भारतीय प्रतिभूति और विनिमय बोर्ड
Securities and Exchange Board of India

CIRCULAR

SEBI/HO/MIRSD/MIRSD-PoD-1/P/CIR/2023/187 **December 12, 2023**

To,
Stock Brokers through recognized Stock Exchanges
Depository Participants through recognized Depositories
Clearing Members through recognized Clearing Corporations

Dear Sir/Madam,

Subject: Upstreaming of clients' funds by Stock Brokers (SBs) / Clearing Members (CMs) to Clearing Corporations (CCs)

1. With a view to safeguard clients' funds placed with Stock Brokers (SBs) / Clearing Members (CMs), SEBI, vide circular no. SEBI/HO/MIRSD/MIRSD-PoD-1/P/CIR/2023/084 dated June 08, 2023, and vide circular no. SEBI/HO/MIRSD/MIRSD-PoD-1/P/CIR/2023/110 dated June 30, 2023 (collectively hereinafter referred to as "June Circulars"), had specified the framework requiring SB/CMs to upstream (i.e. placed with) clients' funds to CCs.

2. Representations have been received from various stakeholders viz. stock brokers, and Brokers' associations citing certain operational difficulties in implementation. In order to address the issue, SEBI advised the industry associations to consult with MIIs under the aegis of Broker's Industry Standards Forum (ISF) and submit a proposal to SEBI so that the principle of upstreaming is complied with and operational difficulties are suitably addressed.

3. The recommendations made by ISF have been considered by SEBI and accordingly as a step towards ease of doing business, the revised framework is specified below.

4. Principle: SBs/CMs shall upstream all the clients' clear credit balances to CCs on End of Day (EOD) basis. Such upstreaming shall be done only in the form of either cash, lien on Fixed Deposit Receipts (FDRs) created out of clients' funds, or pledge of units of Mutual Fund Overnight Schemes (MFOS) created out of clients' funds.

A. Receipt/payment of funds by SBs and CMs from/to their clients:

I. Clause 15.3.2.1 of SEBI's "Master Circular on Stock Brokers" dated May 17, 2023 mandates stock brokers to maintain designated client bank account(s) ("Name of

SB/CM - Client Account") to receive/pay funds from/to their clients. The nomenclature of all such accounts shall be changed to either of the following two categories of bank accounts:

a. Up Streaming Client Nodal Bank Account (USCNBA): SB/CM shall receive clients' funds in USCNBA. The nomenclature for such accounts shall be "Name of the SB/CM – USCNB account".

b. Down Streaming Client Nodal Bank Account (DSCNBA): Payment to clients shall be done only from DSCNBA account. The nomenclature for such accounts shall be "Name of the SB/CM – DSCNB account".

II. In addition, CMs, who clear trades for other SBs, shall only use the designated bank account(s) maintained with the nomenclature "Name of the CM –TM prop account" to receive/pay proprietary funds from/to stock brokers.

III. Payment to Clients: The clients may request SBs/CMs to release funds at any time during the day. The processing of such release requests shall be as per respective risk management practices of SB/CMs. All payment requests of the client received on a day shall be processed on or before the next settlement day. In cases, where the payment request is not processed on the same day, SB/CMs need to ensure that the funds of the client are placed with CC in terms of this circular.

B. Upstreaming via FDRs created out of clients' funds:

I. FDRs created out of clients' funds by SBs/CMs shall satisfy the following conditions:

a. The FDR shall be created only with banks which satisfy the CC's exposure norms as specified by CCs/SEBI from time to time.
b. FDRs shall be created only from 'Up Streaming Client Nodal Bank Account (USCNBA)'.
c. Such FDRs shall necessarily be lien-marked to one of the CCs at all times, and CCs shall have explicit precedence on the FDR funds over every other stakeholder, including over the bank providing the FDR.
d. The tenor of such FDRs shall not be more than one year and one day; and the FDRs should be pre-terminable on demand.
e. The principal amount of the FDR shall remain protected throughout the tenure, even after accounting for all possible pre-termination costs.
f. SBs/CMs shall not avail any funded or non-funded banking facilities based on FDRs created out of clients' funds.

II. It is clarified that existing FDRs (created out of clients' funds and having tenor of more than one-year) created prior to June 30, 2023 shall be allowed to be grandfathered till maturity. Such FDRs at the time of renewal shall meet the conditions specified at clause 4.B.I of the circular.

C. Upstreaming via pledge of units of Mutual Fund Overnight Schemes (MFOS):

I. Units of Mutual Fund Overnight Schemes (MFOS) is a new avenue being made available to SBs/ CMs to deploy client funds into. MFOS ensures minimal risk transformation of client funds (that are withdrawable on demand) available with SBs/ CMs because of overnight tenure and exposure to only risk-free government securities.

II. SBs/CMs shall ensure that client funds are invested only in such MFOS that deploy funds into risk-free government bond overnight repo markets and overnight Tri-party Repo Dealing and Settlement (TREPS). Such MFOS units should be in dematerialized (demat) form, and must necessarily be pledged with a CC at all times.

III. SBs/CMs shall maintain a dedicated demat account (hereinafter referred to as "Client Nodal MFOS Account") for subscription/ redemption of MFOS units. The depositories shall allow subscription/redemption transactions only in the said account.

IV. From "Client Nodal MFOS Account", SBs/CMs shall provide MFOS units as collateral to the CC. While providing the units as collateral, SBs/CMs shall identify the end clients. In order to implement the same, a pledge shall be created from the Client Nodal MFOS account to SB/CM margin pledge account of the SB/CM. The SB/CM shall further repledge the same to CC using the existing pledge re-pledge mechanism.

V. Clause 15.3.2.3 of SEBI's "Master Circular on Stock Brokers" dated May 17, 2023 mandates stock brokers to maintain demat accounts under 5 defined categories. The said clause of master circular is being modified to include 'Client Nodal MFOS Account' as sixth category of permissible demat account that can be maintained by stock brokers.

5. To improve operational efficiency and reduce transaction costs, CCs shall build a mechanism for utilization of surplus unutilized collateral (i.e. collateral in excess of margin blocked) lying with CC in cash form, towards fund pay-in requirements across segments.

6. Further, to improve operational efficiency and to reduce costs, CCs shall also facilitate a mechanism to adjust the margin blocked in the form of cash, towards client fund pay-in obligations. As CCs are in the process of evolving such a mechanism since issuance of June Circulars, the same shall be made available by January 01, 2024.

Eligibility of bank instruments as collateral:

7. The bank instruments provided by clients as collateral (i.e. client FDRs and BGs) cannot be upstreamed to CCs, and they shall be ineligible to be accepted as collateral in any segment of securities market.

8. However, in the interest of encouraging and development of hedging in the commodity derivatives market, it has been decided to allow Bank guarantees provided only by non-individual clients, based on certain terms and conditions. Such clients shall provide a declaration and underwriting that they shall have no recourse to SEBI or exchanges in case of wrongful invocation of such BGs by SB/CM. These BGs shall bear a condition that on invocation, the moneys shall be credited only to the (USCNBA) account and thereafter upstreamed to the CC. The other terms and conditions are mentioned in the **Annexure A**. The CCs are at liberty to apply stricter conditions other than those specified based on their risk assessment.

9. The cut-off times for upstreaming of clear credit balance of clients shall be determined by the CCs in consultation with ISF. Any clear credit balance that could not be upstreamed to CCs due to receipt of funds from clients beyond cut-off time shall necessarily remain in UNSCBA until it is upstreamed to CC on the next day.

10. The provisions of this framework shall not be applicable to bank-CMs (including Custodians that are banks), and for proprietary funds of SBs/CMs in any segment and SB's proprietary funds deposited with CM in the capacity of a client.

11. This revised framework supersedes the framework issued by SEBI in June Circulars.

12. The provisions of this circular shall come into force with immediate effect.

Monitoring mechanisms

13. The stock exchanges, depositories, and clearing corporations are directed to:

a. bring the provisions of this circular to the notice of stock brokers, depository participants, and clearing members, as the case may be, and also disseminate the same on their websites;
b. jointly issue the following within 15 days from the date of issuance of this circular
   i. operational guidelines in consultation with relevant stakeholders;
   ii. an SOP for monitoring the implementation of provisions of this circular (including determination of cut-off times) and
   iii. a penalty structure for non-compliance;
c. make amendments to the relevant bye-laws, rules and regulations for the implementation of the above provisions; and
d. communicate to SEBI, the status of the implementation of the provisions of this circular in their monthly development report.

14. This circular is issued in exercise of powers conferred under Section 11(1) of the Securities and Exchange Board of India Act, 1992 read with Regulation 30 of SEBI (Stock Brokers) Regulations, 1992 and Regulation 51 of Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2018, to protect the interests of investors in securities and to promote the development of, and to regulate the securities markets.

Yours faithfully,

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Annexure A

Eligible clients:

1. Only non-individual clients shall be allowed to give BGs as margins, specifically for commodities segment.

2. Net worth of such clients should be at least Rs. 1000 crores. If the net worth of the client is less than Rs. 1000 crores and client is a part of a group company of a MNC group or large conglomerate in India and that MNC or large conglomerate has Ultimate Beneficial Ownership of more than 50% in the concerned client, then the net worth of the MNC group as a whole or the net worth of the large conglomerate can be considered which should be minimum Rs. 5000 crores.

Eligibility conditions for BGs

3. Only Banks approved by CCs shall be considered for issuance of such BGs.

4. BG terms and conditions should clearly mention the Upstreaming Client Nodal Bank Account (USCNBA) bank account number where the funds shall be credited in case of invocation by SB/CM.

5. In the event of invocation of BG, the funds shall be credited only to USCNBA bank account of the SB/CM and the funds shall be up-streamed on the same day to CC.

6. SB/CM shall mandatorily inform the CC at the time of invocation of BG.

7. SB/CM cannot accept BGs as margins from the above mentioned clients in excess of 25% of its net worth.

Declaration and undertaking to be given by clients

8. CFO / COO / CEO / MD of such clients should give an undertaking to the Member at the time of giving BG as margins:

    a. We agree to issue the BG lien in favour of trading member __________ for trading in capital markets for client code _______ as per the contractual arrangement with the said trading member.

    b. We declare that we clearly understand that in case trading member wrongly invokes the BG, we shall not have any recourse to Exchange or SEBI to the extent of BG amount and shall not be compensated in any manner from Investor Protection Fund.

<u>Other conditions</u>

9. SB/CM shall put its own funds with CC to the extent of BG amount towards the margin requirements of these clients.

10. SB/CM cannot use borrowed funds for this purpose. Trading member shall give auditors certificate on half yearly basis to CC in this regard.

As mentioned in para 5 of the circular, the CCs are at liberty to apply stricter conditions other than those specified above based on their risk assessment.