Annexure C

Guidelines pertaining to Investment in Derivatives

1. The portfolio manager offering discretionary or non-discretionary or advisory services to the clients may be permitted to invest or advise for investment in equity exchange traded derivatives and exchange traded commodity derivatives (ETCDs). Provided that investment in ETCDs shall be permitted for the purpose of hedging and portfolio rebalancing only.

The detailed guidelines in this regard are proposed as under:

2. The portfolio manager shall be permitted to undertake a **total exposure** not exceeding 1.25 times of the Assets Under Management (AUM) of the client's funds. The additional exposure of 25% is permitted through exchange traded derivatives only.

Illustration: If a client's AUM is INR 1 crore, its total exposure (comprising Long and short positions) after accounting for permitted offsetting positions shall not exceed INR 1.25 crore.

3. Within the total exposure limit specified in clause 2 above, the Portfolio Manager may undertake **unhedged short exposure**, only through equity exchange traded derivatives, up to 50% of the client's AUM, in addition to the derivative exposure undertaken for hedging and portfolio rebalancing.

4. The exposure to derivative contracts shall be calculated as below:
- Futures (long and short) = Futures Price * Lot Size * Number of Contracts
- Options bought = Option premium paid* Lot size * Number of contracts
- Option sold = Market price of the underlying * Lot size * Number of contracts
- In case of any other derivative exposure, the exposure is proposed to be calculated as the notional market value of the contract.

5. The total exposure related to option premium paid and received shall not exceed 10% of client's AUM.

6. Offsetting of exposure (i.e., only one side exposure is calculated) at the portfolio level of the client shall be allowed for:
- Cash and derivative positions on the same underlying security
- Between derivative positions on the same underlying security.

7. The detailed illustration on offsetting of derivative positions is enclosed at **Annexure C1.**

8. Portfolio Managers may participate in derivatives only after entering into an agreement with the clients. To facilitate informed decision-making, portfolio managers shall clearly disclose the high risks inherent in derivative investments. Further, the portfolio manager must obtain the client's explicit positive consent for investing in derivatives at the time of on boarding of client in the form as may be specified.

9. Portfolio Managers may execute addendums to the existing client agreements to permit participation in derivatives on their behalf. Such addendums shall be executed only after obtaining positive explicit consent from the existing clients in the specified format.

10. A standard format of such declaration shall be specified by APMI, in consultation with SEBI.

Annexure C1

Offsetting of transactions:

Below are some of the illustrative scenarios for offsetting of positions on the same underlying security.

Sr. No.	**Position 1**	**Position 2**	**Offsetting allowed/not?**	**Net exposure to be considered**
1	Equity Long	Futures Short	Yes	Equity Long only
2	Equity /Futures Long	Call option Short	Yes	Equity /Futures Long only
3	Equity /Futures Long	Put option Long	Yes	Equity /Futures Long only
4	Futures Short	Call option Long	Yes	Futures Short only
5	Futures Short	Put option Short	Yes	Futures Short only
6	Call option Long	Call option Short	Yes	Call option Short only
7	Put option Long	Put option Short	Yes	Put option short only
8	Equity Long	Futures Long	No	Equity Long + Futures Long
9	Equity /Futures Long	Call option Long	No	Equity /Futures Long + Call option Long
10	Equity /Futures Long	Put option Short	No	Equity /Futures Long + Put option Short
11	Futures Short	Call option Short	No	Futures short + Call option short
12	Futures Short	Put option Long	No	Futures short + Put option Long
13	Call option Long	Put option Short	No	Call option Long + Put option Short
14	Call option Short	Put option Long	No	Call option Short + Put option Long

**For offsetting of positions, the futures and options contracts shall be on the same underlying security and having same expiry date.*