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The Managing Director and CEO
Bombay Stock Exchange
Phiroze Jeejeebhoy Towers
Dalal Street
Mumbai 400001

The Managing Director
National Stock Exchange of India Ltd.,
Exchange Plaza
Bandra Kurla Complex
Bandra (E)
Mumbai- 400 051.

Dear Sir,

Sub:- Introduction of Direct Market Access facility

Direct Market Access (DMA) is a facility which allows brokers to offer clients direct access to the exchange trading system through the broker's infrastructure without manual intervention by the broker. Some of the advantages offered by DMA are direct control of clients over orders, faster execution of client orders, reduced risk of errors associated with manual order entry, greater transparency, increased liquidity, lower impact costs for large orders, better audit trails and better use of hedging and arbitrage opportunities through the use of decision support tools / algorithms for trading.

While ensuring conformity with the provisions of the Securities Contract (Regulations) Act, 1956 (42 of 1956), Stock Exchanges may facilitate Direct Market Access for investors subject to the following conditions:

1. Application for Direct Market Access (DMA) facility

Brokers interested to offer DMA facility shall apply to the respective stock exchanges giving details of the software and systems proposed to be used, which shall be duly certified by a Security Auditor as reliable.

The stock exchange should grant approval or reject the application as the case may be, and communicate its decision to the member within 30 calendar days of the date of completed application submitted to the exchange.

The stock exchange, before giving permission to brokers to offer DMA facility shall ensure the fulfillment of the conditions specified in this circular.

2. Operational specifications

All DMA orders shall be routed to the exchange trading system through the broker's trading system. The broker's server routing DMA orders to the exchange trading system shall be located in India.

The broker should ensure sound audit trail for all DMA orders and trades, and be able to provide identification of actual user-id for all such orders and trades. The audit trail data should be available for at least 5 years.

Exchanges should be able to identify and distinguish DMA orders and trades from other orders and trades. Exchanges shall maintain statistical data on DMA trades and provide information on the same to SEBI on a need basis.

The DMA system shall have sufficient security features including password protection for the user ID, automatic expiry of passwords at the end of a reasonable duration, and reinitialisation of access on entering fresh passwords.

Brokers should follow the similar logic/priorities used by the Exchange to treat DMA client orders. Brokers should maintain all activities/ alerts log with audit trail facility. The DMA Server should have internally generated unique numbering for all such client order/trades.

A systems audit of the DMA systems and software shall be periodically carried out by the broker as may be specified by the exchange and certificate in this regard shall be submitted to the exchange.

The exchanges and brokers should provide for adequate systems and procedures to handle the DMA trades.

3. Client Authorization and Broker – Client agreement

Exchanges shall specify from time to time the categories of investors to whom the DMA facility can be extended. Initially, the permission is restricted to institutional clients.

Brokers shall specifically authorize clients for providing DMA facility after fulfilling Know Your Client requirements and carrying out due diligence regarding clients' credit worthiness, risk taking ability, track record of compliance and financial soundness. Brokers shall ensure that only those clients who are deemed fit and proper for this facility are allowed access to the DMA facility. Brokers shall maintain proper records of such due diligence. Individual users at the client end shall also be authorized by the broker based on minimum criteria. The records of user details, user-id and such authorization shall be maintained by the broker. Details of all user-ids activated for DMA shall be provided by the broker to the exchange.

The broker shall enter into a specific agreement with the clients for whom they permit DMA facility. This agreement will include the following safeguards:

- (a) The client shall use the DMA facility only to execute his own trades and shall not use it for transactions on behalf of any other person / entity.
- (b) Electronic/Automated Risk management at the broker's level before release of order to the Exchange system. The client shall agree to be bound by the various limits that the broker shall impose for usage of the DMA facility.
- (c) Right to withdraw DMA facility if the limits set up are breached or for any other such concerns
- (d) Withdrawal of DMA facility on account of any misuse or on instructions from SEBI/Exchange.

Exchanges shall prepare a model agreement for this purpose. The broker's agreement with clients should not have any clause that is less stringent/contrary to the conditions stipulated in the model agreement

4. Risk Management

The broker shall ensure that trading limits/ exposure limits/ position limits are set for all DMA clients based on risk assessment, credit quality and available margins of the client. The broker system shall have appropriate authority levels to ensure that the limits can be set up only by persons authorized by the risk / compliance manager.

The broker shall ensure that all DMA orders are routed through electronic/automated risk management systems of the broker to carry out appropriate validations of all risk parameters including Quantity Limits, Price Range Checks, Order Value, and Credit Checks before the orders are released to the Exchange.

All DMA orders shall be subjected to the following limits:

- (a) Order quantity / order value limit in terms of price and quantity specified for the client.
- (b) All the position limits which are specified in the derivatives segment as applicable.
- (c) Net position that can be outstanding so as to fully cover the risk emanating from the trades with the available margins of the specific client.
- (d) Appropriate limits for securities which are subject to FII limits as specified by RBI.

The broker may provide for additional risk management parameters as they may consider appropriate.

5. Broker to be liable for DMA trades

The broker shall be fully responsible and liable for all orders emanating through their DMA systems. It shall be the responsibility of the broker to ensure that only clients who fulfill the eligibility criteria are permitted to use the DMA facility

6. Cross Trades

Brokers using DMA facility for routing client orders shall not be allowed to cross trades of their clients with each other. All orders must be offered to the market for matching.

7. Other legal provisions

In addition to the requirements mentioned above, all existing obligations of the broker as per current regulations and circulars will continue without change. Exchanges may also like to specify additional safeguards / conditions as they may deem fit for allowing DMA facilities to their brokers.

8. The Stock Exchanges are advised to:

- make necessary amendments to the relevant bye-laws, rules and regulations for the implementation of the above
- bring the provisions of this circular to the notice of the member brokers/clearing members and also disseminate the same on their website.
- communicate to SEBI, the status of the implementation of the provisions of this circular in the Monthly Development Report.

9. A review of the working of this facility shall be undertaken after six months from its introduction.

10. This circular is being issued in exercise of powers conferred under Section 11 of the Securities and Exchange Board of India Act, 1992 to protect the interests of investors in securities and to promote the development of, and to regulate the securities market.

Yours faithfully,

S V Murali Dhar Rao