UNIT-IV
Depositories in India

Dr S Rukhsana Khalid (Phd Finance(UOHYD))

History

- The first depository was set up way back in 1947 in Germany.
- In India it is a relatively new concept introduced in 1996 with the enactment of The Depositories Act, 1996.
- Their operations are carried out in accordance with regulations made by SEBI, bye-laws and rules of Depositories Act and SEBI (Depositories and Participants) Regulations Act, 1996 .

What is Depository ?

- A Depository holds securities of investors in electronic form.

- A system in which securities of an investor are held by depository on behalf, and at the request, of an investor in an Electronic Form.

- This system is also know as ***Scrip Less Trading System or Paper- Less*** Trading System.

Need for Depository

Before introduction of Depository system, the problems faced by investors and corporate in handling large volume of paper were as follows:

- Bad deliveries
- Fake certificates
- Loss of certificates in transit
- Mutilation of certificates
- Delays in transfer
- Long settlement cycles
- Mismatch of signatures
- Delay in refund and remission of dividend etc

Features of Depository System

- In the depository system, securities are held in depository accounts, which is more or less similar to holding funds in bank accounts.
- Transfer of ownership of securities is done through simple account transfers.
- This method does away with all the risks and hassles normally associated with paperwork.
- Consequently, the cost of transacting in a depository environment is considerably lower as compared to transacting in certificates.

Constituents of Depository System

There are basically four participants:

- The Depository Participants
- The Depository
- The Issuing Company
- The Beneficial Owner

Depository Participant

- A Depository Participant (DP) is an agent of the depository through which it interfaces with an investor.
- A DP can offer depository services only after it gets proper registration from SEBI.
- A Depository Participant (DP) offers depository services to investors.
- The DP is a CDSL or NSDL-authorized agent who serves as a link between the account holder or Beneficial Owner (BO), the issuing company, CDSL, the BO's broker and the Stock Exchange

Who can be a Depository Participant?

- In terms of the Depositories Act, 1996, SEBI (Depositories & Participants) Regulations,1996, only the following entities are eligible to become a Depository Participant:
- Financial Institutions,
- Banks, including approved foreign bank
- Custodians,
- Stockbrokers,
- A clearing corporation or a clearing house of a stock exchange
- A non-banking finance company,
- A registrar to an issue or share transfer agent.

2. **Depository** : A firm wherein the securities of an investor are held in electronic form. It Functions as a custodians of securities of its clients.
3. **Issuer:** The company which issues security. Agreement by issuer
4. **Beneficial Owner:** Investors using depository services of the depository is known as the Beneficial Owner (BO), and they have to maintain a demat account to access the functions of the CDSL as well as NSDL, including the facilities of dematerialization and transferring of securities. A person whose name is recorded as such with a depository. He is the Real owner of the securities.

Advantages/Merits of Depository System

To the Investors –

1) Quick transfer of funds and securities
2) Elimination of all risks associated with physical certificates
3) No stamp duty
4) Minimized chances of fraud, theft and counterfeiting of securities
5) Provides insurance cover
6) Statement of accounts
7) Direct disbursement of non-cash benefits
8) Faster settlement cycle
9) Reduction in brokerage

To the Company –

1) Information about the beneficiary owners and their holdings.
2) Easy to declare dividends, bonus, etc.
3) Reduction in investors complaints
4) No delays in sending notices and annual reports

BANK	DEPOSITORY
Holds funds in an account	Hold securities in an account
Transfers funds between accounts on the instruction of the account holder	Transfers securities between accounts on the instruction of the account holder
Facilitates transfer without having to handle money	Facilitates transfer of ownership without having to handle securities
Facilitates safekeeping of money	Facilitates safekeeping of securities

Depositories in India

At present two Depositories are registered with SEBI.

1. **NSDL (National Securities Depository Limited) -** It was registered by the SEBI on June 7, 1996 as India's first Depository to facilitate trading and settlement of securities in the demat form. It is promoted by IDBI, UTI, NSE.
2. **CDSIL (Central Depository Services (India) Limited)** - It commenced its operations during Feb 1999 and was promoted by Stock Exchange, Mumbai in association with Bank.

CDSL's & NSDL's primary focus is to provide safe, useful, reliable and secure depository services.

NSDL

Technology, Trust & Reach

NSDL (National Securities Depository Limited)

- NSDL is the oldest and largest electronic depository of securities in India, which started its operation in the year 1996, based in Mumbai, Maharashtra.
- It is the first depository in Indian to offer trading and settlement of securities in electronic or demat form.
- The NSDL is promoted by the country's some of the largest banks and institutions, i.e. IDBI Bank, UTI and National Stock Exchange (NSE).
- There are more than 1.5 crore active investor's accounts in NSDL.

- NSDL is having around 26000 service centers covering approx 1900 cities.
- Their demat custody is not limited to only shares and their service includes shares, bonds, debenture, commercial papers, mutual funds and so on.
- Basic services facilitated by NSDL include account maintenance, dematerialization, settlement of trade, and re-materialization.
- It also facilitates inter-depository transfers, off-market transfers, pledge, lending, and hypothecation of securities.

CDSL

BO PROTECTION FUND

CDSIL (Central Depository Services (India) Limited)

- CDSL is another electronic depository of securities in India, which started its operation in the year 1999 and also based in Mumbai, Maharashtra.
- It is the second largest securities depository in India and facilitates a book-entry transfer.
- It is promoted by some prominent banks and financial institutions of India, such as State Bank of India (SBI), HDFC Bank, Bank of Baroda, Bank of India, Standard Chartered Bank, and Bombay Stock Exchange (BSE).

- It provides the same function as NSDL like holding of securities in dematerialized form and facilitates trading and settlement of securities in electronic or Demat form.
- In CDSL, they offer services to hold equity, debentures, bonds, commercial papers, government securities, certificate of deposit, mutual funds etc.
- As of 2017, CDSL has around 161 branches and approx 1.10 crore client accounts operating with them.

DEPOSITORY

NSDL	CDSL
National Securities Depository Limited	Central Depository Services Limited
Market: National Stock Exchange (NSE)	Bombay Stock Exchange (BSE)
Promoters: Industrial Development Bank of India (IDBI) Unit Trust of India (UTI)	State Bank of India (SBI) Bank of India (BOI)

DEMATERIALISATION

- When one buys a share (a share represents a part ownership in a company) the only way to claim your ownership is by producing your share certificate.

- A share certificate is nothing but a piece of document entitling you as the owner of the shares in a company.

- Before 1996, the share certificate was in paper format however post 1996, the share certificates were converted to digital form.

- The process of converting paper format share certificate into digital format share certificate is called ***"Dematerialization"*** often abbreviated as ***DEMAT***.

- The share certificate in DEMAT format has to be stored digitally.

- The storage place for the digital share certificate is the ‘DEMAT Account’ which is linked to a trading account.

- NSDL and CDSL will do exactly the same, offers the service of Demat account in which your name will have all the shares in electronic format you have bought.

Bottom line : NSDL or CDSL is a corporate entity which holds the shares in electronic form, against your name, in your account and linked with your trading account.

Definition of Dematerialization

- Dematerialization can be defined as the process in which, at the request of the investor, the company takes back the traditional share certificates of the investor, and same number of securities are credited to his/her trading account in the electronic form.
- Shares in dematerialised form do not contain the distinctive number.
- Moreover, the shares are fungible in the sense that all the shareholdings are identical and interchangeable.
- First of all, the investor needs to open the account with the Depository Participant (DP), after which the investors request dematerializing the shareholdings through the DP so that the dematerialised shares are credited to the account.

ADVANTAGES OF DEMAT ACCOUNT

- The bonus/right shares allotted to the investor will be immediately credited into his account.
- There is no risk due to loss on account of fire, theft or mutilation.
- Transaction costs are usually lower than that in the physical segment.
- A demat account also helps avoid problems typically associated with physical share certificates.

  For example: delivery failures caused by signature mismatch, postal delays and loss of certificate during transit.

- Further, it eliminates the risks associated with forgery and due to damaged stock certificates.
- Demat account holders also avoid stamp duty (as against 0.5 per cent payable on physical shares) and filling up of transfer deeds.

DISADVANTAGES OF DEMAT

- Trading in securities may become ***uncontrolled*** in case of dematerialized securities.
- It is incumbent upon the capital market regulator to keep a close watch on the trading in dematerialized securities and see to it that trading does not act as a detriment to investors.
- For dematerialized securities, the role of key market players such as ***stock-brokers needs to be supervised*** as they have the capability of manipulating the market.
- Multiple ***regulatory frameworks*** have to be conformed to, including the Depositories Act, Regulations and the various Bye-Laws of various depositories.
- Agreements are entered at various levels in the process of dematerialization. These may cause worries to the investor desirous of simplicity.

Process of dematerialization

The following are the steps involved in the process of dematerialization:

1. The investor is required to fill up the **Demat Request Form** (DRF) available with the DP and submit it along with the physical certificates which need to be dematerialized.
2. Depository participant (DP) intimates the Depository of the request from his approved user hardware system.
3. Depository participant submits the certificates to the Registrar.
4. Registrar confirms the dematerialization request from depository.

5. After dematerializing certificates, Registrar updates the accounts and informs depository of the completion of dematerialization.
6. Depository updates its accounts and informs the depository participant.
7. Depository participant updates the account and informs the investor.


Investor opens account with DP
Fills DRF for registered shares
Investor lodges DRF and certificates with DP
DP intimates the depository
Depository intimates registrar / issuer
DP sends certificates and DRF to Registrar / issuer
Registrar / Issuer confirms demat to Depository
Depository credits investor account