POLICY ON INTERNAL SHORTAGE OF SECURITIES

1. Background & Regulatory Framework

This policy is framed in accordance with SEBI Master Circular for Stock Brokers and Exchange Guidelines issued by National Stock Exchange of India Limited (NSE) and BSE Limited regarding the handling of internal shortages arising during pay-in/pay-out of securities.

An Internal Shortage occurs when a selling client fails to deliver securities to fulfill their settlement obligation, and another buying client of the same Trading Member is entitled to receive those securities in the same settlement cycle (T+1 settlement cycle). Since the Exchange clearing house does not recognize internal netting between clients of the same broker, the broker must have a transparent, non-discriminatory policy to resolve such shortages.

2. Objective

The objective of this policy is to establish a clear, fair, and systematic procedure to deal with internal shortages of securities, protecting the interest of buying clients while ensuring compliance with SEBI and Exchange guidelines.

3. Procedure for Handling Internal Shortage

When an internal shortage occurs (i.e., Seller Client A fails to deliver shares bought by Buyer Client B in the same settlement), the Trading Member shall adopt the following process:

A. Internal Auction / Buy-In from Market:

- The Trading Member shall attempt to purchase the required quantity of shares from the open market on T+1 day / T+2 day (Auction Day) on behalf of the defaulting seller.
- The purchased securities shall be delivered to the buyer client's demat account upon settlement.

B. Financial Close-Out (If Shares are Not Available / Illiquid / Circuit Stocks):

If the shares cannot be bought back from the open market due to illiquidity, price filters, upper circuit, or non-availability, the short position shall be financially closed out as per Exchange-prescribed close-out mechanism.

4. Valuation & Close-Out Rate Determination

The close-out rate for internal shortage settlement shall be calculated as follows (whichever is higher):

- **Highest Price on Exchange:** The highest price recorded for the security on the Exchange from the Trade Date (T day) up to the Auction/Close-out Day (T+1 / T+2).

- **Valuation Price + Mark-Up:** The closing price of the security on the day of close-out plus a mandatory penalty/mark-up (typically 20% or as prescribed by the Exchange from time to time).

5. Accounting Treatment & Debits/Credits

A. **Defaulting Seller:** The account of the defaulting selling client shall be debited with the actual cost of buy-in from the market OR the calculated close-out price plus Exchange/Internal penalty and statutory costs.

B. **Purchasing Buyer:** The account of the purchasing buying client shall be credited with the close-out amount if shares cannot be delivered, ensuring zero financial loss to the buyer.

C. **Broker Role:** The Trading Member shall not retain any profit arising out of the internal shortage buy-in or close-out process. Any difference/profit shall be passed on to the buyer or credited to the Investor Protection Fund as per Exchange norms.

6. Penalty Mechanism for Defaulting Clients

A. A penalty/handling fee may be levied on the defaulting seller client to discourage repeated delivery defaults.

B. If a client defaults on internal delivery repeatedly, the Risk Management System (RMS) team shall restrict further sell permissions or increase upfront margin requirements for such clients.

7. Client Communication & Intimation

A. The Trading Member shall notify both the defaulting seller and the buyer client regarding the internal shortage, buy-in details, or close-out credit/debit via email / SMS on T+1 / T+2 day.

B. Detailed breakdown of close-out calculations shall be reflected in the client's quarterly statement of accounts and contract notes/bills.

8. Record Keeping & Audit Trail

A. All logs, auction buy-in trade sheets, close-out calculations, and client communication records shall be maintained by the Compliance/Settlement department.

B. These records shall be preserved for a statutory period of 5 years and made available during Exchange audit inspections.

9. Policy Review

This policy shall be reviewed annually or as and when new guidelines or circulars regarding securities settlement and close-out procedures are issued by SEBI or Stock Exchanges.