# CIRCULAR

**F. No. 286/IFSCA/PM(CMD-DMIIT)/2021/4** **March 31, 2022**

To,

**All Stock Exchanges in the International Financial Services Centre (IFSC)**

Dear Sir/Madam,

**Sub: Guidelines for Liquidity Enhancement Scheme**

Liquidity in the listed securities is a crucial determinant of success of Stock Exchanges in any jurisdiction. However, in a nascent stage of a jurisdiction, attracting liquidity on a Stock Exchange may require certain incentives for market participants. To facilitate this, the Authority has decided to review the Liquidity Enhancement Scheme being operated in IFSC.

**Introduction of Liquidity Enhancement Schemes**

1. The Stock Exchange may introduce liquidity enhancement schemes in any security/ listed products subject to the following:

   a) The scheme shall have the prior approval of the Governing Board of the Stock Exchange and its implementation and outcome shall be monitored by the Board at quarterly intervals.
   b) The scheme shall be objective, transparent, non-discretionary and non-discriminatory.
   c) The scheme shall specify the incentives available to the market makers / liquidity providers and such incentives may include discount in fees, adjustment in fees in other segments, cash payment or issue of shares, including options and warrants.
   d) The scheme shall not compromise market integrity or risk management.
   e) The effectiveness of the scheme shall be reviewed by the Stock Exchange every six months and the Stock Exchange shall submit half-yearly reports to IFSCA.
   f) The scheme, including any modification therein or its discontinuation, shall be disclosed to the market atleast 15 days in advance.

g) Outcome of the scheme (incentives granted and volume achieved – market maker wise and security wise) shall be disseminated monthly.
h) The scheme shall comply with all the relevant laws.

**Securities eligible for Liquidity Enhancement Schemes**

2. The Stock Exchanges shall formulate their own benchmarks for selecting the securities for liquidity enhancement with the broad objective of enhancing liquidity in illiquid securities.

   a) The Stock Exchanges shall introduce liquidity enhancement schemes on any security for a maximum period of five years. Once the scheme is discontinued, the scheme can be re-introduced on the same security provided it is less than the five year period since the introduction of scheme on that security.

   b) Further, a Stock Exchange may introduce liquidity enhancement schemes in securities where liquidity enhancement scheme has been introduced in another Stock Exchange. Such schemes cannot be continued beyond the period of liquidity enhancement schemes of the initiating Stock Exchange.

   c) The list of securities eligible for liquidity enhancement shall be disseminated to the market.

**Market Integrity**

3. The Stock Exchange shall ensure the following:

   a) The Stock Exchange shall have systems and defined procedures in place to monitor collusion between stock brokers indulging in trades solely for seeking incentives and prevent payment of incentives in such cases.
   b) Incentives shall not be provided for the trades where the counterparty is self, i.e., same Unique Client Code (UCC) is on both sides of the transaction.
   c) Any violations of clauses in this para shall be viewed most seriously.

**Market maker / liquidity enhancer**

4. The exchange shall prescribe and monitor the obligations of liquidity enhancers (liquidity provider, market-maker, maker-taker or by whatever name called)

a) All market maker / liquidity enhancer orders / trades should be identifiable by the Stock Exchange
b) A conflict of interest framework shall be put in place by the Stock Exchange for the liquidity enhancement scheme. Such a framework shall provide for obligation on the part of the market maker / liquidity enhancer to disclose any conflict of interest while participating in the scheme. The same shall be disclosed by the Stock Exchange on their website.

5. The Stock Exchange shall create a reserve specifically to meet incentives/expenses of the Liquidity Enhancement Scheme, based on the normative study of the LES in the domestic market and such reserves shall not be included in the calculation of net worth.

6. The Stock Exchanges are directed to:

a) take necessary steps to put in place systems for implementation of the circular, including necessary amendments to the relevant byelaws, rules and regulations;
b) bring the provisions of this circular to the notice of the stock brokers and also disseminate the same on its website;
c) communicate to IFSCA the status of implementation of the provisions of this circular.

7. This circular is issued in exercise of powers conferred by section 12 of the International Financial Services Centres Authority Act, 2019 to develop and regulate the financial products, financial services and financial institutions in the International Financial Services Centres.

8. A copy of this circular is available on the website of the International Financial Services Centres Authority at www.ifsca.gov.in

**Yours faithfully,**

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