

Query No. 1

Subject: *Treatment of contribution to Settlement Guarantee Fund/Core Settlement Guarantee Fund in consolidated financial statements under Ind AS.*¹

A. Facts of the Case

1. ABC Ltd. (hereinafter referred to as the ‘company’) is a recognised stock exchange and offers trading services in equity, equity derivatives, debt and currency derivatives segments in India. DEF Ltd. is a wholly owned subsidiary of ABC Ltd. and is a recognised clearing corporation which carries out the clearing and settlement activities in respect of the trades executed in various market segments of ABC Ltd., such as, cash market, futures & options and currency derivatives.

2. On June 20, 2012, Securities Exchange Board of India (‘SEBI’) notified the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 (‘the Regulations’) to regulate recognition, ownership and governance in stock exchanges and clearing corporations in India. The said ‘Regulations’, inter alia, stated the following:

“39 Fund to guarantee settlement of trades

(1) Every recognised clearing corporation shall establish and maintain a Fund by whatever name called, for each segment to guarantee the settlement of trades executed in respective segment of a recognised stock exchange.

(2)...

(3)...

(4)...

(5) In the event of a clearing member failing to honour his settlement obligations, the Fund shall be utilised to complete the settlement.

(6) The corpus of the Fund shall be adequate to meet the settlement obligations arising on account of failure of clearing member(s).

(7) The sufficiency of the corpus of the Fund shall be tested by way of periodic stress tests, in the manner specified by the Board.”

3. The Regulations required, inter alia, every recognised stock exchange to transfer 25% of its annual profits every year to a fund (Settlement Guarantee Fund (‘SGF’)) maintained by the recognised clearing corporation (subsidiary of the stock exchange), which clears and settles trades executed on that stock exchange. In order to guarantee settlement of trades, the Regulations required such recognised clearing corporation to establish and maintain a Fund, for each market segment, to guarantee the settlement of trades executed in respective segment of a recognised stock exchange.

4. The Regulations also required a recognised stock exchange to transfer its required SGF contribution to a recognised clearing corporation which carries out the clearing and settlement functions of the stock exchange. The SGF will be utilised by the recognised clearing corporation to settle the obligations in the event of a default by a clearing member i.e., clearing member failing to honor its settlement obligations (i.e., trading defaults/losses).

¹ Opinion finalised by the Committee on 23.8.2017.

5. After the notification of the Regulations, SEBI in its Press Release No. 66/2012 dated June 21, 2012, announced the formation of an expert committee to look, inter alia, into matters relating to feasibility of a single clearing corporation or interoperability among multiple clearing corporations and the operational aspects of the same, norms for utilization of profits and investments by recognised clearing corporations and norms for adequacy of the core corpus of the SGF and its sourcing, including transfer of profits by stock exchanges to the SGF in the long run.

6. Subsequently, on August 27, 2014, SEBI, *vide* its circular no. CIR/MRD/DRMNP/25/2014, issued granular norms relating to *Core Settlement Guarantee Fund ('Core SGF')*, stress testing and default procedures to bring greater clarity and uniformity as well as to align with international best practices while enhancing the robustness of the present risk management system in the clearing corporations. (Copy of the Circular has been furnished by the querist for the perusal of the Committee). These norms are aimed at achieving mainly the following objectives:

- (a) create a core fund (called core settlement guarantee fund), within the SGF, against which no exposure is given and which is readily and unconditionally available to meet settlement obligations of clearing corporation in case of clearing member(s) failing to honour settlement obligation,
- (b) ...
- (c) ...
- (d) harmonise default waterfalls across clearing corporations,
- (e) ...
- (f) ring-fence each segment of clearing corporation from defaults in other segments, and
- (g) bring in uniformity in the stress testing and the risk management practices of different clearing corporations especially with regard to the default of members.

7. As can be observed, the norms mentioned in paragraph 6 above amongst various matters related to stress testing and default waterfalls, *also* aimed to create a core fund namely the Core Settlement Guarantee Fund (Core SGF) *within the SGF* (emphasis supplied by the querist). Further, as stipulated, no exposure is to be given and the fund is readily and unconditionally available to meet settlement obligations of clearing corporation in case of clearing member(s) failing to honor settlement obligations.

8. As per the Circular cited in paragraph 6 above, the clearing corporation (CC) shall have a fund, called Core SGF, for each segment of each recognised stock exchange (SE) to guarantee the settlement of trades executed in respective segment of the stock exchange. In the event of a clearing member failing to honor settlement commitments, the Core SGF shall be used to fulfill the obligations of that member and complete the settlement without affecting the normal settlement process.

9. The corpus of the fund should be adequate to meet out all the contingencies arising on account of failure of any member(s). The risk or liability to the fund depends on various factors such as trade volume, delivery percentage, maximum settlement liability of the members, the history of defaults, capital adequacy of the members, the degree of safety measures employed by the CC/SE etc. A fixed formula, therefore, cannot be

prescribed to estimate the risk or liability of the fund. However, in order to assess the fair quantum of the corpus of Core SGF, CC should consider the following factors:

- Risk management system in force
- Current and projected volume/turnover to be cleared and settled by the CC on guaranteed basis
- Track record of defaults of members (number of defaults, amount in default)

10. As per the circular cited in paragraph 6 above, the contributions of the following three contributors to Core SGF in respect of any market segment shall be as follows:

- (a) **Clearing Corporation (DEF Ltd.) contribution:** Contribution to Core SGF shall be at least 50% of the Minimum Required Corpus (MRC). This contribution will be made by clearing corporation from its own funds.
- (b) **Stock Exchange (ABC Ltd.) contribution:** Stock Exchange contribution to Core SGF shall be at least 25% of the MRC. This can be adjusted against transfer of profit by Stock Exchange under SGF (see paragraph 3 above).
- (c) **Clearing Member primary contribution:** Total contribution from clearing members shall not be more than 25% of the MRC. Further, clearing corporation shall have the flexibility to collect contribution from clearing members either upfront or staggered over a period of time. In case of staggered contribution, the remaining balance shall be met by Clearing Corporation to ensure adequacy of total Core SGF corpus at all times. Such Clearing Corporation contribution shall be available to the Clearing Corporation for withdrawal as and when further contributions from clearing members are received.

11. The management of Core SGF and access to the same are as follows:

- The Defaulter's Committee/SGF utilisation Committee of the Clearing Corporation shall manage the Core SGF.
- The CCs shall follow prudential norms of Investment policy for Core SGF corpus and establish and implement policies and procedures to ensure that Core SGF corpus is invested in highly liquid financial instruments with minimal market and credit risk and is capable of being liquidated rapidly with minimal adverse price effect.
- The instruments in which investments may broadly be made are Fixed Deposit with Banks (only those banks which have a net worth of more than INR 500 Crore and are rated A1 (or A1+) or equivalent, Treasury Bills, Government Securities and money market/liquid mutual funds subject to suitable transaction/ investment limits and monitoring of the same. The CCs shall further ensure that the financial instruments in which the Core SGF corpus is invested remain sufficiently diversified at all times.
- SEBI may prescribe the investment norms in this regard from time to time.
- CC may utilise the Core SGF in the event of a failure of member(s) to honour settlement commitment.

12. Subsequently, SEBI, in its Circular No. SEBI/HO/MRD/DRMNP/ CIR/2016/54 dated May 4, 2016, notified that the amounts carried forward in the 'Provisions' in respect of the period up to March 31, 2015 shall be transferred by the Stock Exchange to

the Core SGF maintained by the Clearing Corporation within one month of the date of issuance of the said Circular and that the amounts in respect of the period from April 1, 2015 till the date of amendment of the Regulation 33 of the Regulations shall be transferred within such time as to be specified by SEBI. (Copy of the Circular has been furnished by the querist for the perusal of the Committee).

13. Further, as per the Circular cited in paragraph 12 above, “the unutilized portion of contribution made by the stock exchange towards the Core SGF, for any segment(s), maintained by the Clearing Corporation, as available with the Clearing Corporation, shall be refunded to the stock exchange, in case the stock exchange decides to close down its business or decides to avail the clearing and settlement services of another Clearing Corporation for that segment(s), subject to its meeting all dues of the clearing corporation”. In the latter case, the stock exchange will have to transfer such amount to another clearing corporation.

14. In ABC Ltd’s standalone financial statements, the company records the contribution to the Core SGF as an item of expenditure by debiting the same to the statement of profit and loss based on the understanding stated below:

- (1) The sum of money paid by the Stock Exchange to the Core SGF of the Clearing Corporation is something which has irreversibly and irretrievably gone out of the control of the Stock Exchange.
- (2) Thus, whatever corpus is available with the Fund, it is completely ring-fenced at all times with both the contributing parties, namely, the Stock Exchange and the Clearing Corporation permanently and irrevocably losing their entire domain and control over the funds contributed by them.
- (3) Also, in the Regulations and the SEBI’s Circular, there is no mechanism by which any contribution made to the Core SGF can come back to the contributors- whether the contribution is made by the Stock Exchange or the Clearing Corporation, except on closure of business as mentioned above.
- (4) Another significant feature of the SEBI’s Circular is that the MRC of Core SGF mentioned in paragraph 10 above can only go up and can never be lower than the high water mark reached. To illustrate, if the high water mark is Rs. 100 reached in (say) February 2015 and Rs.20 is utilized in the month of March 2015, then not only the utilization has to be made good but if the MRC is determined at, say, Rs.103 in the next month not only would Rs. 20 be required to be contributed to make up for the utilization but Rs 3 added to bring it up to the level determined by applying the norms prescribed in the Circular.
- (5) More pertinently, though the SEBI’s Circular dated May 4, 2016 contemplates a refund if and when a stock exchange closes down its business; but that is a contingency which arises at the time when its business is closed and not when it is *a going concern*.
- (6) In any event, it is SEBI which is the deciding and paramount authority as to the amount, contributions, investment, utilization and use of the Core SGF.
- (7) The establishment, administration and management of the Core SGF is in due compliance with the SEBI directives with all the substantive powers such as deciding the structure, the purpose, the composition and contribution, investment of the funds as well as the utilization of the funds etc. lying fully with SEBI, including giving various directives, as SEBI deems it appropriate,

from time to time.

- (8) In view of the above, the Core SGF is considered and disclosed as a separate Fund, independent of its contributing entities and their own funds, in the financial statements. This is considered to be befitting and ascribed as a matter of accounting prudence and conservatism, ABC Ltd. has been charging the contribution made to the Core SGF to its statement of profit and loss in both the standalone and consolidated financial statements.

15. The Central Board of Direct Taxes ('the CBDT') has notified the Core SGF set up by DEF Ltd., under clause (23EE) of section 10 of the Income-tax Act, 1961 (hereinafter referred to as the 'Act'). Under clause (23EE) of section 10 of the Act, income by way of contributions received from a recognised stock exchange, a recognised Clearing Corporation and the members thereof are exempt from taxation. Further, any specified income of such Core SGF set up by a recognised clearing corporation in accordance with the Regulations is also exempt from tax under clause (23EE) of section 10 the Act. As per the above Income-tax regulations:

- The amount of contributions received and related income accumulated in the Core SGF in DEF Ltd.'s financial statements from contributions made by ABC Ltd. and members will be exempt from current taxation;
- DEF Ltd.'s own contribution into the Core SGF is tax deductible in DEF Ltd.'s standalone financial statements; and
- The SGF contribution paid by ABC Ltd. to DEF Ltd. towards Core SGF is allowed as a current tax deduction in ABC Ltd.'s standalone financial statements.

16. The querist has separately clarified the following:

- (i) CBDT has specifically notified the Core SGF set up by DEF Ltd. under clause (23EE) of section 10 of the Act. The purpose and the idea of notifying the Core SGF, according to the querist, specifically appears to be with a purpose of treating it as a separate entity independent and regardless of where it is created and who are its contributors. This understanding gets further affirmed by the fact that the Finance Act, 2017 has stipulated that every notified Core SGF is required to obtain a separate PAN and also to file a separate return of income, again independent and regardless of where it is created and who are its contributors.
- (ii) It is mandatory to maintain Core SGF as per SEBI guidelines as long as DEF Ltd. continues to carry on business as a Clearing Corporation and ABC Ltd. carries on the business as Stock Exchange. In other words, the clearing corporation and stock exchange would stand to lose their recognition by SEBI, if Core SGF Fund is closed. Hence, on a going concern basis, Core SGF cannot be closed. More importantly, though the SEBI circular dated May 4, 2016 contemplates a refund, if and when a stock exchange closes down its business, such closure is a contingency. However, till such time the Stock Exchange and /or the Clearing Corporation continues to carry on its business as a going concern, the contributions made by them to the corpus of the Core SGF cannot come back, once contributed.
- (iii) Since currently Core SGF is not a separate legal entity, the investments are held in the name of DEF Ltd. This is especially so, since, it is a regulatory

requirement to provide KYC documents, especially PAN, for such investments. While this was the situation till March 2017, going forward, post the obtaining of a separate PAN, a possibility is being explored to hold the investments pertaining to the Core SGF directly in the name of Core SGF. Nevertheless, even today, all the funds pertaining to Core SGF are maintained in separate bank account designated for the Core SGF in the books of the clearing corporation. All investments/redemptions pertaining to the funds of Core SGF are carried out from the designated bank account only. Also, all investments/funds pertaining to Core SGF are not only identified separately for accounting purposes but are also disclosed separately in the financial statements of the clearing Corporation. This is mainly due to the fact that Core SGF is completely ring-fenced at all times with all the contributing parties permanently and irrevocably losing domain and control over the funds contributed by them.

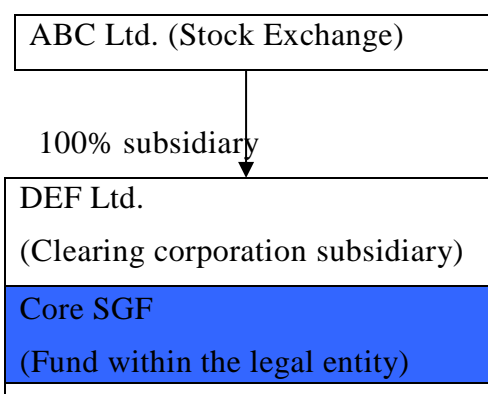
- (iv) According to the default waterfall mechanism prescribed in SEBI's Circular mentioned in paragraph 6 above, in case where the Core SGF is not sufficient to meet the settlement default, then, resources of the Clearing Corporation may be utilised only with the approval of SEBI. However, there is no such requirement for Stock Exchange. Accordingly, the resources available with DEF Ltd. may have to be utilised (post and as approved by SEBI) in the event the amounts available with Core SGF are not sufficient to meet the settlement default. However, it is important to note that ABC Ltd. is not required to utilise any of its own resources over and above the contributions already made by ABC Ltd. to the Core SGF.
- (v) The entire domain and control regarding Core SGF is with SEBI. Further, once the contributions are made to the Core SGF, the contributors completely lose domain and control over the funds and the amount contributed to the Core SGF can only be utilised for the object of the fund and cannot be utilised for any other purpose. It may, therefore, as per the querist, be considered that the Clearing Corporation manages the Core SGF in a fiduciary capacity only. It has absolutely no discretion/authority of its own to manage, utilise, invest, divest, etc. It has to strictly follow the guidelines issued by SEBI from time to time. In other words it is merely carrying out the activities, administratively, with regard to Core SGF on behalf of SEBI.

17. As per the querist, there can be two treatments for the contribution to SGF/Core SGF in the consolidated financial statements prepared under Indian Accounting Standards (Ind AS) as described in paragraphs 18 and 19 below.

18. *Option I:*

- In ABC Ltd's standalone financial statements, the company records the contribution to the Core SGF as an item of expenditure by debiting the same to the statement of profit and loss based on the understanding stated in points (1) to (8) mentioned in paragraph 14 above.
- With the same principles and understanding, the contribution towards the SGF/Core SGF is recorded as an expense in ABC Ltd.'s standalone Ind AS financial statements, as such amount meets the definition of 'provision' under Indian Accounting Standard (Ind AS) 37, 'Provisions, Contingent Liabilities and Contingent Assets', based on the following:

- there is a present obligation (legal/statutory) to transfer 25% of profits to the Core SGF maintained in another legal entity – DEF Ltd., a subsidiary of ABC Ltd.;
 - it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation by paying to DEF Ltd. (cash moves out from ABC Ltd. to DEF Ltd.); and
 - reliable estimate can be made of the amount.
- As per the Regulations, the unutilized portion of contribution into the Core SGF shall be refunded to the stock exchange only on closure of business or if stock exchange decides to avail the clearing and settlement services of another clearing corporation. In the latter case, the stock exchange will have to transfer such amount to another Clearing Corporation. The refund event i.e., winding up operations/changing Clearing corporation (i.e., DEF Ltd. in this case) is not considered virtually certain. Accordingly, no contingent asset shall be recognised.
 - The above expense recorded in ABC Ltd.’s standalone financial statements is not eliminated and continues to be recorded as an expense in ABC Ltd.’s consolidated financial statements also (including presentation as Core Settlement Guarantee Fund balance in the consolidated balance sheet separately between equity and liability – a mezzanine presentation). This is based on the premise that the contribution to the Core SGF is regulatory in nature and has restricted use and purpose i.e., the amounts of the Core SGF can be utilised for settling the obligations in the event of a default by clearing member/clearing member failing to honor its settlement obligations (trading defaults/losses).
 - Also, the company has lost its domain and control over the Fund unless it is assumed that the company is not a going concern (i.e., funds are refunded to the company on closure of business).
 - Both ABC Ltd.’s and DEF Ltd.’s contributions accumulated in the Core SGF balance will be presented as Core Settlement Guarantee Fund balance separately between equity and liability i.e., mezzanine presentation on ABC’s consolidated balance sheet.



19. *Option II:*

- a) Under Ind AS 110, ‘Consolidated Financial Statements’, consolidated financial statements are prepared keeping in view the economic entity model. This requires recording of assets, liabilities, equity, income, expenses and cash

flows of the parent and its subsidiaries as those of a *single economic entity*.

- b) Based on the above, intra-group transactions are to be eliminated in consolidated financial statements. In this regard, since ABC Ltd., DEF Ltd. and the Core SGF fund are all part of the consolidated ABC Group (in accordance with all requirements of Ind AS 110), in ABC's consolidated financial statements, the SGF contribution expense recorded by ABC Ltd. in its standalone financial statements paid/payable to DEF Ltd.'s Core SGF should be eliminated against the corresponding credit balance of Core Settlement Guarantee Fund recorded by DEF Ltd. in its standalone financial statements. This intra-group transaction does not survive in the consolidated financial statements as:
- 1) it is not an expense and liability to an entity outside the consolidated ABC Group;
 - 2) there exists no present obligating event relating to member losses on account of settlement obligations at the reporting date (trading defaults/losses) for which any provision is required. Consequently, the current liability pertaining to any such contributions payable by ABC Ltd. towards the Core SGF maintained within DEF Ltd. and appearing in ABC Ltd.'s standalone financial statements should also get eliminated in the consolidated financial statements of ABC Group. There should not be an expense or a liability payable to a consolidated entity within the Group as per Ind AS 110. This accounting in the consolidated financial statements will also be consistent with the accounting followed by DEF Ltd. in its standalone financial statements in respect of DEF Ltd.'s own share of contribution towards the Core SGF. DEF Ltd. records such contributions as an appropriation from reserves (and not an expense), since, the Core SGF is a fund within the legal entity DEF Ltd. (the Core SGF Fund is not a separate legal entity). DEF Ltd.'s accounting in its standalone financials statements is considered appropriate under Ind AS.
- c) It is also to be noted that under Ind AS, a credit balance on the balance sheet would either be classified as equity (see Ind AS 32, 'Financial Instruments: Presentation') or as a liability (see Ind AS 32, Ind AS 109, 'Financial Instruments' and Ind AS 37). There is no conceptual basis to present an item on the balance sheet between equity and liability (mezzanine) under Ind AS. For example, under Ind AS, minority interest which could have earlier been presented as a mezzanine item on the balance sheet under previous Indian GAAP, is required to be presented as non-controlling interest within equity under Ind AS.

Thus, ABC Ltd. has charged the contribution made to Core SGF to the statement of profit and loss and also reported and disclosed the Core SGF separately in its consolidated financial statements with the understanding that the Core SGF is regulatory in nature and the amount pertaining to Core SGF is required to be ring-fenced at all times from its contributors. Also, on a going concern basis, the amount contributed to the Core SGF has irreversibly and irretrievably gone out of the control of the contributors. Both ABC Ltd. and DEF Ltd. have lost domain and control over the funds once contributed by them to the Core SGF. Further, as stated above, all the powers related to the

establishment, management and administration of Core SGF and deciding on the structure, contribution, composition, investment etc. lie solely with SEBI.

There are two matters which merit attention here in relation to deferred tax accounting under Option II described in (d) and (e) below.

- d) ABC Ltd. is allowed current tax benefit in its standalone financial statements in respect of the SGF contribution expense recorded in its standalone financial statements. Since, this expense gets reversed and credited in the consolidated profit and loss, ABC Ltd. will record a corresponding deferred tax liability to the extent of related current tax benefit in the consolidated financial statements. This deferred tax liability will get reversed either if and when trading settlement defaults/losses occur and to the extent it is in respect of the said losses, the same is recognised as an expense in the consolidated statement of profit and loss (as at that time there will be no tax deduction available for such expense) or when ABC Ltd. discontinues business and the contributions are refunded to ABC Ltd. resulting in taxable income.
- e) DEF Ltd. is also allowed current tax benefit in its standalone financial statements. Based on conclusion in (d) above in case of ABC Ltd., a deferred tax liability will also be recorded for DEF Ltd.'s own contribution toward Core SGF. This deferred tax liability will get reversed either if and when trading settlement defaults/losses occur and to the extent it is in respect of the said losses, the same is recognised as an expense in the consolidated statement of profit and loss (as that time there will be no tax deduction) or when DEF Ltd. discontinues business at which time such amounts become taxable.

Based on the above, accounting treatment under Option II is as described in (f)-(j) below:

- f) Core SGF expense recorded in ABC Ltd.'s separate financial statements pertaining to its contribution paid to its subsidiary DEF Ltd. towards the Core SGF will get eliminated on consolidation (being an intra-group transaction);
- g) Both ABC Ltd.'s and DEF Ltd.'s contributions into Core SGF will be presented as a special reserve and restricted cash/investments separately in the consolidated financial statements. There would be an explanatory note in the financial statements that such special Core SGF reserve/funds can be used for specified/restricted purposes (resulting in alignment of accounting policies within the ABC group);
- h) Core SGF contributions received from clearing members will continue to be presented as current liability (as the amounts are refundable on demand) and amounts invested from such contributions will be presented as restricted cash/investments.
- i) Upon recognition of expense in the consolidated financial statements, similar amounts will be appropriated back from the special reserve to free reserve (both within equity).
- j) Deferred tax liability will be recorded in consolidated financial statements of ABC group and DEF Ltd.'s standalone financial statements to the extent of current tax benefit availed (see (g) and (h) above).

B. Query

- 20. The querist has sought the opinion of the Expert Advisory Committee on the

following issues:

- (i) Whether the accounting for contribution to Settlement Guarantee Fund/Core Settlement Guarantee Fund in the consolidated financial statements of the company ABC Ltd. as a charge to the statement of profit and loss will be correct and consistent with the accounting mentioned in Option I above.
- (ii) In case the answer to (i) above is in the negative, then, whether the company can follow the accounting as explained under Option II above i.e., elimination of expense related to contribution to SGF/Core SGF by ABC Ltd. to its subsidiary DEF Ltd. in the consolidated financial statements of ABC Ltd. under Ind AS.

C. Points considered by the Committee

21. The Committee notes that the basic issue raised in the query pertains to treatment of the contributions made by ABC Ltd. (hereinafter referred to as the 'company'/'Stock Exchange') to SGF/Core SGF in line with the Regulations prescribed by SEBI in the consolidated financial statements of the company in the context of Indian Accounting Standards notified under the Companies (Indian Accounting Standards) Rules, 2015. The Committee has, therefore, considered only this issue and has not considered any other issue that may arise from the Facts of the Case, such as, treatment of contributions in the financial statements of DEF Ltd. (hereinafter referred to as the 'subsidiary'/'Clearing Corporation'), accounting for the company's share of income of the SGF/Core SGF, if any, determination of the amount to be contributed to SGF/Core SGF, legal interpretation of and compliance with SEBI's Circulars and provisions of Income-tax Act, 1961, current and deferred tax accounting, etc. The Committee expresses its views purely from accounting angle. The Committee notes that the querist has made references to contributions to both SGF/Core SGF and makes reference to 'ring-fencing' in the case of Core SGF, which is mentioned as 'Fund within SGF'.

22. The Committee notes that the SEBI is the regulatory authority for the company, which is a recognised Stock Exchange and its subsidiary which is a recognised Clearing Corporation in the extant case and that the SEBI has prescribed the Regulations and issued some Circulars applicable for the company and its subsidiary, certain features of which are as follows:

- (i) The company is required to transfer 25% of its annual profits every year to the SGF maintained by its subsidiary, which is a Clearing Corporation. The SGF will be utilised by the recognised Clearing Corporation to settle the obligations in the event of a default by a clearing member i.e., clearing member failing to honor its settlement obligations (i.e., trading defaults/losses). The Committee notes that the legal requirement of contributing 25% of profits was subsequently amended to be subject to SEBI's directions as may be specified from time to time.
- (ii) The company, its subsidiary and members of the clearing corporation are required to contribute to MRC of the Core SGF maintained by the subsidiary, which is a Clearing Corporation. The sufficiency of the corpus of the Fund shall be tested by way of periodic stress tests prescribed.
- (iii) The company's contribution to Core SGF can be adjusted against transfer of profit by it under SGF (see (i) above).
- (iv) Against the Core SGF, no exposure is given. The Core SGF is readily and

unconditionally available to meet settlement obligations of Clearing Corporation in case of clearing member(s) failing to honour settlement obligation. The Core SGF is for each segment of the subsidiary, which is ring-fenced from defaults in other segments.

- (v) While the management of the Core SGF rests with the Defaulter's Committee/SGF utilisation Committee of the subsidiary, it is fully in compliance with the directives issued by SEBI. SEBI is the deciding and paramount authority as to the amount, contributions, investment, utilisation and use of the Core SGF.
- (vi) Unutilised portion of contributions made by the company to the Core SGF for any segment(s) will be refunded to the company only when the company decides to close down its business or decides to avail the clearing and settlement services of another Clearing Corporation for that segment(s).

From the above features of the Regulations and the Facts of the Case provided by the querist, the Committee notes that Core SGF is a Fund maintained by the company's subsidiary and is managed by a committee of the subsidiary fully in compliance with the directives of SEBI. The Core SGF is regulatory in nature and is available for restricted use and purpose. The company is required to make mandatory transfer to the Fund. The amount contributed to the Fund goes out of the control of the company. It is not refundable to the company so long it remains as a going concern. The possible event of closure of business resulting in refund from the Fund should be disregarded on 'going concern' considerations. Similarly, the possible switch over to another clearing corporation resulting in refund from the Fund is a future contingency to be disregarded. MRC is computed on a monthly basis considering all relevant factors, reflecting the quantum of risk involved.

23. From the above, the Committee is of the view that the company's contribution to the Fund represents its share of expenditure in meeting a statutory obligation. Hence, contribution to the Fund should be expensed in its stand-alone financial statements. Consequently, the said expense should be included in its consolidated financial statements also. This expense cannot be eliminated in the consolidated financial statements.

D. Opinion

24. On the basis of the above, the Committee is of the following opinion on the queries raised in paragraph 20 above:

- (i) Option of accounting for the company's contribution to Settlement Guarantee Fund/Core Settlement Guarantee Fund in the consolidated financial statements of the company i.e., ABC Ltd., as a charge to the (consolidated) statement of profit and loss will be correct.
- (ii) In view of the answer (i) above, the question (ii) does not arise.