

Capital Market: Structure and Emerging Trends

Part-5

Topic- Depository system in India

1.1 Depository System: Meaning and its working

Depository System is concerned with conversion of securities from physical to electronic form, with script less trading and quick settlement cycles. In the Depository System, the ownership and transfer of securities takes place by means of electronic book entries.

National Security Depository is first Depository registered on June 7, 1996 with SEBI. It was set up as a result of the Depositories Act, 1996 as a public limited company and promoted by Industrial Development Bank of India, Unit Trust of India and National Stock Exchange to facilitate trading and settlement of securities in Dematerialised form. Launching of NSDL is a significant reform in the Capital market, which is playing a crucial role in driving market efficiency.

The Depository and Depository Participants are the service providers to the investors. The service is that of custody of securities and settlement of trades therein. The services that the Depositories provide revolve around the securities issued by corporate. The securities have to be formally admitted to the Depository System to enable the Depository to provide its services to the investors.

The first step for the investors in the Depository System is to open an account with any of the Depository Participant of their choice. Then for getting the shares dematerialised, they have to file one request form together with share certificates.

The Depository Participant will send the share certificates to the Company Registrars through Depository for confirmation of its genuineness. After checking the record, the Registrar will destroy the Certificates and send confirmation of dematerialisation of shares to the Depository Participant to credit the holding in the investor account electronically.

In the Depository System, the ownership and transfer of securities take place by means of electronic book entries. At the outset, this system rids the capital market of the dangers related to handling of paper. Dealing in physical securities, the investor has to take the brunt of security risks of theft stocks,

mutilation of Certificates, loss of certificates during movements through and from the Registrars, thus exposing him to the cost of obtaining duplicate Certificates and advertisements etc. The Depository System provides secured and faster transfer of securities.

1.2 Objectives of the Depository System

- It removes the occurrences of forgery, duplicate share certificates, and bad deliveries.
- This can increase the liquidity of securities by making a way for easy transfer.
- Also, it can avoid the delay caused in the transfer of securities.
- Furthermore, it reduces the cost of a transaction for the investors.
- It enables withdrawal and surrender from the securities with great ease.
- It also maintains a perfect record of the holdings for an investor. This is because all the details are stored in electronic form.
- This also provides infrastructure for services in capital markets.
- By complying to global standards, it does attract foreign investors.

1.3 Services provided by Depository

Following are the services offered by depository:

- Dematerialization (usually known as Demat) is converting physical certificates to electronic form
- Rematerialisation, known as Remat, is reverse of Demat, i.e. getting physical certificates from the electronic securities
- Transfer of securities, change of beneficial ownership
- Settlement of trades done on exchange connected to the Depository
- Inter-Depository Transfers i.e. transfer of securities from an account in one depository to an account in another depository. This facility is quite similar to the account transfers within NSDL.

1.4 Structure of Depository System

- Central Depository
- Share Registrar Transfer Agent
- Clearing and Settlement Corporation
- Depository Participant

➤ **Central Depository**

Central depository is an organization with which all the shares, belonging to the shareholders are kept and the electronic system takes care of them.

There are two central depositories in India, namely National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited (CDSL) that are registered with SEBI.

a) National Securities Depository Limited (NSDL)

It was registered by SEBI on June 7, 1996 as India's first depository to facilitate trading and settlement of securities in the dematerialized form. It deals with National Stock Exchange (NSE).

b) Central Depository Service (India) limited (CSDL)

It commenced its operations in February 1999. It was promoted by Stock Exchange, Mumbai in association with Bank of Baroda, Bank of India, State Bank of India and HDFC Bank. It deals with Bombay Stock Exchange(BSE).

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➤ **Share Registrar:**

Share Registrar is an authority who controls the issue of securities. Along with this, the transfer agent arranges for the transfer of securities in the case of buying or selling of securities.

➤ **Clearing and Settlement Corporation:**

A clearing corporation is an organization associated with an exchange to handle the confirmation, settlement and delivery of transactions. Clearing corporations fulfil the main obligation of ensuring transactions are made in a prompt and efficient manner. Clearing corporations are also referred to as "clearing firms" or "clearing houses."

➤ **Depository Participant (D.P):**

Depository interacts with its clients or investors through its agents, called Depository Participants normally known as DPs. For any investor or client, to avail the services provided by the Depository, has to open Depository account, known as Demat A/c, with any of the DPs.

In this way, a depository participant (DP) serves as a mediator between the depositories (NSDL and CDSL) and investors. Considered similar to a bank, traders can get a Demat account opened with a DP along with other facilities that help them invest and or trade efficiently.

As per SEBI regulations, financial institutions, banks, stockbrokers, etc., can be Depository Participants.

Benefits of Depository system:

- a. Reduction in paper work.
- b. Elimination of risks associated with physical scrips such as theft, forgery, mutilation, loss of share certificates etc.
- c. Elimination of bad delivers.
- d. Increased liquidity of scrips through speedy settlement and reduction in delays in registration.
- e. Low transaction costs for purchase and sale of securities compared to physical mode.
- f. No stamp duty on transfer of securities.
- g. Facilities the issuer companies to update the information regarding shareholders and to communicate with them in better ways.
- h. Attract foreign investors and promoting foreign investment.
- i. Emergence of healthy and efficient capital market.
- j. Greater opportunity for the development of sophisticated custodial services etc.