भारतीय प्रतिभूति और विनिमय बोर्ड
Securities and Exchange Board of India

Consultation Paper on

"Introduction of optional T+0 and optional Instant Settlement of Trades in addition to T+1 Settlement Cycle in Indian Securities Markets"

I. Objective:

To solicit comments and inputs from stakeholders and members of public at large on introduction of the facility for clearing and settlement of funds and securities on T+0 and instant settlement cycle on optional basis in addition to the existing T+1 settlement cycle in secondary markets for equity cash segment.

II. Background:

i. Over the last few years, Indian securities markets has seen tremendous growth, both in terms of volumes, value, as well as number of participants. This increase in participation of new investors in securities market puts greater onus on SEBI to make markets more efficient and safer for its participants, with a special focus on retail participants.

ii. SEBI, in its endeavour to keep pace with the changing times and carry out its mandate of development of securities markets and investor protection, shortened the settlement cycle to T+3 from T+5 in 2002 and subsequently to T+2 in 2003. Further in 2021, T+1 settlement was introduced in a phased manner which was fully implemented from January 2023.

iii. The significant evolution of payment systems in the country in recent years coupled with sophisticated and robust technologies used by Markets Infrastructure Institutions (MIIs) appears to present further opportunities for advancing the clearing and settlement timelines, on an optional basis.

iv. Further, it is noteworthy to mention that Indian Banking System is efficient to provide real time transfer of funds and the depository system also has visibility of client level holdings and hence the ability to enable instant debit and credit of securities. The average Indian has rapidly embraced UPI and instant payment platforms. This flexibility can be extended to equity dealing as well.

v. In today's age, reliability, low cost and high speed of transactions are key features that attract investors to particular asset classes. To that extent, reducing settlement time and hence increasing operational efficiency of dealing in Indian securities can further draw and retain investors into this asset class.

vi. In this regard, it is envisaged that for equity cash segment, in addition to the existing T+1 settlement cycle, a shorter settlement cycle may be introduced as an option.

III. <u>Features of T+0 and Instant Settlement Mechanism</u>

It is observed that high percentage of retail investors bring upfront funds and securities before placing the order. For the period June 2023, for around 94% of delivery based trades with value up to INR 1, 00,000 per transaction, investors made early pay–in of funds and securities. An instant settlement mechanism:

i. Enables instant receipt of funds and securities, vis-a-vis existing pay-out on T+1 day.

ii. Eliminate the risk of settlement shortages, since both funds and securities will be required to be available before placing the order. This also eliminates the risk for market participants and reduces the risk exposure of Clearing Corporations (CCs).

iii. Strengthens investor protection by enhancing the control of the investor over the securities and funds as funds and securities would be credited into the clients' account directly for those who are trading through blocked amount using UPI facility ("UPI Clients").

Further, for other modes of payment, the funds would be credited directly into the clearing bank account of the member, which is as today and can then be credited to the client account and the securities can be credited to the Clearing Member (CM)/ Trading Member (TM) pool account.

iv. Providing the option for instant settlement will help establish Indian equities as an asset class with the features of resilience, low cost and time for transaction, superior in all ways to emerging claimants of alternative asset classes.

IV. Benefits of the proposed mechanism

(A) For Clients

i. The option is expected to provide flexibility in terms of faster pay-out of the funds against the securities to the sellers and faster pay-out of securities against the funds to the buyers.

ii. The option will allow better control over funds and securities by the investors.

(B) For the Securities Market Ecosystem

i. Shorter settlement cycle will further free up capital in the securities market thereby enhancing the overall market efficiency.

ii. The option will enhance the overall risk management of CCs as the trades are backed by upfront funds and securities.

V. Potential Concerns of the Proposed Mechanism

Two different segments for order placement viz. orders for T+0 or Instant settlement cycle and T+1 settlement cycle, may -

i. lead to liquidity fragmentation and affect efficient price discovery.

ii. increase the cost of trading, as funds and securities shall have to be made available upfront before placing the orders.

iii. result in divergence in the price of same security in T+0 or instant settlement cycle, and T+1 settlement cycle.

iv. increase impact cost in case of lack of liquidity in this segment.

VI. Mitigation of Potential Concerns

i. On liquidity fragmentation, there will be participants who can access both T+0 (or instant settlement) and T+1 markets and would bridge price and liquidities gaps between the two segments.

ii. It is envisaged that divergence, if any, that emerge between the T+0 / instant settlement cycle and T+1 settlement cycle may be bridged by the arbitrageurs thereby allowing for liquidity and effective price discovery in both segments.

Possible Arbitrage Opportunities

For instance, in forex markets the arbitrage between today (cash) and TOM, or Today (cash) and SPOT, or TOM and SPOT reflects interest rate parity across the two tenors. If the prices of TOM or SPOT deviates from this parity, an arbitrage opportunity may arise. Such opportunities are being captured by the arbitrageurs leading to efficient price discovery and liquidity transfer across tenors.

iii. On the issue of cost of funding, it is pertinent to note that in around 94% of delivery based trades, the investors do early pay-in for trade value of up to INR 1,00,000 per transaction. Thus, this client base already has funds and securities made available before placement of order.

iv. The issue of divergence of prices for same scrip between the two segments (T+0 or Instant settlement cycle, and T+1 settlement cycle), can also be addressed by introduction of price bands between segments (of say ± 100 basis points), which ensure limited divergence in the prices between the T+1 settlement cycle and T+0 or instant settlement cycle. Further, with increase in participation in this segment and active arbitrages, the divergence in prices may be reduced.

VII. Consultation with Stakeholders

i. SEBI held discussions with various stakeholders including Stock Exchanges (SEs), Depositories, Clearing Corporations (CCs), and stock brokers in the matter. A Working Group of SEs, Depositories and CCs was formed in order to examine the feasibility of introduction of shorter settlement cycle and its associated legal, operational, technological and market impact, etc. For this purpose, the Working Group proposes implementation of the same in two phases - Phase 1: T+0 Settlement Cycle and Phase 2: Instant Settlement Cycle.

ii. The brief of recommendations of working group are placed as **Annexure – A** below.

VIII. Public Comments:

i. SEBI solicits public comments on proposals at paragraphs 1 to 3 of Annexure–A.

ii. Apart from the proposals mentioned at Annexure-A, public comments are also solicited on the following:

a. Should SEBI move towards a shorter settlement cycle in the form of instant settlement?

b. Is the proposed mechanism a right step towards developing and increasing investor confidence in the securities markets?

c. Do you see any challenges and risks associated with the proposed mechanism apart from those highlighted in the consultation paper? If yes, please highlight the same along with possible mitigation measures

d. Should the proposed mechanism be made available only for top 500 listed equity shares?

e. Any other additional suggestions on the proposed mechanism.

Kindly mention the subject of the communication as ***"Consultation Paper on Introduction of optional T+0 and optional Instant Settlement of Trades in addition to T+1 settlement cycle in Indian Securities Markets"***

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<tr><td colspan="4">Name of the person/entity proposing comments</td></tr>
<tr><td colspan="4">Name of organizations (If applicable)</td></tr>
<tr><td colspan="4">Contact Details</td></tr>
<tr><td colspan="4">Category: whether market intermediary/ participant (mention type/ category) or public (investor, academician, etc.)</td></tr>
<tr><td colspan="4">Comments on the Proposals at Annexure-A</td></tr>
<tr><td>S. No.</td><td>Relevant paragraphs/ sub-paragraphs of proposals mentioned at Annexure A</td><td>Concern/issues</td><td>Rationale</td></tr>
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<tr><td colspan="4">Comments on other queries mentioned at paragraph VIII(ii) above</td></tr>
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Comments/suggestions may be sent by email to Shri Suman Kumar, Assistant General Manager (e-mail id: sumank@sebi.gov.in), Shri Dhanush Kumar Reddy, Manager (e-mail id: dhanushs@sebi.gov.in) and mrd_pod3@sebi.gov.in latest by **January 12, 2024.**

Issued on: December 22, 2023

Annexure – A

1. Basic Propositions

The proposal to be implemented in two phases as under:

i. In Phase 1, an optional T+0 settlement cycle (for trades till 1:30 PM) is envisaged, with settlement of funds and securities to be completed on the same day by 4:30 PM.

ii. In Phase 2 an optional immediate trade-by-trade settlement (funds and securities) may be carried out. In the second phase, trading will be carried out till 3.30 pm.

After the implementation of phase 2 (optional instant settlement), the mechanism of optional T+0 settlement implemented under phase 1 will be discontinued.

Summary of the two proposed phases:

	Phase 1: Optional T+0 Settlement	**Phase 2: Optional Instant Settlement**
Participation	All clients (including TM proprietary trading), excluding clients settling through custodians.	All clients (including TM proprietary trading).
Approach	Settlement completion by 4:30 PM on T day.	Settlement at the earliest. It will be trade-by-trade settlement i.e. each trade settled separately.
Trading	Exchange shall create a separate series/group/scrip code.	Exchange shall create a separate series/group/scrip code.
Order Type	-	Limit order

Trading period	Trading will be up to 1:30 PM.	Trading will be up to 3.30 PM.
Obligation	For UPI Clients: Net obligation at client level. For other Clients and Proprietary: Net obligation at member level across clients.	Each trade settled separately.
Trades settled through Custodians	Not permitted.	Permitted.
Risk Management	Based on margin, as per existing mechanism.	Order level risk management system and mandatory prefunding of funds and securities.
Funds Settlement	For UPI Clients: – UPI block debit to CC Pay-out account to Client's account. For non-UPI Clients and Proprietary: – pay-in and pay-out at member level with CC.	For UPI Clients: – UPI block debit to CC Pay-out account to Client's account. For non-UPI Clients and Proprietary: – pay-in and pay-out at member level with CC.
Securities Settlement	– Early pay-in by 01:45 PM. – Securities pay-out to client's demat account for UPI Clients. – Securities pay-out to member pool account for non-UPI clients and proprietary. – Pay-in validation will be done by CCs.	– Early pay-in mandatory before trading. – Securities pay-out to client's demat account for UPI Clients. – Securities pay-out to member pool account for non-UPI clients and proprietary. – Pay-in validation will be done by CCs.

2. Phase 1: Optional T+0 settlement

2.1 Eligible Investors

2.1.1 All clients (including TM proprietary trading), excluding clients settling through custodians.

2.1.2 Considering the timelines required for processing of custodial trades, and limited availability of time for completion of settlement, and as they are currently exempt from margin requirements, it is proposed to exclude custodian clients in phase 1.

2.2 Eligible Securities

2.2.1. To begin with, T+0 settlement shall be made available in top 500 listed equity shares based on the market capitalisation. This will be done in three tranches of 200, 200, 100 from lowest to highest market cap.

2.2.2. The exchanges shall co-ordinate to publish a common list of securities and calendar for migration under T+0 settlement.

2.2.3. The surveillance measures applicable in T+1 settlement cycle shall be applicable to securities in T+0 settlement cycle. Securities under trade-for-trade settlement shall not be permitted for T+0.

2.2.4. Securities trading in periodic call auction sessions shall not be permitted.

2.3 Trading

2.3.1 Exchange shall create a separate series/group/scrip code for T+0.

2.3.2 Price Band: A price band will be of ±100 basis points, which will be re-calibrated after a 50 basis points movement in the underlying securities in the regular T+1 market.

2.3.3 There shall be only one continuous session from 09:15 AM to 1:30 PM; No pre-open/special pre-open/block/auction/post close sessions in this segment.

2.3.4 No trading on settlement holiday/ex-date of corporate action in regular market (including scheme of arrangement).

2.3.5 Client code modifications permitted till 1:45 PM.

2.3.6 T+0 prices not to be considered in index calculation/settlement price. There shall be no separate close price for securities based on trading in T+0 segment.

2.4 Risk Management

2.4.1 The risk management shall be done on a post-trade basis as per the current mechanism. In case of UPI Clients, the UPI block created by clients or securities belonging to the clients that are re-pledged to CC shall be considered towards the margin requirements of the respective client. In case of shortfall, proprietary collateral of the TM/CM shall be utilized towards margin requirements.

2.4.2 In case of other permitted clients, the margins shall be checked against the collateral allocated by the clearing members as per prevailing practice.

2.4.3 There shall be no pre-trade validation of funds or securities for T+0 orders, as with T+1 segment.

2.5 Clearing and Settlement

2.5.1 In case of UPI Clients, a single net funds obligation, and a single net obligation per security shall be arrived at for each client. The netting of obligations will be at client level, without any offset across clients.

2.5.2 In case of other permitted clients, net obligations at member level shall be arrived at as per the existing framework.

2.5.3 A new settlement type to be introduced at the Clearing Corporation and Depository level for settlement of T+0 transactions.

Pay-In

2.5.4 Early pay-in (EPI) of securities using block mechanism shall be mandatory for delivery in the T+0 market, using the new settlement type. The depositories shall provide details of the unique client code (UCC) for securities early pay-in to the CCs. CCs will match early pay-in against actual sale obligations. In case of excess EPI, CCs shall reverse the same.

2.5.5 EPI transaction files will be shared by depositories to respective CCs at the pre-defined fixed time intervals.

2.5.6 In case of UPI Clients: To conduct funds pay-in, the CC shall debit the UPI blocks created by the clients by sending necessary instruction to its sponsor banks. In case of shortfall of UPI block, i.e., the amount being inadequate to meet the obligation at client level, the obligation shall be devolved on the member who will be responsible for settling the same through clearing bank account. In case of devolvement, any securities pay-out due to the client will be provided to client demat account with auto-pledge to the CM's client unpaid securities pledgee account (CUSPA). CC shall provide the details of TM ID and /or CM ID along with the Auto pledge Flag for CUSPA.

2.5.7 In case of other permitted Clients: The net funds pay-in (including devolvement) shall be collected from the clearing bank account of the clearing member as per the existing mechanism.

2.5.8 The CC shall receive securities pay-in from the depositories after reversal of excess early pay-in.

Pay-Out

2.5.9 In case of UPI Clients: The CC shall provide funds pay-out directly to the designated primary bank account of the client, subject to the fulfilment of securities pay-in obligations. In case of securities pay-out, the CC shall credit the same to the primary demat account of the client. In case of primary demat account of client is closed or frozen, securities pay-out will remain in CC pool account.

2.5.10 In case of other permitted Clients: The funds/securities pay-out shall be provided to the clearing bank account/depository pool account of the clearing member.

2.5.11 In case of securities shortfall, there shall be a direct close-out at 110 % of the highest price of the day in T+0 session. In case of UPI clients, such close-out amount shall be recovered from UPI blocks of the client if any, and any residual amount shall be devolved on the clearing member. In case of other permitted clients, the same shall be collected from the clearing bank account of the clearing member.

2.6 Settlement Timelines

The settlement timelines are as under-

Activity	Time
Regular Market Close	13:30
Client code modification window close	13:45
Cutoff to mark early pay-in in the depository	13:45
Cutoff for funds pay-in	13:45
Sending last EPI file by depository to CC	14:00
Validation early pay-in by CC and reversal of excess EPI	14:45
Calculation of obligation including devolved on member for UPI Clients (UPI block shortfall + Securities shortfall square off amount)	15:00
Funds pay-in from UPI Blocks through sponsor bank	15:15
Securities Pay-in from depositories	15:30
Funds Pay-in and pay-out through clearing banks	16:00
Funds pay-out for UPI clients through sponsor banks	16:00
Securities Pay-out, round 1 (Internal CC payout + Delivery to Inter-CC)	16:00
Securities Pay-out, round 2 (Received from Inter-CC)	16:30

3. Phase 2: Optional Instant Settlement

3.1 Eligible Investors

All clients including TM proprietary trading and clients settling through custodians.

3.2 Eligible Securities

To begin with, all securities available under Phase 1 will be available under Phase 2.

3.3 Trading

3.3.1 In case of instant settlement, only limit orders shall be allowed, so that adequacy of prefunding can be validated by the CC against the limit price.

3.3.2 Trading hours will be from 09:15 AM to 03:30 PM, i.e. identical to T+1 segment.

3.3.3 Since settlement will be conducted on trade by trade basis without any time gap, client code modifications shall not be permitted.

3.3.4 Other rules under Phase 1 will continue to be applicable.

3.4 Risk Management

3.4.1 An API-based interface shall be built between depositories and CC to facilitate real-time intimation of early pay-in to facilitate validations, and to carry out instant settlements.

3.4.2 All orders placed on the exchanges will be first sent to CCs for validation of prefunding. In case of buy orders, the CC will check availability of adequate pre-funding to cover the trade value along with other charges (STT, stamp duty and TM specified charges). In case of UPI clients, the pre-funding shall be validated against the UPI block created by the client. In case of non-UPI clients and proprietary trading, the pre-funding shall be validated against the funds early pay-in done by the member and allocated to the respective entity. In case of custodian clients, the funds early pay-in shall be allocated at Trading member – Custodial Participant (TM-CP) code level. In case of sell orders, the CC will check that early pay-in of securities has been done. In case custodian trades, the securities early pay-in shall also be required to be allocated at TM-CP code level.

3.4.3 Only the orders that are successfully validated by CCs shall be allowed for matching.

3.4.4 Any order modification (involving price/quantity change) to be validated by the exchanges once again with CC.

3.4.5 In case of any order cancellations, the same shall be transmitted by exchanges to CC.

3.5 Clearing and Settlement

3.5.1 Funds pay-in or pay-out for UPI Clients:

a) After each trade, the CC shall send a single instruction to the sponsor bank to debit the UPI block and

b) CC shall instruct its sponsor banks to provide funds pay-out to credit the primary bank account of the seller.

3.5.2 Funds pay-in/pay-out for other permitted Clients:

a) CC will utilize the funds early pay-in towards the obligation.

b) CC will provide funds pay-out to the clearing bank account of the member.

3.5.3 Securities pay-in or pay-out for UPI Clients: After each trade, the CC shall send a single instruction through API to the depository to debit securities from the early pay-in done by the seller and credit to the primary demat account of the buyer. For pay-in, depositories will create hop-skip entries in TM/CM account as applicable.

3.5.4 Securities pay-in or pay-out for other permitted Clients: After each trade, the CC shall send instructions through API to the depository to debit securities from the early pay-in done by the seller and credit to the pool account of the clearing member of the buyer. For pay-in depositories will create hop-skip entries in TM/CM account as applicable.

3.5.5 Since the settlement is taking place on trade-by-trade basis and the client may execute sell trades throughout the day, the remaining securities early paid-in by the client will not be released upon part debit against a trade. The remaining quantity of securities early pay-in done by clients will be released by the CC after the end of the instant settlement market. Thus, against an early pay-in, there can be multiple debits throughout the day for multiple sell trades of client, and any excess remaining after all such trades will be reversed after market close.

3.5.6 In case the above transfers require an inter-depository transfer, i.e., if the seller has done early pay-in of securities in one depository and the primary demat account of the buyer is in another depository, the inter-depository settlement shall be handled by the depositories.

3.5.7 In case any trade involves inter-CC settlement (i.e., the buyer is clearing through one CC and the seller is clearing through another CC), then the CCs will provide pay-out in each other pool account/clearing bank account. The receiving CC shall complete the onward settlement to the client. This will introduce an additional leg in some settlements.

3.6 Settlement timelines for Phase 2

Trades will be settled as soon as possible. Settlement will be done on a trade-by-trade basis. The inter-CC settlement can take longer due to additional leg of settlement between the CCs.

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