

EY Regulatory Alert

Amendments to the regulatory framework providing flexibility for increased contribution by NRIs, OCIs and RII, in the corpus of FPIs located in IFSCs

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Executive summary

The Securities and Exchange Board of India (SEBI) had in its 205th Board Meeting¹ *inter-alia*, approved the regulatory framework for increased participation of Non-resident Indians (NRIs), Overseas Citizens of India (OCIs) and Resident Indian Individuals (RIIs) into the Indian Capital Markets through Foreign portfolio Investors (FPIs) that are based out of International Financial Services Centers (IFSCs) in India and regulated by the International Financial Services Authority (IFSCA). The IFSCA had also issued a circular² dated 2 May 2024 providing details of the regulatory framework approved by SEBI³. However, a circular from SEBI was awaited.

SEBI has now issued Circulars⁴ on 26 June 2024 and 27 June 2024 (Circulars) amending the SEBI (FPI) Regulations, 2019 to give effect to the framework approved in the 205th Board Meeting.

This alert summarises the regulatory framework approved by SEBI in the Circulars.

¹ Press release (PR No 08/2024) dated 30 April 2024

² F. No. IFSCA-IF-10PR/2/2024-Capital Markets

³ Please refer EY Alert dated 3 May 2024 for a summary of the regulatory framework approved by SEBI and the circular issued by IFSCA.

⁴ SEBI/LAD-NRO/GN/2024/185 and SEBI/HO/AFD/AFD-POD-2/P/CIR/2024/89

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Background

- ▶ Historically i.e., under the Foreign Institutional Investors (FII) regime and under the SEBI (FPI) Regulation, 2014, NRIs/ OCIs/ RIIs were not allowed to be registered as FIIs/FPIs or its sub-accounts (SAs)
- ▶ However, Funds in which NRIs were investors were allowed to be registered as FIIs/ SAs/ FPIs and any companies promoted, or majority owned by NRIs were allowed to be registered as non-investing FIIs/ FPIs to manage funds of other FIIs/ SAs/ FPIs and to act as Investment Manager (IM) for other FPIs.
- ▶ Even under the extant FPI Regulations [i.e. SEBI (FPI) Regulations, 2019], an FPI applicant cannot be an NRI or OCI. However, NRIs or OCIs or RIIs may be constituents of an FPI, provided they meet the following conditions:

Primary Conditions		
Sr. No.	Particulars	Limit
1.	Contribution of a single NRI/OCI/RII ⁵	<25%*
2.	Aggregate contribution of NRIs/ OCIs/ RIIs ⁵	<50%*
*Of total contribution in the corpus of the applicant		
Additional Conditions		
<ul style="list-style-type: none"> ▶ The NRIs/ OCIs/ RIIs shall not be in control of the applicant FPI. Note: The aforesaid condition is not applicable if the applicant FPI is an 'offshore fund' for which a 'No Objection Certificate' has been issued in terms of the SEBI (Mutual Funds) Regulations, 1996, or is controlled by an IM which is controlled and/or owned by NRI/ OCI/ RI if the following conditions are satisfied: <ul style="list-style-type: none"> ▶ such IM is appropriately regulated in its home country and registered as a non-investing FPI, or ▶ such IM is incorporated or setup under the Indian laws and appropriately registered with SEBI. 		

- ▶ The aforesaid conditions shall not apply to non-investing FPIs or if the applicant FPI proposes to invest only in mutual fund units in India.
- ▶ The IFSCA and SEBI have amended the regulatory framework to provide flexibility to NRIs/ OCIs/ RIIs to contribute upto 100% in the corpus of FPIs based in IFSCs in India, given that a lot of interest is being received from such investors.

Conditions for increased participation

- ▶ The regulatory framework envisages 100% participation by NRIs/ OCIs/ RIIs in an FPI in two alternate modes to manage regulatory risk:
 - ▶ **Alternative 1 - 100% participation by NRI/ OCI/ RII subject to furnishing prescribed documentation**
 - ▶ FPI applicant to submit a declaration to the Designated Depository Participant (DDP) at the time of registration stating its intent of having aggregate contribution by NRIs/ OCIs/ RIIs exceed 50%. The declaration can be reviewed only at the time of renewal of FPI registration.
 - ▶ For existing FPIs, the declaration has to be provided within 6 months from 27 June 2024.
 - ▶ Copies of PAN cards of all NRIs/ OCIs/ RIIs along with their economic interest in the corpus of the FPI.
 - ▶ In absence of PAN, the following documents need to be submitted:
 - Declaration from NRIs/OCIs stating that they neither have a PAN nor any taxable income in India.
 - Declaration from RIIs stating that they are exempted from obtaining PAN by the Indian tax authorities alongwith the legal provisions under which they are exempt.
 - Copy of Indian Passport by NRIs, OCI card by OCIs and any identity document issued by the Government of India (eg Aadhar card, passport etc) in case of RIIs.
 - ▶ A similar disclosure would also be required in case of non-individual constituents of FPIs which are controlled directly or indirectly by one or more NRIs/ OCIs/ RIIs or where NRIs/ OCIs/ RIIs together hold 50% or more ownership or economic interest on a full look through basis. The percentage of ownership/ economic interest/ control of the NRIs/ OCIs/ RIIs is to be indicated at the non-individual entity and FPI level.
 - ▶ Any change in the above information is to be

⁵ The contribution of RIIs shall be made through the Liberalised Remittance Scheme notified by the Reserve Bank of India (RBI)

and shall be in global funds whose exposure in Indian assets is less than 50%.

submitted to the DDP within 7 working days.

▶ **Alternative 2 - 100% participation by NRI/ OCI/ RII without documentation requirements but subject to additional conditions**

▶ Documentation requirements mentioned in Alternative 1 shall not be applicable where the following conditions are met:

Sr. No.	Particulars	Conditions
1	Pooling	Contribution received from all investors is required by law to be pooled into one investment vehicle that is registered as the FPI with no side-vehicles.
2	Pari-passu and Pro-rata rights	By law, corpus of the FPI is a common pool without any segregated portfolios. All the investors of the FPI shall have pari-passu and pro-rata rights. For the limited purpose of segregation of currency of the contribution, issuance of separate class of units shall be permitted. However, post conversion to a common currency, the same should be pari-passu and pro-rata in all respects.
3	Diversification of investors	Fund shall have a minimum of 20 investors, with each investor contributing not more than 25% to corpus of the Fund.
4	Diversification of investments	Fund may invest a maximum of 20% of its corpus in equity shares of an Indian listed entity
5	Independent Investment Manager (IM) / Fund Manager	No investor shall have any say in the investment decisions of the FPI. IM shall be independent from the investors and in respect of taking investment decisions for the FPI. The IM of the FPI shall be an Asset Management Company, of a SEBI registered Mutual Fund, which is sponsored by a bank regulated by the Reserve Bank of India (the Central bank of India) or its IFSC based subsidiary/ branch.

▶ The FPI would also be required to adhere to certain granular additional disclosure obligations⁶ with respect to entities holding any ownership, economic interest or exercising control in the FPI on a full look through basis if:

- ▶ Such FPI holds more than 33% of its Indian equity assets under management (AUM) in a single corporate group; or
- ▶ Such FPI along with its investor group holds more than INR 250,000 million of equity AUM in the Indian markets.

Comments

The Circulars released by SEBI provides a detailed framework which enables upto 100% participation by NRIs, OCIs and RIIs in FPIs set-up in IFSCs in India. Funds set-up in IFSCs should ensure that relevant documentation is obtained from their investors to avail of the flexibility and relaxation provided by SEBI.

Additionally, as already provided in the extant SEBI (FPI) Regulations, 2019, for FPIs set-up in IFSCs which are controlled by NRIs/ OCIs/ RIIs through the IM, it shall be mandatory for the IM to be appropriately regulated in India and also be registered as a non-investing FPI or be appropriately registered with SEBI.

⁶ SEBI circular SEBI/ HO/ AFD/ AFD - PoD - 2/CIR/ P/ 2023/ 148 dated 24 August 2023. Also, please refer to EY Alert dated 29 August 2023.

