

# **DEPOSITORIES & THE REGULATIONS GOVERNING THEM IN INDIA – AN ANALYSIS**

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## **INTRODUCTION TO DEPOSITORY**

In simple terms the depositories the word itself means that something is being deposited into it. Depositories is basically act as a bank where in deposits, securities, shares are deposited here, likewise if you buy shares from the share market or purchase of bonds from government in an electronic form then it is stores at the depositories. The way you deposit the cash in the bank and in an electronic from you receive the amount in your account in an electronic form. There are two depositories in India

1. National Securities Depositories Limited (NSDL)
2. Central Depositories Service Limited (CDSL)

Whenever you open a De-mat account the cart-man tell you that which one is their depositories NSDL or CSDL. Depositories keep your securities safe in an electronic form. Depository agent are also one of the party to the depositories. This agent are appointed by depository but by the approval of sebi. They are also very important participants as they provide front end to the customers for buying and selling of securities.

## **MEANING OF DEPOSITORY**

Depositories are the bank for shares, debentures, bonds, government securities in an electronic form. The work of the bank and the depositories are similar.

## **Depositories ACT 1996**

*“The depositories ACT, 1996 was one piece of legislation that has got an appreciation of all concerned due to the benefits it carried to the capital market activity.<sup>1</sup> It provided for establishment of depositories in securities for ensuring free transferability of securities with speed, accuracy and security by making securities of public limited companies freely transferable subject to certain exceptions. Dematerialization of securities in depository mode and for maintenance of ownership records of securities in a book entry form were others objectives of the ACT”.*<sup>2</sup>

### **ELIGIBILITY CRITERIA FOR DEPOSITORY**

Any of the following may market a depository

- 1) DP shall have net worth of Rs. 50 crore or even more than is acceptable.
- 2) DP shall be either a clearing bank or clearing member of any of the clearing corporations.<sup>3</sup>
- 3) DP shall have appropriate arrangements for receipt and remittance of money with a designated Authorized Dealer (AD) Category - I bank.<sup>4</sup>
- 4) A bank of abroad is also eligible but prior permission of RBI is required.
- 5) A very well recognized stock exchange.
- 6) A person not holding more than 5% of equity.

### **REGISTRATION OF DEPOSITORY**

SEBI always has an upper hand over depository until and unless the permission is not received by the SEBI or the certificate is not issued depository cannot work and it also has to match the proper

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<sup>1</sup> S.Mohan and R.Elangovan, Financial services, 483,2008.

<sup>2</sup> S.Mohan and R.Elangovan, Financial services, 483,2008.

<sup>3</sup> [http://www.sebi.gov.in/legal/circulars/jan-2012/eligibility-criteria-for-qualified-depository-participant\\_22031.html](http://www.sebi.gov.in/legal/circulars/jan-2012/eligibility-criteria-for-qualified-depository-participant_22031.html), 4th november.

<sup>4</sup> [http://www.sebi.gov.in/legal/circulars/jan-2012/eligibility-criteria-for-qualified-depository-participant\\_22031.html](http://www.sebi.gov.in/legal/circulars/jan-2012/eligibility-criteria-for-qualified-depository-participant_22031.html), 4th november.

parameters and guidelines of it because SEBI will not be allowing a single glitch in anything because it is responsible for everything so due care is to be taken by them.

## COMPARISON BETWEEN BANK AND DEPOSITOR

### Differences:

Depository	Bank
It keeps the securities in account. <sup>5</sup>	It keeps the funds in account. <sup>6</sup>
Zero balance accounts can also functions.	Zero balance accounts cannot function.
Beneficial owner is the main holder.	Account holder is the party to it.
It keeps securities safe of an individual.	It keeps funds and money safe of an individual.

### Similarity:

- 1) **Safe holding services:** Both banks and depositories a have similar work as bank safely holds the funds of an individual and on the other side depositories hold securities of an individual.
- 2) **Offices:** Both the banks and depositories have the office at the particular location and we can say a head office and different office at different places in the country.
- 3) **Fees:** Both banks and depositories are charge some and the other fees like bank charges transaction fees, safe fees and depositories.

## LEGAL ASPECTS OF DEPOSITORY

The depositories in India are managed and controlled by different authorities, bodies, which keep eye on the working of depository, as investor, have a large interest on depository, and trust on it so someone checking the working of depository is must.

<sup>5</sup> <http://short-note-on-the-difference-between.blogspot.in/2015/11/what-is-difference-between-bank-vs.html> 4th november.

<sup>6</sup> *Ibid.*

### **1. The Depositories ACT, 1996:**

The background of the act is that before the ACT came in 1996 there was an ordinance in 1995 of the depository for the legal framework of it. Depository Act made few amendments in the Companies Act, 1956; the Securities and Exchange Board of India Act (SEBI), 1992; the Indian Stamp Act, 1899; the Income tax Act, 1961; and the Benami Transactions (Prohibition) Act, 1988.<sup>7</sup>The Depositories Act, 1996 provides a legal outline for the establishment of depositories to facilitate holding of securities including shares in the e-way (electronic).<sup>8</sup>

### **2. SEBI Regulations 1996:**

The depository before starting and coming in to existence, it has to take a permission and has to receive certificate from the SEBI then and only the depository can function. It has to stick to its rules and regulation and cannot do the work except the depository are supposed to do. Any problem or grievance of the investor has to redress with in a period of month or less. Directions of SEBI can amend the byelaws.

### **3. Bye –Laws By Depository:**

The permission taken from SEBI and the approval received by it, will allow depository to make BYE-laws with the particular provisions mentioned in regulations:

- The eligibility criteria for admission and removal of securities in depositories.<sup>9</sup>
- The securities in which the conditions are attached to it.
- The criteria for admission of any investors.
- The procedure for the transaction within depository.<sup>10</sup>
- The procedure for conveying information to the participants and beneficial owners on dividend declaration, shareholders meetings and other matters of interest to beneficial owners.<sup>11</sup>

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<sup>7</sup> <http://www.shareyouressays.com/knowledge/summary-of-the-the-depositories-act-1996/112245,4th-november,12:34pm>.

<sup>8</sup> *Ibid.*

<sup>9</sup> M.Y KHAN, INDIAN FINANCIAL SYSTEM, 8.23, 2007.

<sup>10</sup> *Ibid.*

<sup>11</sup> *ibid.*

- The procedures for the depository and the internal controlling of the depository and the reviewing and monitoring.

#### 4. **The Certificate Of Commencement Of Business:**

The depository has to take permission from the SEBI and act as per the guidelines and depository has to take certificate before commencement of business, SEBI considers the regulations and functioning the followings,

- The depository should have a minimum net worth of 100crores.
- The depository must have adequate procedure and to ensure so it records each transaction.
- The depository has established standard transmission and encryption formats for the electronic communication of data between the depository, participants and issuer.<sup>12</sup>
- The certificate granting leads to commencement of business in the favor of the investors.

### **JUDICIAL STAND**

#### **Integrated Enterprises (India) Vs. Chairman, Securities**

With effect from 19.3.1999 even persons who were Registrars were eligible to seek registration as a DP.<sup>13</sup> Accordingly, the Regulations were amended on 20.5.1999 to include Registrars to an issue as an eligible category of applicant to apply for grant of certificate of registration as a DP on certain conditions.<sup>14</sup> In the expressions of SEBI, the reasons were: "This correction will help build the quantity of vault members.<sup>15</sup> This will likewise empower the framework to get favorable position of involvement and foundation of RTIs/STAs.<sup>16</sup>

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<sup>12</sup> M.Y KHAN,INDIAN FINANCIAL SYSTEM,8.25,2007

<sup>13</sup> legalcrystal.com/57906

<sup>14</sup> Ibid.

<sup>15</sup> Ibid.

<sup>16</sup> Ibid

## **WORKING OF DEPOSITORY**

### **DEPOSITORY SYSTEM:**

Depository system provides us with the electronic form of saving and securing securities in the modern World. It has increased the ease of operation and increased the trust amongst the investors, which has led to increase in the number of healthy investors in the market. The background of this system is about the lot of chaos and previous malpractices and frauds, which brought up the system in the market.

### **Dematerialization:**

The system, which came as depository system it completely, removed the old system

Of giving shares, hand to hand to the different people. This system also brought a ease of operation and removed the bad practices which were previously done by the people. The basic understanding of Dematerialization is that everything is e-way and you cannot see anything physical and it is so much cost and time saving.

### **Functioning of Depository:**

The depository framework won't just keep up the records of the investor however will likewise embrace to gather profits, extra offers, and so on., in the interest of the investor.<sup>17</sup> Occasionally, the investors will be educated of their property by a Depository specialist through an announcement of records.<sup>18</sup> Any deal or buy of offers will happen through the Depository.<sup>19</sup>

### **Framework of Depository:**

The depository has four important things in it

- 1) **Depository participants:** DP acts like an agent which act as a share broker or a middle man in trading of securities . A specific ID is given by them to deal within the securities,

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<sup>17</sup> <https://accountlearning.com/depository-system-and-dematerilization-functions-procedure-benefits/4th>  
november,7:38pm.

<sup>18</sup> *Ibid.*

<sup>19</sup> *ibid.*

DP acts as an intermediary which just informs and gives information to the investors and which help them to deal in the securities.

- 2) **Central Depository:** SEBI guidelines are so strict and has to be followed by the depository so there is one place where all the securities are stored at one place in centralized form and each and transaction is being watched.
- 3) **Share Registrar:** Share Registrar is a body, which controls every issue of the securities. The transfer agent manages the transfer of securities in trading of securities.<sup>20</sup>
- 4) **Clearing and Settlement Corporation:** Trading of securities happens in the markets every day, and there are millions of transaction so to maintain the funds between traders this corporation works for these major things.<sup>21</sup>

### **Trading of shares in depository system:**

Trading can only happen when there are two parties to it, and even when both the parties agrees to buy and sell there securities then only trading can happen in the system. The seller must be ready to sell the securities and then when he is ready he is supposed to give delivery form to the buyer.<sup>22</sup> The form also contains the information about the parties so as a safe side.<sup>23</sup> There are two type of delivery form

1. Market trade: Market trade is a trade in an actual market.<sup>24</sup>
2. Off-market trade: This is trade between the acquaintance or known house members.<sup>25</sup>

### **TYPES OF DEPOSITORIES**

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<sup>20</sup> <https://accountlearning.com/depository-system-and-dematerilization-functions-procedure-benefits/4th> novemeber,8:02pm.

<sup>21</sup> *Ibid.*

<sup>22</sup> *Ibid.*

<sup>23</sup> *ibid.*

<sup>24</sup> *ibid.*

<sup>25</sup> *ibid.*

There are only two existing depositories in India NSDL and CDSL. They both act like a bank and store various securities in an electronic form. They are authorized by SEBI and also inspected and governed by it.

**NSDL (National securities depositories limited):** It was set up as the first depository in India, it was set up as a public company and a board of directors manages it.<sup>26</sup> NSDL was formed in August 1996 at Mumbai, financial capital of India. Industrial Development Bank of India (IDBI), Unit Trust of India (UTI), and National Stock Exchange (NSE) promotes NSDL. Some of the prominent banks in the country also have stake in NSDL.<sup>27</sup>

**Functions:**

The NSDL perform multiple functions through agents .

- 1) It enables the dematerialization and rematerialisation of the different securities.
- 2) It maintains the holding of the government bonds ,shares and debentures in an electronic way.
- 3) Carries out settlement of trades not done on the stock exchange .<sup>28</sup>
- 4) Receipts of non-cash corporate benefits like bonus, rights and so on in electronic form.<sup>29</sup>

**CSDL (Central Depositories Service Limited):** It is the one of the second largest depositories in india and based in Bombay, established in 1999. Each transaction of CSDL is being done at one place and each transaction is in the eye of centralized system. It charges some fees on every transaction and customer can prefer any depositories whichever price is suitable for them.

**Functions:**

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<sup>26</sup> M.Y KHAN,INDIAN FINANCIAL SYSTEM,8.31,2007.

<sup>27</sup> <http://www.prostocks.com/faq/13-demat/194-what-is-nsdl.html,3rd> november,5:15pm.

<sup>28</sup> M.Y KHAN,INDIAN FINANCIAL SYSTEM,8.32,2007.

<sup>29</sup> *Ibid.*



The CDSL performs various functions

- 1) It provide wide range of network and convenience to people participating through it.
- 2) Protecting and storing the wide range of securities of the people .
- 3) To provide complete help and guidelines to the participants .
- 4) To provide customer requirements.
- 5) Its provide very diverse and wide range of securities and give wide options to customers and also give competitive rates then others .

It is basically same as the NSDL but it came later into picture .

### **BENEFITS OF DEPOSITORY**

- 1) It is a secure way of keeping and holding securities in an electronic form.
- 2) The securities can be immediately transferred to some other.
- 3) Its saves the stamp duty cost as they are being dealt in e-way.
- 4) Its basically reduces the cost and time .
- 5) It is also possible to get securities allotted to in public offerings directly in the electronic form, in public issue application from there is a provision to indicate the manner in which an investor wants the securities allotted.<sup>30</sup>
- 6) The market opportunities for a broker are substantially increased due to the elimination of forged documents ,his exposure with the person gets over once he receives the securities in his account, this is unlike in the case of a physical securities where the broker is exposed over a substantially longer time.<sup>31</sup>
- 7) Elimination of a bad delivery and transfer of the title of security the time of exchange of assets ,eliminates the buyers disadvantage with respect to the genuineness and title of the assets received, compared to a seller.<sup>32</sup>

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<sup>30</sup> S.Mohan and R.Elangovan, Financial services, 486,2008.

<sup>31</sup> S.Mohan and R.Elangovan, Financial services, 487,2008.

<sup>32</sup> Ibid

- 8) The easy way of dealing in depositories may also attract the foreign investors and it would boost our economy.
- 9) The safety and security given by depositories would attract the healthy investors and would bring more and more money to the secondary market.
- 10) Transfers to different persons and at different places would not be possible with depositories as it is physically hard to transfer because of the huge geographical location of the India.
- 11) Money arising out of bonus, split or etc. will be directly added to your respective account automatically, this also gives ease of dealing with securities.

### **SAFEGUARDING OF SECURITIES**

On being satisfied that it is necessary in public interest/in the interest of the investors, the SEBI can call for information from, or make an enquiry or inspection in relation to the affairs of, the issuer or participants.<sup>33</sup> SEBI has also powers to give an proper way in the benefit of investors for their orderly growth and appreciation in their money. To avoid the malpractices or the bad events which effects the interest of the investors in the market and the protection of the investors is very necessary as the trust in them allows to run the depositories if the trust goes away from the investors they will not invest anything and the slowly and gradually market will get stagnant and the money will not move in the economy and that is not good for the development of the country. The money in circulation is the money useful and so safeguarding the securities of the investors. SEBI is there to help and protect the rights but if one is not satisfied with it he/she can move to SAT.

*“Penalty for failure(a)by a person to (1)furnish nay document /book /returns report to SEBI within the specified time,(2)file any return/furnish any information,books,other documents within the time specified by-laws,(3)maintain books of accounts;(b)by a depository participant ,issuer/agent/any person registered with SEBI as an intermediary to enter into agreement under SEBI any*

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<sup>33</sup> M.Y KHAN,INDIAN FINANCIAL SYSTEM,8.22,2007.

*grievances out of depository within specific timeperiod,(c)comply with directions issued by the SEBI is rs 1lakh for each default or 1 crore whichever is less. ”<sup>34</sup>*

## **CURRENT CHANGES IN DEPOSITORY SYSTEM**

Markets regulator SEBI has decided that all demat accounts would be considered as a basic services demat account (BSDA) unless the demat account holder specifically opts to continue with a regular demat account.<sup>35</sup> Depository is the institution, which is very dynamic and keeps on changing as per the need of the people and the investors because at the end of the day it should be customer friendly and help the investors in ease of operation.

This SEBI on the day of August 27, 2012, which allowed existing qualified demat account holders to change over their customary demat accounts into BSDAs.<sup>36</sup> Storehouse Participants (DPs) need to survey the qualification of the advantageous proprietor (demat account holder) toward the finish of the present charging cycle and change over qualified demat accounts into BSDAs.<sup>37</sup> Discovering couple of takers after the BSDA was presented and the transformation alternative set up, SEBI brought this choice with the target of accomplishing more extensive money related consideration and to support holding of demat accounts.<sup>38</sup>

The Securities and Exchange Board of India (SEBI) planned to bring down on the depository receipts (DRs) as to keep an eye on the flow of black money into the market.<sup>39</sup> The new principles are relied upon to expand consistence for storehouse banks as they will be solicited to give month

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<sup>34</sup> M. Y KHAN, INDIAN FINANCIAL SYSTEM, 8.23.2007

<sup>35</sup> SEBI changes demat account rules, THE HINDU BUSINESS LINE, DECEMBER 11, 2015 Available at- <http://www.thehindubusinessline.com/markets/stock-markets/sebi-changes-demat-account-rules/article7977219.ece>

<sup>36</sup> *Ibid.*

<sup>37</sup> *Ibid.*

<sup>38</sup> *Ibid.*

<sup>39</sup> shrimi choudhary, *Sebi planning to tighten deposit receipt regulation*, Business standard , july 20, 2017 Available at- [http://www.business-standard.com/article/markets/sebi-planning-to-tighten-depository-receipt-regulations-117072000068\\_1.html](http://www.business-standard.com/article/markets/sebi-planning-to-tighten-depository-receipt-regulations-117072000068_1.html)

to month subtle elements from supporters if there should arise an occurrence of recoveries and exchanges.<sup>40</sup>

## CONCLUSION

- There are only two depositories in India named (NSDL and CDSL)
- There are depository participants which act as intermediary amongst the investors so it lead to smooth functioning of the system and they also help in converting out old style of securities in the de-mat form for the ease of operation.
- There is also and unique ISIN number which is allotted to each and every securities in the prescribed standard form so it gives unique identity and it reduces the chances of cheating and mal-practise among the investors
- The depository has created a wave of healthy and safe environment for the securities in the market so it increased the number of investors in the market and would overall lead to development in the society.
- Dematerialisation is a facility or we can say a good thing for the investors that it company takes the shares of the investors which are in the physical form and for the ease of operation convert them into the electronic way and credited to the account at the discretion of the investors.
- Market trade and Off market trade are the two type of trades .
- Depository is very customer friendly and work as per the need of investors for example there is also one option of Re-materialisation of securities where the electronic form of securities are converted in the physical form
- Depository is very time and cost reducing thing so it gives ease of operation and promotes the investors.
- It basically acts as bank it keeps your securities safe and in electronic form in one place
- The system of depository is completely automatic the money and everything is credited to the account directly and you don't have to work and waste time on it.

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<sup>40</sup> *Ibid.*

- The depository is also controlled or we can say there are bodies which have an upper hand over the depository and keeps eye on the working of depository,(SEBI).

