September 2018

Foreign Portfolio Investment (FPI) – Know Your Client (KYC) Requirements

Background

The Securities and Exchange Board of India (SEBI) had issued a Circular dated April 10, 2018 with respect to KYC requirements for FPIs, especially Beneficial Ownership (BO) related disclosures. Following representations received from various stakeholders, SEBI had constituted a Working Group (the Group) to review the same. The Group released its interim recommendations on September 8, 2018. Subsequently, the SEBI Board in its meeting held on September 18, 2018, had after considering the interim recommendations of the Group and comments received from public, decided that BO criteria in Prevention of Money-laundering (Maintenance of Records) Rules, 2005 (PMLA Rules) should be made applicable for purpose of KYC and not for determining eligibility of FPIs. It was also decided that for investment limit purposes, investments by FPIs should not be clubbed on the basis of BO as per PMLA Rules.

SEBI Circulars

In accordance with the above decisions, SEBI has issued two Circulars dated September 21, 2018 specifying the revised norms on eligibility conditions for FPIs and KYC Requirements for FPIs. Further, SEBI will be issuing another Circular on the issue of clubbing of investment limit of FPIs.

Key takeaways relevant to FPIs from the Circulars issued today are summarised below:

A) Eligibility conditions for FPIs

- Non Resident Indians (NRIs) and Overseas Citizens of India (OCIs) and Resident Indians (RIs) should be allowed to invest in FPIs subject to the following conditions:
- Contributions by NRIs/ OCIs/ RIs (including contributions by an Investment Manager ('IM') controlled by an NRIs/ OCIs/ RIs) should not exceed:

  i. 25% of the FPIs corpus from a single NRIs/ OCIs/ RIs; and
  ii. 50% of the FPIs corpus from aggregate of such investments by NRIs/ OCIs/ RIs.

- NRIs / OCIs / RIs should not be in control of FPI.
- RIs contributions in global funds with Indian exposure of less than 50% made by way of remittances under the RBI's Libralized Remittance Scheme (LRS) permitted.
- No restriction imposed on NRIs / OCIs / RIs to manage non-investing FPIs or SEBI registered offshore funds provided any of the following conditions are satisfied:
- IM of the FPI is appropriately regulated in its home jurisdiction and registers itself with SEBI as a non-investing FPI; or
- IM is incorporated or set up under the Indian laws and appropriately registered with SEBI; or
- Where such FPIs are 'offshore funds' for which no-objection certificate has been provided by SEBI under the Mutual Fund Regulations.
- The above restrictions will not apply to FPIs investing only in mutual funds in India.
- Existing and new FPIs will need to satisfy these eligibility conditions within 2 years from the date of coming into force of the amended regulations or from the date of registration, whichever is later.
- In case of temporary breach, a time period of 90 days will be given to ensure compliance.

B) KYC requirements for FPIs

1. Identification and verification of Beneficial Owners – For Category II & III FPIs

- BOs are the natural persons who ultimately own or control an FPI and should be identified in accordance with Rule 9 of the PMLA Rules. FPIs are required to maintain a list of BOs and should provide following details of their BOs:
- Name & Address of the Beneficial owner (Natural person);
- Date of birth;
- Tax residency jurisdiction;
- Nationality;
- Whether acting alone or through one or more persons as group with their name and address;
- BO Group's percentage Shareholding/Capital/Profit in ownership in the FPIs; and
- Tax Residency Number / Social Security Number / Passport Number of BO (please provide any).
- In respect of FPIs coming from "high risk jurisdictions", the intermediaries may apply lower materiality threshold of 10% for identification of BO and also ensure KYC documentation as applicable for category III FPIs.
- The materiality threshold to identify the BO should be first applied at FPI level and next look through basis shall be applied to identify the BO of the intermediate shareholder/ owner entity. For intermediate material shareholder/ owner entities, name and percentage holding shall also be disclosed in the prescribed format. Intermediate shareholder/ owner entities eligible for registration as Category I FPI are exempted from this requirement.
- The term Senior Managing Official (SMO), for identification as BO, means an individual as designated by the FPI who holds a senior management position and makes key decisions relating to the FPI.
- In case of companies/ trusts represented by service providers like lawyers/ accountants, FPIs need to provide information of the real owners/ effective controllers. If the BO exercises controls through means like voting rights, agreements, arrangement etc., that should also be specified.
- BO should not be a nominee of another person.
- Offshore Derivative Instrument (ODI) issuing FPIs shall also identify and verify the BOs in the subscriber entities.

2. Periodic KYC review

- The KYC review (including change in BOs / their holdings) should be done based on risk categorization of FPIs as and when there is any change in material information / disclosure.
- For Category II & III FPIs from high risk jurisdictions, KYC review should be done annually.
- For all other cases, KYC review should be done at the time of continuance of FPI registration.

In the event of failure to submit KYC documents, if any, no further purchase transactions shall be permitted.

3. KYC documentation for Category III FPI

- Category III FPIs have to mandatorily submit "Financial Data" i.e. audited annual financial statement or a net worth certificate from the auditor.
- For newly formed funds/ companies/ family offices, the audited financial statements of promoter person may be obtained.
- Where a constitutive document is not available, the prospectus and information memorandum would be acceptable.

4. Exempted documents to be provided during investigations/ enquiry

Category III FPIs exempted from submission of proof of address of BOs, Senior Management and Authorised Signatories need to furnish a "declaration on letter head".

5. Data Security

The KYC Registration Agencies (KRAs) shall protect the BO personal information provided by the FPI. Such information should be made available to intermediaries only on 'need to know basis' using an authentication procedure.

6. Period for maintenance of records

The Custodian should maintain the KYC records in original for a minimum period of 5 years.

7. Timelines for compliance

Existing FPIs should provide the list of BOs and KYC documentation within 6 months from the date of this circular. In the event an FPI fails to comply with the above deadline:

i. No fresh purchases will be permitted till the time requirements are complied with. They will however be allowed to sell their positions.

ii. Non-compliant FPIs will need to disinvest its holdings within a period of 180 days from the expiry of the timeline. Beyond that period the FPI registration will not be valid and it would need to disinvest its holdings immediately.

Amendments in SEBI (Foreign Portfolio Investors) Regulations, 2014, wherever necessary, will be notified separately in due course.

Please click here to access the SEBI circulars specifying the revised norms on eligibility conditions for FPIs and here to access the circular on KYC Requirements for FPIs

If your interest lies in a specific area or subject, do advise us so we can send you only the relevant alerts. For any additional information, please reach out to your PwC relationship manager or write in to ***pwctrs.knowledgemanagement@in.pwc.com***

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