Consultation Paper on "Introduction of Closing Auction Session in the Equity Cash Segment"

Objective:

1. A Consultation Paper was issued on December 05, 2024 with respect to the introduction of Closing Auction Session (CAS) in the equity cash segment. Taking into account the feedback received from the stakeholders and subsequent deliberations in the Secondary Market Advisory Committee of SEBI, several changes have been incorporated in the proposed revised CAS design.

2. The objective of this consultation paper is to seek comments/ views/ suggestions from the public on the proposed revised CAS design.

3. Further, comments/ views/ suggestions are also sought from the public to permit Passive Mutual Funds to undertake overnight borrowing to meet the liquidity requirements arising out of any net negative cash balances on account of the trades undertaken in CAS.

Background:

4. Passive investment through mutual funds and foreign portfolio investors (FPIs) has seen significant growth in India. Passive funds AUM invested by FPIs, as on July 31, 2025, is approximately INR 20.5 lakh crore, constituting around 29% of the total equity AUM of FPIs. Further, passive funds AUM invested by domestic Mutual Funds is approximately INR 9.18 lakh crore, constituting around 27.5% of the total equity AUM invested by Mutual Funds.

5. The increasing presence of Indian stocks in major global indices such as FTSE and MSCI, where they command weights between 17% and 30%, has also amplified the demand for the ability to trade at closing price, to reduce the tracking error.

6. Data and research suggest that CAS provides a more stable and less volatile closing price compared to the volatility often observed under a Volume Weighted Average Price (VWAP) based closing price methodology, even when handling the same level of trading volumes. Under the VWAP approach, large institutional trades executed towards the end of the VWAP calculation window, can create sharp intraday price swings as the market absorbs these flows in real time. This volatility is especially pronounced during index rebalancing days or large portfolio adjustments, where execution timing within the VWAP window can meaningfully impact the price path. In contrast, CAS concentrates liquidity in a single transparent auction, allowing all buy and sell interests to interact simultaneously. This results

in single equilibrium price formation based on maximum matching of supply and demand even when overall volumes are high. CAS ensures that for the same total traded volume, the market experiences lower price disruption and a more reliable closing price, improving execution certainty for all participants.

7. Further, moving to CAS would ensure alignment with global benchmarks (viz. NYSE, LSE, Euronext, HKEX, ASX, etc.) which have adopted CAS as the closing price determination mechanism. India is the only major market where the VWAP mechanism is utilized to determine the closing price. Aligning the methodology of determining closing price with the global practices will help in achieving cross-market consistency.

8. CAS can also facilitate large institutional trades at a well-discovered price as it can serve as an efficient, transparent alternative to the current block deal window for executing large institutional transactions. In the block deal window, counterparties pre-negotiate prices and execute trades in a separate session. While effective for confidentiality, these trades may occur away from the prevailing market price and may attract concerns over price justification and market signaling. In contrast, the CAS aggregates all buy and sell interests from diverse market participants — including institutional investors, domestic Mutual Funds, FPIs, and retail investors into a single, liquid price discovery process. The institutional investors can achieve execution certainty at the closing price, without relying solely on negotiated block deals, thereby improving market transparency and reducing information leakage risk.

9. In light of the above and based on the feedback received from various market participants, several changes are proposed in the initial CAS design. The same is discussed in the ensuing paragraphs.

Proposed CAS design:

10. **Applicability of CAS:**

Initial Proposal	Revised Proposal
• CAS would be applied to stocks in a phased manner. • Initially CAS to be applicable only to the stocks included in the Nifty 50/ Sensex 30 indices, to ensure that the same is applicable on stocks that have sufficient liquidity.	• CAS would be applied to stocks in a phased manner. • Initially CAS would be applicable only to the stocks that are available for trading in derivative segment, i.e. the stocks with sufficient liquidity. • Based on the experience gained, the same may be extended to all stocks at a later stage.

Rationale/ Regulatory Intent:

10.1. Passive funds typically track a broad spectrum of indices. If CAS is implemented only for Nifty 50 / Sensex 30 constituents, many stocks in the indices tracked by passive funds would continue to have their closing prices determined by the VWAP methodology, while a subset would have their closing prices determined by the CAS mechanism. This mixed regime would complicate execution and increase operational complexity for the passive funds.

10.2. Keeping in view the above, it appears prudent to extend the CAS framework to all the highly liquid stocks, i.e. all stocks included in the derivative segment, to reduce operational complexity for the passive funds.

Proposal 1:

Should CAS framework be implemented for determining the closing price of stocks in the cash segment?

Proposal 2:

Should CAS framework be implemented initially on the stocks that are available for trading in the derivative segment?

11. **Timings of CAS:**

<table>
<tr><th>Initial Proposal</th><th>Revised Proposal</th></tr>
<tr><td>

CAS would be implemented as a separate session of 15 minutes from 3:30 pm to 3:45 pm.
CAS would be split into 3 sessions, in line with the architecture of the call auction in the pre-open session.

<table>
<tr><th>Session</th><th>Begin time</th><th>Duration</th></tr>
<tr><td>Reference Price Calculation period, transition from continuous</td><td>3:30 pm</td><td>1 min</td></tr>
</table>
</td><td>

CAS would be implemented as a separate session of 20 minutes from 3:15 pm to 3:35 pm.
CAS may be split into 4 sessions. The timings along with the sessions is given below:

<table>
<tr><th>Session</th><th>Begin time</th><th>Duration</th></tr>
<tr><td>Reference Price Calculation/ Transition from continuous</td><td>3:15 pm</td><td>5 mins</td></tr>
</table>
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<table>
<tr><th>Initial Proposal</th><th>Revised Proposal</th></tr>
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<table>
<tr><td>trading session to CAS</td><td></td><td></td></tr>
<tr><td>Order Input Period including Random Close in the last 2 minutes</td><td>3:31 pm</td><td>10 min</td></tr>
<tr><td>Trade confirmation and order matching period</td><td>3:41 pm</td><td>4 min</td></tr>
</table>
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<td>
<table>
<tr><td>trading session to CAS</td><td></td><td></td></tr>
<tr><td>Order entry period for both limit and market orders</td><td>3:20 pm</td><td>5 mins</td></tr>
<tr><td>Order Entry Period only for limit orders, including Random Close in the last 2 minutes</td><td>3:25 pm</td><td>5 mins</td></tr>
<tr><td>order matching</td><td>3:30 pm</td><td>5 min</td></tr>
</table>

The post close session in the cash market operates between 3:40 pm to 4:00 pm, where trades can be executed only at the closing price for stocks.
In order to ensure concurrent closure of the cash and the derivative segment, on non-expiry days for stocks, all the derivative contracts for stocks may continuously function for the period till 4:00 pm.
However, on the expiry day of the near month derivative contracts for stocks, such contracts may expire at 3:35 pm, while all other stock derivative contracts continue trading until 4:00 pm.
The close time of index derivatives i.e. 3:30 pm on all the days, remains unchanged.

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</table>

Rationale/ Regulatory Intent:

Timing of CAS post 3:30 pm

11.1. In case the closing auction is executed post 3:30 pm, there may be issues with trade allocation and settlement processes. Fund managers typically finalize trade allocations immediately post-close based on the 3:30 pm price. An extended closing time under CAS would compress the already tight window post-closing time for allocating trades to multiple client accounts, confirming trades with custodians and matching trades in clearing systems. This raises the risk of operational errors and missed settlement cut-offs, particularly for foreign investors.

11.2. If CAS extends beyond 3:30 pm, the Fund of Funds (FoFs) industry, especially those investing in domestic mutual funds, will be hit harder than single-layer funds, because FoFs are dependent on two layers of NAV calculations. FoFs calculate their NAVs only after receiving the NAVs of the underlying schemes they invest in. If CAS delays the availability of final closing prices, underlying schemes' NAV computation would also be delayed. Thus, FoFs can start their NAV computation only after they receive underlying NAVs. This creates a cascading delay, which may make it difficult for FoFs to meet SEBI's same-day NAV disclosure requirements.

11.3. Further, for Indian FoFs investing in international funds, or overseas FoFs investing in Indian funds, execution of CAS post 3:30 pm, may cause spill over into other time zones.

Allowing entry/ modification/ cancellation of market orders during the initial 5 minutes of order entry period

11.4. During CAS, indicative equilibrium prices are visible to the market. If large market orders are introduced too late, there may not be adequate reaction time for counter-parties to place limit orders to balance the order book. Hence, it is envisaged to allow entry/ modification/ cancellation of market orders only in the initial 5 minutes of the order entry period. This will ensure that the auction price path is more stable and predictable, helping the market participants to build a balanced order book.

11.5. Further, allowing the limit orders throughout the order entry period encourages continuous fine-tuning of bid/ offer to converge on a fair equilibrium price and provides market makers and investors sufficient time to adjust to indicative price movements.

Extending the derivative segment post CAS

11.6. Extending the derivatives segment post-CAS would enable funds to achieve intended end-of-day exposures despite incomplete CAS fills, and would allow arbitragers to square off unmatched positions, thereby improving risk management, enhancing liquidity, reducing settlement mismatches, and aligning with global market practices.

Solving the issue of physical delivery obligation for option contracts arising due to sudden price movement on expiry day

11.7. In order to mitigate the risk of unforeseen physical delivery obligations for option contracts arising from abrupt price movements near the close of trading on expiry day, it is proposed that the near month derivative contracts operate until 3:35 pm, on the expiry day. Under this framework, the closing price would be determined at 3:30 pm, thereby providing market participants with certainty regarding their physical delivery obligations. Further, allowing trading in near-month stock derivative contracts to continue until 3:35 pm, on the expiry day would enable participants to undertake offsetting positions in the derivatives segment, thereby facilitating effective management of such physical delivery obligations.

Proposal 3:

Should the CAS be conducted without extending the existing market hours?

Proposal 4:

Do you agree with the proposed framework as stated at para 11.4 with respect to market orders during the CAS?

Proposal 5:

Do you agree with the proposed framework for extending the timing for derivatives segment, as stated in para 11.6?

12. **Application of price bands:**

Initial Proposal	Revised Proposal
• Price band of +/- 5% around the reference price may be applied during the CAS.	• Price band applicable during CAS may be +/- 3% from the reference price of the stock in the cash segment.

Rationale/ Regulatory Intent:

12.1. A broader permissible range during CAS may facilitate execution of trades at prices significantly away from the reference price, thereby undermining the price discovery process. Execution at prices materially divergent from the market levels prevailing during the continuous trading session could result in disadvantageous outcomes for investors, thereby affecting investor confidence and market credibility.

Proposal 6:

Whether a price band of +/- 3% from the reference price should be applied to the CAS in the cash segment?

13. **Computation of Reference Price:**

Initial Proposal	Revised Proposal
• The reference price for CAS may be determined based on the VWAP in the cash segment for the last 30 minutes of the continuous trading session i.e., between 3:00 pm to 3:30 pm.	• The reference price for CAS may be determined based on the VWAP of the stock in the cash segment, during the period 3:00 pm to 3:15 pm in the continuous trading session.

Rationale/ Regulatory Intent:

13.1. The computation of the reference price for CAS in the cash segment based on the VWAP of trades executed during the last 30 minutes of the trading session may result in a material deviation from the Last Traded Price (LTP). Hence, a lower time window for computation of reference price may be considered to enhance alignment of the reference price with the LTP, while mitigating the potential for price manipulation.

Proposal 7:

Should the reference prices for the cash segment be determined based on the VWAP of trades executed during the 15 minutes period from 3:00 pm to 3:15 pm?

14. **Order execution priority in CAS**

Initial Proposal	Revised Proposal
• At the time of order execution in CAS, limit orders shall be given priority over market orders. The sequence of order execution in CAS may be similar to	• Pursuant to the discovery of closing price in CAS, at the time of order execution, market orders shall be given priority over limit orders. Accordingly, the revised sequence

Initial Proposal	Revised Proposal
the priority of the Pre-Open Call Auction Session, as given below: - Eligible limit orders shall be matched with eligible limit orders in the price-time priority at the final equilibrium price. - Residual eligible limit orders, in the order of price-time priority, shall be matched with market orders, in the order of time priority. - Market orders to be matched with market orders, in the order of time priority.	for order execution in CAS shall be as given below: - Eligible market orders shall be matched with eligible market orders in the order of time priority at the final equilibrium price. - Residual eligible market orders, in the order of time priority, shall be matched with limit orders, in the order of price time priority. - Remaining limit orders shall be matched with limit orders in the order of price time priority.

Rationale/ Regulatory Intent:

14.1. In case limit orders are given priority over market orders during execution in CAS, the same may result in reduced execution certainty for market orders, thereby affecting the volume maximization objective of CAS. Limit orders may dominate execution, potentially skewing the final equilibrium price towards the interests of limit order placers.

14.2. Further, many institutional investors use market orders in CAS to ensure execution at the closing price. Lower priority could discourage them from participating in CAS.

14.3. It is noted that the proposed order execution priority in CAS is different from the order execution priority applicable in the pre-open session. Thus, there may be a need to align the order execution priority in both, CAS and pre-open session.

Proposal 8:

Should the execution priority in CAS be accorded to market orders over limit orders?

Proposal 9:

Should the order execution priority in pre-open session be aligned with the order execution priority in CAS?

15. **Unexecuted orders of the continuous trading session:**

Initial Proposal	Revised Proposal
• All unexecuted orders of the continuous trading session in cash segment may be automatically carried forward to CAS. However, all the orders with price outside the price limits applicable to CAS would be cancelled.	• All unexecuted limit orders of the continuous trading session may be automatically carried forward to CAS. However, all the orders with price outside the price limits applicable to CAS would be cancelled. • Given that orders entered directly into CAS are subject to order-level margins, whereas limit orders transitioned from the continuous trading session into CAS are not, to ensure preservation of market integrity, such transitioned limit orders not to be eligible for modification. These orders may, however, be cancelled.

Rationale/ Regulatory Intent:

15.1. Orders entered directly into CAS are subject to order-level margin requirements. However, orders transitioned from the continuous trading session into CAS, if permitted, would not be subject to such order-level margins. Typically, margin sufficiency is verified by the Clearing Corporations at the time of trade execution. In the event that all limit orders from the continuous trading session, falling within the CAS-applicable price band, are transitioned into CAS without the application of margins, market participants could subsequently modify these orders to significantly higher quantities. Such modifications may adversely affect the integrity of the price discovery process and compromise overall market integrity.

Proposal 10:

Should limit orders carried over from the continuous trading session to CAS be disallowed from modification during CAS?

16. **Information to be disseminated during CAS**

Initial Proposal	Revised Proposal
• The following information may be disseminated during CAS:	• The following information may be disseminated during CAS:

Initial Proposal	Revised Proposal
- Indicative equilibrium price of the stock - Indicative cumulative buy and sell quantity of the stock - Indicative Index	- Indicative equilibrium price of the stock - Indicative cumulative buy and sell quantity of the stock - Cumulative imbalance quantity of the stock - Imbalance quantity based on market orders of the stock - Indicative Index

Rationale/ Regulatory Intent:

16.1. In order to enhance transparency and support efficient price discovery during CAS on a real-time basis, both the cumulative imbalance quantity and the imbalance quantity attributable solely to market orders, may be disseminated.

16.2. While the cumulative imbalance quantity will provide participants with a comprehensive view of the overall demand-supply gap, the market-order-specific imbalance will allow them to assess the urgency and firmness of trading interest, given that market orders reflect immediate execution intent. Dissemination of both data points is expected to improve participant decision-making, strengthen market integrity and mitigate the scope for misinterpretation or manipulation of the indicative price.

Proposal 11:

Should real-time dissemination be provided during the CAS for the cumulative imbalance quantity and the imbalance quantity attributable to market orders in a stock?

Potential issues of domestic passive Mutual Funds:

17. The domestic passive funds have highlighted the risk of having negative cash balances on index rebalancing days, as the final net consideration of incoming and outgoing stocks may not be certain till the close of CAS.

18. If the passive funds have a net purchase position in CAS, it will result in negative cash balances for such passive funds. Considering the fact that the passive funds do not hold cash balances to avoid tracking error, they might not be in a position to meet the pay-in requirement of funds.

19. As per Regulation 44(2) of the SEBI (Mutual Fund) Regulations, 1996, Mutual Funds shall not undertake borrowing of funds except to meet the short-term liquidity needs arising due to the purpose of repurchase, redemption of units or

payment of interest or dividend to the unitholders. Further, the Mutual Funds shall not undertake borrowing exceeding 20% of its net assets and the duration of such borrowings may not exceed a period of 6 months.

20. Accordingly, in order to facilitate the domestic passive funds to participate in CAS, they may be permitted to undertake overnight borrowing to meet the liquidity requirements arising out of net negative cash balances, on account of the trades undertaken in CAS.

Proposal 12:

Should the passive Mutual Funds be allowed to borrow funds on an overnight basis, to meet the liquidity requirements arising due to net negative cash balances, on account of the trade undertaken in CAS?

Proposal 13:

Should any other relaxation be allowed to the market participants, from the extant regulatory requirements, to enable greater participation in CAS?

Public Comments:

21. Considering the implication of the aforesaid proposals on the market participants, public comments are invited on the proposals 1 to 13. The comments/ suggestions should be submitted latest by September 12, 2025 through the following link.

https://www.sebi.gov.in/sebiweb/publiccommentv2/PublicCommentAction.do?doPublicComments=yes

22. In case of any technical issue in submitting the comment through web based public comments form, the comments may be sent via e-mail to Mr. Abhishek Agarwal, Assistant General Manager (abhisheka@sebi.gov.in) or Mr. Sanjay Singh Bhati, Deputy General Manager (ssbhati@sebi.gov.in). While sending the e-mail kindly mention the subject as: “Comments on Introduction of a Closing Auction Session (CAS) in the Equity Cash Segment”.

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