Committees of MIIs,
- Reviewing the requirements related to appointment and role and responsibilities of Directors on the Board and KMPs,

- c. Developing effective metrics for monitoring various aspects of the functioning of MIIs and KMPs,
- d. Enhancing accountability and transparency,
- e. Reviewing the policy on safekeeping and sharing of information held by MIIs,
- f. Revisiting the Code of Conduct and Code of Ethics for Directors of the Board and KMPs and
- g. Any other measures that the committee may consider appropriate.

## V. Approach

The Committee had 21 meetings over a period of approximately 7 months with the first meeting held on April 11, 2022 and the last meeting on November 02, 2022.

The Committee consulted various stakeholders, including Public Interest Directors, Chief Regulatory Officers, representatives of MIIs and other relevant persons, in order to ascertain their views on the current regulatory framework. It also took into consideration the past committee reports on Governance of MIIs.

The Committee further took note of relevant regulations and practices of regulated entities, including MIIs in international jurisdictions. While certain roles undertaken by the MIIs in India are common with those of similar international institutions, they face certain unique context-specific challenges. Accordingly, relevant themes from international best practices were taken on board after taking cognizance of and informed by such unique challenges.

As stated earlier, the Committee recognized that the MIIs are unique type of institutions vested with regulatory responsibilities, while pursuing commercial interests like any other profit oriented entities. Given their vital role in the capital market ecosystem, they cannot engage themselves exclusively in pursuit of profits which results in dilution of their focus on the regulatory role. At the same time, they have to be viable institutions generating sufficient surpluses to effectively discharge their role of public utility with an eye on robust investor protection. The business model of an MII is thus inherently conflicting. Policy makers would need to ponder over the appropriateness of this model and perhaps look for alternatives which would ensure a clean separation of the two roles now vested with the MIIs. This would necessitate creation of separate institutions to take on these vastly different roles and it could

possibly pave the way for greater competition in the commercial role so that, ultimately the investors stand to benefit. Since this issue was not within the remit of the Committee, the Committee took the existing business model of MII as given and channelized its thought process on streamlining the system within this given model, so that the MIIs do not lose sight of their regulatory focus.

While taking note of the recent instances of lapses in the governance of MIIs, the Committee was of the view that tightening of the norms should not deter innovation or cause unintended consequences for the MIIs. The committee also viewed that the rule-based approach for the regulation of MIIs should be balanced with a principle-based approach in order to achieve the intended outcomes.

This report of the Committee (“Report”) sets out recommendations which include, *inter alia*, amendments to certain provisions of the SECC Regulations, 2018, the D&P Regulations, 2018 and modifications in various related circulars issued by SEBI. The report is divided into 11 chapters.

## **Chapter 2: Organisational Structure and Accountability of MIIs**

This chapter sets out the recommendations with respect to strengthening the organisational structure and accountability mechanisms of MIIs.

### **I. Organisational Structure of MIIs – Core Functions**

The term ‘MIIs’ encompasses Stock Exchanges, Clearing Corporations as well as Depositories in the context of this report. The Committee appreciates that there is a great deal of specificity of the functions discharged by each type of MII. The functions of MIIs, however, can be broadly categorised under the following three heads:

- a) providing continuity of critical operations, including by leveraging a robust technology infrastructure for facilitation of trading, holding of securities, clearing and settlement activities as well as information dissemination, as applicable;
- b) acting as a first-line regulator for the securities market, driving towards compliance and risk management objectives set by the regulator; and
- c) other functions including business development.

The SCRA, the SECC Regulations, 2018, the Depositories Act and the D&P Regulations, 2018 contain provisions which refer to the key activities of the different types of MIIs. There are also provisions which specifically set out the regulatory role of an MII. For example, Schedule II, Part C of the SECC Regulations, 2018, sets out the different functions of the regulatory department and requires the MIIs to ensure that such department is adequately staffed with persons who have professional and relevant experience in that field. SEBI has also issued various circulars from time to time, which identify the core and critical functions of the MIIs and prohibit outsourcing of such functions to third-parties or outsourcing agencies. To clearly outline the roles and responsibilities of the Board and Management of the MII, the Committee felt that there was a need to review the specific tasks forming the core functions of the MII.

The Committee further discussed the need to assign specific functions of the MIIs to designated KMPs more clearly for effective discharge of such functions and to strengthen the individual accountability mechanisms of the MIIs. The PFMI Principles also suggest that an FMI should have documented governance arrangements that provide clear and direct lines of responsibility and accountability. In connection with the

above, the Committee took note of the Senior Managers Regime in the United Kingdom and compared it with the existing structures in India for accountability and performance evaluation of the KMP of MIIs.

The Committee acknowledged the need to ensure that the MIIs deploy adequate resources for carrying out each core and critical function. The Committee also took note of the recommendations of the Bimal Jalan Committee and the Gandhi Committee on allocation of resources and deliberated whether further importance should be provided to resource allocation for the core functions such as continuity of critical operations as well as functions related to regulatory, compliance and risk management role of the MIIs.

The Committee felt that, the resources allocated to the regulatory, compliance and risk management vertical should be further enhanced for effective discharge of statutory requirements, such as ensuring compliance with various regulatory requirements, conducting periodic inspections, continuous monitoring of various activities of the MII and also of the members (through use of technology), etc.

**Recommendations:**

- 1) *Each MII should identify and clearly define its functions based on the specific requirements as applicable to such MII. Such functions should be divided across the following three verticals:*
  - a) *Critical Operations (continuity of the critical operations of such MII to be ensured by leveraging a robust technology infrastructure to enable trading, holding of securities, clearing and settlement and information dissemination, etc. as applicable);*
  - b) *Regulatory, Compliance and Risk Management; and*
  - c) *Other functions including business development.*
- 2) *MIIs should have adequately developed infrastructure and technology to support all core functions and more specifically for the functions under the first two verticals.*
- 3) *Each core function of the MII should be headed by a designated KMP. It is further recommended that the KMPs heading the functions under the first two verticals*

*should be at least at par in hierarchy with the KMPs heading functions under the third vertical.*

- 4) The functions under the first two verticals, should be given higher priority by the MII over functions under the third vertical in terms of resource allocation. SEBI may provide indicative list of functions that shall be part of first two verticals. The MIIs should periodically assess the adequacy of resource allocation for these two verticals based on objective parameters, such as gravity of the function and volume of activities.*
- 5) There should be a periodic assessment for any future contingencies and a specific budget should be allocated towards fulfilment of the requirements relating to technology development.*

## **II. Mechanism for Effectiveness and Accountability**

An MII is expected to balance its role as a public utility infrastructure service provider in the securities market and a first line market regulator while also being a corporate entity that is profit-oriented. Given that an MII's role in the efficient functioning of markets as well as protecting investors' interest and integrity of the securities market is important, the Committee felt the need to review the existing performance metrics and accountability mechanisms at the level of the MIIs to ensure that the MIIs do not pursue business objectives in a manner which dilutes the focus on their critical operations and regulatory, compliance & risk management activities.

The Committee noted that the existing regulatory norms prescribe the duties and responsibilities of the Board and its members, its Committee Members, MD and CEO and KMPs of the MIIs, including automatic imposition of financial disincentive on the MD and Chief Technology Officer ("CTO") for technical glitches at MIIs without giving them a reasonable opportunity to be heard. While the Committee was in favour of a clear cut accountability structure, the Committee was of the view that the element of personal accountability can be invoked only with the due legal process without compromising on the principles of natural justice. Given this backdrop, the Committee felt the existing process of automatic imposition of financial disincentive does not look appropriate and hence needs to be reviewed.

The Committee further discussed the need for well-defined metrics to assess the effectiveness of the functioning of MIIs in discharging their core functions along with the manner and periodicity of such assessment. The Committee is of the view that the external evaluation of the MIIs will also help to minimise conflict of interests.

**Recommendations:**

- 6) *Periodic review through an internal as well as external mechanism, should be conducted to evaluate the effectiveness of the MIIs in discharging their core and critical functions. Accordingly, the MIIs, as an entity, should internally evaluate its own performance on an annual basis and engage an external agency for evaluating its performance once in every three years. It is recommended that the MII may frame its own evaluation metrics based on the indicative parameters as specified by SEBI. The first external evaluation should be conducted within a period of twelve months from the date of implementation of the recommendations. The indicative parameters for evaluation of the MII is placed at **Annexure-A**.*
- 7) *There should be no automatic imposition of financial disincentive on the individuals at an MII and the principles of natural justice should be followed while imposing any financial disincentive.*

### **Chapter 3: Board of the MII – Role, Effectiveness and Accountability**

This chapter sets out the recommendations with respect to the role of the Board of MIIs, including the individual members of the Board, with a view to improve their effectiveness and accountability.

#### **I. Roles, responsibilities and accountability of the Board of the MII**

Under the current regulatory framework, the Board of an MII consists of the following three categories of directors: “Shareholder Directors” (“SHDs”); “Public Interest Directors” (“PIDs”); and the Managing Director (“MD”). The existing regulations, *inter-alia*, mandate that the Chairperson of the Board of the MII shall be appointed with the prior approval of SEBI from among the PIDs, the MD should be considered under the category of SHD and the number of PIDs should be not less than the number of SHDs.

Further, Regulation 26 of the SECC Regulations, 2018 and Regulation 27 of the D&P Regulations, 2018 read with the corresponding schedules to the regulations prescribe a Code of Conduct for the directors on the Board of the MII (including a specific Code of Conduct for PIDs) as well as a Code of Ethics for all the directors and KMPs at the MII. Accordingly, the existing regulatory framework sets out the broad principles and expectations from the directors of an MII.

The Committee noted PFMI – Principle 2.2 which states that “*An FMI should have documented governance arrangements that provide clear and direct lines of responsibility and accountability*”. In addition, Explanatory note 3.2.3 of the principles states that “*Governance arrangements should provide clear and direct lines of responsibility and accountability, particularly between management and the board, and ensure sufficient independence for key functions such as risk management, internal control, and audit.*”

In view of the above, a need was felt to clearly define the supervisory and operating roles of the Board of MIIs. In addition, certain recent instances of governance lapses have demonstrated the challenges in casting accountability on the board and management. Therefore, the Committee examined whether there was a need to affix specific accountability in respect of decisions taken by the Board of the MII and in



particular, whether the concept of individual accountability of the members of the Board of the MII and its management should be specifically introduced in the regulations.

On the term “shareholder director”, it was noted that the appointment of SHDs and their roles and responsibilities were not specific to any particular shareholder, hence this term may have lost significance from its historical origin, and an alternative nomenclature should be proposed. The Committee noted that the categorization of the MD as an SHD was based on the recommendation of the Gandhi Committee and was for the limited purpose of determining the composition of PIDs and SHDs on the Board of the MII.

The Committee also discussed the framework for directors under the Companies Act, 2013 and the LODR Regulations, 2015, including the responsibilities of, and the liability regime for executive, non-executive and independent directors.

### **Recommendations:**

- 8) *The term “shareholder director” should be replaced with the term “Non-Independent Director” (“NIDs”) in the regulations, such that the revised categorization of directors of MIIs will be as follows:*
- a) *PIDs (Independent Directors (IDs));*
  - b) *NIDs; and*
  - c) *MD.*

*NIDs may include nominees of shareholders and executive directors other than the MD.*

- 9) *Given the role of MIIs in the securities market, it is recommended that PIDs should have a higher representation on the Board of the MII to bring efficiency, transparency and accountability in the operations of the MIIs. Accordingly, the number of PIDs should be increased such that they constitute at least two-thirds of the total strength of the Board (total strength consists of all the members of the Board of the MII, including PIDs, NIDs and the MD). SEBI should provide sufficient time to existing MIIs to comply with the proposed changes (twelve months from the date of implementation).*

10) *The roles and responsibilities of directors should be clearly defined with a focus on supervision of regulatory, compliance and risk management functions. The existing directions issued to MIIs on the key roles and responsibilities of PIDs should be included in the Code of Conduct.*

11) *The Board of the MII should play an active role in defining the risk management framework for such MII, including the following:*

- a) Establishing and documenting risk management framework, covering risk appetite or risk tolerance policy of the MII.*
- b) Framing a clearly defined and calibrated policy such that breaches (i) are not considered acceptable and (ii) trigger response / action from the Board of the MII, its committees and the management.*
- c) Making key stakeholders (executive and non-executive) aware of the use and value of risk appetite across the organisation (including implications of breaches).*
- d) Risk appetite policy should include clear quantitative metrics and thresholds to monitor performance of the MII Board's appetite for risk.*
- e) Review of risk appetite metrics and thresholds should be approved by the Board of the MII.*
- f) Outlining and documenting role of risk appetite in key processes.*

12) *The Board of the MII also needs to ensure the following:*

- a) Adequate independence of key functions such as regulatory and control functions (risk management, compliance and audit functions) such that;
  - i. Regulatory and control functions have sufficient stature to perform their tasks effectively.*
  - ii. Regulatory and control functions operate independently and have appropriate direct access to the Board of the MII and senior management.*
  - iii. Control functions are proactively involved in all relevant decisions and activities.**
- b) A culture of effective communication and challenge (i.e., alternate views or questions from individuals and groups are encouraged) is valued and respected.*

c) *Embed three lines of defense construct:*

- i. *The first line of defence incorporates business units and support functions as it has the responsibility to own and manage risks associated with day to day operational activities.*
- ii. *Various oversight functions comprise the second line of defence, i.e., regulatory, risk management, compliance teams. This line of defence assumes leadership role in implementation of the risk management framework including policies and procedures established by the Board of the MII, collaborating with business as credible challenger and partner.*
- iii. *The third line of defence comprises the internal audit function.*

*The roles and responsibilities of management in relation to three lines of defence are clearly specified and understood. It should be clear that all employees have responsibility for regulatory, risk management and compliance outcomes.*

d) *Any new product, service, revenue stream must be examined by the concerned department of the MII from regulatory, compliance and risk management perspectives in addition to normal viability issues and should be approved by the Board of the MII. All existing products, services, revenue streams must also be periodically reviewed for the aforesaid parameters.*

13) *The Committee agrees that the principle of collective responsibility should continue to govern all board activities. The principle of individual responsibility should be applied in accordance with the existing provisions of the Companies Act, 2013, and it should be guided by the principles of natural justice.*

14) *Minutes of the Board meetings should be recorded in accordance with applicable Secretarial Standards, including any dissent. Both video and audio recordings of all the meetings of the Board of the MIIs and its committees (whether held virtually or physically) should be mandatorily recorded and maintained for at least eight years (similar to the current requirement on minutes book of Governing Board meetings of MIIs prescribed under Regulation 40(2) of the SECC Regulations, 2018). Such video/audio recording will also be helpful in evaluating the effectiveness of the members as well as gauge individual accountability if any lapses are noted in future.*

## II. Evaluation metrics for effectiveness of the Board of MII and its members

As noted above, the provisions of the SECC Regulations, 2018 and the D&P Regulations, 2018 prescribe a Code of Conduct and a Code of Ethics which is applicable to the directors and KMPs of the MIIs. Regulation 33 of the SECC Regulations, 2018 and Regulation 31 of the D&P Regulations, 2018 also prescribe disclosure and corporate governance norms which are applicable to stock exchanges, clearing corporations and depositories. In addition, the Committee took note of SEBI circular dated January 5, 2017 to listed entities, which provides guidance note on performance evaluation of the board, the independent directors, and various committees of the board. The existing requirement for performance review of PIDs, at the time of their re-appointment, was also discussed.

The Committee noted the requirements in certain other jurisdictions, which recommend an external review of the effectiveness of the Board of companies including MIIs (e.g. United Kingdom, Hong Kong, Singapore). Such reviews cover a number of dimensions including:

- a. Operating framework for the Board
  - i. Terms of reference (including frequency, attendance and duration of meetings).
  - ii. Mandate and objectives.
  - iii. Agendas.
- b. Individual membership
  - i. Experience and expertise.
  - ii. Skills and capabilities.
  - iii. Institution specific knowledge and understanding.
- c. Group performance
  - i. Overall breadth, mix and comprehensiveness of experiences, skills and expertise.
  - ii. Group culture and dynamics.
  - iii. Individual leadership behaviour.

- iv. Decision making: quality of the regulatory, risk management and compliance roles; quality of the strategic and other business-related advice.
- d. Interactions between the Board and the MII
  - i. Visibility of the institution: Reporting mechanisms; Relationship with and lines of communication to senior management.
  - ii. Influence on the institution: Role in key processes, e.g., strategy, planning; Influence on Executive Committee and Senior Management; Delegation of authority.

In such jurisdictions, the Chairperson of the Board of the MII or a Board committee (typically, the nominating committee) is usually explicitly made responsible for the following:

- a. Drive the process, involve the right people, and ensure that colleague-directors are actively engaged.
- b. Deliver feedback to the group and to individual directors.
- c. Act on the results of the performance evaluation by recognizing the strengths and addressing the weaknesses of the board and, where appropriate, proposing new members be appointed to the board.

In addition, the Committee felt there was a need to have well-defined metrics to objectively assess the effectiveness of the Board of the MII as a whole and each of the members individually.

### **Recommendations:**

*15) In addition to the existing annual self-assessment of the Board of the MII and its members, an external agency should assess the performance of the Board and its members once every three years or such other period as may be specified by SEBI. The first assessment of the performance of the Board and its members by an external agency should be conducted within twelve months from the date of implementation of the recommendations.*

- 16) *SEBI should issue broad indicative parameters to assess the effectiveness of the Board of an MII and its members. Each MII can frame its own specific parameters. The proposed list of broad indicative parameters to assess the effectiveness of the Board of an MII and its members is annexed as **Annexure B and Annexure C**, respectively.*

### **III. Accountability for PIDs**

Existing regulatory norms prescribe a Code of Conduct and a Code of Ethics for directors and KMPs. Taking into account, however, the past instances of governance lapses where PIDs and the Board may have failed to initiate timely corrective action, a need was felt to revisit the accountability regime for PIDs, including imposition of monetary and other penalties and actions.

The Committee noted that Regulation 26(4) of the SECC Regulations, 2018 and Regulation 27(4) of the D&P Regulations, 2018, provide powers to SEBI, including, to initiate appropriate action against directors who fail to abide by the regulations or the Code of Conduct or the Code of Ethics. This includes the power to remove or terminate the appointment of any director, after providing them a reasonable opportunity to be heard. There is scope, however, to specify additional actions that can be taken by SEBI under the regulations.

#### **Recommendations:**

- 17) *In order to ensure that there is no ambiguity in terms of disciplinary powers of SEBI under Regulation 26(4) of the SECC Regulations, 2018 and Regulation 27(4) of D&P Regulations, 2018, an indicative list of actions that can be taken by SEBI may be specifically included in the regulations. Such actions could include the power to issue warnings or advisories, suspend or remove PIDs or bar the PIDs from attending meetings or impose monetary penalty in such amounts as determined by SEBI.*

### **IV. Mandatory periodic reporting norms for PIDs and NIDs**

The code of conduct for PIDs under Regulation 26(1) of the SECC Regulations, 2018 read with Schedule II Part-A require PIDs to identify and report to SEBI important issues which may involve conflict of interest or have significant impact on functioning of MIIs.

During the past instances of governance lapses in MIIs, it was noticed that adverse issues concerning the MIIs may not have been duly reported. In view of this, the Committee deliberated on the need to supplement the current reporting requirements with more specific reporting by the PIDs. The Committee also noted the current requirements under Regulation 26(1) of the SECC Regulations, 2018 read with Schedule II Part A of the regulations, as well as the requirements issued under various SEBI circulars and directions to MIIs, regarding holding six-monthly meetings of the PIDs and specifying certain matters to be discussed therein. Also, it was noted that presently there is no requirement for the non-executive directors to interact with SEBI and directly give their views to the regulator on the functioning of the MII.

**Recommendations:**

- 18) SEBI should meet the PIDs and NIDs (without the presence of MD and any executive director) of all MIIs at least once a year, in a manner as determined by SEBI. Such an interaction with these directors will provide an opportunity to discuss any concerns in the MII and improve accountability standards in the MII.*
- 19) PIDs of an MII should meet every six months, as is the current practice. They should submit a report to SEBI and the Board of the MII after the meeting (within a time bound manner). The report should cover the themes specified by SEBI, including identifying any important issues concerning the MII. In this context, SEBI may review its existing regulatory provisions and align the reporting requirements, including the contents of the six-monthly report.*

## **Chapter 4: Appointment process of the Board members of the MII**

This chapter sets out the recommendations with respect to the appointment process of the board members and the required skill-sets of such members.

### **I. Sufficient mix of skill-set for members of the Board of MIIs**

It was noted that Regulation 24(11) of the SECC Regulations, 2018 and Regulation 25(11) of the D&P Regulations, 2018, read with the corresponding schedules for appointment of directors, set out the skill-set requirements for the board of directors of the MII. The current regulations require a Managing Director to have sufficient experience in the field of capital market, finance and management. The skill-set requirement for PIDs includes qualification in the areas of law, finance, accounting, economics, management, administration or any other area relevant to the financial markets. In addition, persons who are currently holding or have previously held positions of trust and responsibility in reputed organizations are given preference in the appointment process of PIDs.

With the development of a more inter-connected global financial market and the ever-increasing reliance on technology by MIIs, the inclusion of skills such as technology and risk management, assumes importance while appointing a director for an MII. The Committee noted that the explanatory note to PFMI Principle 2 on Governance states the following:

*“The board should be composed of suitable members with an appropriate mix of skills (including strategic and relevant technical skills), experience, and knowledge of the entity (including an understanding of the FMI’s interconnectedness with other parts of the financial system).”*

It was also noted that the governing boards of international financial market - institutions, such as the NASDAQ, the NYSE and the LSE, have also upgraded their skill-set requirements to ensure adequate representation from persons with technology background. In the Indian context, however, it was observed that the current regulatory norms did not mandate skill sets such as experience in technology or risk management. The existing regulations are also silent on any desired skill set for the NIDs. Therefore, a need was felt to review the existing skill-set requirements



in MIIs considering the evolving need and challenges in the securities market.

**Recommendations:**

20) *The board members of MIIs should be required to have a sufficient mix of the following six (6) areas of expertise/skill-sets:*

- (i) technology;*
- (ii) finance and accounts;*
- (iii) legal and regulatory;*
- (iv) risk management;*
- (v) capital markets; and*
- (vi) management/ administration.*

*In addition, each MII may also decide to place due regard to other areas of expertise/skill-sets which may be specific to the requirements of the MII and evolve with the changing nature of the business and environment in which the MII operates. The minimum skill-set prescribed above for MIIs can be tested on a collective basis at the level of the Board of the MII.*

21) *MIIs should provide an undertaking on such pre-defined skill sets being possessed by the candidates at the time of submission of an application to SEBI for its prior approval for fresh appointment or re-appointment and as well as at the time of an existing member ceasing from the Board of the MII. SEBI, however, may provide a timeline for compliance in case of unforeseen circumstances.*

22) *The NRC shall be responsible for ensuring that the board level skill-diversity is monitored and maintained at all times subject to exceptions in case of unforeseen circumstances.*

23) *In assessing the skill-set for a particular member, relevant work experience in the field/domain should also be taken into consideration and such assessment should not be based just on educational qualifications.*

## **II. Specific Skill sets for PIDs**

PIDs constitute a majority of the Board of the MII and have representation on most of

the statutory committees of the MIIs. Therefore, it is important to align their experience, qualification and skill set to the functioning of the MIIs, including as a first level regulator.

The current regulations already give weightage to certain specific areas of expertise during the appointment of PIDs. It was felt, however, that the current norms should also cover additional areas of expertise for PIDs, such as technology and risk management. The Committee also referred to a preliminary MII-wise data analysis undertaken by SEBI in July 2022 to ascertain the skill set representation of the PIDs on the Board of existing MII on the basis of four parameters, namely, technology, law, finance and accounting and capital markets. The results of the preliminary analysis noted that certain MIIs did not have any PIDs with technology, law or finance and accounting skill-set. Considering the above results, the Committee felt a need to review the skill set requirement for PIDs to ensure that the Board of the MII is composed of suitable members with an appropriate mix of expertise/skill sets.

**Recommendations:**

*24) At least one PID each must possess dominant expertise/skill-sets in the following four areas:*

- (i) technology,*
- (ii) legal and regulatory;*
- (iii) finance and accounts; and*
- (iv) capital markets.*

*To clarify, in any MII, at least one PID should be mapped to each of the above expertise/skill-sets.*

*25) The NRC shall be responsible for ensuring that the PIDs have the skill sets mentioned in the above four areas and shall be required to certify such compliance while seeking the approval of SEBI of a new PID at the time of fresh appointment and re-appointment as well as at the time of an existing PID ceasing to be the member of the Board of the MII. SEBI, however, may provide a timeline for compliance for unforeseen circumstances.*

26) *The Committee is of the view that SEBI should prescribe a glide path for monitoring compliance of MIIs with the skill set requirements under the regulatory norms.*

### **III. Skill evaluation metrics for processing applications of PIDs**

As discussed above, the current regulations prescribe certain qualifications for appointment of PIDs. SEBI circular dated February 5, 2019, also stipulates, *inter alia*, that a minimum of two names shall be submitted at the time of re-appointment of PIDs and that there shall be an annual internal performance review of each PID along with an external evaluation by the management or human resources consultants during their last term.

The existing regulatory norms, however, only set out the broad principles of evaluation for the applicants seeking appointment or re-appointment as PIDs. The performance review for re-appointment of PIDs focuses on the general competencies and personal attributes of the applicant, such as commitment, integrity, independence and judgment, among others. The Committee noted that such attributes are relatively difficult to assess and could leave room for subjectivity in the process. In view of this, the Committee felt a need to devise objective assessment criteria for applicants seeking appointment and re-appointment as PID on the boards of the MIIs.

Accordingly, the Committee discussed the significance of a skill-based evaluation metrics with indicative parameters for objectively assessing the applicants being considered for the position of PID. In addition, the Committee also deliberated whether the NRC should be the authority responsible for evaluating the applicants based on such skill-based evaluation metrics. The Committee believed that a comprehensive and objective approach should be devised by MIIs, which includes criteria such as prior responsibilities as a PID (Independent Director), domain expertise in technology/ law/ finance and accounts/ capital market and sufficient mix of skillset on the Board of the MII, in addition to the general competencies and personal attribute-related parameters.

The Committee was of the view that the above skill evaluation metrics should also be

considered for other directors such as the NIDs.

**Recommendations:**

27) *Basic skill evaluation metrics should be developed to assess the applications for PIDs and NIDs and such metrics should be applicable to both the appointment and re-appointment process for the PIDs and NIDs. This skill evaluation metrics should be developed by the NRC of each MII based on the indicative parameters as listed for PIDs in **Annexure D**.*

#### **IV. Appointment process for the Directors on the Board of MIIs**

##### **A. Public Interest Directors**

In respect of appointments, Regulation 24(2) of the SECC Regulations, 2018 and Regulation 25(2) of the D&P Regulations, 2018 stipulate that the public interest directors on the Board of MII shall be “*nominated by*” SEBI. SEBI circular dated February 5, 2019 further requires that a minimum of two names shall be submitted by the MIIs at the time of requesting for approval for appointment of PID and extension of the term of an existing PID. In addition, Regulation 24(3) of the SECC Regulations, 2018 and Regulation 25(3) of the D&P Regulations, 2018 states that PIDs shall be nominated for a term of three years, which is extendable by another term of three years and followed by a cooling-off period of one year. In total, PIDs can be nominated for a maximum of three terms, the maximum tenure of a PID in an MII shall not exceed six years and the maximum age limit for PIDs is 75 years.

Under the existing SEBI norms, the PIDs are stated to be “nominees” of SEBI, who represent the interests of investors in securities market. In fact and practice, however, the names of PIDs are submitted by the MII themselves, and SEBI only selects out of the pool of names proposed by the MII. Accordingly, the approval of the proposed names does not reflect a nomination process by SEBI. Further, under the provisions of the Companies Act, 2013, the tenure of an independent director is for a period of five years. The SECC Regulations, 2018, however, stipulate a shorter period of three years in the case of PIDs. Given the nature of MIIs, the Committee felt that the PIDs should be governed by higher standards, and therefore status quo with respect to the

total tenure and extension of tenure for the PIDs may be maintained.

Further, it is noted that the existing norms allow a PID to continue holding the post until a new PID is appointed, but the circumstance for such extension is not defined.

The Committee deliberated on the above areas of concern. The view that emerged was that the phrase “*nominated by*” SEBI should be revised since SEBI was merely acting as an approving authority. The existing appointment process, however, may continue with minor changes to account for any delays or conflict of interest. The Committee discussed but did not find merit in proceeding with certain other proposals for revisiting the appointment process such as shortlisting of candidates by external agencies, submission of four names for each post, newspaper advertisements and creation of a pool of PIDs due to inherent logistical and procedural difficulties. The Committee agreed that the current position regarding the tenure of PIDs should be retained but clarity was needed on the terms and conditions for extension of the tenure for PIDs to limit any regulatory ambiguity.

The Committee also noted the existing provisions under SCRR, which allows SEBI to nominate up to 3 members on the Board of Stock Exchanges without going through normal process. The Committee felt that the said provisions may also be made applicable for Clearing Corporations and Depositories and suitable amendments may be made in SECC Regulations 2018 and D&P Regulations 2018.

**Recommendations:**

*28) The concept of PIDs as being “nominees” of SEBI in the current regulations should be replaced with being “appointed with the prior approval” of SEBI.*

*29) With respect to the re-appointment of PIDs, MIIs should submit one name (the existing PID) for SEBI’s approval, at least four months prior to the end of the term of the relevant PID. In cases other than re-appointment, the present process may continue.*

*30) In case a new PID is yet to be appointed in place of an existing PID, and the Board of the MII does not meet mandatory regulatory requirements on its composition, the tenure of the existing PID may be extended but limited to a maximum period*

*of three months after the expiry of their term. The existing PID should be required to immediately vacate their position after expiry of such extended term.*

*31) The SECC Regulations, 2018 and D&P Regulations, 2018 may be amended to include nomination of PID on the Board of the MII directly by SEBI as provided in the SCRR.*

## **B. Non-Independent Directors (NIDs)**

Regulation 24(1) of the SECC Regulations, 2018 and Regulation 25(1) of the D&P Regulations, 2018, read with corresponding schedules for appointment of SHDs (recommended to reclassify as NIDs) provide that “*The appointment and re-appointment of all shareholder directors on the governing board of every recognised stock exchange/ clearing corporation / depository shall be with the prior approval of the Board.*” Accordingly, the names of persons proposed to be appointed as shareholder directors are currently first approved by the Board of the MII, followed by shareholders’ approval and then submitted to SEBI for approval.

The Committee deliberated whether there was any need to review the current appointment procedure for NIDs and whether the validity of SEBI’s approval for NIDs should be increased to three years (to make it at par with process for PIDs).

The Committee did not find merit in changing the existing process of appointment and re-appointment for NIDs. Accordingly, status quo should be maintained in this regard.

## **C. Managing Directors**

Regulation 25(3) of the SECC Regulations, 2018 and Regulation 26(3) of the D&P Regulations, 2018 states that a person may be appointed as the MD by the MII for a maximum of two terms not exceeding five years each, subject to a maximum age limit of 65 years. After completion of the first term, the MIIs are required to conduct the appointment process for MDs afresh. Accordingly, the Committee, during its discussions, deliberated whether the tenure, and thereby maximum number of terms,

of the MDs in one MII needs to be reviewed.

It was noted that the regulatory norms should only prescribe a maximum limit on the tenure of the MDs and thereby provide the MIIs with flexibility in determining the total number of terms.

**Recommendations:**

*32) With respect to the term of the MD, the regulations should be amended to clarify that (i) each term of an MD should not exceed five years; and (ii) the maximum number of years that an MD can be appointed for is ten years, irrespective of the number of terms.*

**V. Knowledge upgradation for PIDs**

PIDs form the majority of the Board of an MII. They are expected to be well-versed with the functioning of the MII, the technicalities involved therein and the regulatory framework. Part H(III)(3) of Schedule II of the SECC Regulations, 2018 provides that *“Public interest directors shall peruse the relevant laws, code of conduct, code of ethics, etc. and submit an undertaking to the stock exchange/clearing corporation that they are aware of their role, responsibilities, and obligations. The stock exchange/clearing corporation shall provide at least seven days of training to every public interest director each year.”*

While the current norm requires MIIs to provide training to PIDs for a week each year, the effectiveness of such training needs to be examined. There is a need to ensure that the PIDs are abreast with on-going developments in capital markets and related technology and regulatory space. Accordingly, the Committee deliberated the effectiveness of a regulatory mandate on MIIs to ensure that their PIDs are up to date in their knowledge. The role of SEBI was also discussed in prescribing knowledge upgradation standards for PIDs in certain areas, including technology and the regulatory framework. The Committee was also of the view that the existing knowledge requirements of all the directors should be reviewed and suitable changes should be recommended by the regulator to increase the effectiveness of the Board

of an MII.

**Recommendations:**

33) *The training and knowledge upgradation requirement as applicable to PIDs should be extended to cover all the directors.*

34) *MIIs, in coordination with reputed institutions, may organize online or offline learning modules related to ongoing development in capital markets and regulatory space.*



## **Chapter 5: Functioning of Board and Statutory Committees of the MIs**

This chapter sets out the recommendations for strengthening the functioning, composition and effectiveness of the Board and the Statutory Committees of the MIs.

### **I. Minimum agenda and frequency of the meetings of the Board of the MI and Statutory Committees of the MI**

The Board of the MI plays an important role in striking a balance between the regulatory and business functions of MIs. As a first line of oversight over the MIs, there is an expectation that the Board of the MI should discuss all relevant agendas at their meetings to ensure that the regulatory role of MIs is effectively discharged. In relation to statutory committees of MIs, SEBI circular dated January 10, 2019 stipulates, *inter-alia*, that the MIs shall set out the policy on the frequency of meetings and have separate meetings of PIDs every six months with a specified objective. Other than the above, there is no stipulation in the SECC Regulations, 2018 and the D&P Regulations, 2018 with respect to a ‘minimum agenda’ for the meetings of the Board and statutory committees of MIs.

Accordingly, the Committee deliberated whether there was a need to define a ‘minimum agenda’ for the meetings of the Board and statutory committees of MIs. Based on a review of past meetings of the Boards of certain MIs by SEBI, it was brought to the attention of the Committee that significant time of the Board and the statutory committees was taken up on operational matters. The Committee discussed that day-to-day operational matters should ordinarily not be placed before the Board of the MI on a routine basis, since the focus of the Board should be on strategy, policy level issues and other important items. At the same time, a need was also felt to place greater emphasis on the role of the Board of the MI in overseeing, by exception, the operations, technology, risk management, compliance and regulatory areas of the MIs. The Committee also noted the existing terms of reference (“TOR”) of the statutory committees and discussed merits in revisiting them with a view to provide MIs with guidance on minimum agenda for committee meetings. The Committee, however, felt that a “minimum agenda” may not be prescribed for the meetings of the Board and its statutory committees.

The Committee also discussed whether the agenda of Board meetings should be approved and cleared by the Chairperson of the Board of the MII. In this regard, the prescribed Secretarial Standards on the meetings of the Board of Directors were noted. The Committee further discussed the current practice of MIIs circulating the agenda paper and notes to the Board and its committees only after the approval of the MD. Therefore, the issue of whether there was any merit in permitting the Chief Regulatory Officer (“CRO”)/ Compliance Officer (“CO”) of MIIs to independently place any additional agenda paper and/or notes before the Board was discussed. The Committee was of the view that this need not be examined further since the CRO/CO already report to the Regulatory Oversight Committee (“ROC”) under the existing regulatory framework. The Committee deliberated on periodic meetings of CRO/compliance officer, the chief risk officer, the chief information security officer (“CISO”) and the statutory auditors with the PIDs and NIDs (without the presence of the MD and any other executive director) to discuss important issues concerning the MIIs.

The Committee noted the requirements under the LODR Regulations, 2015 and the Companies Act, 2013 which prescribe the periodicity of meetings of committees and of independent directors. The Committee further took note of a summary prepared by SEBI on the frequency of meetings of statutory committees of MIIs and noted that certain MIIs held an inordinately large number of committee meetings than what could be considered reasonable. The Committee felt that the efficacy of the role played by an MII is not commensurate with the number of committee meetings, but it has a lot to do with the oversight exercised by the committees on an exception basis. It was agreed that the Board of the MII should review this aspect and adopt a rational and reasonable approach.

**Recommendations:**

*35) The Board of the MII should focus on strategy, policy level issues and important matters; day-to-day operational matters in the ordinary course need not be placed before the Board on a routine basis. These matters may be reviewed on an exception basis. The Board of the MIIs should oversee the critical operations including technology as well as the regulatory, risk management and compliance functions of the MIIs.*

- 36) *The terms of reference of the statutory committees should be reviewed and streamlined by SEBI in consultation with the MIIs.*
- 37) *Agenda items of the Board of the MII and its statutory committee should be approved by Chairperson of the Board and Head of statutory committees, respectively (in accordance with the prescribed Secretarial Standards). Further, any member of the Board or the statutory committee of the MII should be allowed to place an agenda item during their respective meetings.*
- 38) *The Board of the MII (without the presence of the MD and any other executive director) or the Chairperson of the Board, on a periodic basis as specified by SEBI, shall meet the Chief Regulatory Officer (CRO)/ Compliance Officer, the Chief Risk Officer (CRO), the Chief Information Security Officer (CISO), the Statutory Auditor of the MII and any other person as determined by the PIDs and NIDs to discuss important issues concerning the MII.*
- 39) *The MD and CEO of the MII shall meet skip level employees (without the presence of their reporting heads) to discuss important issues concerning the MII. The MII shall specify the periodicity of such meetings.*
- 40) *The Board of the MII should periodically review the frequency of meetings and agenda items of the Board and statutory committees to ensure that the number of meetings is rationalized and all important issues are discussed.*

## **II. Function and composition of Statutory Committees of the MIIs**

The SECC Regulations, 2018 and the D&P Regulations, 2018 require MIIs to mandatorily constitute certain statutory committees. These comprise three functional committees: (i) Member and Core Settlement Guarantee Fund Committee (for stock exchanges and clearing corporations)/ Member Committee (for depositories); (ii) Grievance Redressal Committee (“GRC”); and (iii) Nomination and Remuneration Committee (“NRC”) and four oversight committees: (i) Standing Committee on Technology (“SCOT”), (ii) Advisory Committee, (iii) Regulatory Oversight Committee (“ROC”) and (iv) Risk Management Committee (“RMC”). The composition, quorum and functions of the statutory committees are further prescribed under SEBI Circular dated January 10, 2019.

The Committee deliberated whether there was a need to review the role, function and composition of the statutory committees. The Committee also discussed rationalization of the existing structure of the committees to ensure that all the areas were appropriately covered.

The Committee noted that under the current framework, SHDs (NIDs) were not permitted to be members of some statutory committees (for example, the NRC and the RMC) or could only attend as invitees (for example, the ROC). It was further noted that the exclusion of SHDs was historically based on the need to separate the regulatory and commercial functions of the MIIs. The Committee felt that the SHDs may have the ability to provide important inputs to the functioning of an MII and this should be fully leveraged upon. The Committee discussed the need to revisit such exclusion (of SHDs), provided checks and balances were present to ensure that the number of PIDs is always greater than or equal to the other members on all committees. Further, in view of technological advancements, the Committee also discussed giving the MII the discretion to make the MD a member, and the Chief Technology Officer (“CTO”) an invitee, to the SCOT, given the specialist nature of the SCOT. The requirement of PIDs being greater than or equal to the other members may be diluted for SCOT with respect to the Independent External Persons (IEPs) (who should not be considered in the calculation of the number of members other than the PIDs).

The Committee while taking note of the fact that as ROC is responsible for the oversight of the regulatory and compliance function of the MII, the RMC should be responsible for oversight of the critical operations of the MII. In this regard, the Committee felt that the MD and CEO may be allowed to be a member of the RMC.

A specific issue was raised in relation to the GRC being considered a statutory committee, since it does not have any representation from members of the Board of the MII and is comprised solely of independent experts. The Committee discussed the functioning of GRC which in practical terms functions like panels of independent experts pan India for resolving investor grievances and does not hold any committee meetings. The Committee further noted that the monitoring and supervision of GRC currently rests with the ROC.

Further, the role of Advisory Committee was also discussed where the committee noted that it essentially is a committee of trading members which was created at the time of demutualization of stock exchanges to advise on non-regulatory and operational matters, including product design, technology, charges and levies. In this regard, the Committee felt that advisory committee is essentially a mechanism for interaction between the MII and its members and may not be deemed as a statutory committee. The MII may develop internal mechanisms to obtain feedback and views of its members.

The Committee further discussed the existing framework for the eligibility criteria, tenure, and performance of the IEPs. The Committee took note of SEBI circular dated January 10, 2019, which imposed an obligation on the MIIs to formulate specific guidelines for the appointment, tenure, and code of conduct for the IEPs.

### **Recommendations:**

- 41) The NIDs (other than Executive Directors) should be permitted to be members of all statutory committees. Also, the MD may be included as a member of SCOT and RMC while the CTO may be made an invitee on the SCOT committee. This is subject to the condition that the total number of PIDs on a statutory committee is equal to or greater than the number of all the other members of such committee, provided however, for the SCOT committee, the IEPs shall not be considered in the calculation of the number of other members on such committee.*
- 42) The RMC should be responsible for overseeing critical operations vertical of the MII. The TORs for the RMC should include the roles and responsibilities mandated under the Companies Act, 2013 and the LODR Regulations, 2015.*
- 43) The GRC does not need to be considered as a Statutory Committee. It can be categorised as a “Grievance Redressal Panel”. The existing SEBI guidelines for GRC shall be made applicable to such panel.*
- 44) The Advisory Committee may not be considered as a Statutory Committee and the MIIs should develop internal mechanisms (including an internal committee) to obtain suggestions/feedback from its members.*

### III. Evaluation metrics for assessment of effectiveness of Statutory Committees of the MIs

While statutory committees perform various duties and responsibilities under the current legal framework, the regulations should also provide a mechanism to assess the effectiveness of the committees. Therefore, a need was felt to devise a set of objective metrics to evaluate the performance of such statutory committees. The Committee agreed that the evaluation process of the statutory committees can be combined with that of the Board of the MII and accordingly, the evaluation process as provided under Chapter 3(II) of this Report can be made applicable to the statutory committees as well. A list of indicative parameters for evaluating the statutory committees was also discussed.

#### **Recommendations:**

45) *In addition to the annual self-assessment of the statutory committees and its members, the performance of the statutory committees of the MII and its members (including IEPs) should be evaluated by an external agency at least once in every three years with the first evaluation being conducted within twelve months of the date of implementation of the recommendations. An indicative set of metrics for evaluating the effectiveness of statutory committees and its members is set out in Annexure E.*

## **Chapter 6: Key Managerial Personnel (KMPs)**

The regulatory framework for each MII provides for certain roles in the securities market ecosystem to be undertaken by such MII. The responsibility to ensure that the MII undertakes its functions in a manner that enshrines the spirit of the regulatory requirement lies collectively with the management of MII and its Board of Directors. Individual KMPs and other employees play an important role in carrying out various responsibilities cast upon an MII. They also play an important role in establishing the right culture and governance within an MII.

This chapter sets out the recommendations with respect to strengthening the process of appointment and designation of KMPs in MIIs, reviewing their role, effectiveness and compensation related norms and placing accountability on them.

### **I. KMP Designation and Appointment Process**

It was noted that in the context of MIIs, the term “key management personnel” is currently defined under Regulation 2(1)(j) of the SECC Regulations, 2018 and Regulation 2(1)(k) of the D&P Regulations, 2018. These regulations, further prescribed certain requirements from KMPs, such as meeting “fit and proper” criteria, complying with the Code of Ethics and trading restrictions. Compensation of KMPs and their tenure in regulatory department are based on the compensation policy determined by the NRC of each MII.

In the past, however, governance lapses had been reported in designating certain personnel as KMPs, which resulted in non-application of the prescribed requirements that are otherwise applicable to KMPs. Further, the MDs and KMPs of subsidiaries of MIIs have also not been considered under the existing definition of KMP, even if some of these subsidiaries performed important functions for the relevant MII. Conversely, it was noted that given the wide definition of KMPs (in particular, the reference to any persons up to two levels below the CEO/MD), certain junior level employees were being covered, which needed rationalization. There was also a need felt to revisit the role played by the NRC of the MII in the appointment and removal of KMPs.

Based on recent experiences, the Committee discussed the need to review the current definition of KMP and deliberated on whether to adopt a principle-based or a rule-

based approach or combination of both, for such definition. The view that emerged was that it is important to review the definition of the term KMP and a practical and pragmatic approach should be followed to ensure that individuals with the ability to influence decisions as well as those involved in the core functions in the MII should be brought within the ambit of the new definition. The Committee also discussed the need to include any additional roles that require classification as a KMP. The view was that to designate a person as a KMP, the test should be role-based rather than level-based. Further, the definition should cover members of the core management team, including persons handling core and critical activities of the MII, as well as any other personnel involved in important decision-making roles as determined by the MD or the NRC. The Committee believed that this would ensure sharper focus in terms of defining a KMP's responsibility, reviewing their effectiveness and fixing individual accountability. Finally, for purposes of clarity and to remove any ambiguity, the definition of KMP should specifically include the MD, the CEO and any executive director.

The Committee also discussed whether to specifically bring under the purview of the definition of KMP any key functionaries of subsidiaries of the MII. It was felt that this should be left to the determination of the MII's NRC, which could take into consideration the role of such personnel in case the subsidiary is material or has an important bearing on the functioning of the MII or the capital markets in India. If the subsidiary is already an entity regulated by a financial services regulator, the norms prescribed by SEBI or such other financial services regulator could be considered by the MD or the NRC to determine whether or not the subsidiary's personnel should be designated as a KMP of the MII.

Further, the Committee deliberated on the need to review an MII's organization structure on a periodic basis so that the identification of KMPs could be a dynamic process. The need for oversight of the NRC over consultants appointed by the MD by way of a half-yearly reporting by such consultants was also discussed. The Committee deliberated whether the regulations should explicitly mention that the NRC should be solely responsible for appointment and removal of the KMPs and concluded that while the NRC should be the recommending authority, the Board of the MII should remain the final approving authority.



### **Recommendations:**

46) *The definition of KMP shall be as under:*

- (i) any person appointed as the managing director or executive director or the chief executive officer; or*
- (ii) a person serving as head of any department who directly reports to the managing director or executive director or chief executive officer or to the directors on the Board of the MII; or*
- (iii) a person serving as head of any core functions under the three verticals; or*
- (iv) a person in such position that stands higher in hierarchy to the head of any department(s) handling core functions in the MII; or*
- (v) any person defined as a “key managerial personnel” under the Companies Act; or*
- (vi) any other person who is key decision making authority, at the level of the MII or its direct or indirect material subsidiaries, as identified by the MD/CEO or its NRC.*

*Provided that in the case of subsidiaries of MIIs regulated by a financial sector regulator, the norms prescribed by such regulators (including SEBI) can be considered in determining whether or not such person at the subsidiary should be designated as a KMP.*

47) *The NRC should also ensure that no KMP reports to a non-KMP.*

48) *A detailed report should be placed before the NRC on a half yearly basis on any consultant (individual or firm) (by whatsoever name called) directly reporting to the MD/ED/CEO.*

49) *The Key Responsibility Areas (“KRAs”) of each KMP should be finalised, on MD’s recommendation, by the NRC based on their role in the MII at the beginning of the year and should be reviewed on periodic basis.*

50) *The NRC of the MII should undertake a review of hierarchical set ups across the departments, at least once a year, in order to identify KMPs due to a change in*

*role and responsibilities assigned to them. Such review should necessarily include, consultants reporting to the MD/ED/CEO and any person (including employees/consultants) drawing pay higher than any KMP.*

*51) With respect to the appointment and removal of any KMP, the regulations should specify that this will be subject to the approval of the Board of the MII, based on the recommendations provided by the NRC.*

## **II. Responsibility and Accountability among KMPs and Other Employees**

The responsibility to ensure that the MII undertakes its functions in a manner that enshrines the spirit of the regulatory requirements lies collectively with the management personnel within MII together with the Board of the MII. The existing regulations, however, do not explicitly stipulate norms mandating the MII to define the responsibility and individual accountability among KMPs and review their performance *vis-à-vis* the role entrusted to such personnel.

The Committee took note of the prevalent norms defining responsibility and accountability of senior managers at financial institutions in certain international jurisdictions. For example, under the UK Financial Service and Markets Act, 2000 (“FSMA”), senior managers are required to have a statement of responsibility which sets out their roles and responsibilities. Further, every senior manager has a duty of responsibility under the FSMA, which states that if a firm breaches any regulatory requirement, the senior manager responsible for that area could be held accountable if they did not take reasonable steps to prevent or stop the breach, supported by evidence. It was also noted that such senior management regime of the UK has played an important role in improving conduct and accountability standards across financial service institutions. Similarly, the Monetary Authority of Singapore (“MAS”), has introduced guidelines on ‘Individual Accountability and Conduct’ that require financial institutions to clearly identify the senior managers responsible for managing and conducting their core functions.

In India, given the dual role of MIIs as a business/commercial entity as well as a frontline regulator, the need to clearly identify responsibilities and duties to the relevant positions within the MII assumes importance. This is also to ensure that business objectives do not gain undue precedence over the regulatory role of the MII. The

Committee felt that the business teams in an MII also should be responsible for regulatory, compliance and risk related matters.

The importance of effective evaluation of performance of KMPs (including business teams) and giving due weightage to the regulatory, compliance and risk metrics were also discussed.

**Recommendations:**

- 52) *The MII should be required to clearly delineate and segregate roles and responsibilities of KMPs within the MII. This should include mapping legal and regulatory duties to the concerned position within the MII and defining delegation of powers to each position within the organization. Business and support teams should also be assigned responsibilities related to regulatory, risk management and compliance related aspects, as they are the first line of defense of the MII.*
- 53) *Each KMP should be required to submit a half-yearly self-assessment report mapping discharge of all their responsibilities vis-à-vis the assigned KRAs backed by necessary details to their respective heads, who in turn will furnish the regulatory aspects of their assessment to CRO. CRO shall place such regulatory assessment report to ROC in a time bound manner. The functional head and CRO (incorporating the comments of ROC, if any) in a time bound manner should place their respective assessment reports before NRC. The comprehensive report should be placed before the Board of the MII on an annual basis through the NRC and a standardised format may be prescribed for recording the specific functions performed by the KMPs and ensuring uniformity in reporting.*
- 54) *The existing metrics on performance evaluation of KMPs should be reviewed to comprehensively cover the roles and responsibilities, including to introduce appropriate and adequate weightage to regulatory, risk management and compliance related aspects in accordance with the roles being performed by the KMPs in the organisation.*
- 55) *The metrics for performance evaluation of MDs should provide fair amount of weightage (at least 50%) to regulatory, risk management, compliance outcomes as well as resilience of MIIs' infrastructure and conduct-related aspects.*

56) SEBI should adopt accountability-based regime, wherein persons who have breached their roles and responsibilities or applicable regulations are identified and held accountable. If any event highlights lapse or deficiencies in the functioning of the MII or its KMPs, the Board of the MII should be responsible for identifying individuals accountable for the breach or lapses noted, along with classifying the reason for such breach or lapse. SEBI and the MII can consider the following factors in attributing fault on an individual: (a) a mala fide intent/ act of commission, (b) an act of omission/ negligence, or (c) genuine decision-making that went wrong. Due care should be exercised in fixing accountability in respect of factors under category (c), so as not to discourage genuine business decisions, while at the same time, repeated instances of wrong decisions are taken cognizance of.

### III. Variable Pay and Other Compensation Related Norms

Regulation 27 of the SECC Regulations, 2018 and Regulation 28 of the D&P Regulations, 2018, read with the corresponding schedules, prescribe the current norms for compensation of KMPs (including MDs of MIs), which include, among others, the following:

- (a) *“The variable pay component shall not exceed one-third of total pay.*
- (b) *50% of the variable pay shall be paid on a deferred basis after three years.*
- (c) *ESOPs and other equity linked instruments in the stock exchange/ clearing corporation/ depositories shall not be offered or provided as part of the compensation for the key management personnel.*
- (d) *The compensation policy shall have malus and clawback arrangements.”*

Under the current compensation policy applicable to KMPs (including MDs), it was noted that while there is a cap on the variable pay not exceeding one-third of the total pay, there is no minimum amount required to be paid to a KMP as variable pay. This anomaly may result in ineffectiveness of the current clauses relating to deferred payment and malus. Further, it was noted that ESOPs and other equity-linked instruments are currently not permitted to be offered as part of the compensation. It was noted that the Bimal Jalan Committee had specifically recommended that the compensation should not include any form of equity/ equity-linked or stock options in MIs in order to ensure autonomy of regulatory departments, and this recommendation had been taken into account while drafting the regulations.

Over time, a need has been felt to strike a balance between incentives to and performance of KMPs in MIs, to attract the best talent and at the same time hold KMPs accountable for their performance. With respect to variable pay, the Committee took note of the Financial Stability Board (FSB) Principles for Sound Compensation Practices and Implementation Standards – implementation standard 6 which, *inter alia*, states that:

*“...for senior executives as well as other employees whose actions have a material impact on the risk exposure of the firm: a substantial proportion of the compensation should be variable and paid on the basis of individual, business-unit and firm-wide measures that adequately measure performance.”*

The Committee also noted that in the case of compensation of managing directors of banks, the existing norms prescribed by the RBI provide for a minimum variable pay of 50% of the total pay (in addition to a maximum of 75% of total pay). Accordingly, the Committee believed that a minimum threshold of variable pay should be introduced. The Committee, however, noted that an MII also plays the role of a regulator, unlike other commercial entities such as banks, and therefore, the minimum variable pay for an MII need not be as high as that applicable to banks. It was also felt that ESOPs, as part of compensation to KMPs, had become an important and prevalent tool in attracting and retaining talent in the corporate world, including corporate entities in other regulated sectors as well as listed entities. Accordingly, the Committee was of the view that ESOP-related compensation should be permitted in MIIs and should be included as part of the variable pay component.

**Recommendations:**

*57) The regulations should be amended to provide for a minimum as well as maximum amount as variable component of the KMPs' compensation. Accordingly, the range of variable pay should be from 25% to 50% of the total pay. Perquisites and contributions towards superannuation/retirement benefits (other than Gratuity) will be treated as part of the fixed (and total) pay. It is clarified that the MII is under no obligation to actually make any payment on the variable component and the same may be based on the policies of the MII considering various performance parameters.*

*58) ESOPs should be permitted to be granted to KMPs of MIIs. Any ESOPs granted should form part of the variable pay component of the KMP. The value of the ESOPs should not be more than 50% of the variable pay. The MII should have a proper balance between the cash and share-based components, taking into account the role of the MII as a regulator as well as any commercial objective. Similar to the provisions prescribed by RBI for banks, share-based instruments should be fair valued on the date of grant by the MII, using the Black-Scholes model. This fair value should be recognised as an expense beginning with the accounting period for which the approval has been granted.*

59) *The existing deferral period (50% of the variable pay for three years) should continue for an MII. It should be clarified that the deferral period is for a minimum period of three years, and any longer period will be based on the policies of the MII. The deferral period should be applicable to both cash and non-cash components of the variable pay.*

60) *The MII should continue to have the requirement to have malus and claw-back arrangements. MIIs should have appropriate policies to incorporate malus/claw-back mechanisms, which should take into account regulatory, risk and compliance aspects, in addition to any other criteria as specified by the MII. A sunset period during which the malus and claw-back arrangements can be applied, taking into account the minimum deferral and retention periods, may be introduced by SEBI.*

#### **IV. Incentive Mechanism for Discharging Regulatory Roles of KMPs**

As noted above, Regulation 27 of the SECC Regulations, 2018 and Regulation 28 of D&P Regulations, 2018, read with the corresponding schedules, prescribe the current norms for compensation of KMPs (including MDs).

To strike a balance between regulatory and business functions, the Committee was of the view that the compensation structure of KMPs of MIIs (including MD and CEO) should be designed in such a manner that it incentivises them to ensure that the MII performs its regulatory function in an efficient manner. While the current regulations permit variable pay and provide overall guidance for determining the MII's compensation policy, they do not spell out the factors to determine variable pay. In this regard, the Committee discussed certain indicative parameters which could act as a guide to NRCs in determining the list of parameters and methodology based on which the variable component of the total pay of KMPs could be determined.

##### **Recommendations:**

61) *For each KMP, due weightage should be provided to the regulatory, risk management and compliance related aspects including Code of Conduct/Ethics for determining variable pay. In this regard, SEBI may, in consultation with the MIIs, issue certain indicative and illustrative parameters which NRCs could consider to evaluate KMPs (including MDs). An indicative list of parameters is*

given in **Annexure F**. The NRC should review the relevant metrics/parameters for the KMP evaluation on a periodic basis.

## V. Disincentive Structure in Relation to Misdemeanor/Misconduct

Regulation 26(2) of the SECC Regulations, 2018 and Regulation 27(2) of D&P Regulations, 2018, read with the corresponding schedules, prescribe the Code of Ethics for directors and KMPs of MIs. The objective of the Code of Ethics is to enhance the level of market integrity and investor confidence and it currently covers the following aspects:

- a. Objectives and underlying principles of the code.
- b. Regulatory Oversight Committee for overseeing implementation of the code.
- c. General standards of conduct.
- d. Disclosure of dealings in securities by KMPs and directors.
- e. Avoidance of conflict of interest.
- f. Disclosures of beneficial interest.

Further, Regulation 28 of the SECC Regulations, 2018 and Regulation 29 of D&P Regulations, 2018 deal with measures to ensure segregation of regulatory departments and state, *inter-alia*, that the employees in the regulatory departments shall not communicate any information concerning regulatory activity to any one in other departments.

While the current regulations envisage a minimum level of business/professional ethics to be followed by directors and KMPs of MIs towards establishing a fair and transparent marketplace, they may need to be strengthened for mechanisms and consequential actions to disincentivise KMPs and other employees when misdemeanour or misconduct is noted. While MIs, in practice, have internal policies for taking disciplinary action against employees, this was not based on a specific regulatory requirement nor it followed a standardised disciplinary action mechanism. The Committee felt that there is a need that MIs should introduce a standardised process for disciplinary actions.



### **Recommendations:**

- 62) *MIIs should devise internal standard operating procedures (“SOPs”) for disciplinary actions and the same should be approved by NRC and the Board of MII. This SOP may include advisory notes, warnings, impact on annual increment/promotion, invocation of malus-claw-back provisions, termination, among other actions, as may be suggested by the NRC.*
- 63) *The NRC may also be required to list out an illustrative set of situations which may require them to invoke the malus and claw-back clauses. NRCs should be responsible for the implementation of these situations.*
- 64) *Disciplinary actions and penalties on the MD or other KMPs should be premised on a fact and inquiry-based process (adhering to the principles of natural justice) by the MII to prevent unfair consequences.*

## **VI. Policy for Employees with Poor Record of Adherence to Code of Conduct/ Code of Ethics**

The provisions of the SECC Regulations, 2018 and D&P Regulations, 2018 prescribe the Code of Ethics applicable to directors and KMPs. Regulation 28 of the SECC Regulations, 2018 and Regulation 29 of D&P Regulations, 2018, read with corresponding schedules, require measures to ensure the autonomy of regulatory departments of MIIs. These include:

- a. “Chinese Wall” policy which separates the regulatory departments from the other departments.
- b. The employees in the regulatory departments should not communicate any information concerning regulatory activity to any one in other departments.
- c. The employees in regulatory areas may be physically segregated from employees in other departments including with respect to access controls.

Further, the regulations also require the period of posting of KMP in a regulatory department to be for a fixed period.

Given the regulatory responsibilities imposed on an MII, it is important that its employees strictly follow the Code of Conduct/Ethics. The MII should consider whether employees that have violated such Code should continue to be a part of the regulatory department of the MII.

Based on discussions with the MIIs, the Committee noted that most MIIs had internal policies which required ongoing compliance with the Code of Conduct/Ethics as a pre-requisite for continuation of employment. The Committee was of the view that there was no need to include additional requirements in this regard.

## **VII. Annual Review of Increase in Compensation of Employees (other than KMPs) by the NRC**

As noted above, the SECC Regulations, 2018 and D&P Regulations, 2018, prescribe norms for determining the compensation policy of directors and KMPs.

While the regulations mandate periodic review by the NRC for KMPs (including the MD) compensation, there is no requirement of review for compensation of employees that are not KMPs. The Committee discussed situations where in the past there have been instances of arbitrary and disproportionate increases in compensation, resulting in undue favouritism to a non-KMP consultant who was performing the role of a KMP.

After deliberations, the Committee noted that extending the scope of NRCs to cover compensation of non-KMP employees could impose additional burden on the functioning of the NRC. In any event, if the proposed change in the definition of KMP, as well as the periodic review of identification of KMPs (as recommended above) are implemented, the persons performing important functions in the MII and those drawing pay more than any KMP would be automatically subject to the NRC review. Accordingly, the Committee felt no changes are required in the regulations in this regard.

## **VIII. Mandatory Periodic Reporting by KMPs to PIDs**

Under the regulatory framework applicable to MIIs, PIDs are required to report any issues concerning MIIs to SEBI. While the Board of the MII, including the relevant committees, are briefed on matters, the effectiveness of such briefing has come up for question in past instances where governance lapses were highlighted.

The suggestion of provision of periodic reports by KMPs to PIDs, including submission of 'nil reports', was discussed by the Committee. While such a submission could enhance the accountability by a KMP and provide a direct access to the PIDs, it was also discussed that under the current framework, there was no restriction on direct access by a KMP since they were regularly reporting to various committees where PIDs were members. Further, if a KMP or any other employee wished to flag any major lapses, they could also do so by way of a whistle-blower complaint. The Committee was of the view that no changes were required to the existing requirements.

## **IX. Mandatory Periodic Reporting by Chief Regulatory Officer/Compliance Officer to SEBI**

Under Regulation 30 of SECC Regulations, 2018, and similar regulation in D&P Regulations, 2018, the compliance officer of the MII is required to immediately and independently report to SEBI any non-compliance with relevant SEBI regulations that has come to her/his notice.

Based on the above requirement, a compliance officer of an MII is required to report any non-compliance to SEBI independently, on an as-required basis. Any failure on the part of the compliance officer to carry-out their obligation may not be discovered until non-compliances with norms come to light subsequently.

It was also discussed that the CRO/CO of an MII submits a monthly report to SEBI, inter-alia, containing compliance with various recent regulatory developments. Further, it was noted that the compliance officers also submit quarterly compliance reports to the MII's Board. The Committee, however, was of the view that periodic compliance and the type of report should be submitted to SEBI in a structured manner to increase the accountability.

### **Recommendations:**

65) *The CRO/CO should submit a quarterly report on non-compliances of extant regulatory norms to SEBI, in a format to be prescribed by SEBI.*

## **X. Designated KMP for Compliance and Regulatory Functions of the MII**

As noted above, MIIs are required to appoint a compliance officer under the relevant regulations. Further, under Regulation 28 of the SECC Regulations, 2018, read with Schedule II Part C, and similar requirements under D&P Regulations, 2018, an MII is required to

*“..ensure that the regulatory departments viz., surveillance, inspection, risk management, default, investor protection, investor services etc., are sufficiently staffed with adequate number of persons having professional and relevant experience at all times.”*

In addition, Regulation 33 of the SECC Regulations, 2018, and similar requirements under D&P Regulations, 2018, state the following:

*“Recognised stock exchange and a recognised clearing corporation shall disclose resources committed towards strengthening regulatory functions and towards ensuring compliance with regulatory requirements applicable to the recognised stock exchange or recognised clearing corporation, as the case may be, backed by an activity based accounting in the report under section 134 of the Companies Act, 2013.”*

Further, PFMI Principle 2.6 under the head ‘Roles and responsibilities of management’ states that

*“Governance arrangements should ensure that the risk-management and internal control functions have sufficient authority, independence, resources, and access to the board”.*

In this regard, it was discussed that while MIIs are required to ensure that the regulatory departments are sufficiently staffed, and disclose resources committed towards strengthening regulatory functions, , there is no specific responsibility cast on

an MD or any other KMP to ensure that the MII adequately allocates financial, human and technological resources to its regulatory function.

The Committee discussed that the following compliance and regulatory functions need to be discharged by an MII:

- a) compliance with the Companies Act and related rules and regulations;
- b) compliance with SEBI Regulations, rules, circulars and directions, and with the rules and regulations of any other financial services regulator if applicable to the MII;
- c) role of the MII as a first-level regulator, including investor protection and regulation of its members; and
- d) monitoring risks associated with the MII.

Each of the four functions require a KMP to ensure that the compliance and regulatory functions of an MII are effectively discharged. In this context, it was also noted that the regulations already contemplate a compliance officer who shall immediately and independently, report to SEBI any non-compliance of provisions under the SEBI Act, the SCRA, the Depositories Act and rules, regulations, or directions issued thereunder and for the redressal of investors' grievances.

**Recommendations:**

*66) MIIs should identify KMPs responsible for regulatory, compliance and risk management functions stated above. The CRO/CO can discharge more than one function. The MII should have a separate Chief Risk Officer, who would be in-charge of handling risks associated with the MII.*

## **XI. Fixed Tenure of KMPs in Regulatory Departments**

Under the current regulations, the tenure of a KMP is required to be decided by the NRC. This requirement was based on one of the recommendations of the Bimal Jalan Committee, as a measure suggested by the committee towards ensuring autonomy of regulatory departments of MIIs.

There was a suggestion to revisit the requirement of fixed tenure in the context of the regulatory department of an MII since it may impact continuity in functioning of the department. The current practice of rotation, followed by some of the MIIs, was noted.

The Committee noted that requirements relating to tenure, conflicts of interest and succession planning were already covered under the current regulations. Accordingly, no further suggestions were made.

## **Chapter 7: Code of Conduct and Code of Ethics**

This chapter sets out the recommendations in relation to the Code of Conduct and the Code of Ethics for the MIIs and their directors, KMPs and other persons associated with such institutions.

### **I. Code of Conduct and Code of Ethics for Directors, Committee Members and KMPs**

The SECC Regulations, 2018 and the D&P Regulations, 2018 prescribe the Code of Conduct and Code of Ethics for the directors and KMPs of the MIIs. The Code of Conduct applies to all directors of an MII and prescribes, *inter alia*, the manner of conducting board meetings, maintaining records of the board minutes and the minimum number of meetings for the PIDs. The Code of Ethics is applicable to both the directors as well as KMPs and prescribes, among others, the guidelines for avoiding conflict of interest, preventing misuse of position, improving access to information and disclosure requirements.

The Committee felt the need to strengthen the accountability mechanism so that the persons responsible could be held accountable when violations or misconduct are noticed. The scope of the Code of Conduct is currently limited to the directors of the MIIs and does not cover the conduct of the KMPs and the non-director members of the committees of the MIIs such as IEPs. Therefore, the Committee felt there was a need to review the existing regulatory framework and recommend changes to the Code of Conduct such that it applies to all directors, KMPs and committee members of MIIs.

In connection with the above, the Committee also discussed the adequacy of the current regulatory norms, including those prescribed for the IEPs. The Committee took note of SEBI circular dated January 10, 2019, which requires MIIs to frame a code of conduct for the IEPs, and the Code of Conduct under the SECC Regulations, 2018 and D&P Regulations, 2018, which extends the general standards of conduct to all committee members including the IEPs. Further, the Committee discussed the existing provisions with respect to the role of the Board of the MIIs and the ROC in ensuring compliance of the directors and KMPs with the Code of Conduct and Code of Ethics. The Committee also noted that non-KMP employees were typically

governed by the service rules of their respective MIIs which draw guidance from the Code of Conduct prescribed under the regulations.

**Recommendations:**

67) *The existing Code of Conduct and Code of Ethics prescribed under the SECC Regulations, 2018 and D&P Regulations, 2018 should be combined into a single standardized Code of Conduct. The new Code of Conduct shall apply to all the Board members, KMPs and committee members. Certain specific items shall apply only to Board members, Committee members or KMPs as the case may be. The proposed new Code of Conduct is annexed at **Annexure G**.*

68) *KMPs shall comply with all internal policies of the MII. If there is a conflict with or standards are lower in the internal policy of MII then the Code of Conduct as specified by SEBI shall prevail.*

69) *The Board of the MII should be responsible for monitoring compliance with the Code of Conduct by the members of the Board of the MII. The ROC should be responsible for monitoring compliance with the Code of Conduct by the KMPs and the other members on the committees of the MIIs.*

## **II. Code of Conduct of the Stock Exchanges and Clearing Corporations**

Regulation 17 of the D&P Regulations, 2018 mandates that a depository holding a certificate of commencement of business shall, at all times, abide by the Code of Conduct as specified in Part-D of the Third Schedule of such regulations. Therefore, the depositories are required to abide by a separate code of conduct and have an overall responsibility to, *inter-alia*, act in good faith, proactively protect interests of the investors and monitor compliance of norms by the participants. On the other hand, the SECC Regulations, 2018 do not include a similar separate code for regulating the overall conduct of the stock exchanges and clearing corporations at an entity level. Accordingly, the Committee deliberated on the need to amend the SECC Regulations, 2018 and include a separate Code of Conduct for such MIIs (Stock Exchanges and Clearing Corporations).



**Recommendation:**

70) *The SECC Regulations, 2018 should be amended to introduce a separate Code of Conduct for stock exchanges and clearing corporations and such code should include the principles currently prescribed for the depositories under the D&P Regulations, 2018. Accordingly, proposed Code of Conduct applicable to MIIs (i.e., Stock Exchanges and Clearing Corporations) is annexed as **Annexure H**.*

71) *The Code of Conduct of all MIIs should specifically include regulatory, compliance and risk management, good governance and due diligence as important components of operations. Accordingly, the D&P Regulations, 2018 should be amended to include such items in the Code of Conduct applicable to depositories.*

## **Chapter 8: Enhancing Transparency**

This chapter sets out the recommendations with respect to enhancing transparency in the operations of the Board and statutory committees of MIIs, including reviewing the activity-based resource utilization structure in MIIs.

### **I. Agenda and Minutes of meetings of Board of MIIs and Statutory Committees**

Regulation 33 of the SECC Regulations, 2018 and Regulation 31 of D&P Regulations, 2018 extend application of the disclosure requirements and corporate governance norms for listed companies to a recognized stock exchange, clearing corporation and depository. The current regulations applicable to MIIs also stipulate the broad expectations from directors of the MII *vis-à-vis* the manner of proceedings of meetings. These guidelines emphasize, among others, best practices, such as the agenda for the meeting to be circulated well before the meeting, comprehensive discussion to be held on important matters and measures to handle conflict of interest, for both the Board and the statutory committee meetings of MIIs. In addition, the important decisions taken by the Board of the MII are required to be disclosed to SEBI in the format specified under a monthly development report.

The existing norms are however silent on the public disclosure of agenda and minutes of the meetings of the Board and statutory committees of MIIs. In order to review the requirement on making information public, SEBI team also undertook a review of the agendas and minutes of certain MIIs' Board meetings held over a one-year period. From the study, it was observed that the agendas contained both confidential and other information which could be disclosed. The Committee observed that confidential information relating to MIIs need not be disclosed in the public domain.

The Committee deliberated on the implication of public disclosure of such items with a view to enhance transparency and encourage adoption of best practices for MIIs. In this regard, the Committee felt that to begin with certain agenda items of the Board meeting of the MII may be disclosed; however, agenda items of Statutory Committees may not be disclosed at this juncture.

### **Recommendations:**

72) *The MIIs should disclose the agenda and minutes of meetings of the Board, keeping in mind their role as a ‘first-level regulator’, i.e., to begin with agendas related to regulatory, compliance & risk management areas may be disclosed on the website of the MII after the minutes are approved. MIIs should have a Board approved policy for disclosure of agenda and minutes of the Board in public domain. Information that is confidential to an MII need not be made available publicly, and the MII should internally note the reasons for non-disclosure to the public. Once implemented, the public disclosures by MIIs may be subsequently standardized.*

## **II. Activity-based resource utilization of MIIs**

The MIIs perform a dual role as a public infrastructure service provider with regulatory functions and as a profit-making corporate entity. It is important for the MII to ensure that adequate resources are deployed in the regulatory and risk as well as the operations and technology functions/departments of the MIIs. In view of this, Regulation 33 of the SECC Regulations, 2018 and Regulation 31 of D&P Regulations, 2018 require the recognized stock exchange, clearing corporation or depository to disclose the resources committed towards strengthening regulatory and related functions and ensuring compliance with regulatory requirements, as the case may be, and backed by an activity-based accounting in the report under Section 134 of the Companies Act, 2013.

It was, however, observed, that the current disclosures by the MIIs are generic in nature and do not provide specific details regarding the break-down of employees working in different departments as well as the technological and financial resources deployed in these departments, including in regulatory and risk as well as operations and technology. In addition, it was observed by SEBI that employees in regulatory departments were being assigned to operational and revenue generation responsibilities without clear disclosures regarding such responsibilities in the annual reports of MIIs.

**Recommendations:**

*73) Utilization of resources for core functions under critical operations vertical and separately under regulatory, compliance and risk management vertical vis-à-vis other functions should be specifically quantified and disclosed in the annual report of the MIIs. This may include the human resources as well as financial and technology resources deployed by the MII for each of the core functions.*

## **Chapter 9: Net Worth requirements of the MIs and Monitoring of their members and Empanelled Entities**

This chapter sets out the recommendations with respect to strengthening the net worth requirements of the MIs and the role of such institutions in monitoring the members and empanelled entities.

### **I. Net-worth Requirements for the MIs**

The SECC Regulations, 2018 and the D&P Regulations, 2018 require the MIs to have a minimum net worth of not less than Rs.100 crore on a continuous basis. For clearing corporations, the net worth is required to be at least Rs.100 crore or capital as determined under Regulation 14(3)(a) and 14(3)(b) of the SECC Regulations, 2018, whichever is higher. The term “net worth” has been specifically defined in the relevant regulations. In the context of stock exchanges and depositories, net worth has been defined as follows:

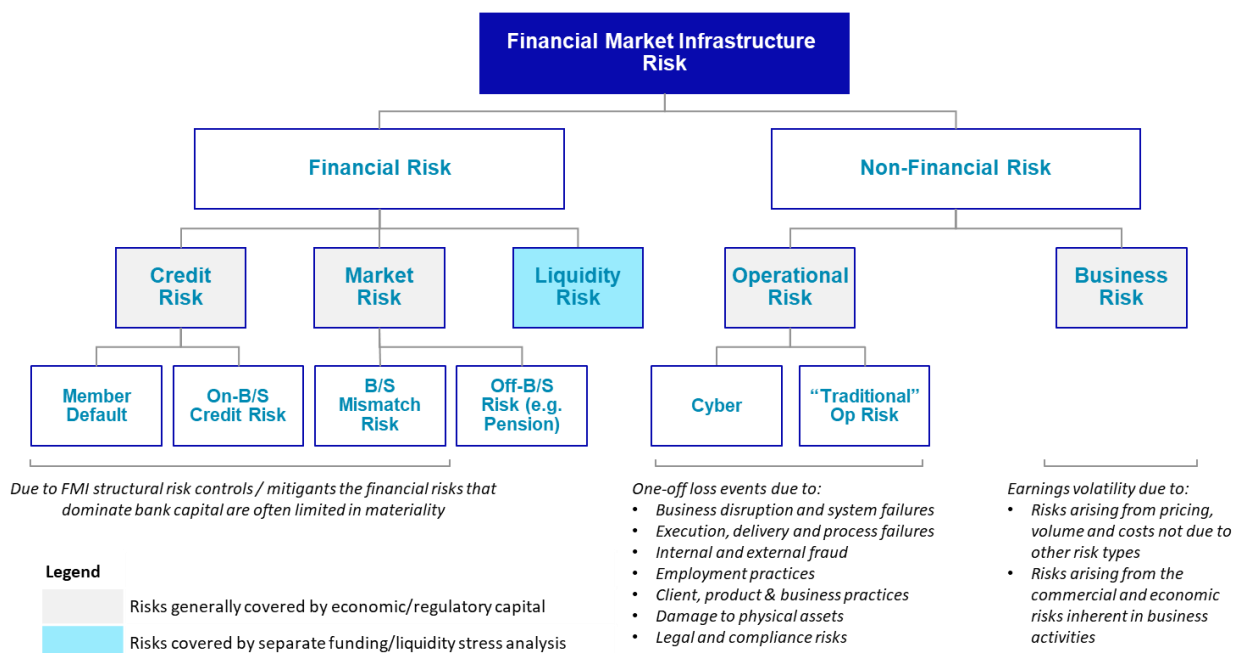
*“aggregate value of paid-up equity share capital plus free reserves (excluding statutory funds, benefit funds and reserves created out of revaluation) reduced by the investments in businesses, whether related or unrelated, aggregate value of accumulated losses and deferred expenditure not written off, including miscellaneous expenses not written off.”*

In the context of clearing corporations, “net worth” has been defined as the aggregate value of its liquid assets calculated in the manner as specified by the Board from time to time. In this regard, SEBI has issued a detailed circular dated April 10, 2019 prescribing the manner in which the risk-based capital and net worth requirements for clearing corporations should be calculated.

Given that the MIs are market infrastructure institutions that play a key role in ensuring the continuity and smooth functioning of the securities markets and taking into account the recent increase in the volume and value of investments and trade of securities in India, the Committee felt that there was a need to review the current net worth requirements for MIs to ensure that MIs are well capitalized to withstand various exigencies. Therefore, the Committee examined whether a risk-based approach should be adopted for all MIs, including the stock exchanges and depositories, and

reviewed the adequacy of the minimum net worth requirements prescribed under the current regulations. The Committee also noted the practice in certain international jurisdictions. In the global context, MIIs have adopted an approach to estimate their risk capital requirements to adequately cover a variety of risks in alignment with the risk appetite statement of the MII. A typical scope of such risk capital estimation is indicated in the diagram below:

Example of typically-observed risk taxonomy



In the international context, MIIs use independent internal and external frameworks that can work separately or in parallel to quantify risk capital requirement. Given that non-financial risks can be a significant category for MIIs such as stock exchanges, global MIIs typically deploy a number of approaches such as scenario-based estimation, formulae-based approaches with necessary adjustments as well as benchmarking with other MIIs.

The Committee further discussed the need to include additional factors, such as unencumbered liquid assets and activity-based risk factors, for computing the net worth of MIIs. It was noted that the wind-down plan for the depositories required such institutions to maintain a part of the net worth in the form of liquid assets. Accordingly, the Committee deliberated on the need to amend the existing regulations to require all MIIs to maintain a part of their net worth in form of liquid assets.

### **Recommendations:**

74) *The net worth requirement of MIIs should include a variable component (over and above the minimum net worth requirement under the existing regulations) based on the following factors:*

- a) Level of activity of the MIIs.*
- b) Adequacy of the net worth to cover various risks, such as the operational risk, legal risk, credit risk, and cyber security/technology risk faced by the respective MII.*

*SEBI should specify the details for the above factors taking into account the risk-based capital requirements currently prescribed for clearing corporations (other than the credit risk requirement which is specific to clearing corporations).*

75) *The Board of the MII should have a well-defined policy to ensure that adequate capital is available in liquid form to meet net worth requirements, including as specified by SEBI from time to time.*

76) *A mechanism should be devised to determine the adequacy of the Investor Protection Fund (“IPF”) and the Settlement Guarantee Fund (“SGF”) on a regular basis and based on this assessment, a specific percentage of the profits of the MII should be shifted to the IPF in consultation with SEBI. Such mechanism should be reviewed by an external agency on a periodic basis.*

## **II. Monitoring Mechanism for the Members and Empanelled Entities**

SEBI has issued circulars for inspection of trading members and clearing members by the stock exchanges and the clearing corporations respectively. The stock exchanges and the clearing corporations have been advised to continuously assess the risks posed by their members and review/revise the policy of annual inspection, as and when required, in consultation with SEBI. In addition, SEBI has also issued circulars requiring the stock brokers and the clearing members to conduct an internal audit on a half-yearly basis by appointing independent qualified chartered accountants. Such audit is required to cover, among others, internal control systems, compliance with

provisions of SEBI Act, the SCRA, SEBI (Stock Brokers) Regulations, 1992 and other relevant circulars issued by SEBI. The findings, however, of such inspections by MIIs and internal audits by members are currently not required to be shared with SEBI.

The Committee took note of the current information sharing mechanism established among the stock exchanges for sharing the outcome of the inspections on members with membership at multiple exchanges. It was noted however, that the coordination to share such information could be improved. Therefore, the Committee discussed the need to standardise the inspection framework for common brokers. Other measures for strengthening the enforcement mechanisms and reducing repeated non-compliances by the stock brokers and clearing members were also discussed.

In addition, the Committee noted that SEBI has also created a framework for empanelment of back-office vendors by the stock exchanges which aims to ensure access of back-office of the vendors or trading members to authorised individuals and bring accountability and transparency in their operations. This should be monitored regularly for effectiveness. The Committee also discussed the use of technology by the stock brokers and clearing members in view of SEBI's discussion paper dated December 9, 2021 on automation of trading.

**Recommendations:**

*77) MIIs should enhance sharing of information in a structured manner with other MIIs on non-compliances by its members holding membership of multiple MIIs.*

*78) The MIIs should require their members (stock brokers, clearing members and depository participants) to adopt technology to reduce reliance on physical information sharing and explore measures to enhance effectiveness of the present systems.*

*79) MIIs should have internal policies for appointment and periodic monitoring of back office vendors or outsourced agencies by the MII and/ or their members to ensure compliance with various regulatory requirements.*



### III. Default Detection and Prevention Systems of the MIIs

In accordance with SEBI circular dated December 17, 2018, the stock exchanges, clearing corporations and depositories have jointly put in place an early warning and information sharing mechanism. The Early Warning Mechanism (“EWM”) helps the MIIs to detect the diversion of client’s securities by a stock broker at an early stage and to implement appropriate preventive measures. Further, the information sharing mechanism requires an MII to immediately share an alert relating to a stock broker’s deteriorating financial health or any unauthorised transfer of funds or securities of the client with the other MIIs. In view of this, the SOP set out in SEBI circular dated July 1, 2020 harmonises the actions taken by the MIIs after detection of the early warning signals and other triggers relating to default by a trading or clearing member.

The Committee noted that around 30 stock brokers have defaulted in the last few years on multiple grounds, such as misuse of client funds, non-resolution of investor complaints and non-cooperation with exchanges, which may have undermined the effectiveness of the current system and prompted further policy measures by SEBI to prevent defaults by the stock brokers. The Committee felt a need to develop specific metrics to assess the effectiveness of the systems and procedures in the MIIs for prevention of default of stock brokers.

The Committee noted that the parameters for filtration of alerts and initiation of action were not standardised and faced frequent delays. In addition, the alerts were generated based on the data submitted by the stock brokers themselves and concerns were raised regarding reliability on such alerts. Therefore, the Committee discussed the need to issue additional SOPs for the actions taken by the MIIs and evaluated the suggestions proposed for strengthening the default prevention systems and procedures of the MIIs.

The committee noted that the disclosure with respect to compliances and adverse remarks against members of the MII is important information for public and can be enhanced. Presently, the disclosures against members of the MII are scattered on the website of the MII and are not easily accessible for the public.

**Recommendations:**

- 80) MIs should frame an indicative list of parameters to assess the risks associated with their members.
- 81) MIs should provide a list of disclosures that should be made to them by their members, on a periodic basis to further strengthen the oversight of MIs.
- 82) Information that is material to investors related to members of MIs should be made public in a consolidated and structured manner on the website of the MI.
- 83) There should be continuous supervision by MIs of all its members by leveraging technology. Members with higher risk index should be inspected on-site on an annual basis. Other members should be inspected at such other intervals as specified by SEBI.
- 84) The MIs should conduct periodic reviews of their member audit mechanisms to effectively monitor their members and for timely identification of potential defaulters.
- 85) MIs should take additional actions against the defaulting members, such as declaring the defaulting person/entity as wilful defaulters.
- 86) The MIs should be granted recovery powers, similar to the powers granted to banks under the SARFAESI Act, 2002, to ensure compliance with any order or direction issued by them.
- 87) There should be accountability on the MI, if the MI is found wanting in its systemic supervision resulting in the default or contravention by its members that has consequences for investor protection and the capital markets in India.

## **Chapter 10: Information Sharing and Technology Governance**

This chapter sets out the recommendations with respect to strengthening the data sharing systems of the MIIs and enhancing the use of technology for regulation of the MIIs.

### **I. Policy framework for confidential and sensitive information**

The SECC Regulations, 2018 and the D&P Regulations, 2018, require the MIIs to maintain and preserve certain books of accounts and records for a minimum period of eight years. SEBI has also issued circulars which require the MIIs to conduct annual system audits and implement measures to ensure that confidentiality of information is not compromised during the exchange and transfer of information with external parties. In addition, SEBI circular dated May 20, 2022, requires the MIIs to identify and designate critical assets based on their sensitivity and criticality for business operations and carry out periodic Vulnerability Assessment and Penetration Testing (“VAPT”) for all critical systems. The Committee also noted that under the PFMI Principles, the Board of the MII is required to ensure that there are adequate internal controls to protect against the misuse of confidential information.

In light of the recent governance lapse noted where sensitive and confidential MII information/data was shared with unauthorized/external persons over external e-mails, the Committee felt that there was a need for the MIIs to improve the framework for maintaining sanctity of confidential information and restricting sharing of sensitive information outside the organisation. Accordingly, the Committee discussed various aspects relating to information sharing by the MIIs and also felt a need to clearly specify the accountability mechanisms for the employees and other persons associated with the MIIs in the event of non-adherence with the identified framework for the safekeeping and sharing of confidential and sensitive information.

#### **Recommendations:**

*88) The regulations should require MIIs to frame an internal policy framework for sharing and monitoring of confidential and sensitive data.*

- 89) *The MII's policy should adequately cover all methods of data sharing (including, e-mails and social media) with appropriate delegation of powers for sharing data. An MII can determine the types of data that can (or cannot) be shared, including pursuant to directions of any regulatory authority or court.*
- 90) *The MIIs should develop escalation matrix (including any approvals) for sharing confidential and sensitive information for any legitimate purpose. Accordingly, the MIIs should record the details of the information shared with the specific person/authority and the reason for sharing in a manner provided by way of a structured digital database under SEBI (Prohibition of Insider Trading) Regulations, 2015 (PIT Regulations, 2015).*
- 91) *The MIIs should adopt policies to monitor the data being shared on a regular basis through technology and conduct periodic audits to ensure compliance with the data sharing policy.*
- 92) *The MIIs' policies should have an accountability regime, including individual accountability for breach of the data sharing policy. Data sharing should be done on a non-discriminatory basis. The MII should be responsible for continued monitoring of the data sharing policy.*

## **II. Deploying Technology such as RegTech and SupTech systems for Governance in MII**

The Companies Act, 2013 and the LODR Regulations, 2015 prescribe the broad principles and parameters for evaluation of the Board of the MIIs, the directors and the committee members. SEBI has also issued a guidance note on Board evaluation which has recommended the effective use of IT by the MIIs in the Board evaluation software and related applications.

Accordingly, the Committee discussed the use of regulatory technology ("RegTech") (defined under an FSI Insight published by the Financial Stability Institute of the Bank for International Settlements, July 2018, as the application of innovative technologies that support compliance with regulatory and reporting requirements by regulated financial institutions) and supervisory technology ("SupTech") (defined as the use of innovative technology by supervisory agencies to support supervision) for real-time

governance of the MIIs and for automating the evaluation process for the KMPs, MD/CEO, the Board of the MII and committee members.

The Committee further discussed the application of technology to develop early-warning systems that proactively identify lapses and detect fraud on a real-time basis. In view of this, the Committee referred to the technological solutions adopted by the other regulators, such as RBI and noted that RBI had introduced a web-based end-to-end workflow automation system called the Platform for Regulated Entities for Integrated Supervision and Monitoring (“PRISM”) to strengthen compliance by the supervised entities. RBI vide press release dated October 06, 2022 also informed launch of a new SupTech initiative named “दक्ष (DAKSH) - Reserve Bank’s Advanced Supervisory Monitoring System”, which is expected to make the Supervisory processes more robust.

**Recommendations:**

*93) Use of technology (such as RegTech and SupTech) should be further enhanced by the MIIs to implement a transparent governance framework.*

*94) The Technology Advisory Committee (“TAC”) of SEBI and the members of the SCOT committee of MIIs should meet at least once on an annual basis to discuss measures for strengthening technology governance in the MIIs. SEBI can determine the manner in which such meetings are held.*

## Chapter 11: Other Governance issues

This chapter sets out the recommendations with respect to strengthening other governance related aspects of the MIIs such as the MII's whistle blower policy, organizational culture and values in MIIs, penalty mechanism applicable to MIIs and persons related to MIIs and governance of subsidiaries of MIIs.

### **I. Whistle Blower Policy**

Under Regulation 33 of the SECC Regulations, 2018 and Regulation 31 of D&P Regulations, 2018, the disclosure requirements and corporate governance norms applicable to listed companies have also been made applicable to MIIs. In addition, LODR Regulations, 2015 and PIT Regulations, 2015 require listed companies to frame an effective whistle blower policy which allows any person to report any illegal or unethical practice and enables the concerned authorities to take timely corrective action. The regulatory norms further require listed companies to adequately safeguard whistle blowers against victimisation. Also, by a SEBI Circular dated March 3, 2021, MIIs are required to have a code of conduct and institutional mechanism to prevent fraud and market abuse, as per the requirements of PIT Regulations, 2015. Finally, the Committee noted that the statutory auditor also reviews whistle blower complaints as part of the audit process.

The Committee, however, noted that the whistle blower policies across MIIs differed in terms of the scope, protection afforded and consequences of *mala fide* or frivolous complaints. In addition, in certain cases, the policies did not clearly identify an authority for escalating the matter in case of victimisation or unfair treatment of the whistle blower.

The Committee felt that the whistle blower policies should be strong enough and provide protection so that any Board member or KMP are not deterred to highlight issues. On the contrary, if any Board Member or KMP are aware of any wrongdoing and fail to inform SEBI or Board of the MII, then such Board member(s) or KMP(s) should be held accountable for such lapses.

The Committee felt that the MIIs should review the current whistle blower requirements to encourage effective reporting of cases requiring timely corrective actions. The Committee further reviewed the role of the Board of the MII and discussed the need to periodically apprise the Board of the MII regarding the whistle blower complaints. The Committee also discussed the need for mechanisms to monitor misuse of the policy and at the same time, ensuring that genuine whistle blowers are not dissuaded from reporting irregularities.

**Recommendations:**

- 95) *The whistle blower policy of the MIIs should be in accordance with the requirements set out in the LODR Regulations, 2015 and PIT Regulations, 2015. In addition, the MIIs should put in place a system for ensuring effective implementation of the whistle blower policy, including identifying senior persons within the organisation that would review any victimisation or unfair treatment of a whistle blower. Also, appropriate checks and balances should be implemented by the MII to ensure that any disincentives for misreporting do not dissuade genuine whistle blowers from reporting irregularities.*
- 96) *The MII's policies should include a provision for the Board of the MII to be made aware of concerns highlighted by whistle blowers, on a prompt basis, along with the actions taken by the MII to address the concerns*
- 97) *If any KMP or Board member becomes/ is aware of any acts of wrongdoing and fails to report the same to the Board of the MII or to SEBI, respectively, then such person will be held accountable, subject to principles of natural justice.*

## II. Organisational Culture and Values in MIIs

As discussed in other chapters, the SECC Regulations, 2018 and the D&P Regulations, 2018, currently prescribe a Code of Conduct for the directors and a Code of Ethics for the directors and KMPs of the MIIs. The Board of the MII and the KMPs are entrusted with the responsibility to ensure that the MII conducts its operations in a manner that enshrines the spirit of the regulatory requirement and follows the good governance principles.

The Committee noted that the Board of the MII, its members and the individual KMPs play an important role in establishing the right culture and values in the MIIs. They are expected to be highly visible in championing the desired values and conduct. The Committee was of the view that the regulations should expressly require such persons to follow the highest standards of governance and ethical behaviour in their operations. In this context, the Committee also referred to the RBI discussion paper on Governance in Commercial Banks in India and discussed the values and norms required to establish a good governance culture within the MIIs.

Globally, financial institutions, including market infrastructures, have been focusing on strengthening culture, especially focused on conduct, compliance and risk management. Specifically for market infrastructures, the PFMI by IOSCO and CPMI and global regulations also highlight the role of the Board with respect to culture, including:

- a) The Board and senior management have a clear vision of the institution's target risk, compliance and conduct culture.
- b) The target culture is actively promoted from the top through behavior, actions and effective communication.
- c) The Board and senior management encourage and support openness. Also, mechanisms are in place to ensure that decision-making is not dominated by a single individual or a small group in a way that is detrimental to the firm.
- d) The prevailing risk management, compliance and conduct culture is regularly assessed and reviewed by Board and Senior Management; and any identified issues are proactively addressed.



### **Recommendations:**

98) *The role of the Board of the MII and its senior management team in upholding a strong culture in the MII should be clearly outlined. The Board and senior management should have a clear vision of the institution's target regulatory, compliance, risk and conduct culture. They should communicate the guiding principles for the culture, especially focused on regulatory, compliance, risk and conduct related aspects. The target culture should be actively promoted from the top through behavior, actions and effective communication. The Board should endeavour that the MII put in place key elements related to culture such as:*

- i) Adequate training programs to help employees better understand expectations of behavior (for example, trainings on dilemmas);*
- ii) Mechanisms to measure and track indicators related to culture at regular intervals;*
- iii) Accountability mechanisms; and*
- iv) Performance management mechanisms which take into account adherence to culture, conduct and behaviour related dimensions. MIIs should note global practices, including those identified above, in establishing principles.*

### **III. Penalty mechanism applicable to MIIs and persons related to MIIs**

The current regulatory norms for the MIIs prescribe a Code of Conduct for the directors and a Code of Ethics for the directors and the KMPs. In addition, Regulation 26(4) of the SECC Regulations, 2018 and Regulation 27(4) of D&P Regulations, 2018 set out the applicable actions for any non-compliance or breach of the regulations and the codes mentioned therein. For reference, the provisions of Regulation 26 of the SECC Regulations, 2018 are given below:

*“Code of Conduct for directors and key management personnel*

- 1. Every director of a recognised stock exchange and a recognised clearing corporation shall abide by the Code of Conduct specified under Part- A of Schedule- II of these regulations.*
- 2. Every director and key management personnel of a recognised stock exchange and a recognised clearing corporation shall abide by the Code of Ethics specified under Part- B of Schedule- II of these regulations.*

3. *Every director and key management personnel of a recognised stock exchange and a recognised clearing corporation shall be a fit and proper person as described in regulation 20.*
4. *The Board may, for any failure by the directors to abide by these regulations or the Code of Conduct or Code of Ethics or in case of any conflict of interest, either upon a reference from the recognised stock exchange or the recognised clearing corporation or suo moto, take appropriate action including removal or termination of the appointment of any director, after providing him a reasonable opportunity of being heard.”*

Regulation 49 of the SECC Regulations, 2018, also provides SEBI with powers to issue directions in certain instances.

Considering the various recent lapses at MIIs, the Committee felt that as per the existing provisions under the SCRA, the SEBI Act and the Depositories Act, the penalty amount for contravention of any governance norms may not be sufficient, especially in case of grave violations.

The Committee noted that there was a need to strengthen the penalty mechanisms to ensure that relevant persons associated with MIIs (such as, among others, KMPs and members of committees who are not on the Board of the MII) are clearly covered for a breach or contravention of the regulations.

The Committee also discussed the need to specifically empower SEBI with a wider range of penal actions, such as issuing warning or advisories, removal, suspension or termination of the services of the director and other persons associated with the MII, and barring the directors or other persons from attending the meetings of the Board of the MII or its statutory committees. In exceptional circumstances including situations where MIIs are repeatedly found in violation of the regulatory requirements, SEBI may explore harsher options such as debarring issuance of new products/ services and /or restricting the MIIs' existing activities, products and services, etc.

### **Recommendations:**

- 99) *Existing provisions under SECC Regulations, 2018 and D&P Regulations, 2018 should be expanded to cover MIIs, individuals in the MII, including its directors,*

*members of statutory committees of the MIIs, KMPs, employees and other persons associated with the MIIs, for any contravention, attempt to contravene or abetting the contravention of the regulations (including the Code of Conduct) or any circulars or directions issued by SEBI.*

*100) Such provisions should include a list of indicative actions that SEBI may take against MIIs and their relevant persons, such as issuance of advisory, warning, termination, suspension, barring directors or other persons from attending meetings of the Board of the MII and/or Statutory committees, invoking malus/ clawback clause. In exceptional cases ( including repeated breaches or violations), SEBI may explore the harsher options of debarring MIIs from introduction of new products/ services, restricting MIIs' existing activities, products and services etc.*

*101) Such provisions should also include a graded mechanism for the imposition of monetary penalty with due regard to certain factors such as repetitive nature of the default, etc.*

*102) The SCRA, the SEBI Act, and the Depositories Act may be reviewed by SEBI to increase the penalty amount that may be applicable for MII and relevant persons associated with MII.*

#### **IV. Governance norms for Subsidiaries of MIIs**

As noted in other chapters of the Report, there is a need to strike a balance between the regulatory functions and the business functions of the MIIs, including in particular, the utilization of profits and investments by the MIIs towards their subsidiaries, associates and joint ventures. The current regulations impose certain restrictions on the scope of commercial activities permitted to be carried out by the subsidiaries of the MIIs. The Committee noted the prior deliberations and recommendations of the Bimal Jalan Committee and the Gandhi Committee as background to the current governance framework for subsidiaries, associate companies and joint ventures (JVs) of MIIs, including the requirement of the prior approval from SEBI.

It was, however, noted that the scope of the activities carried out by such subsidiaries, associates and JVs of the MII after receipt of SEBI's approval often skipped

regulatory oversight and such subsidiary/associate companies/JV further expanded their business, organically as well as inorganically, including by forming or investing in further step-down entities. Therefore, a need was felt to define the broad guidelines on the governance and activities of subsidiaries (direct and indirect), associate companies and joint ventures of the MIIs. The Committee also deliberated the need to extend the application of the LODR Regulations, 2015 to such entities and took note of the differences in the current regulatory norms relating to listed companies and MIIs, such as prohibition on the appointment of PIDs on the Board of the subsidiaries of MIIs.

In this regard, the Committee agreed that while the MIIs may continue investing in related areas, after obtaining prior approval from SEBI, their investments in unrelated areas may not be justified. There could be some unintended consequences of investing into unrelated areas including indirect linkages with trading members, common directors etc.

The Committee discussed mandatory phasing out of the existing investee companies with activities not incidental to the role of MII. In this regard, the Committee opined that SEBI may examine such instances on a case to case basis.

The Committee further agreed that an Investment Committee (IC) at the MII should approve any potential investment opportunity before any proposal is taken to the Board of the MII. This IC shall evaluate the proposal with respect to its pros and cons and provide a report along with a recommendation to the Board of the MII.

The Committee also discussed other issues relating to the subsidiaries of MIIs, such as segregation of resources between the MII and its subsidiary, use of the name and logo of the MII by its subsidiary/associate companies/JVs in light of reputational impact on MIIs, application of “Chinese Wall” policy in relation to the activities undertaken by the subsidiaries/associate companies/JVs and mechanisms for tracking the flow of investments from the MII to its subsidiaries/associate companies/JV etc.

**Recommendations:**

- 103) *MIIs should have an Investment Committee that will evaluate each investment proposal (other than treasury investments). This Investment Committee shall file a report along with a recommendation to the Board of the MII with respect to the proposed investment.*
- 104) *Considering the public utility infrastructure service provider and first-level regulatory role of MIIs, the governance of subsidiaries/ associate/ joint ventures (including their step-down entities) (hereafter collectively referred as “investee companies”) of MIIs should also conform to high standards. Accordingly, at the very minimum, certain governance norms in LODR Regulations, 2015 as specified by SEBI should be extended to the subsidiaries of the MIIs.*
- 105) *MII shall not be permitted to carry out activities that are not incidental to its activities as an MII, whether involving deployment of funds or otherwise, unless the same is assigned to the MII by the Government or by any financial sector regulator, with prior approval of SEBI.*
- 106) *MIIs shall be allowed to invest in investee companies which are incidental to its activities with prior approval of SEBI. In case, the cumulative fresh investments during a financial year is more than 10% of the cumulative investments into the first level investee companies, the MII shall take prior approval of SEBI. Expansion in scope of activities, however, by any investee companies shall require prior approval of SEBI. Further, the investment by the MII shall be subject to compliance with its net worth requirement at all points of time.*
- 107) *MII’s investee companies may not be permitted to carry-out activities for which MII is directly / indirectly a first-level regulator including by any existing investee company.*
- 108) *The existing investee companies which are carrying out activities that are in conflict with the role of the MII, should be phased out on priority in a time bound manner as specified by SEBI. In case of other investee companies whose activities are not incidental to the role of MII, SEBI may examine the same on a case to case basis.*

- 109) No employee of the MII shall be permitted to be an employee of the subsidiaries of the MII simultaneously. In addition, no financial benefits, compensation or other incentives (other than fees and expenses related to Board and Committee meetings) should be given by subsidiaries of the MII to the directors, employees and members of statutory committees of the MII.*
- 110) The data sharing policy of the MII as recommended in Chapter 10 of the Report shall also be applicable to subsidiaries.*

## Annexures

### Annexure A

#### Indicative regulatory parameters for evaluating the functioning of the MII

| Criterion                                                                                                                                  | Indicative Parameters                                                                                             |                                                                                      |                                                                                                                                               |
|--------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                                                                            | Exchange                                                                                                          | Clearing Corporation                                                                 | Depository                                                                                                                                    |
| <b>1. Resilience in Functioning of core activity of MII viz. a public utility infrastructure service provider in the securities market</b> | Robustness of Trading mechanism & its technology towards smooth functioning of market & reliable price discovery. | Robustness of clearing and settlement systems, including timely settlement of trades | Robustness of Depository's system towards protecting investors' assets & appropriate segregation of securities (including pledged securities) |
|                                                                                                                                            | Suitable trading control mechanisms to deal with volatile markets                                                 | Robustness of the Online real time Risk Management Framework for managing all risks  | Robustness of Depositories system to prevent unauthorised creation or deletion of securities                                                  |
|                                                                                                                                            | Adequacy & effectiveness of surveillance and supervision of trading systems                                       | Proper management of large exposures and market disruption                           | Periodic reconciliation of securities & taking necessary action to ensure the same                                                            |
|                                                                                                                                            | Timely dissemination of real-time information about trades, quantities and quotes, along-with index values        | Appropriateness of Collateral Management                                             | Timely settlement of securities and inter-depository transfer system                                                                          |

|                                                                                      |                                                                                                                                                                                                |                                                                                                                                                                  |                                                                                                                                                                       |
|--------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                      | Trading systems resilient to cyber security related risks & technical glitches (especially that of similar nature), backed by effective system audit mechanisms                                | Clearing systems resilient to cyber security related risks & technical glitches (especially that of similar nature), backed by effective system audit mechanisms | Depositories' systems resilient to cyber security related risks & technical glitches (especially that of similar nature), backed by effective system audit mechanisms |
| <b>2. Fair access &amp; treatment to all stakeholders and information disclosure</b> | Fair, equal, unrestricted and transparent access of MII infrastructure to all persons, without any bias.                                                                                       |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Timeliness and adequacy of information required to be disclosed to stakeholders.                                                                                                               |                                                                                                                                                                  |                                                                                                                                                                       |
| <b>3. Governance Practices &amp; Integrity Issues</b>                                | Efficient management of conflict of interest & its disclosure by concerned personnel.                                                                                                          |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Adherence to code of conduct by MII.                                                                                                                                                           |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Timely implementation of the action items emanating from Board of MII and statutory committees meetings.                                                                                       |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Not mis-using position for any pecuniary benefit.                                                                                                                                              |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Keeping the Regulator informed of material development and/or issues concerning MII. Failure in this regard, may be considered deterrent.                                                      |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Keeping the Board of MII informed of critical issues concerning the MII, including whistle blower complaints and resolution thereof, etc. Failure in this regard, may be considered deterrent. |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Responsibilities for acts of omission or commission or sharing confidential & sensitive information to third party                                                                             |                                                                                                                                                                  |                                                                                                                                                                       |
| <b>4. Adequacy of resources allocated for performing regulatory role</b>             | Adequacy and skilled staff in regulatory department.                                                                                                                                           |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Financial resources committed for regulatory function's vis-a-vis the non-regulatory functions.                                                                                                |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Adequacy and effectiveness of technology resources deployed in regulatory functioning                                                                                                          |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Internal policies & procedures for carrying-out various functions of MII                                                                                                                       |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Timely & adequate implementation of SEBI Circulars/Directives.                                                                                                                                 |                                                                                                                                                                  |                                                                                                                                                                       |



|                                                                  |                                                                                                                                                                                               |
|------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>5. Compliance with Regulatory norms</b>                       | Timely & adequate compliance/implementation of SEBI's inspection observations.                                                                                                                |
|                                                                  | Critical / High risk audit observations (including internal/ statutory/ system / cyber-security audit observations) & timely corrective action taken thereof, especially to avoid repetition. |
|                                                                  | Enforcement actions/ warning/ advisory letters issued by Regulators for non-compliances.                                                                                                      |
| <b>6. Efficient discharge of regulatory role vested upon MII</b> | Suo-moto identification of cases on non-compliance by issuer with LODR, ICDR, PIT and other regulatory norms.                                                                                 |
|                                                                  | Suo-moto identification of cases on non-compliance by its members with applicable Intermediary regulation, PFUTP Regulation and other norms.                                                  |
|                                                                  | Suo-moto identification of cases on violation by investors with PIT, PFUTP and other regulatory norms.                                                                                        |
|                                                                  | Disciplinary action taken that are deterrent.                                                                                                                                                 |
|                                                                  | Suo-moto policy initiatives/ circulars/ taking up the matter with regulator to address any concerns.                                                                                          |
|                                                                  | Instances of Non-compliances by market participants identified by SEBI, but not by concerned MII.                                                                                             |
| <b>7. Investor Protection related measures</b>                   | Adequacy of Investor Grievances Redressal Mechanism.                                                                                                                                          |
|                                                                  | Adequacy of Arbitration Mechanism.                                                                                                                                                            |
|                                                                  | Effectiveness of Investor Education.                                                                                                                                                          |
| <b>8. Cost Effectiveness</b>                                     | Cost effectiveness in its functioning.                                                                                                                                                        |
|                                                                  | Benefits to investors by improving cost effectiveness.                                                                                                                                        |

## Annexure B

### Indicative parameters for evaluating the functioning of the Board of MII

| Criterion                                                                            | Indicative Parameters                                                                                                                                                                               |
|--------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>1. Efficacy of decisions taken by Board: In respect of regulatory role of MII</b> | Resilience in Functioning of core activity of MII viz. a public utility infrastructure service providers in the securities market.                                                                  |
|                                                                                      | Fair access & treatment to all stakeholders and information disclosure.                                                                                                                             |
|                                                                                      | Adequacy of resources allocated for performing regulatory role.                                                                                                                                     |
|                                                                                      | Compliance with Regulatory norms.                                                                                                                                                                   |
|                                                                                      | Efficient discharge of regulatory role vested upon MII.                                                                                                                                             |
|                                                                                      | Investor protection related measures.                                                                                                                                                               |
|                                                                                      | Cost effectiveness in its functioning.                                                                                                                                                              |
|                                                                                      | Appropriateness of the decisions taken on information provided by the management concerning the MII, including whistle blower complaints, etc. Failure in this regard, may be considered deterrent. |
| <b>2. Structure of the Board</b>                                                     | Competency of Directors                                                                                                                                                                             |
|                                                                                      | Experience of Directors                                                                                                                                                                             |
|                                                                                      | Mix of Qualifications                                                                                                                                                                               |
|                                                                                      | Diversity in Board under various parameters                                                                                                                                                         |
|                                                                                      | Appointment to the Board                                                                                                                                                                            |
| <b>3. Meetings of the Board</b>                                                      | Regularity of meetings                                                                                                                                                                              |
|                                                                                      | Frequency                                                                                                                                                                                           |
|                                                                                      | Agenda                                                                                                                                                                                              |
|                                                                                      | Discussions and dissent.                                                                                                                                                                            |
|                                                                                      | Recording of minutes.                                                                                                                                                                               |
| <b>4. Functions of the Board</b>                                                     | Role and responsibilities of the Board                                                                                                                                                              |
|                                                                                      | Strategy and performance evaluation                                                                                                                                                                 |
|                                                                                      | Governance and compliance                                                                                                                                                                           |
|                                                                                      | Evaluation of Risks                                                                                                                                                                                 |
|                                                                                      | Grievance redressal for Investors                                                                                                                                                                   |

|                                          |                                                                                                                                                                                            |
|------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                          | Conflict of interest                                                                                                                                                                       |
|                                          | Stakeholder value and responsibility                                                                                                                                                       |
|                                          | Corporate culture and values                                                                                                                                                               |
|                                          | Review of Board evaluation                                                                                                                                                                 |
|                                          | Facilitation of independent directors                                                                                                                                                      |
| <b>5. Board and management</b>           | Evaluation of performance of the management and feedback                                                                                                                                   |
|                                          | Independence of the management from the Board                                                                                                                                              |
|                                          | Access of the management to the Board and Board access to the management                                                                                                                   |
|                                          | Secretarial support                                                                                                                                                                        |
|                                          | Succession plan                                                                                                                                                                            |
|                                          | Adequacy and efficiency on decision making processes                                                                                                                                       |
| <b>6. Professional development</b>       | Whether adequate induction and professional development programmes are made available to new and old directors                                                                             |
|                                          | Whether continuing directors training is provided to ensure that the Board members are kept up to date                                                                                     |
| <b>7. Integrity and Governance Issue</b> | Efficient management of conflict of interest and its disclosure by concerned personnel                                                                                                     |
|                                          | Adherence to code of conduct by Board of MII                                                                                                                                               |
|                                          | Keeping the Regulator informed of material developments and/or issues concerning MII. Failure in this regard, may be considered deterrent.                                                 |
|                                          | Taking timely action on critical issues concerning the MII as informed to the Board of MII, including whistle blower complaints, etc. Failure in this regard, may be considered deterrent. |
|                                          | Responsibilities for acts of omission or commission or sharing confidential and sensitive information to third party                                                                       |

## Annexure C

### Indicative regulatory parameters for evaluating the functioning of the PID and other Board members (Except MD & CEO)

| Criterion                                                                                   | Indicative Parameters                                                                                                                                                                                               |
|---------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>1. Efficacy of decisions taken by Board members in respect of regulatory role of MII</b> | Resilience in Functioning of core activity of MII viz. a public utility infrastructure service providers in the securities market                                                                                   |
|                                                                                             | Fair access & treatment to all stakeholders and information disclosure                                                                                                                                              |
|                                                                                             | Adequacy of resources allocated for performing regulator role                                                                                                                                                       |
|                                                                                             | Compliance with Regulatory norms                                                                                                                                                                                    |
|                                                                                             | Efficient discharge of regulatory role vested upon MII                                                                                                                                                              |
|                                                                                             | Investor protection related measures                                                                                                                                                                                |
|                                                                                             | Cost effectiveness in its functioning                                                                                                                                                                               |
|                                                                                             | Appropriateness of the decisions taken on information provided by the management concerning the MII, including whistle blower complaints, etc. Failure in this regard, may be considered deterrent.                 |
| <b>2. Qualifications and Experience</b>                                                     | Sufficient mix of the following areas of expertise/skill-sets (i) technology; (ii) finance and accounts; (iii) legal and regulatory; (iv) risk management; (v) capital markets; and (vi) management/administration. |
|                                                                                             | Each PID must possess at least one expertise/skill-sets in the following four areas: (i) technology, (ii) legal and regulatory; (iii) finance and accounts; and (iv) capital markets.                               |
| <b>3. Knowledge and Competency</b>                                                          | Whether the PID/ NID has sufficient understanding and knowledge of the entity in which it operates and the applicable regulatory norms.                                                                             |
|                                                                                             | Whether the PID/ NID has sufficient understanding of the role, responsibilities and obligations of PID/ NID under the relevant regulatory norms.                                                                    |
|                                                                                             | How the PID/ NID fares across different competencies as identified for effective functioning of Board of the concerned MII (The MII may list various competencies and mark all PIDs                                 |

|                                        |                                                                                                                                                                                                                                                                                                       |
|----------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                        | /NIDs against every such competency e.g. Constructive and analytical decision making abilities).                                                                                                                                                                                                      |
|                                        | Whether the PID/ NID has sufficient understanding of the risk attached with the business structure.                                                                                                                                                                                                   |
| <b>5.Fulfilment of functions</b>       | Whether the PID/ NID understands and fulfils the functions as assigned to him/her by the Board and the regulatory norms.                                                                                                                                                                              |
|                                        | Whether the PID/ NID gives views and opinion on various regulatory matters when comments are invited by SEBI through various means.                                                                                                                                                                   |
| <b>6.Ability to function as a team</b> | Whether the PID/ NID is able to function as an effective team-member.                                                                                                                                                                                                                                 |
|                                        | Whether the PID/ NID listens attentively to the contributions of others and gives adequate weightage to the views and perception of other Board members.                                                                                                                                              |
|                                        | Whether the PID/ NID shares good interpersonal relationship with other directors.                                                                                                                                                                                                                     |
| <b>7. Initiative</b>                   | Whether the PID/ NID actively takes initiative with respect to various areas.                                                                                                                                                                                                                         |
|                                        | Whether the PID/ NID insists on receiving information necessary for decision making.                                                                                                                                                                                                                  |
|                                        | Whether the concerned PID/ NID keeps himself well informed about the functioning of MII and the external environment in which it operates.                                                                                                                                                            |
|                                        | Whether the PID/ NID remains updated in terms of developments taking place in regulatory areas.                                                                                                                                                                                                       |
|                                        | Whether the PID/ NID has identified any important issues concerning any matter which may involve conflict of interest for the concerned MII, or may have significant impact on their functioning, or may not be in the interest of securities market, and whether the PID/ NID reported same to SEBI. |
|                                        | Whether the PID/ NID appropriately deals with critical matters.                                                                                                                                                                                                                                       |
| <b>8. Availability and attendance:</b> | Whether the PID/ NID is available for meetings of the Board and attends the meeting of Board of MII and Committees regularly and timely, without delay.                                                                                                                                               |

|                         |                                                                                                                                                                                                                                                              |
|-------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>9. Commitment</b>    | Whether the PID/ NID is adequately committed to the Board and the MII.                                                                                                                                                                                       |
| <b>10. Contribution</b> | Whether the PID/ NID has contributed effectively to the entity and in the Board meetings.                                                                                                                                                                    |
|                         | Whether the PID/ NID participates in the proceedings of Board meetings keeping in mind the interests of various stakeholders.                                                                                                                                |
|                         | Whether the PID/ NID actively deliberates and contributes on proposed business propositions and strategic decisions taking into consideration pros and cons of such propositions, long term outlook, business goals, cost-benefit analysis, etc.             |
| <b>11. Integrity</b>    | Whether the PID/ NID demonstrates highest level of integrity (including conflict of interest disclosures, maintenance of confidentiality, etc.).                                                                                                             |
|                         | Whether PID/ NID strictly adhere to the provisions of SECC Regulations, 2018, D&P Regulations, 2018 and any other regulatory provision, as applicable, along-with the code of conduct and code of ethics prescribed under other applicable regulatory norms. |
|                         | Whether disclosures such as dealing in securities and other regulatory disclosures are provided by PID/ NID on timely basis.                                                                                                                                 |
|                         | Confirmation on PID/ NID being a Fit & Proper person.                                                                                                                                                                                                        |
|                         | Confirmation that PID/ NID doesn't disclose confidential information, including technologies, unpublished price sensitive information, unless such disclosure is expressly approved by the Board of directors or required under the applicable laws.         |
|                         | Responsibilities for acts of omission or commission                                                                                                                                                                                                          |
|                         |                                                                                                                                                                                                                                                              |
| <b>12. Independence</b> | Whether PID is independent from the entity and the other directors and there is no conflict of interest.                                                                                                                                                     |
|                         | Confirmation of PID to be not associated with relevant MII and its member.                                                                                                                                                                                   |
|                         | Whether the PID /NID keeps regulators informed of material developments in the concerned MIIs functioning, from time to time.                                                                                                                                |

|                                            |                                                                                                                                                                                |
|--------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>13. Independent views and judgment:</b> | Whether the PID/ NID exercises his/ her own judgment and voices opinion freely.                                                                                                |
|                                            | Whether PID's/ NID's participation in decisions taken during meetings are unbiased, based on ethical judgment and are in strict conformity to the applicable regulatory norms. |
|                                            | Whether PID/ NID raises his concern if anything is observed contrary to regulatory norms and the expected norms of ethical conduct.                                            |
|                                            | Whether PID/ NID is committed to ensure that there is fairness and integrity in MIs system, in letter as well as spirit.                                                       |

## Annexure D

### Indicative parameters for evaluating the application of PIDs & their skills

| Criterion                                                                                            | Weightage | Indicative Parameters                                                                                                                                                                                                                                 |
|------------------------------------------------------------------------------------------------------|-----------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>Value Assessment</b><br>(Core personal attributes)                                                | 20%       | Proven and demonstrated,<br>-High standards of ethical behaviour<br>-Independence and soundness of judgement<br>-Integrity and commitment<br>-Strong interpersonal and communication skills<br>-Availability                                          |
| <b>General Competencies</b><br>(General skillsets for MII Board level appointment)                   | 20%       | Qualification, experience and knowledge in the relevant skill set                                                                                                                                                                                     |
|                                                                                                      |           | Leadership responsibilities,                                                                                                                                                                                                                          |
|                                                                                                      |           | Corporate Governance,                                                                                                                                                                                                                                 |
|                                                                                                      |           | Stakeholder relationship<br>Strategy and Planning                                                                                                                                                                                                     |
| <b>Domain Expertise in Technology/ Legal/ Accounting/ Capital markets</b> (Specialised competencies) | 20%       | Background and experience:<br>-Technology (Fintech/ Block chain/Cyber Security/ Artificial Intelligence/ Machine Learning etc.)<br>-Legal and Regulatory<br>-Finance and Accounts<br>-Capital Market understanding (including Market risk management) |
| <b>Role Synergy</b> (Prior PID responsibilities)                                                     | 20%       | Credible Contribution as<br>-PID/ID on the Board of other Organization/ Executive Director/ Nominee Director.<br>-Member in committees of other Organization.                                                                                         |
| <b>MI Board alignment</b><br>(Reduce Skill gap in the MII Board)                                     | 20%       | Based on requirement as per regulatory norms and desired skillset matrix of Board of directors prepared by the MII.                                                                                                                                   |



|  |  |                                                                                                                     |
|--|--|---------------------------------------------------------------------------------------------------------------------|
|  |  | Based on new skill requirement assessment vis-à-vis skills and experiences of existing Board of directors of an MII |
|--|--|---------------------------------------------------------------------------------------------------------------------|

## **Annexure E**

### **Indicative parameters for evaluating the functioning of the MII's Statutory Committees**

| <b>Criterion</b>                                       | <b>Indicative Parameters</b>                                                                                                      |
|--------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------|
| <b>1. Mandate and composition</b>                      | Whether the mandate, composition and working procedures of committees of the board of directors is clearly defined and disclosed. |
| <b>2. Effectiveness of the Committee</b>               | Whether the Committee has fulfilled its functions as assigned by the Board and laws as may be applicable                          |
| <b>3. Structure of the Committee and meetings</b>      | Whether the Committees have been structured properly and regular meetings are being held with adequate attendance of its members  |
| <b>4. Independence of the Committee from the Board</b> | Whether adequate independence of the Committee is ensured from the Board                                                          |
| <b>5. Contribution to decisions of the Board</b>       | Whether the Committee's recommendations contribute effectively to decisions of the Board                                          |
|                                                        | Adequacy and efficiency on decision making,                                                                                       |
| <b>6. Structure of the Committee</b>                   | Competency of committee members                                                                                                   |
|                                                        | Experience of committee members                                                                                                   |
|                                                        | Sufficient skill-sets among Committee members to effectively carry-out function of the committee                                  |
| <b>7. Availability and attendance:</b>                 | Availability of the member for meetings of the committee and its attendance.                                                      |

## Annexure F

### Indicative regulatory parameters for evaluating the functioning of the MII's MD and KMPs based on their role

| Criterion                                                                                                                                  | Indicative Parameters                                                                                            |                                                                                      |                                                                                                                                               |
|--------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                                                                            | Exchange                                                                                                         | Clearing Corporation                                                                 | Depository                                                                                                                                    |
| <b>1. Resilience in Functioning of core activity of MII viz. a public utility infrastructure service provider in the securities market</b> | Robustness of Trading mechanism & its technology towards smooth functioning of market & reliable price discovery | Robustness of clearing and settlement systems, including timely settlement of trades | Robustness of Depository's system towards protecting investors' assets & appropriate segregation of securities (including pledged securities) |
|                                                                                                                                            | Suitable trading control mechanisms to deal with volatile markets                                                | Robustness of the Online real time Risk Management framework for managing all risk   | Robustness of Depositories system to prevent of unauthorised creation or deletion of securities                                               |
|                                                                                                                                            | Adequacy & effectiveness of surveillance and supervision of trading systems                                      | Proper management of large exposures and market disruption                           | Periodic share reconciliation of securities & taking necessary action to ensure the same                                                      |
|                                                                                                                                            | Timely dissemination of real-time information about trades, quantities and quotes, along-with index values       | Appropriateness of Collateral Management                                             | Timely settlement of securities and inter-depository transfer system                                                                          |

|                                                                                      |                                                                                                                                                                                                |                                                                                                                                                                  |                                                                                                                                                                       |
|--------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                                                                      | Trading systems resilient to cyber security related risks & technical glitches (especially that of similar nature), backed by effective system audit mechanisms                                | Clearing systems resilient to cyber security related risks & technical glitches (especially that of similar nature), backed by effective system audit mechanisms | Depositories' systems resilient to cyber security related risks & technical glitches (especially that of similar nature), backed by effective system audit mechanisms |
| <b>2. Fair access &amp; treatment to all stakeholders and information disclosure</b> | Fair, equal, unrestricted and transparent access of MII infrastructure to all persons, without any bias                                                                                        |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Timeliness and adequacy of information required to be disclosed to stakeholders                                                                                                                |                                                                                                                                                                  |                                                                                                                                                                       |
| <b>3. Governance practices &amp; Integrity Issues</b>                                | Efficient management of conflict of interest & its disclosure by concerned personnel                                                                                                           |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Adherence to code of ethics & code of conduct by MD&CEO (each sub-point)                                                                                                                       |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Timely implementation of the action items emanating from Board of MII and statutory committee meetings                                                                                         |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Not mis-using position for any pecuniary benefit.                                                                                                                                              |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Keeping the Regulator informed of material development and/or issues concerning MII. Failure in this regard, may be considered deterrent.                                                      |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Keeping the Board of MII informed of critical issues concerning the MII, including whistle blower complaints and resolution thereof, etc. Failure in this regard, may be considered deterrent. |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Responsibilities for acts of omission or commission or sharing confidential & sensitive information to third party                                                                             |                                                                                                                                                                  |                                                                                                                                                                       |
| <b>4. Adequacy of resources allocated for performing regulator role</b>              | Adequacy and quality of staff in regulatory dept.                                                                                                                                              |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Financial resources committed for regulatory function's vis a vis the non-regulatory functions                                                                                                 |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Adequacy and effectiveness of technology resources deployed in regulatory functioning                                                                                                          |                                                                                                                                                                  |                                                                                                                                                                       |
|                                                                                      | Internal policies & procedures for carrying-out various functions of MII                                                                                                                       |                                                                                                                                                                  |                                                                                                                                                                       |

|                                                                  |                                                                                                                                                                                              |
|------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <b>5. Compliance with Regulatory norms</b>                       | Timely & proper implementation of SEBI Circulars/Directives                                                                                                                                  |
|                                                                  | Timely & Adequate Compliance/Implementation of SEBI's inspection observations                                                                                                                |
|                                                                  | Critical / High risk audit observations (including internal/ statutory/ system / cyber-security audit observations) & timely corrective action taken thereof, especially to avoid repetition |
|                                                                  | Enforcement actions/ warning/ advisory letters issued by Regulators for non-compliances                                                                                                      |
| <b>6. Efficient discharge of regulatory role vested upon MII</b> | Suo-moto identification of cases on non-compliance by Issuer with LODR, ICDR, PIT and other regulatory norms                                                                                 |
|                                                                  | Suo-moto identification of cases on non-compliance by its members with applicable Intermediary regulation, PFUTP regulation and other norms.                                                 |
|                                                                  | Suo-moto identification of cases on violation by investors with PIT, PFUTP and other regulatory norms                                                                                        |
|                                                                  | Disciplinary action taken that are deterrent                                                                                                                                                 |
|                                                                  | Suo-moto policy initiatives/circulars/ taking up the matter with regulator to address the concern                                                                                            |
|                                                                  | Instances of Non-compliances by market participants identified by SEBI, but not by concerned MII                                                                                             |
| <b>7. Investor protection related measures</b>                   | Adequacy of investor grievances redressal mechanism                                                                                                                                          |
|                                                                  | Adequacy of arbitration mechanism                                                                                                                                                            |
|                                                                  | Effectiveness of Investor education                                                                                                                                                          |
| <b>8. Cost effectiveness in its functioning</b>                  | Cost effectiveness in its functioning                                                                                                                                                        |

## **Annexure G**

### **Code of Conduct for Directors, Committee Members and KMPs**

The 'Code of Conduct' for directors, committee members and KMPs of the MII is aimed at improving the professional, conduct and ethical standards in the functioning of the MII, thereby creating better investor confidence in the integrity of the securities market.

While the objective of this Code is to enhance the level of market integrity and investor confidence, it is emphasized that a written code of conduct may not completely guarantee adherence to high ethical standards. This can be accomplished only if directors, committee members and KMPs of the MII commit themselves to the task of enhancing the fairness and integrity of the system in letter and spirit.

#### **I. Objectives and Underlying Principles.**

The Code of Conduct for directors, committee members and KMP of the MII seeks to establish a minimum level of business/ professional ethics to be followed by these directors and KMPs towards establishing a fair and transparent marketplace. The Code of Conduct is based on the following fundamental principles:

- (a) Fairness and transparency in dealing with matters relating to the MII and the investors.
- (b) Compliance with all laws/ rules/ regulations laid down by regulatory agencies/ MII.
- (c) Exercising due diligence in the performance of duties.
- (d) Avoidance of conflict of interest between self-interest of directors/ committee members/ KMPs and interests of MII and investors.

#### **II. Applicable to Board Members, Committee Members and KMPs of MII:**

##### **1. General Responsibility.**

Every director, committee members and KMP of the MII shall—

- (a) analyse and administer the MII's issues with professional competence, fairness, impartiality, efficiency and effectiveness;
- (b) submit the necessary disclosures/ statement of holdings/ dealings in securities as required by the MII from time to time as per their Rules/ Bye-laws or Articles of Association;

- (c) unless otherwise required by law, maintain confidentiality and shall not divulge/ disclose any information obtained in the discharge of their duty and no such information shall be used for personal gains;
- (d) maintain the highest standards of personal integrity, truthfulness, honesty and fortitude in discharge of their duties in order to inspire public confidence and shall not engage in acts discreditable to their responsibilities;
- (e) perform their duties in an independent and objective manner and avoid activities that may impair, or may appear to impair, their independence or objectivity or official duties;
- (f) perform their duties with a positive attitude and constructively support open communication, creativity, dedication, and compassion;
- (g) not engage in any act involving moral turpitude, dishonesty, fraud, deceit, or misrepresentation or any other act prejudicial to the administration of the MII.
- (h) promote greater awareness and understanding of ethical responsibilities.
- (i) in the conduct of their business, observe high standards of commercial honour and; just and equitable principles of trade.
- (j) in their conduct in business life be exemplary which may set a standard for others.
- (k) not use their position to give/get favours to/from the executive or administrative staff of the MII, technology or service providers and vendors or suppliers of the MII, or any listed company at the recognised stock exchange/ any issuer company admitted by the MII.
- (l) not commit any act which will put the reputation of the MII in jeopardy.
- (m) comply with the provisions of all applicable laws to the securities market.
- (n) deal in securities in conformation with the requirement laid down under Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015 in this regard (including the trading restrictions for securities about which the MII may have unpublished price sensitive information).

## **2. Regulatory Compliances.**

Every director, committee member and KMPs of the MII shall—

- (a) ensure that the MII abides by all the applicable provisions of the Securities and Exchange Board of India Act, 1992, Securities Contracts (Regulation) Act, 1956, the Depositories Act, 1996, rules and regulations framed thereunder and the circulars, directions or any other instructions issued by the Board from time to time;

- (b) ensure compliance at all levels so that the regulatory system does not suffer any breaches;
- (c) ensure that the MII takes steps commensurate to honour the time limit stipulated by Board for corrective action.

### **3. Disclosures of Beneficial Interest.**

All directors, committee members and KMPs shall disclose to the Board of MII, upon assuming office and during their tenure in office, whenever the following arises:—

- (a) any fiduciary relationship of self and family members and directorship/ partnership of self and family members in any trading member or clearing member or depository participant or registrar and transfer agent;
- (b) shareholding, in cases where the shareholding of the director/ KMP, directly or through his family exceeds 5 percent in any listed company or in other entities related to the securities markets;
- (c) any other business interests.

### **4. Access to Information.**

- (a) There shall be prescribed channels through which information shall move and further there shall be audit trail of the same. Any retrieval of confidential documents/ information shall be properly recorded.
- (b) All such information, especially which is non-public and price sensitive, shall be kept confidential and not be used for any personal consideration/ gain.
- (c) Any information relating to the business/ operations of the MII, which may come to the knowledge of directors/ committee members/ KMPs during performance of their duties shall be held in strict confidence, shall not be divulged to any third party and shall not be used in any manner except for the performance of their duties.
- (d) Directors shall call for information only as part of specific committees or as may be authorised by the Board of MII.

### **5. Misuse of Position.**

Directors/ committee members/ KMPs shall not use their position to obtain business or any pecuniary benefit in the organization for themselves or family members.

### **6. Implementation Oversight.**

- (a) For overseeing implementation of this Code



- (i) By committee members and KMP - ROC of every MII under the respective Board shall be responsible.
- (ii) By Board members - The Board of every MII shall be responsible.
- (b) The ROC and the Board of MII shall respectively lay down procedures for the implementation of the code and prescribe reporting formats for the disclosures required under the code.
- (c) The Compliance Officer shall execute the requirements laid down by the ROC and the Board of MII.

### **III. Applicable to the Board and Committee Members of MIIs:**

#### **1. Meetings and Minutes.**

The directors and committee members of the MII shall—

- (a) not participate in discussions on any subject matter in which any conflict of interest exists or arises, whether pecuniary or otherwise, and in such cases the same shall be disclosed and recorded in the minutes of the meeting;
- (b) not encourage the circulation of agenda papers during the meeting, unless circumstances so require;
- (c) offer their comments on the draft minutes and ensure that the same are incorporated in the final minutes;
- (d) insist on the minutes of the previous meeting being placed for approval in subsequent meeting;
- (e) endeavor to have the date of next meeting fixed at each Board meeting and committee meetings respectively in consultation with other respective members of the Board and committees;
- (f) ensure that all important agendas placed before the Board of MII and committees respectively are deliberated in a timely manner.
- (g) not support any decision in the meeting of the Board of MII and the committees respectively which may adversely affect the interest of investors and shall report forthwith any such decision to the Board.

#### **2. Role of the Chairperson and Directors of the Board and Committee Members in the day to day functioning of the MII.**

- (a) The Chairperson and directors shall not interfere in the day to day functioning of the MIIs and shall limit their role to decision making on policy issues and to issues as the Board of MII may decide.
- (b) The Chairperson and directors shall abstain from influencing the employees of the MIIs in conducting their day to day activities.
- (c) The Chairperson and directors shall not be directly involved in the function of appointment and promotion of employees unless specifically so decided by the Board of MII.

### **3. Avoidance of Conflict of Interest.**

- (a) No director of the Board or committee member of the MII shall participate in any decision making/adjudication in respect of any person/ matter in which he is in any way, directly or indirectly, concerned or interested.
- (b) Whether there is any conflict of interest or not in a matter, shall be decided by the Board of the MII.

### **4. Code of Conduct for the Public Interest Directors (PIDs).**

- (a) In addition to the conditions stated in Para (1) above, PIDs of the MIIs should attend all the Board meetings and they shall be liable to vacate office if they remain absent for three consecutive meetings of the Board or do not attend seventy-five percent of the total meetings of the Board in a calendar year.
- (b) PIDs shall meet separately, at least once in six months to exchange views on critical issues.
- (c) PIDs shall identify important issues which may involve conflict of interest for the MII, or may have significant impact on the functioning of the MII, or may not be in the interest of securities market. The same shall be reported to the Board in a time bound manner as may be decided by the MII.
- (d) PIDs should have regular oversight on regulatory requirements and observations of SEBI inspection particularly on issues of Governance standards, Technology and cyber security and System Audit & Cyber Security. Such issues should also be taken up for discussions with SEBI
- (e) PIDs should be proactive in identifying any issues concerning functioning of MIIs and report the same to SEBI. PIDs should ensure all regulatory communication/letter from SEBI are placed before board with comments/report of MD.

- (f) PIDs shall review the appointment of MD and participation in the respective statutory committees
- (g) PIDs may put in place an evaluation mechanism to assess the performance of CEO/MD on a continuing basis in line with evaluation guidelines for PIDs
- (h) PIDs to ensure that appointments of MD/CEO be held within specified timelines. Identification of KMPs be closely scrutinized as per the laid down procedure and exceptions should be brought to the notice of SEBI.
- (i) PIDs should take proactive part in deliberations of different committees and steer their functioning.
- (j) Adequacy of resource allocations (both financial & human) towards regulatory compliances to be ensured.

## **5. Strategic Planning.**

Every director and committee member of the MII shall—

- (a) participate in the formulation and execution of strategies in the best interest of the MII and contribute towards pro-active decision making at the Board level;
- (b) give benefit of their experience and expertise to the MII and provide assistance in strategic planning and execution of decisions.
- (c) place priority for redressing investor grievances and encouraging fair trade practice so that the MII becomes an engine for the growth of the securities market;

## **6. Disclosure of dealings in securities by Directors of the MIIs.**

- (a) All transactions/ dealings in securities by the directors and their immediate relatives (as defined in PIT Regulations) shall be disclosed to the Board of the MII. (IEPs – should not misuse the information in any manner.)
- (b) All directors shall also disclose the trading conducted by firms/ corporate entities in which they hold twenty percent or more beneficial interest or hold a controlling interest, to the MII.
- (c) The details including time period for disclosure under clause 6(a) and 6(b) above shall be prescribed by the MII, provided that the time period for disclosure shall not be later than fifteen days of the transaction/ dealing.
- (d) Directors who are Govt. of India nominees or nominees of Govt. of India statutory bodies or Public Financial Institutions and are governed by their own codes shall be exempt from this requirement.

## **7. Applicable to IEPs**

- (a) IEPs shall not use or act on any sensitive information received in capacity as a member of the statutory committee for obtaining any undue benefit.

**8. Compliance with internal policies of the MII.**

- (a) Directors of the MII shall at all point of time comply with all the internal policies of the MII as applicable to them.

**IV. Applicable to KMPs:**

**1. Disclosure of dealings in securities by KMPs of the MIIs.**

- (a) KMPs of the MIIs shall disclose on a periodic basis as determined by the MII (which could be monthly), all their dealings in securities, directly or indirectly, to the Board of MII/ ROC/ Compliance Officer.
- (b) All transactions must be of an investment nature and not speculative in nature. Towards this end, all securities purchased must be held for a minimum period of sixty days before they are sold. In specific/ exceptional circumstances, however, sale can be effected anytime by obtaining pre-clearance from the Compliance Officer to waive this condition after recording in writing his satisfaction in this regard.

**2. Compliance with internal policies of the MII.**

- (a) KMPs shall at all point of time comply with all the internal policies of the MII.

## **Annexure H**

### **Code of Conduct for Stock Exchanges and Clearing Corporations**

A Stock Exchange and a Clearing Corporation shall

- (a) always abide by the provisions of the Act, SEBI Act, 1992, Rules, Regulations, circulars, guidelines and any other directions issued by the Board. All acts, rules, regulations, guidelines and any other directions issued by SEBI from time to time.
- (b) adopt appropriate due diligence measures. (to be included in the code of conduct for depositories)
- (c) take effective measures to ensure implementation of proper risk management framework and good governance practices. (to be included in the code of conduct for depositories)
- (d) take appropriate measures towards investor protection and education of investors.
- (e) treat all its applicants/members in a fair and transparent manner.
- (f) promptly inform the Board of violations of the provisions of the Act, SEBI Act, the rules, the regulations, circulars, guidelines or any other directions by any of its members, issuer or issuer's agent.
- (g) take a proactive and responsible attitude towards safeguarding the interests of investors, integrity of stock exchange's or clearing corporation's systems and the securities market.
- (h) endeavour for introduction of best business practices amongst itself and its members.
- (i) act in utmost good faith and shall avoid conflict of interest in the conduct of its functions.
- (j) not indulge in unfair competition, which is likely to harm the interests of any other Stock Exchange or Clearing Corporation, their members or investors or is likely to place them in a disadvantageous position while competing for or executing any assignment.
- (k) be responsible for the acts or omissions of its employees in respect of the conduct of its business.
- (l) monitor the compliance of the rules and regulations by the members and shall further ensure that their conduct is in a manner that will safeguard the interest of investors and the securities market.

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