Most FIIs comply with new norms on structure

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Most foreign institutional investors (FIIs) operating as multi-class share vehicles have changed their structure to meet the new regulatory requirements, officials familiar with the matter have said.

Yesterday, the Securities and Exchange Board of India (Sebi) said FIIs and sub-accounts that had not complied with its guidelines specified on April 15 would not be permitted to take fresh positions in the cash and derivatives markets from Friday.

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"A large number of FIIs with an MCV (multi-class vehicle) structure have already restructured themselves. So, the number of non-compliant entities would be a small percentage of registered FIIs in India and that too mostly fringe players," said Siddharth Shah, head, funds practice, Nishith Desai Associates. "My guess is that there will not be any significant impact on liquidity flows. One may see some increase in the amount of offshore derivative instruments, as the non-compliant entities will now swap their exposure through them."

FIIs have pumped in $18.37 billion (Rs 82,300 crore) in the Indian stock market so far this year, the highest in any calendar year. Sebi is not comfortable with foreign investors from tax havens having a multi-class structure, as some of these are believed to be used for round-tripping (the same capital returning here in the form of foreign investment) of funds.

On April 15, the regulator asked new applicants as well as existing FIIs and sub-accounts to give more information about their structures. It asked applicants to furnish declarations that they were not a protected cell company (PCC) or a segregated portfolio company (SPC). The applicants also have to declare they are not a multi-class share vehicle (MCV) under their constitution. If they are, they need to undertake that common portfolios will be allocated across various share classes and will be broad-based. Sebi had set a deadline of September 30 for all FIIs and sub-accounts for complying with the guidelines.

A structure like a PCC or SPC segregates assets and liabilities of investors by providing for distinct assets, either in the form of a separate class of share, or a dedicated sub-fund attributed to each investor. An entity like an MCV has the flexibility to issue multiple classes of shares having differential benefits attached, so that each class has the ability to represent the interest of a particular investor, or for specific investments.

By rough estimates, around 40 per cent of registered FIIs would have to change their structure to meet Sebi norms. As of September 29, there were 1,726 registered FIIs in India, while the number of registered sub-accounts was 5,523, Sebi data showed.