

# Increasing focus on compliance in New India



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Human race continues to evolve. We learn from our past and work towards making our future better. We tirelessly put in efforts to improve social environment by continuously bringing in social, political, legal and technological changes aiming at better civilisation. Laws can't remain static and have to change from time to time to reflect changes

in circumstances, human behavior, innovation and technological advancements.

Normally changes are resisted and resistance generates friction. We find excuses and try to find ways to avoid changes, most of the time, without realising the consequences. We would have lost more time, energy and opportunities in resisting changes than by implementing. India is no exception to all of these. Current dispensation is working overnight to change a lot of old practices. Demonetisation, GST, RERA and IBC are path breaking and have surprised supporters and critics alike. More than 1200 old Laws have been scrapped. One wonders whether many of them were ever implemented and if so in right spirit.

We are building a New India where implementation and compliance is given as much importance as framing of laws. Awareness and need for privacy as well as data protection has increased many fold.

Financial and regulatory defaults by listed / unlisted entities have been on the rise. Magnitude of recent cases has raised doubts about independence and ethical conduct of Auditors and Rating agencies. Lowering of governance standards by financial institutions and management has surprised all of us. Market has started punishing such companies and we are observing huge erosion in the market capitalisation of such entities.

RBI, SEBI, IRDAI, PFRDA, TRAI, FSSAI, and other regulators are continuously working to find ways to improve compliance standards in their respective fields. Our capital market regulator SEBI is also busy in enhancing compliance levels. Regulations are constantly tightened for listed entities and market intermediaries. In the period between July 2018 and June 2019 SEBI has issued close to one hundred circulars largely with a view to improve governance and compliance, audit procedures, enhancing technological developments etc. SEBI has

enacted or amended more than twenty five Regulations during the same period covering Takeover, Delisting, Insider trading, LODR, Buy-backs and intermediaries.

Some of the important recent circulars / regulations are as under

SEBI circular – 12th July 2018 – *Discontinuation of acceptance of cash by Stock Brokers*. Government is encouraging 'Less Cash' society by promoting electronic and cheque payments which provide necessary trail and avoid dubious transactions. Over a period of time, cash transactions for capital market activities have dropped to negligible levels and by issuing this circular SEBI has ensured that Stock Brokers do not receive or make cash payments while dealing with their clients. This will bring an end to theoretical possibility of cash transactions between stock broker and his clients and will ensure higher transparency in dealings.

SEBI circular – 10th August 2018 – *Enhanced monitoring of Qualified Registrars to and Issue and Share Transfer Agent*. SEBI constituted a committee under chairmanship of Mr R Gandhi, Former Deputy Governor of RBI to look into desirability of bringing more market participants, including large RTA serving more than 2 crore folios (QRTAs), under ambit of Market Infrastructure Institutes (MIIs). Committee suggested not to include RTAs as MII and to continue with their ownership structure. However since QRTAs are critical for servicing MFs and Corporates, SEBI issued a circular to enhance their monitoring and brought in additional stringent norms for their functioning.

Compliance requirements for monitoring QRTA has been enhanced wherein they will have to adopt and implement internal policy framework. They will be subject to periodic reporting involving key risk areas including data security, BCP, governance structures, risk insurance, higher standards of investor servicing and grievance redressing. Their Risk Management Policy is required to be well documented which should cover areas such as frauds, technology risk, market risk, legal risk, cyber security, general business risk and reputational risk. QRTAs must have systems, policies and procedures in place to identify, monitor and manage such risks.

QRTAs are required to have proper Business Continuity Plan (BCP) in place so as to ensure that investors and client servicing is not compromised. QRTAs have to maintain accurate and up to date records and should ensure that proper backups are available in case of loss of records. While providing access to database to other agencies for investor servicing or for legal compliance, necessary confidentiality agreement is required to be signed and such data sharing is required to be done following appropriate protocols, controls and processes without compromising on security aspects. Infrastructure and processing capacity of QRTAs should be scalable

which should be reviewed from time to time to enable upgradation as may be required to maintain smooth functioning and quality of service.

Investor friendly online facility is required to be maintained where investors can post their queries and grievances. Appropriate insurance cover should be available to QRTAs to cover risks arising out of frauds, errors of omission and commission. QRTAs have to form Audit committee, Nomination and Remuneration committee and IT Strategy committee. These committees have to meet regularly and review related areas of operations. Board of Directors of QRTAs have to seek and review incidents to ensure data security and investor protection. Quarterly report on compliance of all above is required to be filed with SEBI.

SEBI circular - 22nd October 2018 - *Total expense ratio and performance disclosure for Mutual Funds (MF)*. This circular aims to bring in transparency, reduce churning of portfolios and avoid mis-selling. Implementation ensures that expenses incurred for a particular scheme is charged to that scheme and should not be borne by AMC or any other entity. This circular directs MFs on how to calculate, provide and pay commission. Circular mandates publishing scheme wise performance on the website in a manner that investor can apply filters on various fields to compare performance of scheme vis a vis benchmark. This will bring clarity on accounting aspect and empower investors to take considered decision while investing in any scheme.

SEBI circular – 17th December 2018 – *Early warning mechanism to prevent diversion of client securities*. Few instances of diversion of securities of their clients by defaulting brokers prompted SEBI to issue this circular to safeguard the interests of investors. This circular directs Stock Exchanges, Clearing Corporations and

Depositories to develop advance warning mechanism to avoid diversion of securities by broker. These agencies are required to work together and share necessary information amongst themselves of lead activities which can point towards a potential default of broker. Threshold for such alarms would also be decided by these agencies. This will minimise the risk of diversion of securities from client account by defaulting broker.

SEBI circular of 21st January 2019 made amendments in Prohibition of Insider Trading (PIT) Regulations of 2015. Board of Directors of listed entity, intermediaries and fiduciaries is required to maintain digital database of persons and entities, along with their PAN, with whom price sensitive information is shared. CEO, MD or such other person would be responsible to ensure that adequate effective system is put in place to prevent insider trading. Audit committee is required to review that proper systems are in place to comply with PIT regulation. Whistle Blower policy to report instances of leakage of unpublished price sensitive information is required to be in place. Promoter group is required to make initial and continual disclosures.

While Government and Regulators are doing what is required at their level, it is important for all stakeholders and participants to honestly perform their roles and duties as well as maintain high standards of integrity while complying with laws of the land. It is necessary to obey the law, even when no one is watching, like not crossing the red signal while driving, knowing that there is no policeman around and the camera above is also not capturing your movement. We all certainly want a better and more compliant India and we also know that it would happen when all of us work together. With our consistent efforts, our compliance index will certainly go up which will help us find respectful place in the World.

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