Business Standard

Sebi to get strict with FII sub-accounts

Ashish Rukhaiyar & Vandana / Mumbai April 30, 2010, 0:29 IST

The Securities and Exchange Board of India (Sebi) plans to tighten the rules for transfer of sub-accounts by foreign institutional investors (FIIs).

Sebi defines sub-accounts as entities that include foreign companies, foreign individuals and institutions, funds or portfolios established or incorporated outside India, on whose behalf FIIs propose to make investments in India.

The market regulator is keen to completely re-work the Know Your Client (KYC) norms along with the application for a sub-account transfer.

"There have been instances where investors have preferred seeking fresh registrations than applying for transfers, merely to avoid the transfer-related hassles," said Nirav Merchant, Associate Partner, Majmudar & Co.

Until now, transfer of a sub-account to another FII required an application to the regulator, accompanied by a declaration from the proposed FII that it was authorised to invest on behalf of the sub-account.

Further, the transferor FII was required to submit a no objection certificate (NOC).

Lawyers said transfer of registrations is a cumbersome process because it requires periodic follow-ups and submission of voluminous documents to Sebi officials. With the new set of declarations by Sebi, many sub-accounts may not be very keen to invest time in the transfer process.

"Sebi would basically look for more information at all levels going ahead and that includes sub-account transfers as well. Prima facie, they will not reject any application, but yes the whole process will take more time now," said Siddharth Shah, Managing Partner at Nishith Desai Associates.

Earlier on April 15, Sebi had asked FIIs to stop using complex structures of protected cell companies and segregated portfolio companies. It had also mandated that the investor base be broadbased in case of multi-class share vehicles.

These moves were aimed to check potential round tripping through FIIs and also increase transparency.

According to the new guidelines, all FIIs, whether registered or not, would have to undertake that they do not follow a protected cell company or segregated portfolio company structure.

Protected cell companies are entities with several cells within the same vehicle. A cell has its own assets, liabilities, a cellular capital, dividends and accounts. Each cell functions as an independent unit within the overall set up and the debtors and creditors of each cell have no claims against the assets or liabilities of another cell.

"Any step-up by Sebi regarding FII and sub-accounts will invariably be welcomed with reluctance. Increased surveillance and diligence will not be appreciated by FIIs and sub-accounts that have been investing in India under relaxed norms. In our view, stringent declarations and disclosure requirements will reduce the flexibility that foreign investors enjoyed in constituting offshore entities," added Merchant.

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