## Consultation Paper

**Role of KYC Registration Agencies (KRAs)/ Market Infrastructure Institutions (MIIs) in performing KYC (Know Your Client) of the client in securities market**

### 1. Objective

1.1. The objective of this paper is to seek comments/views from various stakeholders including market intermediaries and the public on the proposed role of KRAs/MIIs (Stock Exchanges and Depositories) in performing KYC of the clients in Securities Market.

### 2. Background

2.1. SEBI, by issuing circulars from time to time, has prescribed various guidelines with regard to the KYC process, Use of technology for KYC, e-KYC Process, In-Person Verification, KYC Registration Agency (KRA), etc. The circulars and their corresponding details have been summarized in the table below:

| Date of Circular | Circular no. | Circular Name |
|---|---|---|
| August 22, 2011 | CIR/MIRSD/16/2011 | Simplification and Rationalization of Trading Account Opening Process |
| October 05, 2011 | MIRSD/SE/Cir-21/2011 | Uniform Know Your Client (KYC) requirements for the securities market |
| December 02, 2011 | MIRSD/Cir-23/2011 | The Securities and Exchange Board of India (KYC Registration Agency) Regulations, 2011 |
| December 23, 2011 | MIRSD/Cir- 26 /2011 | Guidelines in pursuance of the SEBI KYC Registration Agency (KRA) Regulations, 2011 and for in In-Person Verification (IPV) |

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|---|---|---|
| July 21, 2016 | CIR/MIRSD/ 66 /2016 | Operationalization of Central KYC Records Registry (CKYCR) |
| November 05, 2019 | SEBI/HO/MIRSD/DOP/CIR/P/2019/123 | e-KYC Authentication facility under section 11A of the Prevention of Money Laundering Act, 2002 by Entities in the securities market for Resident Investors |
| April 24, 2020 | SEBI/HO/MIRSD/DOP/CIR/P/2020/73 | Clarification on Know Your Client (KYC) Process and Use of Technology for KYC |
| May 12, 2020 | SEBI/HO/MIRSD/DOP/CIR/P/2020/80 | Entities permitted to undertake e-KYC Aadhaar Authentication service of UIDAI in Securities Market |
| September 08, 2020 | SEBI/HO/MIRSD/DOP/CIR/P/2020/167 | Entities permitted to undertake e-KYC Aadhaar Authentication service of UIDAI in Securities Market – Addition of NSE to the list |

## 3. Present Process:

3.1. At present the KYC process in the securities market is undertaken by SEBI Registered Intermediaries (RI). After completion of KYC, RI uploads KYC records to KRA (the repository of KYC data in securities market) /CKYCR. The role of KRAs inter-alia is centralization of the KYC records, ascertain the KYC documents uploaded by the RI and share KYC records with other intermediaries as and when required. The responsibility of conducting the KYC and maintenance of records rests with the RI and KRA is not expected to verify the credentials of the documents/ information uploaded by the RI.

## 4. Proposed Framework and Rationale

4.1. In order to standardize the KYC process, to make the KYC process more robust, avoid duplication, save cost to RI etc, and to ensure that the end to end secured KYC process including Aadhaar authentication, independent verification of Officially Valid Document (OVD) / Income Tax Permanent Account Number (PAN), document safekeeping, technological innovations, standardization, cyber security norms etc, it has been contemplated that the KYC and account opening process may be separated in the securities market.

4.2. In the current process, every RI needs to invest in infrastructure, manpower, technology, implement process and practices may vary between intermediaries. Further, in the eventuality of failure of any RI leading to cancellation of its registration, KYC documents collected by it may not be available to subsequent RI and Investor has to undergo KYC process again.

Hence it is contemplated that KYC may be done through Stock Exchanges, Depositories, KRAs and documentation for opening of account for entering into transaction shall continue to be the responsibility of concerned RI.

5. **Proposed KYC process:**

5.1. SEBI vide circular dated Nov 05, 2019 has detailed the processes for Aadhaar e-KYC of resident investors in the Securities Market which includes Online Portal based Investor(Resident)e-KYC Process (Aadhaar as an OVD) and Assisted Investor(Resident)e-KYC process (Aadhaar as an OVD). In this regard, it was also mentioned that entities (which would be registered with UIDAI as KYC user agency ("KUA")) in the securities market, as notified by the Central Government and as permitted by SEBI, vide circulars dated May 12, 2020 and Sept 08, 2020 shall be allowed to undertake Aadhaar Authentication under section 11A of the PMLA.

5.2. KYC Procedure has been prescribed by SEBI vide circular dated April 24, 2020.The clients can complete the KYC either through physical mode or through the online system. For the purpose of KYC, client can approach KRA directly or through an RI. Client can complete the KYC directly on the system of KRA or could be facilitated by RIs as frontend for KRA.

The details of the process shall be as under:

5.2.1. Any person who approaches the RI for opening an account shall first complete its KYC with KRA, after which the account may be opened by the concerned RI.

5.2.2. Client can approach KRA directly to complete the KYC or can access the App/system of KRA through an RI.

5.2.3. RI will now work as a frontend of the KRA for KYC process. The RI shall establish connectivity with a KRA to facilitate the KYC of clients. The KRA shall allow the RI to connect through login and password mechanism, upload / download the KYC data / records as well as have interoperability with the other KRAs for fetching and uploading the KYC records.

5.2.4. KRA will independently verify all the record and documents and will be responsible for ensuring the correctness of the KYC data including modifications/ updation of the KYC data submitted by client for KYC and shall maintain the record for same.

5.2.5. KRA shall have their online system/ KYC App for undertaking KYC and IPV/VIPV of clients. The system / App shall have the features as prescribed in the SEBI circular dated April 24, 2020 and as modified from time to time. Further, the online system / App of the RI may be integrated with the online system / App of the KRA so as to allow seamless movement of KYC documents to and from RI to KRA.

5.2.6. In case the client approaches RI for initial KYC, after collecting the initial KYC documents of the new clients, the RI shall forthwith upload the KYC documents i.e Proof of identity (PoI), Proof of Address (PoA), PAN, KYC form and other supporting documents on the online system or App of the KRA. The RI shall allow the operation/ dealings in the investment/ trading account of the client only after receipt of the confirmation from the KRA with respect to completion of KYC of such client.

5.2.7. In case a client's KYC documents sent by the RI to KRA are incomplete, the KRA shall inform the same to the RI who shall forward the required information / documents promptly to KRA.

5.2.8. The clients' KYC shall be completed by the KRA only after the OVD, PAN, mobile number, e-mail id and bank account details have been independently authenticated / verified.

5.2.9. After successful completion of KYC, KRA shall assign a unique number to the client (KRA number/ PAN) and such unique number shall be used by the client for the KYC process with the RI for opening of an account subsequently.

5.2.10. If there is any update required in the KYC information downloaded from KRA website, the RI shall allow transactions/ dealing in the account only after updating the information in the KRA system and receiving a confirmation from KRA that the KYC has been updated. While updating these client's data, the RI shall ensure that no duplicate record is created in KRA system.

5.2.11. In case the client's KYC has already been done by the KRA, the RI before opening of the account of the client for trading / investment purposes, shall fetch the KYC documents from KRA based on the PAN/ unique number (provided by KRA post completion of KYC to client) with OTP based authentication by the client and shall carry out its own due-diligence to ensure that the person is same whose KYC documents have been fetched from the KRA.

5.2.12. Physical mode of KYC will continue to be available as per circulars prescribed by SEBI from time to time.

5.2.13. KRAs will also function as repository of client KYC data in the securities market including that of Mutual Funds clients and will also upload the data to CKYCR.

5.2.14. KRAs in co-ordination with each other shall develop a system to prevent duplication of entry of KYC details of a client and to ensure uniformity in formats of uploading / modification / downloading of KYC data by the RI.

5.2.15. KRA shall maintain an audit trail of the upload / modifications / downloads made in the KYC data.

5.2.16. KRA shall intimate either by the way of a letter, or e-mail or SMS to each client within 10 days of the receipt of initial/ updated KYC documents from the intermediary/client, confirming the same thereof and maintain the proof of such dispatch/intimation.

5.2.17. KRA shall file the suspicious transaction report with FIU in compliance with PMLA, if they come across any suspicious activity while doing the KYC or updating the KYC of client.

## 6. Clients of Mutual Funds

6.1. Presently, in case of clients of mutual funds, the Registrar to an Issue and Share Transfer Agent appointed by the mutual fund performs the initial KYC/due diligence of the client, upload the KYC information with proper authentication on the system of the KRA/CKYCR, and furnish the scanned images of KYC documents to the KRA.

6.2. In the proposed system, the Registrar to an Issue and Share Transfer Agent appointed by the mutual fund shall perform the KYC of the clients of mutual funds through the system of KRA as frontend or else may also seek registration as KRA from SEBI.

6.3. In view of the circulars dated Nov 05, 2019 , May 12, 2020 and Sept 08, 2020 issued by SEBI detailing the processes for Aadhaar e-KYC of resident investors in the Securities Market and notification in respect of nine entities to undertake Aadhaar authentication service of the UIDAI under section 11A of the Prevention of Money-Laundering Act, 2002, it is proposed that RTA which is notified as KUA by Government of India as per the recommendation by UIDAI and SEBI to undertake Aadhaar Authentication service of the UIDAI under section 11A of the PMLA, 2002 shall be eligible to seek registration as KRA under KRA Regulations with SEBI.

6.4. The date of applicability of changes in KYC process through the system of KRA shall be effective after 6 months from the date of gazette notification of the proposed amendments in KRA Regulations. However, the RTA appointed by Mutual Fund or any other eligible entities wanting to perform KYC may seek registration as a KRA under KRA Regulations immediately. Eligible entities would have 6 month time to start doing KYC as KRA and the existing KRAs will also have 6 month time to undertake KYC work and to set up/ upgrade infrastructure, till that time the present process of KYC being performed by RI shall continue.

## 7. <u>Compliance with PMLA and Rules therein</u>

7.1. Rule 9(2) of Prevention of Money-Laundering (Maintenance of Records) Rules, 2005 allows the reporting entities to rely on a third party for their customer due-diligence subject to the following conditions:

a) the reporting entity, within two days, obtains from the third party or from the Central KYC Records Registry records or the information of the client due diligence carried out by the third party.

b) the reporting entity takes adequate steps to satisfy itself that copies of identification data and other relevant documentation relating to the client due diligence requirements will be made available from the third party upon request without delay;

c) the reporting entity is satisfied that such third party is regulated, supervised or monitored for, and has measures in place for compliance with client due diligence and record-keeping requirements in line with the requirements and obligations under the Act;

d) the third party is not based in a country or jurisdiction assessed as high risk;

e) the reporting entity is ultimately responsible for client due diligence and undertaking enhanced due diligence measures, as applicable; and

f) where a reporting entity relies on a third party that is part of the same financial group, the Regulator may issue guidelines to consider any relaxation in the conditions (a) to (d).

7.2. Thus, PMLA Rules provide for reporting entities relying on third party for customer due diligence. In this regard, KRAs are regulated entities registered with SEBI and registered intermediaries can rely on KRAs as a third party for carrying out their customer due diligence while complying with the attendant conditions.

7.3. The concerned RI shall also be responsible for due diligence of client with respect to KYC done by third party i.e KRA and account opening in compliance with the requirement of Prevention of Money-Laundering Act (PMLA) including reporting of the suspicious transactions taking place in such account.

## 8. Handling New/Existing KYC Records

8.1. Since the KRAs shall be responsible for KYC of the client's and they shall continue to be the repository of KYC data, the existing KYC records of clients submitted by RIs shall be re-verified by KRAs and KRAs shall ensure the correctness of the KYC records maintained by it. KRA shall ensure correctness of all KYC records maintained by it by Dec 2021 after due verification.

8.2. **Cost for New KYC:** The cost of conducting KYC by KRA should reasonable and should not cast additional burden on investor.

8.3. **Cost for Onboarding existing client:** As regard to verification/authentication of existing records with KRA, such verification/authentication cost shall be borne by KRA or KRA may be funded (one time) for such verification cost by Investor Protection Fund (IPF) of SEBI/Stock Exchanges/Depositories.

## 9. Amendments to KRA Regulations

9.1. To make the proposed changes, amendments shall be made to the KRA Regulations, 2011 which inter-alia includes changing the definition of KRA, amending the conditions for grant of certificate of registration and amending the functions and obligations of KRA and Registered Intermediary according to the above proposal.

## 10. Public comments

10.1. In order to take into consideration views of stakeholders, public comments are solicited on the proposal.

10.2. Comments may be sent by e-mail or through post. While sending comments through e-mail, kindly mention the subject as "Role KRAs in performing KYC"

10.3. Comments may please be emailed to Shri Narendra Rawat, General Manager at narendrar@sebi.gov.in and Ms. Sushma Upadhyayula, Assistant Manager at sushmau@sebi.gov.in or send by post at the following address latest by February 15, 2021.

**Postal Address:**

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