

EY Regulatory Alert

SEBI Circular mandating additional disclosures by Foreign Portfolio Investors that fulfil certain objective criteria

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Executive summary

This alert summarizes a recent Circular released by the Securities and Exchange Board of India, dated 24 August 2023 (Circular)¹ which outlines a framework for mandating additional granular disclosures from Foreign Portfolio Investors (FPIs) fulfilling certain criteria. The Circular is in furtherance to the consultation paper released by SEBI for public comments on 31 May 2023, which aimed to prevent violation of Minimum Public Shareholding (MPS) rules and guard against possible misuse of the FPI route to circumvent requirements of press note 3².

The requirement to provide additional disclosures has been made applicable to

- FPIs holding more than 50% of their Indian equity Assets Under Management (AUM) in a single Indian corporate group; or
- FPIs that individually, or, along with their investor group, hold more than INR 250 billion of equity AUM in the Indian markets.

However, SEBI has provided carve outs for certain FPIs from complying with the additional disclosure requirements. The list, *inter-alia*, includes FPIs owned and controlled by Government entities, public retail funds, certain Exchange Traded Funds, regulated pooled investment vehicles (fulfilling certain conditions) and FPIs unable to liquidate their investments due to statutory restrictions.

The Circular shall come into force with effect from 1 November 2023.

¹ Circular 'SEBI/HO/AFD/AFD - PoD - 2/ CIR/ P/ 2023/ 148'

² Press Note 3 dated 17 April 2020 provides that investment by an entity from a country which shares land border with India or where the beneficial owner of an investment into India is situated in/ citizen of any such country, shall only be under the Government route. Press Note 3 currently does not apply to FPI investments.



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Background

- ▶ FPIs are regulated by the SEBI and are permitted to invest in, *inter-alia*, shares of listed companies.
- ▶ The SEBI (FPI) Regulations, 2019 (FPI Regulations 2019) provide that investment by FPIs and its investor group³ in equity shares of each company cannot exceed 10% of the paid-up equity capital of such company.
- ▶ Further, the Operational Guidelines issued by SEBI for FPIs and Designated Depository Participants (DDP) in 2019 provide that FPIs are required to provide Know Your Client (KYC) related information/ documents based on the category under which they are registered and the jurisdiction from which the investment is made. The KYC details also, *inter-alia*, include details in respect of beneficial owners (BO)⁴, being natural persons who ultimately own/ control the FPI.
- ▶ While the above measures have been implemented, it has been observed by SEBI that the FPI route is being used by investors to (a) concentrate a substantial portion of their equity portfolio in a single investee company/ company group thereby circumventing regulatory requirements under Substantial Acquisition of Shares and Takeovers Regulations, 2011 or maintaining MPS⁵; or (b) circumvent the restrictions imposed by Press Note 3².
- ▶ Further, while the thresholds for identification of BO are specified in Prevention of Money Laundering (Maintenance of records) Rules, 2005 (PMLR), SEBI has observed that even though the same natural

³ Investor Group is defined in the SEBI (FPI) Regulations, 2019 to mean multiple FPIs, directly or indirectly, having common ownership of more than 50% or common control. Further, 'control' has been defined to mean right to appoint majority of directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of shareholding or management rights or shareholders agreements or voting agreements or in any other manner.

⁴ As per SEBI Operating Guidelines, BOs are required to be identified in accordance with Rule 9 of the Prevention of Money-laundering (Maintenance of Records) Rules, 2005. Rule 9(3) of the aforementioned Rules specifies the thresholds based on ownership, or entitlement to capital or profits (i.e., economic interest), for identifying the BO of legal entities. The thresholds are 10% for companies and trusts, and 15% for partnerships etc. It also specifies that BO includes those natural persons who exercise ultimate effective control over a legal person or arrangement.

⁵ The Securities Contracts (Regulation) Rules, 1957 read with Regulation 38 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 makes it mandatory for

person may hold significant aggregate economic interest in the FPI via various investment entities, often no natural person is identified as the BO of several FPIs based on economic or ownership interest, since each investor entity in the FPI may be below the threshold prescribed in the PMLR.

- ▶ Given the above, SEBI had on 31 May 2023 released for public comments, a Consultation Paper⁶ outlining a framework for mandating additional disclosures from FPIs.
- ▶ Considering feedback received by SEBI, SEBI has on 24 August 2023 released a Circular¹ finalizing the framework for additional granular disclosures from FPIs. The said information is to be provided by FPIs in accordance with Regulation 22(6) and 22(7) of the FPI Regulations⁷.
- ▶ The detailed mechanism for independently validating conformance of FPIs with the conditions and exemptions mentioned in the Circular shall be outlined in a Standard Operating Procedure (SOP) that shall be framed and adopted by all the DDPs, in consultation with SEBI.
- ▶ This alert summarizes the key aspects of the Circular.

Type of FPIs required to provide granular data

- ▶ Granular details of all entities holding any ownership, economic interest, or exercising control⁸ in the FPI, on a full look through basis, up to the level of all natural persons, without any threshold, shall be provided by FPIs, that fulfil any

entities who have listed their equity shares on a stock exchange to maintain MPS of 25%. This ensures balance of promoter and public shareholding and reduces volatility in the market.

⁶ Please refer the EY Alert dated 2 June 2023 summarising the Consultation Paper issued by SEBI.

⁷ SEBI on 10 August 2023 notified the SEBI (FPI) (Second Amendment) Regulations, 2023 and introduced Regulations 22(6) and 22(7), requiring FPIs fulfilling criteria specified by SEBI to provide information/ documents in relation to persons with any ownership, economic interest or control, in the FPI in a prescribed manner.

⁸ Ownership interest means ownership of shares or capital of the entity or entitlement to derive profits from the activity of the entity. Economic interest means returns from the investments made by the FPI. Control - Please refer definition in note 3

of the criteria mentioned below, to the DDP in the format specified in the SOP:

- ▶ FPIs holding more than 50% of their Indian equity AUM in a single Indian corporate group⁹; or
- ▶ FPIs that individually or along with their investor group¹, hold more than INR 250 billion of equity AUM in the Indian markets.

Exemptions from providing granular disclosures

- ▶ FPIs satisfying any of the criteria listed below shall not be required to make granular disclosures as specified above:
 - ▶ Government and Government related investors such as central banks, sovereign wealth funds, international or multilateral organizations or agencies including entities controlled or at least 75% directly or indirectly owned by such Government and Government related investor.
 - ▶ Public Retail Funds (PRFs)¹⁰, subject to independent validation of the same by DDPs.
 - ▶ Exchange Traded Funds (with less than 50% exposure to India and India-related equity securities).
 - ▶ Entities listed on specified Exchanges of permissible jurisdictions as may be notified from time to time by SEBI. Currently, the list of permissible jurisdictions and exchanges mentioned in SEBI Circular dated 28 November 2019 shall be considered¹¹.
 - ▶ Pooled investment vehicles registered with/ regulated by a Government/ regulatory authority in their home jurisdiction/ country of incorporation/ establishment/ formation,

where:

- ▶ holding in an Indian corporate group is below 25% of their overall global AUM at a scheme¹² level, or
- ▶ equity AUM in the Indian markets is below 50% of their overall global AUM at a scheme level.

- ▶ FPIs that are unable to liquidate their excess investments due to statutory restrictions (such as lock-in restrictions of anchor investors in IPOs, moratoriums, freeze on accounts or shares due to regulatory orders etc.), till the time such restrictions exist.

- ▶ Newly registered FPIs, for the first 90 calendar days from the date of settlement of first trade by the FPIs in equity segment in India.

- ▶ FPIs in the process of winding down their investment and having intimated to their DDP, their intention to surrender their FPI registration. Such FPIs shall be required to bring down their holdings to 'NIL' within 180 calendar days from the date of their intimation for surrender, failing which the account of the FPI shall be blocked for purchase as well as sale, and the FPI shall be liable for regulatory action as stipulated by SEBI.

- ▶ Where an FPI investor group consists of FPIs that qualify for exemptions under any of the criteria mentioned above, the net equity AUM of the investor group, shall be calculated after deducting the AUM of such exempted FPIs. After making the aforesaid deductions of AUM of such exempted FPIs, the disclosure requirements shall apply as follows:

- ▶ In case the equity AUM of the investor group (after making the above deductions) is below INR 250 billion, no disclosures are required to be made by the FPI investor group;

⁹ For monitoring compliance with the 50% exposure limit in a single corporate group, a repository containing names of companies forming a part of each Indian corporate group, shall be publicly disseminated on the websites of Stock Exchanges/ Depositories.

¹⁰ Public retail funds means - (i) mutual funds or unit trusts which are open for subscription to retail investors and which do not have specific investor type requirements like accredited investors; (ii) insurance companies where segregated portfolio with one-to-one correlation with a single investor is not maintained; and (iii) pension funds.

¹¹ The below mentioned List of Permissible Jurisdictions and International Exchanges as given Annexure A to SEBI Circular SEBI/HO/MRD2/DCAP/CIR/P/2019/146 dated 28 November 2019 shall be considered -

- United States of America - NASDAQ, NYSE
- Japan - Tokyo Stock Exchange
- South Korea - Korea Exchange Inc.
- United Kingdom excluding British Overseas Territories- London Stock Exchange
- France - Euronext Paris
- Germany - Frankfurt Stock Exchange
- Canada - Toronto Stock Exchange
- International Financial Services Centre in India - India International Exchange,
- NSE International Exchange

¹² Scheme shall mean pooled investment vehicles with structures similar to 'Scheme' as defined in SEBI (Mutual Funds) Regulations, 1996.

the disclosures.

- ▶ Where the equity AUM of the investor group (after making the above deductions) exceeds INR 250 billion, only the non - exempted FPIs of the investor group shall be required to make

Timelines and Implications

No reporting required where investments are realigned within below timelines			
Sr. No.	Particulars	Timeline/ Grace period for realigning investments	Remarks
1	FPIs holding more than 50% of their Indian Equity AUM in a single Indian corporate group	10 trading days*	No fresh purchases of equity shares of any company belonging to such Indian corporate group during the next 30 calendar days*
2	FPIs, including their investor group, holding more than INR 250 billion of equity AUM in the Indian markets	90 calendar days*	Accounts of FPIs individually and/or belonging to such investor group shall be blocked for further equity purchases until the holding is brought below the threshold.
3	FPIs fulfilling the above criterion as on the date of applicability of this Circular	90 calendar days#	Disclosures shall be required to be made by FPIs where holdings are not brought below the prescribed threshold within the given timeline.
Implications where investments continue to exceed the prescribed threshold post expiry of aforementioned timelines			
<ul style="list-style-type: none"> ▶ Make relevant disclosures to their DDPs within 30 trading days from the expiry of aforementioned timelines. ▶ Consequences of non-disclosures shall include: <ul style="list-style-type: none"> ▶ Render registration of the FPI invalid and no further purchases by the FPI would be allowed. ▶ The FPI shall liquidate its securities and surrender its FPI registration within 180 calendar days from the day the certificate becomes invalid. ▶ Investee companies shall restrict the FPI's voting rights to its actual shareholding or its shareholding corresponding to 50% of its equity AUM on the date its FPI registration is rendered invalid, whichever is lower. 			

* From the date on which FPIs exceed the threshold. Also, where the holdings of an FPI exceed the prescribed threshold on a subsequent date, the timeline for FPI to realign with the limits shall restart from such subsequent date.

From the date of applicability of this Circular.

Comments

With the objective of enhancing transparency and to obtain granular information of persons having any ownership, economic interest, or control in some objectively identified FPIs, SEBI had in May 2023 released a consultation paper for public comments.

SEBI has now released the final Circular, outlining the framework for mandating additional disclosure requirements by FPIs.

The Circular takes cognizance of several recommendations made by various stakeholders - expanding the category of FPIs exempt from the additional reporting requirements to include - international or multilateral organizations, entities controlled or at least 75% directly or indirectly owned by such government and government-related investor entities, exchange traded funds, entities listed on specified exchanges of certain jurisdictions, regulated pooled investment vehicles meeting prescribed conditions, etc, stipulating a mechanism to compute 50% exposure limit in a single corporate group, deferring the implementation of the framework thereby providing time to market participants to update their systems, etc.

Also, to ensure that the framework is consistently applied by all DDPs and to avoid any arbitrage, an SOP shall be released by SEBI. The SOP shall also outline a detailed mechanism for validating the exemptions and conditions mentioned in the Circular and the format in which the granular information is to be provided by FPIs where additional reporting requirement is triggered. Once SEBI issues the SOP, the industry would need to consider the same to ascertain and evaluate the extent of simplification which SEBI has introduced for the portfolio investor community.

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