

Assigning responsibility for the use of artificial intelligence tools by Market Infrastructure Institutions, Registered Intermediaries and other persons regulated by SEBI

1. Objective

This Memorandum seeks the approval of the Board to amend the Securities and Exchange Board of India (Intermediaries) Regulations, 2008 (“**Intermediaries Regulations**”), the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2018 (“**SECC Regulations**”) and the Securities and Exchange Board of India (Depositories and Participants) Regulations, 2018 (“**DP Regulations**”) for assigning responsibility for the use of artificial intelligence tools by Market Infrastructure Institutions (‘MIIs’), Registered Intermediaries and other persons regulated by SEBI.

2. Background

2.1. In view of the increased usage of Artificial Intelligence (AI) and Machine Learning (“ML”) tools in products involving investor interface, SEBI vide its Circulars issued in 2019 mandated reporting of AI and ML applications and systems offered and used by-

2.1.1. Stock Brokers and Depository Participants (vide Circular dated January 4, 2019),

2.1.2. MIIs i.e. Stock Exchanges, Depositories and Clearing Corporation (vide Circular dated January, 31, 2019), and

2.1.3. Mutual Funds, Asset Management Companies, Trustee Companies, Board of Trustees of Mutual Funds (vide Circular dated May 9, 2019).

2.2. This reporting mechanism was inter alia aimed at gaining an understanding of the adoption of such technologies in the securities market and to also ensure preparedness for any AI/ML issues that may arise in the future. The provisions of the aforesaid Circulars were suitably incorporated into the Master Circulars issued by SEBI as applicable to the respective intermediaries and MIIs.

2.3. Any set of applications / software / programs / executable / systems

(computer systems) that are offered to investors (individuals and institutions) by MIs and intermediaries (to facilitate investing and trading or to disseminate investments strategies and advice or to carry out compliance operations / activities; where AI / ML is portrayed as a part of the public product offering or under usage for compliance or management purposes), were inter alia included within the ambit and scope of the aforesaid Circulars.

- 2.4. From the information gathered through the aforesaid reporting mechanism, an indicative list of areas where AI/ML Systems/ tools are used by MIs, Registered Intermediaries and other persons regulated by SEBI are tabulated below:

Person regulated by SEBI	Purpose for which AI/ML tools are used
Stock Brokers and Depository Participants	surveillance, order execution, KYC and anti-money laundering
MIs	surveillance, risk management, data analysis, behaviour analysis, generative AI for reviewing documents/order/report, cyber security, cyber infrastructure and chat bot
Mutual Funds	surveillance, customer service (email, whatsapp and chat bots), cyber security and customer segmentation

- 2.5. It is therefore observed that AI/ML tools play an increasingly important role in not only the core operations (such as surveillance, risk management, KYC and cyber security) of MIs/intermediaries but also in operations involving investor interface (such as order execution, customer segmentation and customer service).

- 2.6. Thus the usage of AI tools and systems in the financial markets is meant to provide inherent benefits for various stakeholders such as increased efficiency, accuracy in decision making, risk management, enhanced cyber

security, ease of doing business, compliance for the MIs and intermediaries, ease of carrying out transactions and better customer experience for investors.

- 2.7. While recognizing the need for market intermediaries to embrace latest technologies, it becomes equally important for SEBI to ensure the protection of investors. Hence, a need is felt to assign responsibility to those persons regulated by SEBI that use of AI/ML tools in the conduct of their securities market related activities or while servicing their clients. Mandating such responsibilities is expected to bring in more seriousness to such users while deploying AI/ML tools and at the same time ensure protection of investors.

3. Proposal and public consultation:

- 3.1. SEBI had issued a Consultation Paper dated November 13, 2024 (uploaded on its website) titled “Proposed amendments with respect to assigning responsibility for the use of artificial intelligence tools by Market Infrastructure Institutions, Registered Intermediaries and other persons regulated by SEBI” and comments of the public were solicited. A copy of the said consultation paper is placed at **Annexure A**.
- 3.2. Draft amendments were proposed to the Intermediaries Regulations, SECC Regulations and DP Regulations. These amendments proposed imposing a mandate on a person regulated by SEBI who uses artificial intelligence tools, either designed by it or procured from third-party technology service providers, irrespective of the scale and scenario of adoption of such tools for conducting its business and servicing its investors, that it would be solely responsible –
 - 3.2.1. for the privacy, security and integrity of investors’ and stakeholders’ data including data maintained by it in a fiduciary capacity throughout the processes involved;
 - 3.2.2. for the output arising from the usage of such tools and techniques it relies upon or deals with; and
 - 3.2.3. for the compliance with applicable laws in force.

- 3.3. For the purpose of seeking public comments, the proposals contained in the consultation paper were divided as under-
- 3.3.1. Proposal to assign responsibility for the use of artificial intelligence tools by registered Intermediaries and other persons regulated by SEBI- amendments to Intermediaries Regulations;
- 3.3.2. Proposal to assign responsibility for the use of artificial intelligence tools by MIs- amendments to SECC Regulations and DP Regulations.
- 3.4. **(This has been excised for reasons of confidentiality)** A comprehensive table of the proposal-wise consultation responses/comments received on the proposals for amendments and the responses to the questions posed in the consultation paper are placed as **Annexure-B. (This has been excised for reasons of confidentiality)**
- 3.5. **(This has been excised for reasons of confidentiality)** The summary of comments and detailed analysis thereof is placed as **Annexure-C.**
- 3.6. **(This has been excised for reasons of confidentiality)**

4. Proposal for the consideration of the Board:

- 4.1. In view of the foregoing, in order to impose responsibility on persons regulated by SEBI who use AI/ML tools and techniques, it is proposed to suitably amend the Intermediaries Regulations, SECC Regulations and DP Regulations by way of insertion of new regulations therein as given below:-

(Amendments shall be notified after following the due process)

- 4.2. The Board is requested to consider the proposal and approve the amendments to the Regulations as mentioned under paragraph 4.1 above.
- 4.3. The Board is also requested to authorize the Chairperson to make

consequential and incidental changes and take necessary steps to give effect to the decisions of the Board.

Annexure A

(Consultation paper is available on SEBI website www.sebi.gov.in at Reports & Statistics» Reports» Reports for Public Comments.)

Annexure B

(This has been excised for reasons of confidentiality)

Annexure C

(This has been excised for reasons of confidentiality)