



To,

20<sup>th</sup> April, 2019

**Ms. Jyoti Sharma**

General Manager

Investment Management Department

Securities and Exchange Board of India

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**Sub: Self Regulatory Organizations (SROs) in Securities Market**

At the outset, we, at Indian Association of Investment Professionals (IAIP), a member society of the CFA Institute appreciate the opportunity to submit our response to the **CONSULTATION PAPER ON SELF REGULATORY ORGANIZATIONS (SROs) IN SECURITIES MARKET.**

IAIP is an association of over 2000 local investment professionals who are CFA charter holders and about 4000+ professionals who have cleared exams, eligible and awaiting charter. The Association consists of valuation professionals, portfolio managers, security analysts, investment advisors, and other financial professionals, that; promote ethical and professional standards within the investment industry, facilitate the exchange of information and opinions among people within the local investment community and beyond, and work to further the public's understanding of the CFA designation and investment industry.

CFA Institute is a global non-profit association of investment professionals with over 155,000 members in over 152 countries. In India, the community of CFA charter holders is represented by the Indian Association of Investment Professionals.

Through our global research and outreach efforts, CFA Societies around the world endeavour to provide resources for policy makers, financial services professionals and their customers in order to align their interests. Our members engage with regulators in all major markets.

With regards to the above mentioned consultative paper, we have proposed a few suggestions.

We would be happy to hear and discuss the merits / demerits of suggestions proposed by other practitioners and request to be included in the deliberation process.



Our responses to the various points are mentioned below in the requested format:

**1. Details of our Organisation:**

- **Name:** Indian Association of Investment Professionals (CFA Society India)
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**2. General Comment:**

Before we provide our comments on this consultation paper, we would like to share a link to a research report which SEBI might be interested in:

<https://www.cfainstitute.org/en/advocacy/market-integrity-insights/2013/09/cfa-institute-report-can-self-regulation-work-in-securities-markets>

The CFA Institute report - **Self-Regulation in the Securities Markets: Transitions and New Possibilities** - addresses the questions being raised about the continued utility of self-regulation in today’s markets and highlights the great potential it offers, especially in emerging markets.

This report highlights that, for all the potential benefits, self-regulatory systems also have a number of inherent conflicts that must be addressed in order to remain credible. The report notes a number of them (particularly the failures of prominent SROs like the CBOE and FINRA in policing and controlling conflicts of interest) and urges future improvements to SRO governance structures to enhance market and investor trust.

Despite all the challenges, we do believe that self-regulation holds the potential for alleviating the strain on regulators (which suffer from budgetary pressures and overseeing voluminous regulations), among other benefits.

**3. Suggestions / Comments:**

Sr. No.	Para No.	Suggestions	Rationale
1.	5.1	<p>There should be a single SRO for mutual fund distributors and investment advisers.</p> <p>On a related note, while the consultation paper lays out the need to have an SRO for the distributors of Mutual Fund products, it does not clarify whether the bank intermediaries would be covered under the same umbrella or not.</p>	<p>The SRO is not envisaged to be just an industry association lobbying for its members. It can therefore represent both mutual fund distributors as well as investment advisers, given that these are related, at the current stage of industry development in India. However, it should be clear that these are distinct segments with varied interests. The SRO will need to ensure that it does not become a closed club representing one set of members and be unfair to the other set of members.</p>



			<p>Further the SRO will need to not only address the interests of members (distributors and advisors) but also customers and the regulator. It has to be publicly accountable.</p> <p>This would require a strong governance structure including independent board members and a suitably empowered enforcement committee. It should also have a mandate to be fully transparent to the public and make the compliance information publicly accessible on its website. It will also need to have an effective complaints redressal mechanism, with information on grievance handling being made publicly accessible in a timely manner.</p> <p>On the other hand, if there are separate SROs for distributors and advisors there may be conflicts or overlaps, if both place their own members' interests above public accountability and interest of customers and other stakeholders. Administratively too it will be a challenge for SEBI to deal with several SROs.</p> <p><b>Hence, provided sufficient governance structure, transparency and compliance mechanism it is possible and even desirable to have a single SRO for both mutual fund distributors and investment advisers. Also, all intermediaries need to be covered by the SRO, including banks, else the purpose of regulation may be defeated.</b></p>
2.	5.3	The minimum net worth criteria for an SRO should be much higher than Rs. 1 crore.	The initial contribution will need to support the legal costs of registration, the deposit for office space & initial lease and infrastructure, website costs and sufficient funding of salaries and administrative costs. The annual membership fees will cover the office lease rentals & utilities, website maintenance, telecom bandwidth, salaries, administrative and events costs.



			<p>Rs. 1 crore appears to be a low figure assuming that membership fees will start rolling in and become sufficient only over a period of time. The potential number of members for this SRO is large, and effective compliance, enforcement, redressal etc. is likely to be proportionately large.</p> <p>Further, a higher amount will also show significant commitment of industry members who have an interest in sponsoring the setting up of such an SRO. Conversely, a lower net worth requirement may attract non-serious parties.</p> <p><b>Therefore, the minimum net worth criteria for this SRO should be much higher than Rs. 1 crore, considering the upfront funding requirements as well as in order to ensure that only committed parties can be nominated.</b></p>
3.	4.3.2	The nomination process must consider the source of funds apart from the minimum net worth criteria in evaluating the suitability of an organization or entity to be recognized as an SRO.	Regulating one's members who also fund the operation of the SRO raises obvious conflicts of interest. When an SRO considers sanctioning a large member or investigating a member whose representatives sit on the governing board of the SRO, the organization's enforcement approach may, consciously or unconsciously, be affected. Funding provided by outside sources may lessen the tension.
4.	5.5	<b>Accountability and Conflicts of Interest:</b> In light of the inherent conflicts of interest posed by the self-regulatory system, SROs must, if they are to be credible, have policies and procedures (governance and otherwise) to manage them. Without proper governance structures, not only will investors lack confidence in the SRO but also the marketplace will question the true authority of the entity. The first and foremost requirement for an effective self-regulatory system is a balancing of market integrity with market efficiency.	<p>The quality and the integrity of the procedures an SRO has for managing conflicts of interest are critical to its effectiveness as a respected authority.</p> <p>The clarity and the transparency of procedures for electing governing boards, creating rules, running discipline/enforcement programs, and resolving disputes, among other things, have a direct bearing on the credibility of an SRO. In particular, transparency about the entity's funding sources (as mentioned</p>



			<p>earlier), its procedures for managing conflicts of interest, and the methods used for and reasoning behind its disciplinary decisions should be public information.</p> <p>If the SRO has rule-making and enforcement authority, the scope of this authority should be clear and consistently applied. Market participants should know how to approach resolution of disputes with the SRO, including whether (and to what extent) the SRO can be held legally responsible or whether it can claim immunity from prosecution for its failures or misdeeds.</p> <p>SROs should disclose their decisions on a case-by-case basis and provide aggregate statistics about trends in their decisions.</p> <p>The provisions to ensure that an SRO's actions are independent, objective and free from all kinds of conflicts of interest should also apply to the SRO's sponsor(s).</p> <p>Please refer the section on <b>Accountability</b> on <b>page no. 9</b> of the <b>CFA Institute report</b> for an in-depth evaluation of the issue of accountability.</p>
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If you or your staff have questions or seek further clarification, please do not hesitate to contact Mr. Rajendra Kalur, CFA @ +91 98196 30042 or at [advocacy@iaipirc.org](mailto:advocacy@iaipirc.org)

Sincerely yours,

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Director - Research and Advocacy Committee  
Indian Association of Investment Professionals, Member Society of CFA Institute