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March 13, 2009

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All Registered Intermediaries of ISS
President / Executive Director of Participating Exchanges, Co-ordination Officers at Participating Exchanges / Regional Administrative Offices

Dear Sir,

Sub: Introduction of VAR Margin System on collaterals with effect from March 16, 2009 in NSE, BSE and FNO Segments.

This is to inform all members of ISS that with the objective to introduce a sound risk management system, ISS would like to introduce VAR Margin System on collaterals with effect from March 16, 2009. This is NSE / BSE compliance requirement which was approved by the Internal Audit Committee and the Board of Directors of ISE / ISS.

In the past ISS have applied haircut of 25% across all scrips instead of previous day closing VaR Rate as prescribed by Exchange. Few scrips get less value and other few scripts get more value. (for e.g. the scrip PFIZER the hair-cut is 8% and for the script UNITECH the hair-cut is 96% in NSE, BSE and FNO segments.) We wish to inform all our members from now on with effect from 16th March 2009, it has been decided to apply VaR rates margin on all securities lying in collaterals. Please find attached the notes on the calculation of VaR Margin for your ready reference.

We request all members to kindly take note of the above changes and incase you require any clarification you may contact the undersigned on 9323189537 or **Mr. Arun Kadam,** Trade Process Team Member (TPTM) at custody@iseindia.com or on landline 022 6794 1138..

Thanking you,

Yours faithfully,
For ISE SECURITIES & SERVICES LIMITED

Kevin M. N. Sunder
HEAD CUSTODY

Copy to
OPERATIONAL COMMITTEE MEMBERS (OCM)
Shri C. M. Cheriyan Sir, Smt. Manisha T, Shri Jagdish S, Shri Sweedin S, Shri Hirak D.

Notes on Calculation of VaR Rates from NSE

With the objective that a sound risk management system is integral to an efficient clearing and settlement system, NSE introduced for the first time in India, risk containment measures that were common internationally but were absent from the Indian securities markets.

NSCCL has put in place a comprehensive risk management system, which is constantly upgraded to pre-empt market failures. The Clearing Corporation ensures that trading member obligations are commensurate with their networth.

Risk containment measures include capital adequacy requirements of members, monitoring of member performance and track record, stringent margin requirements, position limits based on capital, online monitoring of member positions and automatic disablement from trading when limits are breached, etc.

Margin stipulation at NSE is based on the categorisation of stocks. Stocks are graded into three categories (Category I, II & III) based on the past statistics of their turnover at the exchange. Daily margin payable by members consist of the following:

1. Value at Risk Margin
2. Mark to Market Margin

Daily margin, comprising of the sum of VaR margin and mark to market margin is payable.

VaR margin is applicable for all securities in rolling settlement. All securities are classified into three groups for the purpose of VaR margin.

- For the securities listed in Group I Scrip wise daily volatility calculated using the exponentially weighted moving average methodology that is used in the index futures market and the scrip wise daily VaR would be 3.5 times the volatility so calculated.
- For the securities listed in Group II the VaR margin shall be higher of scrip VaR (3.5 sigma) or three times the index VaR, and it shall be scaled up by root 3.
- For the securities listed in Group III , the VaR margin would be equal to five times the index VaR and scaled up by root 3.

VaR margin rate for a security constitutes the following:

1. <u>Value at Risk (VaR) based margin</u>, which is arrived at, based on the methods stated above. The index VaR, for the purpose, would be the higher of the daily Index VaR based on S&P CNX NIFTY or BSE SENSEX. The index VaR would be subject to a minimum of 5%.
2. <u>Additional VAR Margin</u> : 6% as specified by SEBI.
3. <u>Security specific Margin</u> : NSCCL may stipulate security specific margins for the securities from time to time.

The VaR based margin would be rounded off to the next higher integer (For Eg: if the VaR based Margin rate is 10.01, it would be rounded off to 11.00) and capped at 100%.

The VaR margin rate computed as mentioned above will be charged on the net outstanding position (buy value-sell value) of the respective clients on the respective securities across all open settlements. The net positions at a client level for a member are arrived at and thereafter, it is grossed across all the clients for a member to compute gross exposure for margin calculation.

For example, in case of a member, if client A has a buy position of 1000 in a security and client B has a sell position of 1000 in the same security, the net position of the member in the security would be taken as 2000. The buy position of client A and sell position of client B in the same security would not be netted. It would be summed up to arrive at the member's exposure for the purpose of margin calculation.