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# **Automation of Securities Transfer in CDS**

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## Background

- In order to further strengthen the securities transfers on CDS, SECP formed a committee represented by CDC, KSE and NCCPL to propose changes in transfer model.
- CDC Board advised Management to lead the review of the current process of transfer of securities in consultation with SE's and NCCPL.
- Recommended model is based on various committee discussions and recommendations of CDC, SEs and NCCPL management and also reviewed and approved by KSE New Product Development Committee, KSE Board, CDC Board & SECP.
- CDC & NCCPL Regulations are also approved by their respective Boards.

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# Issues

## Settlement of securities at CM level

- Intra account movement of securities by Participants to / from Sub House / Main Account
  - Insufficient control in the system to ensure movement of securities to correct account
  - Significant amount of manual processing
  - Substantial number of transactions are generated

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## Salient Features of the Project

- NCSS to generate the balance orders based on client level netting – Securities Only
- All clients need to have Sub Accounts with Clearing member Participants.
- Securities will move directly from respective seller Sub/House Account to the buyer Sub/House Account based on the UIN (*under blocked status*)
- CM will continue to be responsible for money and securities obligations however, there is a provision available to Brokers enabling them to pledge the securities in favor of a Bank, in case of non-payment by their clients on settlement day.

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## **Salient Features of the Project - Cont'd**

- In case of failure of transactions (exceptional cases) the securities will be moved to the Main Account of the Member.
- Blocking and unblocking of Securities directly from House / Sub Account
- Inter Exchange transactions will also settle directly through respective House / Sub Account through NCSS BTB Module
- During BO generation first priority of deliveries will be within the same participant to reduce the number of inter participant free deliveries

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## **Detailed Structure**

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## A/c Level Tagging

- Considering that it is a business requirement of Participants that they maintain multiple Back office IDS and multiple CDS Accounts, it was decided that instead of enforcing Members to have only one Account with one UIN, it would be better if we could see the possibility of “tagging” Back-Office Account with Sub-Account along with UIN of a Client by the Member.
- For this purpose a change has been made in the UIN Registration screen of NCSS. A new field for CDS Account number would be made available in this window and Brokers would be required to select a CDS Account for each back office ID. They may select one account for many Back office IDs of same UIN or may opt for different CDS accounts for different Back office IDs with same UIN. However, the UIN(s) appearing in the CDS account should be exactly similar to the UINs appearing in the Trading Account.
- A Back office ID registered through NCSS UIN functionality which is not linked with any CDS Account would not be considered eligible for trading purposes.

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## **BO Mechanism**

- All Balance Orders (BO) would be established with the combination of UIN and CDS Account number along-with Participant ID basis by NCCPL.
- NCCPL will forward all the BOs to CDC at the EOD on SD-1.
- CDC will take confirmation from NCCPL on the data received and lock the data for further processing.
- CDS will start executing the BOs after completion of its own EOD process and it is envisaged that majority of BOs would be executed before the beginning of SD.
- Remaining BOs would be executed in batches on the SD, however NCCPL would have the control to halt/resume the BO execution process at any given point of time by sending information to CDS.
- CDS will transmit real time information to NCSS of the success and failure of BOs as per the existing mechanism.

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## Unblock & Retrieve

- As the NCCS payment obligation will continue to remain with CM the “Unblock” and “Retrieve” function would remain same as per current mechanism. Whereby upon fulfillment of NCCS settlement obligation of CM NCCPL would forward unblocking instructions to CDC for further processing.
- After the implementation of this project securities will be retrieved directly from relevant Account maintained by the Participant.

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## Failed Trades

- As BOs would be created in NCSS on UIN & CDS Accounts basis and trading would not be allowed on an UIN without having CDS Account tagged with it, the chances of failed trade is now very slim.
- However, where after execution of a trade, an Account is closed or blocked in CDS, in such cases securities would be moved to Main account of the receiving CM.

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## Treatment of Erroneous Trades

- **In case of a Sale transaction:** If securities are erroneously moved out from an incorrect account, due to an error in using the UIN at the time of execution of trade, the Member would move the securities from Correct Account to the Incorrect account while getting this transaction underlined at the relevant Stock Exchange. If securities are not available in the incorrect account, the BO would be failed and the member would be required to make a FD to NCCPL, using the failed trade reason code.
- **In case of a Purchase transaction:** If securities are moved to an incorrect account, the Member will be required to move the securities from Incorrect account to Correct account while getting the transaction underlined at the relevant Stock Exchange.

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## IDS Transaction

- For IDS transactions it is planned that at the time of UIN Registration no tagging would be made by the Broker and they will leave the CDS Account field empty.
- NCCPL Admin users would fill in this field and associate the CDS Account number with their respective CM IDs by collecting the information from CDC where the NBCM have only one House Account however where the NBCM has more than one House Account NCCPL would confirm the target account manually from them.
- Accordingly, in case the institution affirms the transaction, the BO would be generated for its House Account.
- In case the institution does not affirm the transaction, the BO would be generated for the Main Account of the CM.

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## Inter Exchange Transactions / B to B Transactions

- Mechanism for the inter-exchange trades would be quite similar to the existing scenario, the only change would be that now it would be mandatory for Brokers to execute “B to B” transaction for such trades.
- If the requesting Broker affirms the transaction, BO would be generated for the Client Account under the requesting Participant.
- If the requesting participant rejects the transaction, the BO would be generated for the Main Account of the executing trading broker.

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## Custodian Banks

- For transactions related to Custodian Banks, all such Custodians would become Clearing Members of NCCPL of a new category i.e. Custodian Clearing Members and at the time of UIN Registration no tagging would be made by the Broker and they will leave the CDS Account field empty.
- Foreign Investors of Custodian should have at-least one Sub-Account with any Custodian, otherwise such trading accounts shall not be eligible for trading.
- Custodian at the time of affirming the transaction would fill in this field and input the CDS Account number of the foreign investor, with the same UIN, under their own Participant umbrella.
- Accordingly, in case the Custodian affirms the transaction, the BO would be generated for its respective Account.
- In case the Custodian does not affirm the transaction, the BO would be generated for the Main Account of the CM. These un-affirmed transactions can be subsequently dealt with the “Failed trade” Reason code.

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## **Changes in CDS Architecture**

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## FD Inter Mechanism

- Initially in the Concept paper it was envisaged that there would be no involvement of main Account in the FD inter mechanism.
- After the implementation of this project, the routing of transactions from Main Account will only be allowed for certain specific types of transactions such as Off Market transactions and unlisted securities.
- Considering the requirement of different FD inter mechanism for different types of transaction, the FD inter mechanism has been linked with “Reason Codes” in CDS. A detailed description is covered in the upcoming slide.

## FD Inter Mechanisms

<b>Mechanism</b>	<b>Main A/c Allowed</b>	<b>UIN Mandatory</b>
<b>M-1</b> (for codes like Portfolio transfer, Settlement second leg, etc.)	No	Yes (auto checked with one UIN to be same on both the Accounts)
<b>M-2</b> (for codes like Gift, Acquisition of shares, etc.)	No	Yes (UIN required to be input)
<b>M-3</b> (for codes like Off Market transactions, Unlisted securities)	Yes	No

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## Pledge Call & Unit Transfer

- Currently in CDS, all movements resulting in case of a “Pledge” called by a Pledgee, fall in the Main Account of any CDS Participant. After the implementation of this project, all such movements would be directly delivered to the respective beneficiary account.
- For all such movements, Pledgee will need to know the UIN of the target account.
- Units of Open-end Mutual Funds transfer facility in CDS would also work on beneficiary account basis and input of UIN would be required to execute this transaction.

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## **Broker Protection Against Non-payment by Clients**

- Payment obligation would remain on CM level and delivery of securities would be made directly to the Client's Account.
- In case of payment failure by a client, Broker participants will be allowed to move such securities to a separate Account in CDS to the extent of Balance Order, for a maximum of 3 settlement days within which either such securities would need to be underlined for transferring them to the House Account of the broker or transfer back to the sub- account of the client.
- The purpose of separate Account is to enable Brokers to pledge the securities in exceptional cases. In a calendar month only 1 such instance per UIN would be allowed.
- While adequate protection was available to Broker Participant against payment obligations of their clients, necessary changes have been made in CDC Regulations to further enhance such protection.
- For more procedural/compliance details related to such transfers, please refer to KSE and/or CDC website.

For detailed procedure on Broker Protection please visit the following link:

[http://www.cdcpakistan.com/fck\\_images/file/Procedure for Broker Protection/Procedures for Broker Protection.pdf](http://www.cdcpakistan.com/fck_images/file/Procedure%20for%20Broker%20Protection/Procedures%20for%20Broker%20Protection.pdf)

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## Instructions Related to IAS Transactions

- After the implementation of this project, all Transaction Orders (TOs) related to CDC Investor Account Services should carry the target Sub Account Number and the specific reason code. Reason code would not be required only in cases where securities are to be moved as a result of “Portfolio Transfer” (where one UIN should be similar in both IAS and target Account).
- Existing TO books will be utilized by writing the sub account number in place of IAS account number and providing reason code and UIN at the extreme right bottom of TO leaf within the field for Signature where applicable.

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## Action Plan

- Synchronization of UIN in CDS with NCCPL database
- Tagging of CDS Accounts with Trading IDs on NCSS
- System changes to be completed by End of November 2010
- Training of Participants/CMs
- Performance Testing (Mock)
- Authorization by CDC Participants to CDC for automated movement of securities in accordance with NCCPL instructions
- Approval of CDC & NCCPL Regulations by SECP and Gazette notification
- Changes in Regulations of SEs
- CM Status by Custodian Banks
- Target IMPLEMENTATION DATE **(20<sup>th</sup> Dec 2010)**

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# Thank you!

For further details, please feel free to contact:

**Mr. Aftab Diwan/Mr. Shariq Naseem**

Central Depository Company of Pakistan Limited

Tel: 021-111-111-500 (Ext: 3101/4202)

e-mail: [Aftab\\_Diwan@cdcpak.com](mailto:Aftab_Diwan@cdcpak.com) | [Shariq\\_naseem@cdcpak.com](mailto:Shariq_naseem@cdcpak.com)

**Mr. Badiuddin Akbar**

National Clearing Company of Pakistan Limited

Tel: 021-32460822

e-mail: [badi@nccpl.pk](mailto:badi@nccpl.pk)