



भारतीय प्रतिभूति
और विनियम बोर्ड
Securities and Exchange
Board of India

General Manager
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SEBI/HO/IMD/FIIC/OW/P/2020/2451/1

January 17, 2020

Shri Virendra Chavan
Asst Vice President & Compliance Officer,
Custodial Services,
Axis Bank Limited
4th Floor, South Wing, C-2,
Wadia International Centre,
Pandurang Budhkar Marg,
Worli, Mumbai – 400025

Dear Sir/Madam,

Subject: Request for Informal Guidance by way of an Interpretative letter under SEBI (Informal Guidance) Scheme, 2003 in respect of Regulation 15 of the SEBI (Custodian) Regulations, 1996.

1. This has reference to your letter dated September 17, 2019 and subsequent clarifications sent by you vide e-mails dated November 21, 2019 and December 19, 2019 in the captioned matter.
2. In your letter under reference and your subsequent clarificatory e-mails, you have *inter-alia* represented the following:
 - a. You have received requests from few PMS clients to offer custodial services with provision of maintaining demat accounts with another depository Participant.
 - b. Accordingly, you have proposed a structure where PMS would appoint a SEBI registered custodian for the clearing and settlement of funds and securities for the trades executed by the PMS at the pooled level for their underlying clients.
 - c. Accordingly Bank and demat accounts for pooling and settlement purpose will be opened and maintained by the PMS with the Custodian in the name of Portfolio managed by PMS.
 - d. For the purpose of keeping the securities segregated in the demat accounts of the clients of PMS, demat accounts of clients will be used by the PMS. Further, as per the proposal,



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the clients of PMS will grant Power of Attorney to the PMS to operate their demat accounts with the DP and PMS will delegate the powers conferred by the clients of PMS to the Custodian to operate the demat accounts of the clients of PMS.

- e. The correspondence address of the Custodian will be registered in the segregated demat accounts maintained with other DP to ensure that all the physical communication/dividend warrants sent by the issuers are received by the custodian.
- f. Common pool dividend account opened and operated by Custodian (herein after referred as 'Custodian's Bank account') will be mapped in the Demat accounts
- g. Further, you have also proposed the transaction flow w.r.t the trades executed by the PMS.
- h. There is no variation in the existing industry process and what Axis bank has proposed to adopt.
- i. The core functions of the Custodian will be done by the Axis Bank as a Custodian irrespective of whether the demat account is in-house or outside. The safe keeping and operational activities will be exercised by Axis Bank via Power of Attorney (POA) and electronic movement in both cases. The controls that are currently exercised in our DP will also be agreed to be exercised in external DP by way of a MOU which will also include the liability clause.
- j. The proposed structure is as follows:
 - In a PMS relationship where custodian has been appointed, the demat accounts of the PMS and/or the underlying clients of the PMS will be opened with an external DP (means external to Axis Bank custodian),
 - This DP may or may not be another SEBI registered Custodian (means it could be another broker, bank, etc.),
 - Axis Custodian will operate/control the securities in these demat accounts as per the normal process of applying a POA (in its favour) on these accounts

Query

3. Based on the above proposed structure, you have sought the following query:
 - *Whether operating, accessing the demat accounts as mentioned above by the Axis Bank Ltd. as Custodian of Securities for the PMS will be in compliance with the Regulation 15 of the SEBI (Custodian) Regulations, 1996 (Custodian Regulations)''*

Our Comments:

4. We have considered the submissions in your letter and e-mails under reference. Without necessarily agreeing to your analysis and without commenting on the proposed structure and the process flow, our views on the queries raised by you are as under:



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- i. Regulation 15 of Custodian Regulations states:

"No custodian shall assign or delegate its functions as a custodian to any other person unless such person is a custodian...."

Provided that a custodian may engage the services of a person not being a custodian, for the purpose of physical safekeeping of goods or gold belonging to its client including a mutual fund having a gold exchange traded fund scheme, subject to the following conditions—

- (a) the custodian shall remain responsible in all respects to its client for safekeeping of the goods or gold kept with such other person, including any associated risks;*
 - (b) all books, documents and other records relating to the goods or gold so kept with the other person shall be maintained in the premises of the custodian or if they are not so maintained, they shall be made available therein, if so required by the Board;*
 - (c) the custodian shall continue to fulfill all duties to the clients relating to the gold goods or so kept with the other person, except for its physical safekeeping."*
- ii. The above provision of the Custodian Regulations mandate that a Custodian shall not assign or delegate its functions as a custodian to any other person unless such a person is a custodian. In the instant matter, it is noted from the details/clarification provided by you via e-mail dated 21/11/2019 at Point No. 2 that the proposed structure (i.e. availing the DP services of external DP by the PMS clients), would not result in any change in the core functions of the Custodians in terms of the Custodian Regulations, viz. safekeeping of securities, control on the operations, monitoring and proper booking keeping, separate custody account of each client, etc. You have also confirmed that all the said functions are basically done by the Custodian irrespective of whether the demat account is in-house or outside. Vide your last e-mail on December 19, 2019, you have also stated that Axis Bank custodian would operate/control securities in these demat accounts as per normal process of applying a PoA (in its favour) on these accounts.
- iii. Thus, a Portfolio Manager may appoint a custodian with the demat accounts of the PMS, where its underlying clients' demat accounts are with another Depository Participant. However, there should not be any delegation of the functions of the Custodian, i.e. the custodial activities/ functions shall continue to be carried out by the custodian and not by the Portfolio Manager or the DP.
- iv. You may also note that any change in the DP/Custodian shall be subject to the compliance of the provisions of SEBI (Portfolio Managers) Regulations, 1993, SEBI (Custodian Regulations) 1996 and relevant Circulars issued by SEBI from time to time, including the following:
- a. Regulation 16(7) of the Regulations states that *"the portfolio manager shall segregate each client's funds and securities and keep them separately from his own*



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funds and securities and be responsible for safe keeping of clients funds and securities."

- b. SEBI circular dated June 23, 2009 *inter alia* states that Portfolio Managers may keep the funds of all clients in a separate bank account maintained by the portfolio manager subject to, inter-alia, maintenance of clear segregation of each client's funds.
 - c. As per regulation 16(8) of the SEBI (Portfolio Managers) Regulations, 1993 the portfolio manager shall not hold the listed securities belonging to the portfolio account, in its own name on behalf of its clients either by virtue of contract with clients or otherwise and as such the Portfolio Manager shall segregate each clients' listed securities and keep them in a segregated manner as per SEBI (Portfolio Managers) Regulations, 1993.
 - d. It should be ensured that all the physical communication/dividend warrants/corporate action benefits sent by the issuers are received by the custodian.
 - e. As per applicable SEBI (Custodians) Regulations 1996, the Custodians shall remain responsible for safekeeping, and processing / settlement of transactions, reconciliations at the time of transactions as well as periodic basis (as agreed upon between the Custodian and the Portfolio Manager) and regulatory reporting for assets held in custody including reporting at segregated-assets mode at the underlying investor-level.
5. This position is based on the representation made in your aforesaid letter and subsequent clarificatory e-mails under reference. Different facts or conditions might lead to different results. This letter expresses the Division's view on the issue raised by you. This letter does not express a decision of the Board on the question referred.
6. You may also note that the above position/view is expressed only with respect to the interpretation/clarifications sought in your letter and e-mails under reference with respect to Regulation 15 of the SEBI (Custodian) Regulations, 1996, as referred above and does not affect the applicability of any other provisions of the Regulations or law or requirements of any other SEBI Regulations, Guidelines and Circulars administered by SEBI or the laws administered by any other authority.

Yours faithfully,

(Achal Singh)