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Analysing developments impacting business

SEBI GUIDELINES TO SECURITIES MARKET INTERMEDIARIES - UNDER THE PMLA 2002

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A. Introduction

The Securities and Exchange Board of India (SEBI) vide its circular dated 3 February 2023, has updated its 'Guidelines on Anti-Money Laundering (AML) Standards and Combating the Financing of Terrorism (CFT) / Obligations of Securities Market Intermediaries under the Prevention of Money Laundering Act, 2002 and Rules framed thereunder' (Guidelines). The Guidelines are applicable to all intermediaries registered with SEBI and recognized stock exchanges in India. The updated Guidelines have introduced a few key additions and explanations to the previous SEBI Circular dated 15 October 2019 (now rescinded by virtue of this circular) and has incorporated elements from several notifications issued by the Ministry of Home Affairs (India) in the recent past, with respect to powers of the Central Government under Section 51A of the Unlawful Activities (Prevention) Act, 1967 (UAPA).

B. Key pointers

The key points and changes in the updated Guidelines are:

- (i) **Scheduled Offences:** In line with the Prevention of Money Laundering Act 2002 (PMLA), any violation of the prohibition imposed on manipulative and deceptive devices, insider trading and substantial acquisition of securities / control as stipulated under Section 12A read with Section 24 of the SEBI Act, 1992 will be considered as a scheduled offence under Schedule B of PMLA.¹
- (ii) Policy for acceptance of clients by registered intermediaries and stock exchange:
 - (a) Enhanced client due diligence has been prescribed for client of special category (CSC), and 'Non-Face-To-Face clients' have been explained as 'clients who open accounts without visiting the branch / offices of registered intermediaries or meeting the officers of the registered intermediaries'. On the other hand, it is clarified, that video based

¹ Prevention of Money Laundering (Amendment) Act, 2012.

customer identification process will be treated as 'face-to-face' onboarding of clients.

- (b) Registered intermediaries are required to ensure that a client's account is not opened without the intermediary completing the client due diligence measures. When the identity of the client or the information furnished by the client is suspected to be non-genuine, a suspicious activity report is to be filed by the intermediary. Unfortunately, the guidelines are silent on the authority with whom such a report has to be filed i.e. FIU-IND or SEBI.
- (c) In relation to the continuing clients, the intermediary is expected to continually evaluate the identity of its clients. Where there is suspicious trading, it will evaluate and freeze the account and shall discontinue its business with the client.
- (d) Registered intermediaries may permit a client to act on behalf of another person / entity only under specified circumstances. While these circumstances are not articulated in the Guidelines, one will have to assume that the same principle will apply that the other person / entity's identity is capable of evaluation.

(iii) Reliance on third party for carrying out client due diligence

- (a) Registered intermediaries have been previously permitted to rely on third parties for the purpose of identification/ verification of the client. In line with rule 9(2) of the Prevention of Money Laundering (Maintenance of Records) Rules 2005 (PMLA Rules), the Guidelines lay down the following safeguards to be observed by registered intermediaries:
 - the third party should immediately send all client due diligence information of the client to the registered intermediary;
 - ensure that the third party is regulated, supervised or monitored and has measures in place for compliance with client due diligence and record-keeping; and
 - third party is not situated in any country or jurisdiction which is classified as a high risk jurisdiction by the Financial Action Task Force (FATF).
- (b) The registered intermediary will be primarily and ultimately responsible for the diligence of the client.
- (c) All cash transactions exceeding INR 10 lakhs or its equivalent in foreign currency, or series of transactions integrally connected or remotely connected / related, whose aggregate value exceeds INR 10 lakhs, must be recorded by the intermediary. Further, credits / debits into or from any non-monetary account are to be noted and where necessary, suspicious transaction reports are to be filed.

(iv) List of designated individuals / entities

- (a) Registered intermediaries are required to take note of the updated lists of persons designated as 'terrorists' by the Ministry of Home Affairs (MHA), under Section 35(1) of the UAPA.
 - (b) Stock exchanges and registered intermediaries are required to file a suspicious transaction report (STR) with the Financial Intelligence Unit of India (FIU-IND), covering all transaction, specified under Section 35(1) of UAPA.²
 - (c) A copy of STR and communication with the FIU-IND shall be parallelly shared with the UAPA Nodal Officer of the State / Union Territory where the account is held.
- (v) Jurisdictions which do not or insufficiently apply the FATF Recommendations: Registered intermediaries are expected to update themselves with the FATF Statements released from time to time and are also expected to update themselves with publicly available information relating to countries that do not or insufficiently apply the FATF Recommendations.

C. Conclusion

The Regulator has made efforts in guiding the regulated intermediaries over the last 2 (two) years, by specifying the requirement of and tightening the due diligence process for onboarding clients. By introduction of PMLA and UAPA provisions in these guidelines, SEBI is bringing to the attention of the registered intermediaries that breach of PMLA and UAPA provisions would invite serious consequences under the anti-corruption laws in India. The registered intermediaries now have to ensure that they have the necessary KYC policies in place, and due diligence process is conducted accordingly for low risk and high-risk clients. While this may cast an increased burden of cost for the registered intermediaries it will be worth the effort.

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² Section 35(1) of the Unlawful Activities (Prevention) Act, 1967 reads as follows:

"(1) The Central Government, may, by notification in the Official Gazette -

- (a) add an organisation to the First Schedule or the name of an individual in the Fourth Schedule;
- (b) add also an organisation to the First Schedule, which is identified as a terrorist organisation in a resolution adopted by the Security Council under Chapter VII of the Charter of the United Nations or the name of an individual in the Fourth Schedule, to combat international terrorism;
- (c) remove an organisation from the First Schedule or the name of an individual from the Fourth Schedule;
- (d) amend the First Schedule or the Fourth Schedule in some other way."