SEBI issues framework for increased participation of NRIs, OCIs and RIs in funds setup in IFSC

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Summary

The SEBI[1], in its board meeting on 30 April 2024, had approved the regulatory framework to provide flexibility for increased contributions up to 100% by NRIs, OCIs and RIs[2] for funds setup in IFSC[3] and regulated by the IFSCA[4].

In this regard, SEBI has now amended the SEBI (Foreign Portfolio Investors) Regulations, 2019 (FPI Regulations), and the Master Circular for FPIs to give effect to the aforesaid change.

Background

- Funds setup in IFSC and regulated by the IFSCA can invest in Indian securities under the FPI[5] route, post obtaining registration from SEBI under the FPI Regulations.
- Currently, under the FPI Regulations, NRIs, OCIs and RIs can invest in FPIs, provided the contribution of a single NRI/OCI/RI is less than 25%, and the aggregate contribution of all NRIs, OCIs and RIs is less than 50% of the corpus of FPI. These conditions also apply to funds setup in IFSC that invest in India under the FPI route.
- In order to attract more capital investments of NRIs/OCIs into the Indian capital markets, SEBI, in its board meeting on 30 April 2024, approved the regulatory framework to provide flexibility for increased contributions up to 100% by NRIs, OCIs, and RIs in the funds setup in the IFSCs in India, subject to certain conditions to mitigate the regulatory risks.
- To facilitate the implementation of the aforesaid changes, SEBI has notified the amended regulation[6] and the Master Circular for FPIs. Some of the key takeaways of the said amendments are provided below:

Amendments in FPI Regulations

In the erstwhile FPI Regulations, NRIs, OCIs and RI investors could invest in the corpus of FPIs, subject to fulfilment of the conditions specified by SEBI in its Master Circular issued for FPIs. These conditions relating to investments by NRIs, OCIs and RIs in the corpus of the FPIs are now prescribed under the amended FPI Regulations, which are as follows:

- Contribution of a single NRI/OCI/RI to be less than 25% of the total contribution in the corpus of the FPI;
- The limit of the aggregate contribution by NRIs, OCIs, and RIs in the corpus of FPI to be less than 50% of the total contribution in the corpus of FPI will not apply to the funds setup in IFSC which are regulated by IFSCA;
- The RI contribution must be made through the LRS[7] notified by the RBI[8] and must be in global funds having Indian exposure less than 50%.
- FPIs must not be controlled by NRIs / OCIs / RIs; and
- Any other conditions as may be specified by the SEBI from time to time.

1 Securities and Exchange Board of India (SEBI)
2 Non-Resident Indians (NRIs), Overseas Citizens of India (OCIs) and Resident Individuals (RIs)
3 International Financial Service Centre (IFSC)
4 International Financial Service Centres Authority ('IFSCA').
5 Foreign Portfolio Investment (FPI)
6 SEBI (Foreign Portfolio Investors) Second Amendment Regulations, 2024 dated 26 June 2024
7 Liberalised Remittance Scheme (LRS)
8 Reserve Bank of India (RBI)

Amendment in Master Circular for FPI

Below are the key changes introduced in the Master Circular for FPIs:

1 FPIs, while seeking registration, must furnish a declaration to DDPs9, disclosing the intent to have an aggregate contribution of more than 50% from NRIs, OCIs, and RIs in its corpus. In the case of existing FPIs, a declaration must be furnished within 6 months from the date of this circular, which will be reviewed at the time of the registration renewal.

Disclosure of Permanent Account Number or other identity documents

2 **In case of NRI / OCI / RI individual constituents in FPIs:** FPI is required to provide DDPs with a copy of the PAN10 of all NRI/OCI/RI individual constituents and their economic interest in the corpus of the FPI. In absence of PAN of NRIs/OCIs/RIs, a requisite declaration and other identity documents (such as passport for NRIs, OCI card for OCIs, Aadhar/ passport for RIs) are required to be furnished.

3 **In case of non-individual constituents in FPIs:** For non-individual constituents of FPIs controlled directly/ indirectly by NRIs/ OCIs/ RIs, or where these individuals collectively hold 50% or more ownership/ economic interest (on a full look-through basis), an FPI is required to furnish to DDP, a copy of PAN of such NRIs/ OCIs/ RIs, or a suitable declaration and other identity documents, along with the percentage of ownership/ economic interest/ control in the non-individual entity and the FPI.

Exemption from disclosure of prescribed documents

4 Disclosure of PAN or other identity documents stated above will not apply to FPIs in IFSC and regulated by the IFSCA, subject to the following conditions:

- i **Pooling:** The contribution of all investors of the FPI is to be pooled into one investment vehicle at the IFSC - registered as an FPI with SEBI, with no side vehicles.
- ii ***Pari-passu* and pro-rata rights:** Corpus of the FPI is to be a blind pool with no segregated portfolios and all FPI investors should have *pari-passu* and pro-rata rights. Such FPIs may issue separate class of units only for the purpose of segregating the currency of contribution, but they should be *pari-passu* and pro-rata in all respects, post-conversion to a common currency.
- iii **Diversification of investments:** Maximum 20% of corpus of the FPI can be invested in equity shares of an Indian listed entity, at any point of time.
- iv **Diversification of investors**: An FPI needs to have minimum 20 investors, with each investor's contribution being less than 25% of the corpus of the FPI, at any point of time.
- v FPIs not complying with the conditions provided in (iii) and (iv) above at the time of making the FPI application, are required to comply with the conditions within three months from the date of registration. In case of passive breach of the said conditions after three months of registration, the investment manager (IM) is to immediately take requisite steps to rectify within three months of the breach. An active breach will be considered as a violation and dealt with as per the FPI Regulations.
- vi **Independent IM:** Investors must not participate in FPIs' investment decisions, and the IM of FPI should be independent in making investment decisions. Only an AMC[11] of a mutual fund (registered with SEBI and sponsored by a bank regulated by the RBI) or its IFSC subsidiary/ branch can be the IM of the FPI.

5 The requirements mentioned in 1 to 4 above must be fulfilled by the FPIs, irrespective of the actual aggregate contribution of NRIs/ OCIs/ RIs in the corpus of the FPI.

Ultimate beneficial owner related disclosure

FPIs setup in IFSC and regulated by the IFSCA, having increased contributions from NRIs/ OCIs/ RIs, are required to adhere to the disclosure obligations of all entities holding any ownership, economic interest, or exercising control in the FPI on a look-through basis[12], if such FPIs:

- Hold more than 33% of Indian equity AUM[13] in a single Indian corporate group; or
- Combined with its investor group, it holds more than INR 25,000 crore of equity AUM in the Indian market.

9 Designated Depository Participants (DDPs)
10 Permanent Account Number (PAN)
11 Asset Management Company (AMC)
12 As prescribed in SEBI circular dated 24 August 2023
13 Assets under management

Our comments

The amendments introduced in the FPI Regulations and the Master Circular for FPIs are a welcome move that address a long awaited 'Ask' of Indian fund managers, investors and other stakeholders.

This would give a much-needed impetus to the fund industry in IFSC and encourage more funds to setup investment vehicles in IFSC for pooling funds with minimal restriction on NRI/OCI/RI investors. It will also provide the IFSC GIFT City an edge over other offshore jurisdictions, where restrictions regarding raising funds from NRIs/OCIs/RIs as FPI Regulations continue to prevail.

Further, it would broaden the investor base for funds setup in the IFSC GIFT City and promote economic growth and opportunities in India. It would further provide a boost to the government's agenda of 'Onshoring the offshore' and is expected to provide the necessary boost to the IFSC GIFT City and improve its global ranking.

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