

Compliance and Audit of Depository Participant

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Legal Framework

- Depositories Act, 1996
- SEBI (Depositories & Participants) Regulations, 1996
- Circulars issued by SEBI
- Policy / Operating Instructions issued by Depository
- Circulars / Communiqués issued by NSDL/CDSL
- Prevention of Money Laundering Act, 2002 (PMLA)

Regulatory Pronouncements for Audits

- **Re. CDSL**

- Concurrent Audit: Vide communiqué no. 721 dated July 11, 2006 and updated through subsequent communiqués
- Internal Audit: Latest format prescribed vide communiqué no.3626 dated April 16, 2013.

- **Re. NSDL**

- Concurrent Audit: Vide Circular no. NSDL/POLICY/2006/0021 dated June 24, 2006 and updated through subsequent circulars.
- Internal Audit: Latest format prescribed vide circular no. NSDL/POLICY/2013/0068 dated May 07, 2013.

Concurrent Audit - Scope and Sample

Area	Sample prescribed by Depository
Account Opening	100%
Account Modification	100%
-Change of address or name (Only in CDSL)	
- Power of Attorney	
Account Closure initiated By DP	100%
Issue of Instruction Slips	100%
Execution of Instruction Slips	At least 25%
Investor Grievances Redressal received by DP	100%
-Transmission	100%
- Transaction statement	

Internal Audit - Scope and Sample

- Internal Audit to be conducted on sample basis for following areas:
 - Dematerialisation / Rematerialisation
 - Account closure initiated by client
 - Compliance with PMLA guidelines, 2002.
 - Review of out-sourced activities
 - Service Centers / Branches
 - Billing to clients
 - System Areas
 - Compliance to previous internal audit/inspection reports
 - Other Areas
 - Pledge / Hypothecation
 - Forms used by DP
 - POA

How to Select Sample?

- Sample to be selected based on size of operations, state of internal control and confidence gained during concurrent audit.
- Sample should represent all types of transactions handled by DP.
- Sample to be increased, in case of any procedural lapses observed.
- Sample to cover transactions affected by recent regulatory change.
- Periods of extraordinary events in stock market can be selected as sample
- Areas having penalty history should be focused.

Account Opening – Documentation (Individual)

Know Your Client (KYC)

- Proof of Identity (POI) - driving license, voter ID etc.
- Proof of address (POA) - Telephone bill/Electricity bill etc.
 - Mobile bills not allowed
 - not more than 3 month old
 - 3 months to be calculated from data of submission of valid documents to DP.

Account Opening - Documentation

- If correspondence address is different from permanent address, proof is submitted for the same
- Correspondence address can be in the name of investor or third party but Permanent address is of the investor.
- 'Verified with Original' stamp is affixed by DP official after verification of original documentation
- Photocopies of KYC documents are self attested by investor

Account Opening – Documentation...

In- person Verification (IPV)

- In person verification by stock broker, holding or subsidiary, company is allowed. The IPV carried out by one SEBI registered intermediary can be relied upon by another intermediary
- IPV is carried out for individuals, partners in case of partnership firm, karta in case of HUF, trustees in case of trust.

In person verification through Web camera is allowed

- 'Verified in person' stamp is affixed and Employee Id and Signature of official is mentioned under DP stamp
- Attachment of separate sheet to the KYC Application Form or affixing stickers on the KYC Application Form for recording of IPV details are not allowed

Account Opening – Documentation...

Permanent Account Number (PAN)

- PAN is verified from income tax website.
- 'PAN Verified' stamp is affixed on verification.
- PAN card copy is self attested by client, including Promoters/Partners/Karta/Trustees and whole time directors and persons authorized to deal in securities on behalf of company/firm/Trust.
- In case of married female and voluntary name change, PAN card is in new name.
- In case of minor mismatch in name, other due diligence is carried out and other documentary evidence supporting the veracity is obtained.
- Employee Id and Signature of DP official is mentioned under DP stamp
- In case of HUF, Partnership Firm, Unregistered/ Private Trust etc., although the account is opened in the name of karta, partner(s), trustee(s) etc. but PAN of HUF, Partnership Firm, Unregistered/ Private Trust etc. is captured

Account Opening – Documentation...

In case of Corporate entities in addition to POI and POA of the company, following documents are obtained

- Copy of the balance sheets for the last 2 financial years (to be submitted every year)
- Copy of latest share holding pattern(to be submitted every year)
- Photograph, POI, POA, PAN and DIN numbers of whole time directors/two directors in charge of day to day operations.
- Photograph, POI, POA, PAN of individual promoters holding control
- Copies of the MoA, AoA and certificate of incorporation
- Copy of the Board Resolution
- Authorized signatories list with specimen signatures

Account Opening – Documentation...

In case of Partnership Firm / Trust

- Copy of the balance sheets for the last 2 financial years (to be submitted every year).
- Certificate of registration (for registered partnership firms /Trusts).
- Copy of partnership / Trust deed.
- Authorized signatories list with specimen signatures / List of trustees certified by managing trustees/CA.
- Photograph, POI, POA, PAN of Partners / Trustees.
- LLP Client's Account is opened under the Type 'Body Corporate' and sub - type 'Limited Liability Partnership'

Account Opening – Documentation...

Hindu Undivided Family (HUF)

- PAN of HUF.
- Deed of declaration of HUF/ List of coparceners.
- Bank pass-book/bank statement in the name of HUF.
- All documents viz. Photograph, POI, POA, PAN of Karta are required.
- All the documents are signed under HUF stamp.

Non-Residents and Foreign Nationals

- Declaration from client stating compliance with applicable laws
- Copy of passport/PIO Card/OCI Card
- Overseas address proof
- POI and POA Documents to be attested by any of the entities viz; Notary Public, any Court, Magistrate, Judge, Local Banker, Indian Embassy/ Consulate General of the country where NRI/FN is residing to the effect that it has been verified with the originals

Account Opening – Documentation (Others)

Foreign Institutional Investors (FIIs)

- Copy of SEBI registration certificate is obtained.
- Authorized signatories list with specimen signatures and photographs is obtained.
- DP-Client agreement may not be required, provided:
 - (i) FIIs are registered with SEBI and have entered into an agreement with the Participant either directly or through their power of attorney holders as per SEBI (Foreign Institutional Investors) Regulations, 1995; and
 - (ii) Such agreement gives the Participant an authority to act on behalf of the FIIs for availing the services of the Depository; and
 - (iii) Such agreement is filed with SEBI.

Account Opening – Last Leg

Dispatch of Documents to KYC Registration Agency (KRA)

- After KYC, scanned KYC documents are dispatched to KRA within 10 working days from date of execution of documents and proof of dispatch is maintained.
- Electronic records of KYC documents are maintained, if not physical records.

Dispatch of documents to clients (after account opening)

- Client Master Report
- Copy of agreement including charge structure
- First Delivery Instruction Slip (DIS) booklet

Things to Remember

- All the documents submitted by the applicant are Self-attested.
- Name & address of the applicant mentioned on the KYC are matching with the documentary proof
- For Sole proprietor, application is in individual name.
- Account opening form and other documents are completely filled up.
- Photographs are pasted (not stapled) and investor has signed across the photograph.
- IPV details are completely filled up by DP officials
- Precautions are taken while opening accounts for Illiterate person ,Blind person etc. and appropriate remark are captured in system.

Things to Remember...

- Account of investor is opened correctly in depository system. (e.g. unregistered trust account is opened in name of trustee, partnership firm account is opened in the name of partners)
- Details of investor such as name, address, bank mandate etc are captured correctly and as prescribed by the depository.
- SMS alert flag is enabled in the system, in case of POA is registered or mobile number is provided.
- No joint holders allowed for HUF/AOP/Minor demat accounts
- Guardian details are captured for “minor” accounts.

Common Mistakes Observed

- Mismatched address proof
- Address not completely captured in the system or incorrectly captured.
- Mismatch in name when compared with the PAN card.
- Signature not obtained across the photograph.
- Incomplete in-person verification
- 'verified with original' stamp or 'PAN verified' stamp not affixed.
- Signature / Mode of operation not captured in system
- Some of the details in account opening form not filled up.
- Telephone/ Electricity Bill submitted as proof of address is beyond the validity period

Account Modifications

- Change of address
 - Proof of new address is obtained
 - Letter is sent to the old as well as new address
- Change in signature
 - Bank attestation for new signature.
 - Personal visit and submission of POI
- Change in bank details
 - Proof of new bank details is obtained
- Change in name
 - On account of marriage – marriage certificate or other prescribed documents
 - Other than Marriage - Publication of name change in official gazette
- After change is carried out, communication is sent to client and record of dispatch is maintained

Dematerialisation / Rematerialisation

- Request is in prescribed format and completely filled up w.r.t. details required
- Date of receipt stamp is affixed on request
- DP has sufficient provision for safe keeping of physical certificate
- DRF is sent to Issuer \ RTA within 7 days of receipt
- Mechanism is in place to analyze the rejections so as to avoid recurrence of the same.
- Rejected certificates are sent to client within 7 days of receipt and proof of the same to be maintained
- DP has reconciliation procedure to keep control on request received, processed and in transit cases
- DP has a process to follow up the cases of
 - Pending Demat and Remat
 - Requests rejected but documents not received

Delivery Instruction Slips – Inventory Management

- Details of physical stock of DIS and DIS issued are entered in back office software.
- Periodic reconciliation of physical inventory is carried out with the records.
- Reconciliation is carried out by independent person
- Reconciliation statement is signed by the senior official

Delivery Instruction Slips – Issuance

- **First time Issuance**

- Sent to clients along with account opening kit
- Proof of dispatch is maintained
- DIS booklet not handed over to representative of client
- If handed over personally to Client – signature of client is obtained

Delivery Instruction Slips – Issuance

- **Re-Issuance**

- It is strictly based on requisition form duly signed by the client.
- If client approaches in person or through representative, DIS handed over after confirming the identity and signature is obtained in issue register. This register is maintained in prescribed format.
- Signature on requisition slip is prima facie matching with the signature scanned in the system.
- In case of loss of requisition form, written request, stating so, is signed by the client and supported by latest transaction statement.
- If sent through courier, record of the same is maintained
- In case loose DIS is issued whether prescribed procedure is followed

DIS – Execution

- DIS is in prescribed form
- It bears pre- stamped Client ID and pre-printed unique identification number
- Complete w.r.t. various details
- Signature on DIS matches with the signature captured in system
- Date and time of receipt stamp affixed. (Stamped with appropriate remark based on time of receipt.)
- Routed through Back-office. If not, DIS control register is maintained.

DIS – Execution...

- Four eye principle is followed for entry in back office software
- For transaction value more than Rs. 5 lacs or client has 5 or more ISINs & all ISINs are transferred, two step verification is followed. Additionally, confirmation with client and record is maintained
- For transaction in inactive account (no debit instruction in 6 months) for transferring all the securities, Confirmation with client and record of the same is maintained
- Fax Transactions - Original DIS is obtained within 3 working days
- In case transactions are executed based on digitally signed electronic instruction, prescribed regulations are complied with.

Account Closure – Request by client

- Account closure request is in prescribed format
- Completely filled up
- Closure request by POA holder is not accepted
- Request to be initiated within 2 days from the date of receipt
- Transaction Statement for the quarter with the words *"Account Closed / Marked for Closure"* is sent to client and proof of the same is maintained
- In case, demat request is pending in such accounts, the prescribed procedure is followed for cancellation of demat requests
- If annual maintenance charges are collected in advance, proportionate amount is refunded for balance quarters.

Account Closure – By DP

- Notice of 30 days specifying the reasons is sent to client
- Reasons could be Non payment of dues, closure of branch by DP
- Proof of dispatch of notice is maintained

Transaction statement

- Transaction statement is sent at prescribed frequency
 - Non-BSDA client having transaction – monthly
 - BSDA client having transaction – quarterly
 - Clients having holding but nil transaction – annually
 - Clients having nil transaction nil holding – annually in physical form
- Transaction statement is sent from HO and not from branches
- Proof of dispatch is maintained for verification
- In case Transaction statement is sent through email, prescribed requirements are complied with.

Transmission

- Application is complete with details , signed by surviving joint holders or legal representatives.
- Original / Notarized /attested death certificate, succession certificate and probate of will is obtained.
- Transmission request is processed with in 7 days
- If new account with survivors is opened on old documents, whether it is in the same order.

Other Areas

- Pledge:
 - Request is in prescribed format for creation, closure and invocation of pledge
 - Details are correctly filled up
- Power of Attorney (POA)
 - supported by POA document
 - where POA is given to stock broker/DP, its in the format prescribed by SEBI
 - details of POA holder with signature is correctly captured
 - SMS alert is activated

Other Areas

- NISM Certification

All associated persons engaged or employed for following by the DP have DOCE Certification. (NISM-Series-VI: Depository Operations Certification Examination)

- (a) dealing or interacting with clients;
- (b) dealing with securities of clients;
- (c) handling redressal of investor grievances;
- (d) internal control or risk management;
- (e) activities having a bearing on operational risk, or
- (f) maintenance of books and records pertaining to the above activities

Other Areas...

- Formats used by DP:
 - All the format used by the DP is as per the latest communication issued by SEBI/Depository.
 - In case of some documents such as agreements are executed in old format, the revision needs to be communicated to clients separately.
- Rectification action is taken by DP to comply with the observations emerging out of previous internal audit report / inspection report.
- Billing structure is in line with the regulations and correctly displayed on website

Compliance under Prevention of Money Laundering Act, 2002 (PMLA)

- DP has PMLA policy in line with SEBI guidelines and complied with. (CDD, monitoring, reporting, records maintenance)
- PMLA policy is approved by the Board / senior management
- 'Principal Officer' is appointed and details communicated to FIU-IND
- Process is in place to deal with alerts (e.g. STR committee) and action is taken on suspicious transactions
- STR register is maintained in prescribed format

Outsourced Activities

- DP has outsourcing policy in line with SEBI Circular
- Details of outsourced activities communicated to NSDL.
- Core activities are not outsourced
- Agreements entered with vendors in line with the SEBI circular.
- Periodic review of vendors carried out on various parameters stated in SEBI circular.
- Appropriate action is taken on observations emerging out of review.

System Areas

- Two back ups. One at local site and another at remote site.
- Latest version of Anti-virus and regular updation.
- Licensed software are used
- Fallback connectivity and power arrangements are in place and tested regularly
- Adequate physical and logical access restrictions
- Restricted access to server

Service Centre / Branch

- Prior approval is obtained from Depository for opening new branch/ service centre
- Additional aspects in NSDL:
 - Details of branches are correctly displayed on NSDL website
- Additional aspects in CDSL:
 - Adequate infrastructure
 - Control, coordination & supervisory setup
 - Adequate provision for safety and security of documents
 - Reconciliation process for documents

Reporting timelines

Audit type	Frequency	Deadline	Submitted to
Re. CDSL			
Internal audit	Half Yearly	May 15 th and November 15 th	DP
Concurrent Audit of Risk Prone Areas	Monthly	10 th of Next Month	DP
Re. NSDL			
Internal audit	Half Yearly	May 15 th and November 15 th	DP
Concurrent Audit	Monthly	May 15 th and November 15 th	DP

Thank You