CFA Society India

India Insights

June 2023

EDITORIAL

It is our great pleasure to bring to you our tenth edition of India Insights.

During the last quarter The Research, Advocacy and Standards committee of CFA Society India responded on SEBI's consultation papers on Framework for Mandating Additional Disclosures from FPIs, Review of TER Charged by AMCs and Regulatory Framework For MSM REITs.

CFA Institute concluded the 2023 edition of Young Women in Investment program. The program aims to support aspiring girls in building a career in investment industry. After completing a one-month virtual boot camp, 40 passionate women are ready to start internship in financial firms.

At CFA Society India, our 'Women in Finance' committee is busy planning for season 2 of FEMTOR. The program endeavours to create mentor-mentee relationships between women members in early stage of career and senior CFA Charterholders for career guidance. We will soon make an official announcement to open the registrations.

Hope you find this edition of India Insights useful. We will be happy to hear and discuss your suggestions and opinions related to advocacy initiatives.

If you are a member of CFA Society India and wish to volunteer for any of the advocacy initiatives, please drop a message on any of CFA Society India's social media handles and we will get in touch with you.

Best Regards,
Nimisha Pandit, CFA

CONSULTATION PAPER ON REVIEW OF TOTAL EXPENSE RATIO CHARGED BY ASSET MANAGEMENT COMPANIES (AMCS)

In May 2023, SEBI solicited public comments on the changes proposed regarding fees and expenses charged by AMCs to unitholders of mutual fund schemes. The proposed changes aimed to facilitate greater transparency, passing on the benefits of economies of scale to investors, encourage new AMCs, removing dual charges, addressing the issue of churning investors portfolio for higher distribution commission etc.

CFA Society India's team of volunteers, representing diverse set of stakeholders deliberated on the proposed changes, contrasted them with global practices and contemplated potential impact on development of the industry and financial inclusion.

Our analysis showed that interventions on fee structures has not been a policy tool for developed markets. Instead, the main catalysts have been technology, innovation, and regulatory nudges for public to invest.

Some of our specific suggestions on proposed changes are as below:

- Turnover or churn is a part of portfolio strategy, costs associated with churn should be deducted from returns and not included in the expense or TER. Additionally disclosures on those costs can be mandated, so that if there is a sharp increase in brokerage paid, investors or trustees can identify and question.
- Limited purpose membership for AMCs to execute transactions on stock exchange platform is a good move. This will allow AMCs to

Our complete response to SEBI can be accessed here.

trade anonymously, letting the pricing be fair and transparent and prevents the leakage of trade information. However, keeping the move voluntary will allow AMCs to decide based on economic viability.

- We need to take all measures to continue to support and enable distributors, as this is a trust-based industry. Only with a local presence one can reach investors. If we bring in measures to reduce the distribution expense for B-30, we are making it economically unviable for distributors in B-30 locations to exist and function.
- TERs should include GST as well as STT charges so all expenses are captured to give a clearer picture of costs to investors. Further the TER caps should automatically change if the GST rates are changes by the Finance Ministry.
- While we agree that performance based TERs may lead to alignment of interest. However, it could also promote short-termism and unhealthy return focused culture leading to performance hunting.

To read SEBI's proposal, please click here.

CONSULTATION PAPER ON REGULATORY FRAMEWORK FOR MSM REITS.

Web based platforms offering fractional ownership of real estate assets have mushroomed in India in recent years. Given the increasing value of investments with such FOPs and SEBI floated a consultation paper on proposing regulatory framework for Micro, Small & Medium REITs (MSM REITs).
We appreciate SEBI's effort to design a regulatory framework for the MSM REITs to incorporate FOPs in the regulatory ambit. We strongly believe that licensing of such platforms should be made mandatory, as this will bring all the players under the purview of SEBI and on a level playing field. Licensing requirement of these Fractional real estate platforms is important for investor protection and growth of this nascent market.

Following are some of our specific suggestions:

- Requirement of minimum net worth of INR 20 crores for the sponsors will lead to challenge of low ROE for sponsors. Our suggestion is to link the net worth requirement to % of the fund size. This will ensure level playing field for smaller players.
- The requirement of investing at least 95% of the schemes AUM in completed and rent generating real estate properties can be softened to include properties where possession is pending but OC is available. This will allow better yields by entering early in the transaction.
- Further for the remaining 5% of funds which can be deployed in liquid assets, SEBI can look to include overnight and liquid Mutual funds, which is a safe and well-regulated product.

Our complete response to SEBI can be accessed here.

- We support the minimum subscription amount of INR 10 lakhs. A higher amount may have led to exclusion of many retail investors. We would also recommend that SEBI also allows various relaxations on criteria if the REIT is only available to accredited investors. The differential approach for retail and accredited investor is a must to grow a market for sophisticated products and to bring in more stringent regulations for retail plans.
- Instead of SEBI specifying the cap on total expense ratio for MSM REITs, we prefer competitive forces of market decide the cost of the product. Over regulation can kill the nascent market and make it unviable.

CONSULTATION PAPER ON FRAMEWORK FOR MANDATING ADDITIONAL DISCLOSURES FROM FOREIGN PORTFOLIO INVESTORS (FPIS)

In May 2023, SEBI floated a consultation paper for public comments to frame guidelines on additional public disclosures by the Foreign Portfolio Investors with an objective of enhancing trust in the Indian securities markets.

The framework proposes mandatory additional granular disclosures around ownership of, economic interest in, and control of objectively identified high-risk Foreign Portfolio Investors (FPIs) that have either concentrated single group exposures and/ or significant overall holdings in their India equity investment portfolio.

We fully support the SEBI's proposal to tighten the disclosure requirement regarding beneficial ownership for FPIs with a concentrated portfolio.

Following are our key comments on the proposed framework:

- We feel that these proposals can be made even more stringent. holding more than 50% of their equity AUM in a single corporate group is very high threshold and can be lowered.
- Additionally, beneficial ownership is an important step to bring in more transparency to any capital markets. Anonymity enables many illegal activities, such as tax evasion, corruption, money laundering etc.
- SEBI has proposed that existing high-risk FPIs with an overall holding in Indian equity markets of over Rs. 25,000 Cr. shall also be required to comply with additional granular disclosure requirements within 6 months. The additional disclosure would include granular data of all entities with any ownership, economic interest, or control rights on a full look – through basis, up to the level of all natural persons and/ or Public Retail Funds or large public listed entities.

To read SEBI's proposal, please click here.

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- SEBI has objectively classified FPIs into various categories. However, INR 25k crore or USD 3 billion is a high threshold and can be lowered. Moreover, the absolute figure of INR 25k crore may not hold true as the India market evolves. Thus, our suggestion is to link the number to the total market cap of India.

To read SEBI's proposal, please click here.

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