

CIRCULAR

SEBI/HO/MIRSD/MIRSD-PoD-1/P/CIR/2023/84

June 08, 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. SEBI, through various circulars issued from time to time, has given necessary directions/guidelines to stock brokers (SBs)/clearing members (CMs), to ensure orderly functioning of the securities market and to protect the interest of investors in securities market.
2. In this regard, with a view to safeguard clients' funds placed with SBs/CMs, it has been decided to require the upstreaming of all client funds received by SBs/CMs to the Clearing Corporations (CCs).
3. As per the framework, no clients' funds shall be retained by SBs/ CMs on End of Day (EoD) basis. The clients' funds shall all be upstreamed by SB/ CMs to CCs only in the form of either cash, lien on FDR (subject to certain conditions enumerated below), or pledge of units of Mutual Fund Overnight Schemes (MFOS). The details of the framework are as follows:

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

1. FDRs created by SBs/ CMs out of clients' funds shall be allowed only under the following conditions:
 - a. SBs/ CMs may create FDRs out of clients' funds only with those banks which satisfy the CC's exposure norms as specified by SEBI or CCs from time to time.
 - b. Every FDR created out of clients' funds shall necessarily be lien-marked to one of the CCs at all times.
 - c. Through this lien, CCs shall have explicit precedence on the FDR funds over every other stakeholder, including over the bank providing the FDR.

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- d. The tenure of such FDRs shall not be more than one year and the FDR 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.

B. 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.

C. Receipt/payment of funds by SBs and CMs from/to their constituents:

- I. Other than the FDRs (liened to CCs) and MFOS (pledged to CCs), any remaining client funds with SBs/ CMs shall be upstreamed to a CC before a stipulated cut-off time.
- II. 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 constituents. 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 for further upstreaming it to the CCs. 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 should be done only from DSCNBA account post receiving of funds from CC/CM same day and any balance left in the account post cutoff time should be transferred to USCNBA for further upstreaming it to the CCs. The nomenclature for such accounts shall be "Name of the SB/CM – DSCNB account".
- III. 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.
- IV. Upstreaming of funds: Funds received on a given day by SBs shall be transferred to CMs, and by CMs to the CC any time during the day, but not later than the respective cutoff times. The respective cutoff times for upstreaming are as follow:

Sr. No.	Particular	Cutoff time
1	CM upstreaming cutoff time	To be decided by CC – not earlier than 6:00 PM
2	SB upstreaming cutoff time	To be decided by CM – not earlier than 1 hour prior to CM upstreaming cutoff time

- V. To ensure that no residual client funds remain with SBs/CMs, they shall not accept any fresh client funds from 30 minutes before the SB upstreaming cutoff time.
- VI. Downstreaming of funds: The clients may request release of funds to SBs/CMs at any time during the day. The processing of such release requests shall be as per respective risk management practices of SB/CMs. Subject to such validations, the SBs/CMs shall provide the requested funds to the client by requesting for release of cash collateral from the CCs. The respective cutoff times for down-streaming are as under:

Sr. No.	Particular	Cutoff time
1	CM release request cutoff time	To be decided by CC – not earlier than 3:00 PM
2	SB release request cutoff time	To be decided by CM – not earlier than 30 minutes prior to CM release request cutoff time
3	Client release request cutoff time	To be decided by SB – not earlier than 30 minutes prior to SB release request cutoff time

- VII. For release requests received beyond this cutoff time by CCs/CMs/SBs, the payments shall be made on the next settlement day.
- VIII. The release requests received from the clients before “client release request cutoff time” must be processed the same day. Further, such funds received from the CC must either be paid out to the clients on the same day or upstreamed back to the CC on the same day.
- IX. The SBs/CMs may seek withdrawal of client funds from CCs only under following scenarios:
- Client unpaid securities obligations / MTF Obligations
 - Loss due to sale of unpaid securities
 - Penalties
 - Statutory levies (STT / Stamp Duty / SEBI Turnover Fee)
 - Brokerage (including exchange transaction fee)
 - Other charges (DP charges, etc.)
 - Funds to be released to client on account of regulatory requirements such as running account settlement
 - Funds withdrawal request from client

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SBs/CMs shall provide reconciliation statements to stock exchanges/CCs, as may be required by stock exchanges and CCs. Stock exchange/ CCs shall put in place an appropriate reporting mechanism for SBs/CMs for the above mentioned scenarios. The withdrawal request received from SB/CM for point no (a) to (f) above shall be transferred from CC to CM settlement account and from there to CM/SB own account. For release request made for point (g-h) above, funds shall mandatorily be transferred to designated "DSCBA" account for onward payments only to clients.

Clause 15.4.4.2 of SEBI's "Master Circular on Stock Brokers" dated May 17, 2023 stands rescinded to give effect to above-mentioned provisions.

- X. The CC shall endeavor to release the cash as soon as possible, but within two hours from the time requested.
- XI. A schematic representation of flow of funds under the instant framework is enclosed as **Annexure-A** of the circular.
4. 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.
5. 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. Such mechanism shall be provided by CCs by 1st January 2024.
6. 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.
7. The provisions of this circular shall come into effect from July 01, 2023.

Monitoring mechanisms

8. The stock exchanges and CCs shall create an SOP for monitoring the implementation of provisions of this Circular and put in place a uniform penalty structure for non-compliance.
9. The stock exchanges, depositories, and clearing corporations are directed to:

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- 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. make amendments to the relevant bye-laws, rules and regulations for the implementation of the above provisions;
 - c. communicate to SEBI, the status of the implementation of the provisions of this circular in their monthly development report and
 - d. monitor compliance of this circular and submit a compliance report to SEBI in this regard by August 31, 2023.
10. This circular is issued in exercise of powers conferred under Section 11(1) of the Securities and Exchange Board of India Act, 1992, to protect the interests of investors in securities and to promote the development of, and to regulate the securities markets.

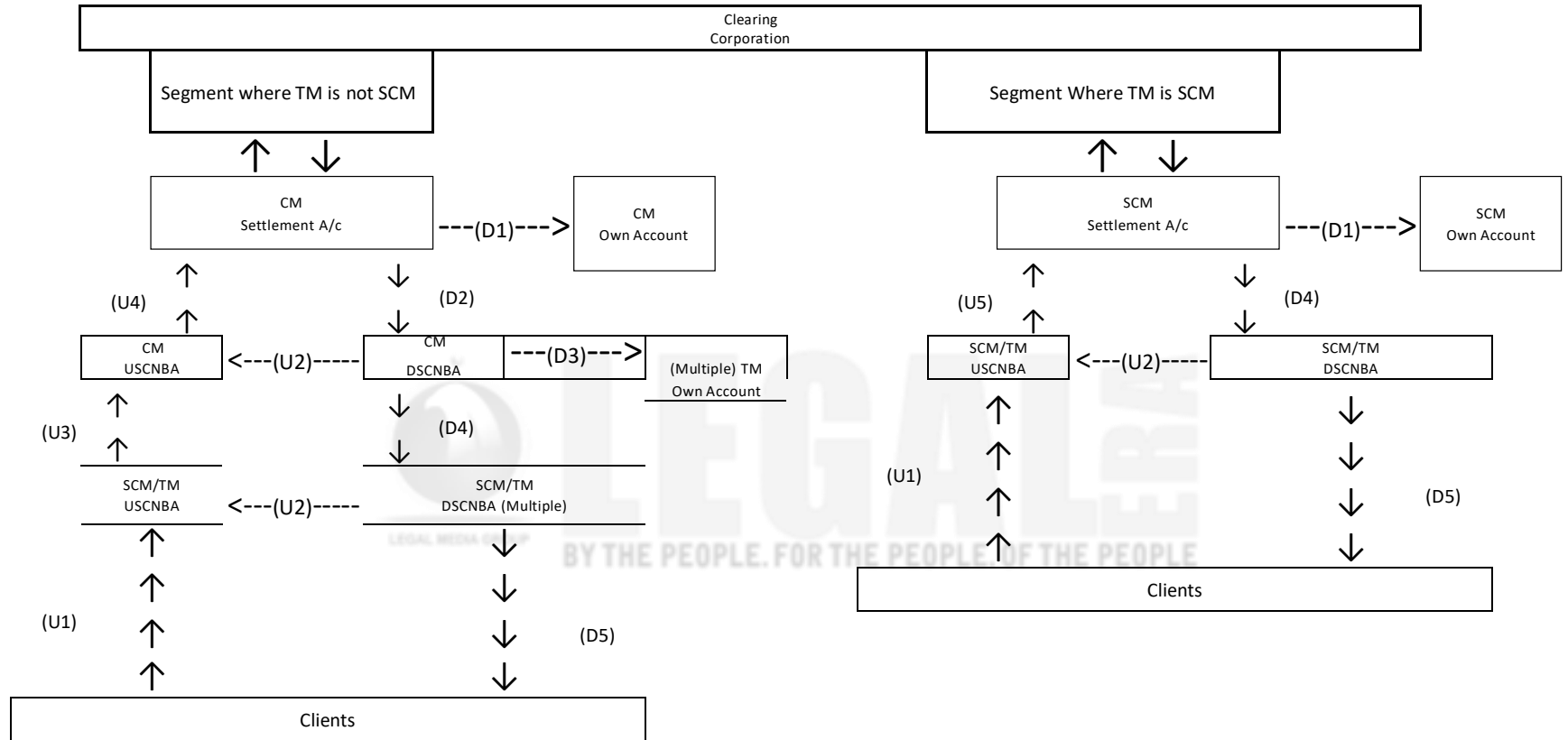
Yours faithfully,



LEGAL
BY THE PEOPLE. FOR THE PEOPLE. OF THE PEOPLE.

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Annexure-A



Notes:

Upstreaming

- (U1) Clients funds shall be received only to Designated Bank Account "USCNBA".
- (U2) Balance left in the DSCNBA post cutoff time should be transferred to USCBA for further upstreaming it to the CCs
- (U3) Funds received in TMs USC NBA will have to be transferred to CMs USCBA only during the day, but not later than the stipulated cutoff times; this step will not be applicable in case of SCM

(U4) Funds received in CM USCNBA will have to be transferred to CC only via CM Settlement account during the day, but not later than the stipulated cutoff times

Downstreaming

(D1) Withdrawal of funds from CC received in Settlement A/c other than client payables shall only be transferred to Member's OWN account (Dues of clients to Member)

(D2) Withdrawal of funds received in Settlement A/c from CC by CM towards TM payables shall only be transferred to Clearing Member's DSCNBA account; this step will not be applicable in case of SCM

(D3) Withdrawal of funds from CM DSCNBA other than client payables shall only be transferred to Trading Member's OWN account (Dues of clients to Member); this step will not be applicable in case of SCM

(D4) Withdrawal of funds from CM DSCNBA towards client payables of TM shall only be transferred to Trading Member's DSCNBA account

(D5) Payout shall be made to clients from TM DSCNBA account only based on the request received before cut off time

