**NATIONAL COMMODITY CLEARING LIMITED**

Circular to all Members of the Clearing Corporation
Circular No. : NCCL/CLEARING-042/2020
Date : July 21, 2020
Subject : Options in Goods - Clearing & Settlement Procedures

Reference is drawn to the Exchange Circular No. NCDEX/TRADING-036/2020 dated July 20, 2020 on Launch of Options in Goods Contract on Rapeseed – Mustard Seed, Wheat and Maize – Feed/Industrial Grade

A detailed note on operational processes pertaining to Clearing & Settlement on Options in goods is provided in the Annexure.

For and on behalf of
**National Commodity Clearing Limited**

Vidyadar Bangera
Vice President

Encl: Annexure

For further information /clarifications, please contact

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**ANNEXURE**

**CLEARING & SETTLEMENT PROCESS**

1. **Premium settlement for option contracts**

   a. Premium settlement in respect of trades in options contracts shall be settled in cash by debit/ credit of the clearing accounts of clearing members with the respective clearing bank.

   b. The premium payable or receivable value of clearing members shall be computed after netting the premium payable or receivable positions at trading member level, for each option contract, at the end of each trading day.

   c. The premium pay-in shall be effected before the start of trading on T+1 day along with pay-in of daily mark to market losses in respect of trades / positions in futures contracts. ('T' is the trade date)

   d. The Clearing Members should make the amount of funds available in their clearing account before 8:30 AM on T+1 day

   e. The pay-out of funds (Options Premium + Futures MTM) shall continue to be done as per the existing time i.e. after 10.30 AM, or as declared by the Clearing Corporation from time to time

   f. The Premium Pay-in / Pay-out obligation of the clearing member for trades in option contracts will be netted with daily MTM Pay-in / Pay-out obligation of trades / positions in futures contracts.

2. **Mark to Market**

   The options positions shall be mark to market by deducting/adding the current market value of options (positive for long options and negative for short options) times the number of long/short options in the portfolio from/to the margin requirement. Thus, mark to market gains and losses would not be settled in cash for options positions.

3. **Exercise Style**

   European Style Options which can be exercised only on the day of Expiration of the Options contract

4. **Final Settlement Price (FSP)**

   Final Settlement Price of the corresponding Futures contract.

5. **Settlement Method**

   On exercise, Option position shall result in physical Delivery of underlying commodity:-

   - Long call position shall result into a buy (commodity receivable) position
   - Long put position shall result into a sell (commodity deliverable) position



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- Short call position shall result into a sell (commodity deliverable) position
- Short put position shall result into a buy (commodity receivable) position

On expiry of Options contract, the net exercised / assigned open position across all option series and option types shall be clubbed with the open position in the underlying futures contract and the resultant long and short open positions shall be marked for delivery.

**6. Exercise Mechanism**

On expiry, following mechanism shall be adopted for exercise of the options contracts:

a. Option series having strike price closest to the FSP of the underlying shall be termed as At the Money (ATM) option series.

   This ATM option series and three option series having strike prices immediately above this ATM strike and three option series having strike prices immediately below this ATM strike shall be referred as ‘Close to the money’ (CTM) option series.

   In case the FSP of the underlying is exactly midway between two strike prices, then immediate three option series having strike prices just above FSP of the underlying and immediate three option series having strike prices just below FSP of the underlying shall be referred as ‘Close to the money’ (CTM) option series.

b. All option contracts belonging to ‘CTM’ option series shall be exercised only on ‘explicit instruction’ for exercise by the long position holders of such contracts failing which they will expire worthless.

c. All In the money (ITM) option contracts, except those belonging to ‘CTM’ option series, shall be exercised automatically, unless ‘contrary instruction’ has been given by long position holders of such contracts for not doing so and in that case shall expire worthless.

d. All Out of the money (OTM) option contracts, except those belonging to ‘CTM’ option series and exercised by the long position holders, shall expire worthless.

e. All exercised contracts within an option series shall be assigned to short positions in that series in a fair and non-preferential manner.

**Examples**

The following are the examples for identification of ITM, CTM, ATM and OTM strikes as per the Final Settlement price.

| **Strike Interval** | **50** |
|---|---|
| **Final Settlement Price** | **3780** |
| **For CALL Options** | |
| **Strike Price** | **Strike Type** |
| 3600 | ITM |

| **Strike Interval** | **50** |
|---|---|
| **Final Settlement Price** | **3850** |
| **For CALL Options** | |
| **Strike Price** | **Strike Type** |
| 3600 | ITM |

| **Strike Interval** | **50** |
|---|---|
| **Final Settlement Price** | **3825** |
| **For CALL Options** | |
| **Strike Price** | **Strike Type** |
| 3600 | ITM |

| | |
|---|---|
| 3650 | CTM |
| 3700 | CTM |
| 3750 | CTM |
| **3800** | **ATM** |
| 3850 | CTM |
| 3900 | CTM |
| 3950 | CTM |
| 4000 | OTM |
| 4050 | OTM |
| | |
| **For PUT Options** | |
| **Strike Price** | **Strike Type** |
| 3600 | OTM |
| 3650 | CTM |
| 3700 | CTM |
| 3750 | CTM |
| **3800** | **ATM** |
| 3850 | CTM |
| 3900 | CTM |
| 3950 | CTM |
| 4000 | ITM |
| 4050 | ITM |

| | |
|---|---|
| 3650 | ITM |
| 3700 | CTM |
| 3750 | CTM |
| 3800 | CTM |
| **3850** | **ATM** |
| 3900 | CTM |
| 3950 | CTM |
| 4000 | CTM |
| 4050 | OTM |
| | |
| **For PUT Options** | |
| **Strike Price** | **Strike Type** |
| 3600 | OTM |
| 3650 | OTM |
| 3700 | CTM |
| 3750 | CTM |
| 3800 | CTM |
| **3850** | **ATM** |
| 3900 | CTM |
| 3950 | CTM |
| 4000 | CTM |
| 4050 | ITM |

| | |
|---|---|
| 3650 | ITM |
| 3700 | CTM |
| 3750 | CTM |
| 3800 | CTM |
| 3850 | CTM |
| 3900 | CTM |
| 3950 | CTM |
| 4000 | OTM |
| 4050 | OTM |
| | |
| **For PUT Options** | |
| **Strike Price** | **Strike Type** |
| 3600 | OTM |
| 3650 | OTM |
| 3700 | CTM |
| 3750 | CTM |
| 3800 | CTM |
| 3850 | CTM |
| 3900 | CTM |
| 3950 | CTM |
| 4000 | ITM |
| 4050 | ITM |

**A table giving gist of exercise procedure under different option series is given below:-**

| Series | Exercise procedure | Effect |
|---|---|---|
| **ITM (Other than CTM)** | Positions shall be exercised automatically | • Positions would get exercised and shall be clubbed with the open position in the underlying futures contract and the resultant long and short open positions shall be settled through delivery of goods.<br>• Difference between FSP and strike price shall be cash settled on T+1 day and form part of the MTM pay-in and pay-out. |
| | ITM long position holder can give contrary instruction | • No positions will get exercised<br>• Expire worthless |

| | | |
|---|---|---|
| **CTM (other than ITM) / CTM (other than OTM)** | No position shall be exercised. An 'explicit instruction' shall be placed for exercise of Options by the long position holders | If the option holder do not give the 'explicit instruction' for exercise<br>● No positions will get exercised<br>● Expire worthless |
| | | If the option holder gives the 'explicit instruction' for exercise<br>● Positions would get exercised and shall be clubbed with the open position in the underlying futures contract and the resultant long and short open positions shall be settled through delivery of goods<br>● Difference between FSP and strike price shall be cash settled on T+1 day and form part of the MTM pay-in and pay-out. |
| **OTM (Other than CTM)** | Positions shall not be exercised | ● All positions will expire worthless |

7. **Marking Instruction for exercising the positions**

   a. The members can mark the instruction to / not to exercise through NCFE post close of trading session of option contract on expiry day
   b. Instruction can be marked by holder of the options contract i.e. long position holder
   c. For ITM option series except CTM, members shall give instruction for the quantity which is **not intended to be exercised**

| Option Status | Position | Contrary instruction (Instruction not to exercise) | Effect |
|---|---|---|---|
| ITM | 100 | 30 | Partial Instruction – Balance 70 quantity shall be exercised |
| ITM | 100 | - | No Instruction – 100 quantity shall be exercised |
| ITM | 100 | 100 | Full Instruction – No positions will get exercised |



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For CTM option series, members shall give instruction for the quantity which is **intended to be exercised**

| Option Status | Position | Explicit instruction (Instruction to exercise) | Effect |
|---|---|---|---|
| CTM | 100 | 30 | Partial Instruction - 30 quantity shall be exercised |
| CTM | 100 | - | No Instruction - No positions will get exercised |
| CTM | 100 | 100 | Full Instruction - 100 quantity shall be exercised |

A user manual for marking the instruction shall be available for download in NCFE

**8. Assignment Process**

a. The long positions in options contracts shall be assigned to short positions in the same contract.
b. The total quantity to be exercised contract shall be computed as per exercise mechanism
c. The total quantity to be exercised in an options contract will be divided by the total long open positions in the options contract to determine the "exercise ratio".
d. The short position of each client in the options contract of same series will be multiplied by the exercise ratio to determine the pro-rata quantity for assignment.
e. Quantity equal to the pro-rata quantity rounded down to the nearest multiple of futures lot size will be assigned to short position holders in the first round of assignments.
f. If the total long quantity to be exercised has not been assigned in this first assignment round then a second assignment round will be carried out to assign the remaining quantity (i.e., the quantity remaining after subtracting the quantity assigned in the first round from the total long quantity to be exercised)
g. The remaining quantity will be assigned one lot at a time in descending order from the short positions with the largest remaining pro-rata quantity to the short position with the smallest remaining pro-rata quantity.
h. In the event that two or more short positions has equal remaining pro-rata quantity, and there is an insufficient quantity to assign to all such short positions, then a random number will be used by systems to determine assignment.

**9. Delivery Request**

On expiry of Options contract, the net exercised / assigned open position across all option series and option types shall be clubbed with the open position in the underlying futures contract and the resultant long and short open positions shall be marked for delivery. The Buyers and the Sellers need to give their location preference through Web NCFE system provided by the Clearing Corporation. If the Sellers fail to give the location preference, then the allocation to the extent of his open position will be allocated to the base location



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**10. Delivery Pay-in / Pay-out**

On Expiry (E)+2 basis in accordance with the settlement calendar issued by the Clearing Corporation periodically. The procedure specified for pay-in and pay-out of underlying commodity futures contract shall be applicable for options.

**11. Non-fulfilment of settlement obligation**

Non-fulfillment of either the whole or part of the settlement obligations will be treated as a violation of the Rules, Bye-Laws and Regulations of NCCL and will attract penal charges as stipulated by NCCL from time to time. In addition and without prejudice to the foregoing, NCCL may, within such time as it may deem fit withdraw any or all of the membership rights of Clearing Member including the withdrawal of trading facilities of all Trading Members clearing through such Clearing Member's, without any notice.



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