FAQS ON ZERODHA'S POLICY ON DELIVERY-BASED SETTLEMENT

1. **Which securities in Futures and Options segment will become eligible for delivery-based settlement?**

   Based on the criteria specified in the SEBI circular Exchange shall identify securities which shall be settled through delivery on expiry. Exchange shall inform list to market participants through a circular from time to time.

   Check this list to stay updated on stocks which are to be compulsorily settled physically.

2. **Will delivery-based settlement be applicable for NIFTY and BANKNIFTY?**

   Delivery-based settlement will not be applicable for Index Derivatives. Index derivatives will continue to be cash settled.

3. **What positions of futures and options contracts in eligible securities shall result in delivery settlement on expiry day?**

   The following positions in respect of securities identified for shall be settled through delivery:

   • All open futures positions after close of trading on expiry day
   • All in-the-money contracts (ITM) which are exercised and assigned. However, in respect of Close to Money (CTM) option contracts the option holder shall have a facility of do-not-exercise

4. **How will be the quantity of stocks to be delivered as buy quantity/sell quantity shall be computed?**

   The deliverable quantity shall be computed as under -

   a. Unexpired Futures

   - Long futures shall result into a buy (security receivable) position
   - Short futures shall result into a sell (security deliverable) position

   b. In-the-money call options

   - Long call exercised shall result into a buy (security receivable) position
   - Short call assigned shall result into a sell (security deliverable) position

c. In-the-money put options

- Long put exercised shall result into a sell (security deliverable) position
- Short put assigned shall result into a buy (security receivable) position

The quantity to be delivered/ received shall be equivalent to the market lot * number of contracts which result into delivery settlement

5. **What is Zerodha's policy on delivery-based settlement ?**

<u>Futures and Short Option (Calls & Puts) positions</u>

1. Span + Exposure margin for all contracts which are going to be physically delivered will be increased to at least 30% or what is charged by the exchange (whichever is higher) 3 days prior to expiry or on Monday leading to the Thursday expiry(This will be increased to 50% on Thursday). These margins will be debited on your trading ledger.

Day	**Percentage of Contract value that will be blocked**
Expiry - 3 days (Mon)	40 %
Expiry - 2 days (Tue)	50 %
Expiry - 1 day (Wed)	60 %
Expiry day (Thu)	80 %

2. These margins debits will be shown on your trading ledger. The increase in margin is to cover for the additional obligation that will arise if these contracts are held till expiry and result in a physical settlement. If the SPAN +Exposure margin is higher than the above-mentioned margins, the exchange margin will be levied.

3. So for example, if the margin required for RCOM futures is normally 25% as SPAN+Exposure of contract value, it will be 40% of contract value from Monday leading to expiry. On Expiry day, 50% of the contract value will be blocked from the account.

4. You can check for all SPAN and Exposure margin on our margin calculator. Alternatively, you can check for these normal %s on margin PDF file.

5. In the event that you do not fulfil these margin obligations on time, your positions are liable to be squared off. Any loss arising out of such square off would be the sole responsibility of the client.

Long/Buy option (Calls & Puts) positions

Exchanges have defined Close to money (CTM) contracts which are a subset of ‘in the money (ITM)’ or contracts which expire with some intrinsic value.

For Call Options – 3 ITM options strikes immediately below the final settlement price shall be considered as ‘CTM’

For Put Options – 3 ITM options strikes immediately above the final settlement price shall be considered as ‘CTM’.

OTM (Out of the money) options are those strikes which are above the final settlement price for calls and below the final settlement price for puts.

Blocking of Delivery Margins

From September expiry onwards, the exchange has mandated that margins be blocked for long options (Call & Put). The margins will be applicable from 4 days before expiry (i.e Friday EOD - the week prior to expiry week). The delivery margins applicable will be a percentage of the VAR + ELM margins (Check out **this** NSE FAQ to know more about VAR & ELM). The delivery margins will be applicable in the following manner -

Day	**Margins applicable**
Expiry -4 Day (Friday EOD)	20% of VAR + ELM
Expiry - 3 Day (Monday EOD)	40% of VAR + ELM
Expiry - 2 Day (Tuesday EOD)	60% of VAR + ELM
Expiry - 1 Day (Wednesday EOD)	80% of VAR + ELM

For example, RCOM has a VaR+ELM of 23.22%. On E-1, the delivery margin will be 20% of the VaR+ELM which is 4.64% of the contract value. If you have RCOM 17.5 CE, you will be required to have Rs 22,755 (20% * 23.22%(VaR+ELM) * 28000(lot size * 17.5(Strike price)).

On the expiry day, you are required to maintain 50% of the contract value(or SPAN+Exposure), whichever is higher.

For ITM Put options, you need to hold deliverable shares(equal to the lot size of the contract) in your Demat Account on the day of expiry along with the applicable margins mentioned above.

OTM (Out of the money) options are those strikes which are above the final settlement price for calls and below the final settlement price for puts. All OTM options will expire worthless. There will be no delivery obligations arising out of this.

In the event that you do not fulfil these margin obligations on time, your positions are liable to pay **margin penalty** & it may be squared off at the discretion of our RMS team. Any loss arising out of such square off would be the sole responsibility of the client.

Random Assignment of short CTM Position

In case you've written an option that expires 'in the money' and have left such position to expire, the assignment of such CTM option is done randomly by the Exchange. In the event that your option contract does not get assigned, you are entitled to retain the premium. However, if an option gets assigned to you, you will have to give/receive delivery of Stock depending on whether you have written a call/put option.

Additional costs of physical delivery

All positions that result in you receiving delivery of shares will require you to have funds equivalent:
- For Futures: Settlement Price * Lot Size * Number of lots
- For Options: Strike Price * Lot Size * Number of lots

In the event that you do not have sufficient funds to meet this obligation, interest at the rate of 0.05% per day will be charged on the debit balance.

All positions that result in you having to give delivery of shares will require you to have shares in your DEMAT account equal to the deliverable quantity. In the event that you do not have the required quantity of shares, this settlement would result in a short delivery. Appropriate penalties shall be charged on such short deliveries. This can be as much as 20% or more. Read more on the consequences of short delivery.

Since there is a substantial increase in effort and risk to settle these F&O positions resulting in physical delivery, a brokerage of 0.5% of the physically settled value will be charged.

As clarified by the exchange based on the direction of the Hon'ble Bombay High Court, all physically settled contracts(both Futures and Option) will carry an STT levy of 0.1% of the contract value for both the buyer and the seller of the contract.

Additional costs of physical delivery

- All positions that result in you receiving delivery of shares will require you to have funds equivalent:
  - For Futures: Settlement Price * Lot Size * Number of lots
  - For Options: Strike Price * Lot Size * Number of lots

- In the event that you do not have sufficient funds to meet this obligation, interest at the rate of 0.05% per day will be charged on the debit balance.

- All positions that result in you having to give delivery of shares will require you to have shares in your demat account equal to the deliverable quantity. In the event that you do not have the required quantity of shares, this settlement would result in a short delivery. Appropriate penalties shall be charged on such short deliveries. This can be as much as 20% or more. Read more on the consequences of short delivery.

- Since there is a substantial increase in effort and risk to settle these F&O positions resulting in physical delivery, a brokerage of 0.5% of the physically settled value will be charged.

- For all physical settled contracts that result in accepting delivery of stocks, STT will be charged at 0.1% as clarified by the Exchange.

Additional Notes

- No BTST transactions shall be allowed for stocks received by means of physical settlement.

- Unencumbered net-worth of an account comprises of free cash, value stock holdings (that are not pledged or have any other lien against them). Value of mutual fund holdings or collateral received from pledging of stocks/mutual funds will not be considered when calculating unencumbered net-worth.

- This policy may be changed at the discretion of the RMS team.

6. **Will my open positions in these scrips be squared off?**

   Only if you do not maintain the required margins as required by our policy, your position will be squared off.

7. **What will Zerodha's policy be if I have a protective call/put (future-option spread) position in any of these scrips?**

   The positions will be net off - i.e if you are short futures & long call options or short put option

   However,

   For the future leg (short/long) of your positions you'll have to maintain margins (50% of contract value or SPAN + Exposure, whichever is higher) from 3 days prior to expiry.

   For Short Option - you'll have to maintain margins (50% of contract value or SPAN + Exposure, whichever is higher) from 3 days prior to expiry.

   For Long Option - On expiry, the unencumbered net-worth of the client's account (Cash balance + Value of Stocks in Demat account + Intrinsic value of Option Premium) should be more than SPAN+Exposure margin (Exchange mandated) or 50% of contract value whichever is higher required to take a position in the Future contract of the same stock for the next expiry.

8. **Will I be able to open new positions in any of these scrips after 4 days prior to square off?**

   You will be allowed to open new positions in these scrips up to 1 day before expiry, if you ensure you the necessary margins.

9. **Will I be allowed to trade Intraday in these contracts?**

   Yes, you will be allowed to trade intraday in these scrips up to 1 day before expiry. However, increased margins will be applicable.

10. **What will happen if my open position in any of these contracts was not squared off due to illiquidity?**

    In the event that Zerodha is unable to square off the position before expiry, for whatsoever reason, you will be liable to make shares/funds available in your account to the extent of the settlement value.

11. What will be the action taken by NSCCL for non-compliance in fulfilling fund settlement obligations?

The current action as mentioned below shall be taken

S. No	Type of Non Fulfillment	Penalty Charge % per day	Action
a)	Value Rs. 5 lakhs or more	0.07	The trading facility of the trading member clearing through such clearing member shall be withdrawn and securities pay out shall be withheld.
b)	Value less than Rs. 5 lakhs	0.07	The amount shall be blocked from the collateral of clearing member. If in the last three months, the member is short over Rs. 2 lakhs on six or more than six occasions, The trading facility of the trading member clearing through such clearing member shall be withdrawn and securities pay out shall be withheld.

12. How will securities shortages (short delivered shares) be handled?

For securities short-delivered, NSCCL shall conduct a buy-in auction for such securities in the Capital market segment of the Exchange. If auction is unsuccessful, or there is a short delivery in auction settlement, the shortages shall be financially closed out.
The buy-in auction shall be conducted on Expiry+3 days along with the auction conducted for Capital Market Segment. Currently, auction is conducted at 2.00 pm.

Settlement for auction shall be conducted on Expiry + 4 day along with auction settlement for capital market segment.

13. What is the STT applicable for delivery-based settlement?

NSE is awaiting for the necessary clarifications from the CBDT (Central Board of Direct Taxes) in this regard.

In the meantime, after seeking opinions from eminent senior tax counsel effective July 26, 2018 (being the first expiry date of the derivatives contracts), it has been decided to levy a **STT @ 0.10%** (i.e the rate applicable for taxable securities transaction settled by actual delivery in the CM segment) on the settlement price to be paid by the purchaser of the futures contract which are settled by way of physical delivery.

In the event if the CBDT issues any clarification or amendment in this regard, in addition to or contrary to the above position, the Exchange reserves the right to recover such additional STT from the members effective from the date as may be notified by the CBDT.

Refer this NSE circular for more information.

14. Where can I learn more about how delivery-based settlement works?

You can refer this **FAQ** from NSE for a detailed explanation on how delivery-based settlement will work.