

CIRCULAR

SEBI/HO/MIRSD/MIRSD-PoD-1/P/CIR/2023/061

April 25, 2023

To,
Stock Brokers through recognized Stock Exchanges
Clearing Members through recognized Clearing Corporations

Dear Sir/Madam,

Subject: Bank Guarantees (BGs) created out of clients' funds

1. Currently Stock Brokers (SBs)/ Clearing Members (CMs) pledge client's funds with Banks which in turn issue Bank Guarantees (BGs) to clearing corporations for higher amounts. This implicit leverage exposes the market and especially the client's funds to risks. Pursuant to discussions with various stakeholders, it has been decided to implement the following measures in order to safeguard the interests of the investors: -
 - a. Beginning May 01, 2023, no new BGs shall be created out of clients' funds by SBs/CMs.
 - b. Existing BGs created out of clients' funds shall be wound down by September 30, 2023.
2. The provisions of this framework shall not be applicable for proprietary funds of SBs/CMs in any segment and SB's proprietary funds deposited with CM in the capacity of a client.

Monitoring and reporting:

3. The stock exchanges and clearing corporations shall take stock of the current position of the BGs issued out of clients' funds by SBs/CMs and monitor the wind down to ensure implementation of the circular without any disruption of services to clients. For the purpose, stock exchanges and clearing corporations shall put in place periodic reporting mechanisms for SBs/CMs.
4. Stock exchanges and clearing corporations are directed to submit the following data to SEBI on fortnightly basis (starting from June 01, 2023):

Collateral data as on <Date> at <Name of the clearing corporation>				
Name of the SB/CM	Nature of the entity (SB/CM/SCM)	Total BG amount as collateral	Total BG amount (out of clients' funds) as collateral	Total BG amount (out of prop funds) as collateral

5. SBs/CMs shall be required to provide a certificate, by its statutory auditor confirming the implementation of this circular. Such a certificate shall be submitted to stock exchanges/clearing corporations by October 16, 2023.
6. Stock exchanges and clearing corporations shall verify the compliance of the provisions of the circular in their periodic inspections/reporting. They shall also evolve adequate mechanisms to address cases of SBs/CMs who do not comply with the provisions of the circular by the stipulated dates.
7. Given the implementation of the above measures, the provisions of following SEBI circulars shall stand modified to the extent as stated hereinabove:
 - a. SEBI circular MRD/DoP/SE/CIR-11/2008 dated April 17, 2008 on 'Collateral deposited by clients with SBs';
 - b. SEBI circular MIRSD/ SE /Cir-19/2009 dated December 03, 2009 on 'Dealings between a client and a stock broker';
 - c. SEBI circular SEBI/HO/MIRSD/MIRSD2/CIR/P/2016/95 dated September 26, 2016 on 'Enhanced supervision of stock brokers/depository participants';
 - d. SEBI circular no. SEBI/HO/MIRSD/DOP/CIR/P/2020/28 dated February 25,2020 on 'Margin obligations to be given by way of pledge/ re-pledge in the depository System';
 - e. SEBI circular SEBI/HO/MIRSD/DPIEA/CIR/P/2020/115 dated July 01,2020 on 'Standard Operating Procedure in the cases of Trading Member / Clearing Member leading to default'; and
 - f. SEBI circular SEBI/HO/MRD2_DCAP/CIR/2021/0598 dated July 20,2021 on 'Segregation and monitoring of collateral at client level'.

8. The stock exchanges and clearing corporations are directed to:
- a. bring the provisions of this circular to the notice of stock brokers 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.
9. 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,

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