REPORT OF THE EXPERT COMMITTEE ON INVESTMENT FUNDS

31 January 2022

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1. Abbreviations and Acronyms

AIF	Alternative Investment Fund
AIFMD	Alternative Investment Fund Managers Directive
AML	Anti-Money Laundering
AP	Authorised Participant
APEC	Asia-Pacific Economic Cooperation
ARC	Asset Reconstruction Companies
ARFP	Asia Region Funds Passport
ASEAN	Association of Southeast Asian Nations
AUM	Assets Under Management
CBDT	Central Board of Direct Taxes
CBOE	Chicago Board Options Exchange
CEO	Chief Executive Officer
CIS	Collective Investment Schemes
COO	Chief Operating Officer
CSRC	China Securities Regulatory Commission
DTAA	Double Taxation Avoidance Agreement
EPFO	Employees' Provident Fund Organisation
ESG	Environmental, Social and Governance
ESMA	European Securities and Markets Authority
ETCD	Exchange Traded Commodity Derivatives
ETFs	Exchange Traded Funds
ETP	Exchange Traded Products
EU	European Union
FATF	Financial Action Task Force
FCA	Financial Conduct Authority
FDI	Foreign Direct Investment
FEMA	Foreign Exchange Management Act, 1999

FIs	Financial Institutions
FME	Fund Management Entity
FPI	Foreign Portfolio Investors
FSA	Financial Services Agency
FY	Financial Year
GHG	Greenhouse gases
GST	Goods and Services Tax
HK	Hong Kong
HNI	High Net-worth Individuals
HUF	Hindu Undivided Family
IBC	Insolvency and Bankruptcy Code 2016
IBU	IFSC Banking Unit
ICA	The Investment Company Act of 1940
IFSC	International Financial Services Centres
IFSCA	International Financial Services Centres Authority
InvIT	Infrastructure Investment Trust
IOSCO	International Organization of Securities Commissions
ITA	The Income-Tax Act, 1961
KMP	Key Managerial Personnel
KYC	Know Your Client
LLC	Limited Liability Company
LLP	Limited Liability Partnership
LP	Limited Partnership
LRS	Liberalised Remittance Scheme
MFO	Multi Family office
MM	Market Makers
MOC	Memorandum of Cooperation
MRF	Mutual Recognition of Funds
NAV	Net Asset Value

NFO	New Fund Offer
NPA	Non-Performing Assets
NPL	Non-Performing Loans
NRI	Non-Resident Indian
NYSE	New York Stock Exchange
OCI	Overseas Citizen of India
ODI	Offshore Derivatives Instruments
PAN	Permanent Account Number
PIO	Person of Indian Origin
PMS	Portfolio Management Service
PPM	Private Placement Memorandum
PTCs	Pass Through Certificates
RBI	Reserve Bank of India
RBIC	Rural Business Investment Company
REIT	Real Estate Investment Trust
RI	Resident Individual
SARFAESI Act	Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002
SEBI	Securities and Exchange Board of India
SEBI IFSC Guidelines 2015	SEBI (International Financial Services Centres) Guidelines, 2015
SEC	Securities and Exchange Commission
SFC	Securities and Futures Commission
SFDR	Sustainable Finance Disclosure Regulations
SFO	Single Family Office
MAS	Monetary Authority of Singapore
SPV	Special Purpose Vehicle
SRs	Security Receipts
STT	Securities Transaction Tax
The Act	International Financial Services Centres Authority Act, 2019

UCITS	Undertakings for Collective Investment in Transferable Securities
UHNI	Ultra-High Net-worth Individuals
UN	United Nations
USD	United States Dollar
VCC	Variable Capital Company
VCF	Venture Capital Fund
WFE	World Federation of Exchanges

2. Letter from Chair to Chairman, IFSCA

31st January, 2022

Shri Injeti Srinivas,
Chairperson,
International Financial Services Centres Authority
Gandhinagar, Gujarat.

Dear Sir,

Recognising the important role of the Fund industry in financial intermediation, the International Financial Services Centres Authority (IFSCA), in May 2021, constituted a Committee of Experts on Investment Funds to review global best practices and make recommendations to the IFSCA on the roadmap for the industry.

At the outset, on behalf of the members of the Committee, I would like to thank you for giving us an opportunity to contribute to this important initiative of the IFSCA.

The main objective of the IFSCA is to develop a strong global connect and focus on the needs of the Indian economy as well as to serve as an international financial platform for the entire region and the global economy as a whole. While working on the terms of reference as mandated by the IFSCA, the Committee kept these principles of the IFSCA in “front and centre”.

In accordance with the terms of reference, the Committee evaluated global best practices in the Asset Management industry and compiled its recommendations to suggest a “best-in-class” regime that will support the growing aspirations of the Asset Management industry. We do hope that, through our report and recommendations, we have been to contribute in some way to the development of IFSC as a leading global destination for the Asset Management industry.

I would also like to take this opportunity to thank all my Committee members who made time from their busy schedules to attend discussions from time to time, participate with great fervour and passion in the deliberations and provide invaluable insights and share experiences. A special mention of Mr. Leo Puri, Mr. Sundeep Sikka and Mr. Neeraj Choksi for leading their Working Groups which delved into different aspects of the report. Compiling this report has been possible only because of their efforts and unflinching support.

Thanking you,

Yours sincerely,

Nilesh Shah
(Chairperson)

3. Constitution of Committee

The International Financial Services Centres Authority (IFSCA), with an objective to develop and enhance the framework for Investment Funds in the International Financial Services Centre (IFSC), has constituted a Committee of Experts on Investment Funds on 25th May 2021 chaired by **Mr. Nilesh Shah, Group President & MD, Kotak Mahindra Asset Management Co. Ltd & Member, PMEAC**. The terms of reference of the Committee are as follows:

- To recommend IFSCA on long term vision for operations of Investment Funds in IFSC.
- To make recommendations with respect to structure of Investment Funds in IFSC. The recommendations may be two-fold:
  - Short term in nature that can be implemented by IFSCA immediately (i.e., less than 3 months). Such suggestions may fall under the exclusive regulatory purview of the IFSCA.
  - Recommendations that may be implemented in mid-term (6 months to 1 year). Such suggestions may also pertain to regulatory purview of other regulators.
- To identify issues that may be critical for development of the Investment Funds industry at IFSCs including inter-regulatory issues.
- Any other relevant item on building the ecosystem inter-alia on asset managers, hedge funds, PE, VC, sovereign funds, family offices, and the accompanying professional services.

The Committee consists of the following members who are accomplished leaders with wide experience in developing asset management business and regulations, and have a strong global network:

1. Mr. Leo Puri, Former MD, UTI AMC Ltd, Chairman of J P Morgan, South Asia & South East
2. Mr. N. S. Venkatesh, CEO, AMFI
3. Mr. Neeraj Choksi, Co-Founder, NJ Group
4. Mr. Nithin Kamath, Co-founder & CEO, Zerodha
5. Mr. Ramamoorthy Rajagopal, Chief Operating Officer, DSP Investment Managers Pvt. Limited.
6. Ms. Shagoofa Khan, Group General Counsel and Head Corporate Affairs, National Investment and Infrastructure Fund Limited (NIIFL)
7. Mr. Sundeep Sikka, CEO, Nippon Life India Asset Management Ltd
8. Mr. Tejesh Chitlangi, Senior Partner, IC Universal Legal
9. Mr. Tushar Sachade, Partner, Price Waterhouse & Co LLP
10. Mr. V. Balasubramaniam, MD & CEO, India International Exchange (IFSC) Limited- India INX
11. Ms. Vinaya Datar, Chief Compliance Officer, SBI Funds Management Pvt. Ltd.
12. Mr. Pavan Shah, Deputy General Manager, IFSCA (Member Secretary to the Expert Group)

4. Acknowledgement

At the outset, we would like to express our sincere gratitude to Mr. Injeti Srinivas, Chairperson, IFSCA for the trust and confidence reposed in the Committee and giving us an opportunity to contribute to the development of the Investment Funds Regime and the Asset Management industry in the IFSC.

We would also like to thank Mr. Manoj Kumar, Executive Director, IFSCA for encouraging the Committee members to think beyond the obvious and giving complete liberty to the Committee members to discuss, deliberate and finalise their thoughts on the Investment Fund Regime.

We would also like to thank Mr. Pavan Shah, Deputy General Manager, IFSCA and Member Secretary to the Committee for his valuable inputs during the discussions and for passionately pursuing with the Committee members to deliberate and complete this important exercise in a time bound manner. We would also like to thank the other IFSCA team members Mr. Arjun Prasad, Mr. Mihir Upadhyay, Mr. Abhilash Mulakala, Deputy General Managers, IFSCA and Mr. Kalpesh Mehta, Manager, IFSCA, for their continuous support, co-operation, and suggestions as we deliberated and finalised the report.

The Committee would like to extend its immense gratitude to Mr. Armin P. Choksey, PwC Singapore, Mr. Neeleshwar Bhatnagar, NB Ventures, Mr. Alok Mehta, Blume Ventures and Mr. Rishiraj Khajanchi, Kedaara Capital Advisors LLP for providing their insights and sharing their experiences with the working groups.

The Committee would also like to acknowledge the contributions of Mr. Rajiv Shastri, NJ Asset Management, Mr. Nagendra Kumar, NSE, Mr. Prateek Jain and Mr. Hemen Bhatia, Nippon Life India Asset Management and Mr. Pritesh Majmudar, DSP Investment Managers which have helped in giving contours to many thoughts discussed in the report.

The Committee would also like to acknowledge the support provided by the teams at Price Waterhouse & Co. LLP (including Mr. Nehal Sampat, Ms. Sneha Bhagat and Mr. Akshay Ganatra) and IC Universal Legal (including Mr. Sanchit Kapoor, Ms. Anita Jain and Ms. Annapurna Sinharay) that not only provided various inputs to the committee but also immensely contributed in preparation of this report.

Chairman & Members of the Committee

5. Executive summary

The role of the Asset Management industry in the development and growth of an economy, more so in the IFSC cannot be under emphasised. A robust Asset Management industry along with a well-developed eco-system is pivotal to the growth of capital markets, which are critical to a developing economy such as India's. Also, a robust Asset Management industry in IFSC can play the role of a corner stone in the larger strategy of the Government of India and the IFSCA of "onshoring the offshore" financial services.

The IFSCA set up this Committee to assess the regulatory landscape for Investment Funds and Fund Managers within the IFSC with the objective of providing the best-in-class platform and regulatory framework to support the growing aspirations of the financial services industry. Meeting new objectives over a long-term period requires reconfiguration of the existing law. This section summarises the expert committee's recommendations for the new fund regime in IFSC.

Fund Regime

Regulating Fund v. Fund Manager

Currently, in the IFSC, there is a framework for Alternative Investment Funds (AIF) which largely regulates "Funds" and through Funds, there is some oversight exercised over Fund Managers. These regulations are largely adopted from the AIF regulations notified by the Securities and Exchange Board of India. There is no detailed regulatory framework for mutual fund type products though there are regulations with respect to Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InvITs). With respect to "separate accounts", there is a regulatory framework for portfolio managers and investment advisers in IFSC.

One of the key aspects to consider as one evaluates the regulatory framework for Investment Funds is determining "who should be regulated" – i.e., the Fund or the Fund Manager or both. Drawing an analogy from the manufacturing sector, it is like determining who should be regulated i.e., the product (the Fund) or the manufacturer (the Fund Manager) or both?

There are pros and cons of each of the alternative approaches. Regulating Fund Managers provides direct oversight to the Regulator over the "manufacturer" whereas regulating Funds implies prescribing more rules for the "product" and less for the "manufacturer". Internationally, certain jurisdictions prefer to regulate Fund Managers whereas certain jurisdictions prefer to regulate Funds.

After much deliberation, the committee was of the view that a comprehensive investment funds regime that is based on regulating the fund managers, with uncomplicated registration and on-going requirements shall facilitate smooth fund launch and fund raising along with an overlay of specific requirements for certain funds (such as retail funds, AIFs, REITs, InvITs and Exchange Traded Funds [ETFs]), would be the right approach for the IFSC. This is intended to ease the onboarding process of Funds or Schemes, thereby facilitating quicker launch, and allowing the Fund Managers to suitably time the launch of the Funds or Schemes. This will also ensure ease of doing business for the fund managers as a single registration would facilitate multiple activities which hitherto required multiple registrations at different point of time. This would give comfort to investors as well.

Thus, it was concluded that it may be more appropriate to exercise regulatory oversight through regulation of Fund Managers as compared to regulation of Funds. Similar to various global jurisdictions, some form of regulation or registration may, nonetheless, be required for Funds as well.

Regulatory oversight

Given the regulated nature of the IFSC or activities permitted therein and the requirements flowing from various regulations such as the Special Economic Zone Act, 2005 (SEZ Regulations), as a baseline attribute, it is proposed that all Fund Managers operating in the IFSC should obtain registration from the IFSCA.

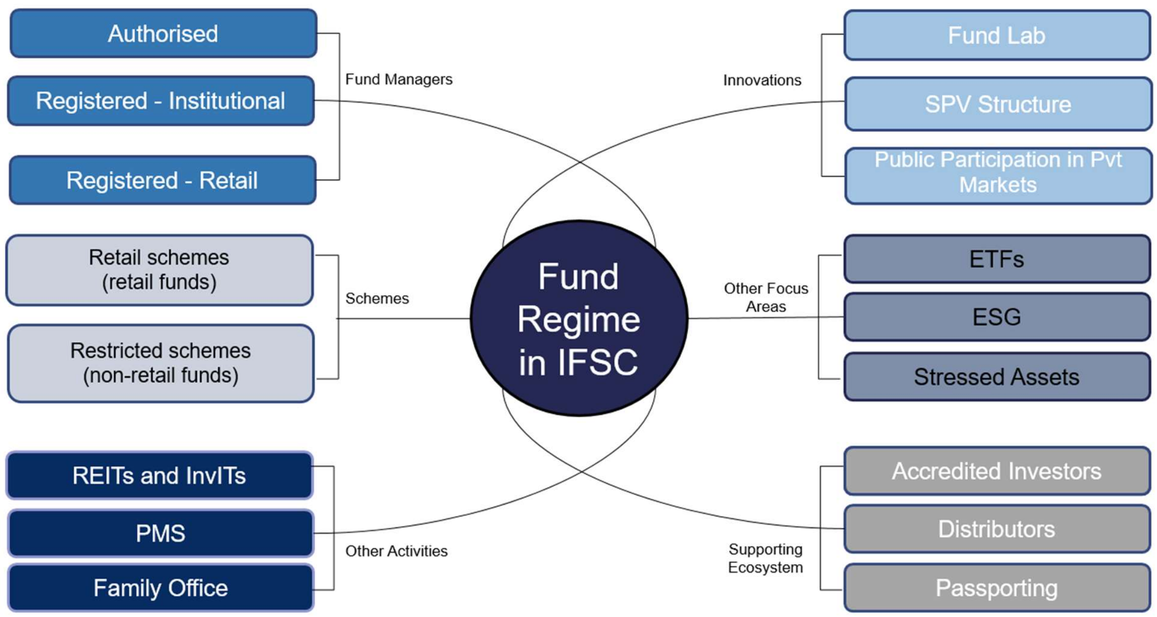
Once the Fund Managers are approved, the requirement for registration of Funds could be fine-tuned depending upon the investor class.

Risk-based approach

Following a 'risk-based' approach emanating from the underling investor class, two categories of FME registrations are envisaged, i.e. (i) - with least regulatory oversight, (ii) - with higher regulatory oversight.

Further, FME should be permitted to set up different schemes depending upon its investment objectives.

Snapshot of proposed fund regime



Type of FME Registration

Broadly, the following Categories of FMEs are proposed:

(a) Authorised FME: FMEs that pool money from accredited investors or investors investing above the specified threshold by way of private placement and investing in start-up or early-stage ventures through Venture Capital Fund (VCF). Single family office investing in securities, financial products and such other permitted asset class may also seek approval under this category.

(b) Registered FME:

(i) Institutional: FMEs that pool money from accredited investors or investors investing above a specified threshold by way of private placement for investing in securities, financial products, and such other permitted asset class through one or more restricted schemes. Such FMEs shall also be able undertake Portfolio Management Services (including for multi-family office) and act as investment manager for private placement of REIT and InvIT. Such FMEs shall also be able to undertake all activities as permitted to Authorised FMEs.

(ii) Retail: FMEs that pool money from retail and non-retail investors under one or more schemes for investing in securities, financial products, and such other permitted asset class through retail or restricted schemes. Registered FME – Retail may act as investment manager for public offer of REIT and InvIT. Such FME shall also be able to launch ETFs. Registered – Retail FMEs shall also be able to undertake all activities as permitted to Authorised FMEs and Registered FMEs – Institutional.

Type of Funds/ Schemes

Retail Schemes (i.e., Retail Funds) – Schemes that are offered to all investors including retail investors and are subject to higher restrictions. Registered FME – Retail would manage such schemes.

Restricted Schemes (i.e., Non-Retail Funds) – Schemes that are offered to relevant persons on private placement basis (accredited investors) or to investors investing above a specified threshold and are subject to lessor restrictions. Such schemes can be managed by any FMEs.

Key aspects of the proposed regime for regulating Fund Managers

Particulars	Categories of FME		
	Authorised FME	Registered FME	
		Institutional	Retail
Regulatory oversight by the IFSCA	Low	High	
Types of Schemes managed	Restricted Schemes offered on a private placement basis		Retail Schemes offered to all investors (including retail investors)
Legal structure	Company, LLP, LP structure or branch thereof	Company, LLP, LP structure or branch thereof	Company or branch
Minimum net worth	USD 75,000	USD 500,000	USD 1,000,000
FME experience	FME or its holding company and/ or its key managerial personnel shall have relevant experience.		FME or its holding company to have not less than five years of experience in managing AUM of at least USD 200m with more than 25,000 investors; or At least one person in control holding more than 25% shareholding or share of profits in the FME to have at least five years of experience in financial markets
Minimum number of key managerial personnel	1	2	3
Substantive fund management activity	Core functions such as investment management and trade execution to be performed from the IFSC.		
Fit and proper criteria	Applicable		
Requirement to have office in the IFSC	Yes		

Key aspects of the proposed regime for regulating the Fund/ Scheme

Particulars	Retail Schemes (Retail Funds)	Restricted Schemes (Non-Retail Funds)
Legal Structure	Trust/ Company/ Variable Capital Company (VCC)	Trust/ Company/ LLP/ VCC
Minimum and maximum number of investors	Minimum – 20 Maximum – no cap	<u>VCF</u> No requirement on minimum number of investors Maximum – 50 <u>Funds other than VCF</u> Minimum – 2 Maximum – 1000 or such higher limit as may be prescribed by the IFSCA
	For master-feeder structures, this limit should be applied on a look-through basis.	
Minimum contribution/ capital commitment from an investor in the Fund/ Scheme	Open-ended – None Close-ended – Minimum investment to be USD 10,000. No restriction to close-ended funds investing less than 15% in unlisted securities	Accredited investors – none Investors in VCFs – USD 250,000 Other investors – USD 150,000
Skin in the game contribution from FME or its group entity	Lower of 1% of the corpus of the Fund or USD 200,000	Close-ended Scheme - Lower of 2.5% of the corpus of the Fund or USD 750,000 Open-ended Scheme - Lower of 5% of the corpus of the Fund or USD 1,500,000
	Skin in the game contribution could be waived for Restricted Funds, subject to fulfilment of certain conditions.	
Maximum holding by a single investor	25%. Not be applicable for skin-in-the-game contribution.	VCF – None Other than VCF – 50%. Not be applicable for skin-in-the game contribution
Infrastructure and office space	The Funds/ schemes should not be required to have any physical office in the IFSC separately.	
Investment restrictions	Permissible to invest in all securities or financial products	VCF - Permissible to invest in early-stage start-ups and other securities/ assets. Others - Permissible to invest in all securities, financial products. May also be permissible to invest in real assets subject to certain caps.
Investment diversification conditions	Investment in single investee company – not more than 10% of the AUM. In case of Index Funds, investment cap in a single investee company to be aligned as per Index weights.	None; to be governed by internal investment policy of the fund.

Particulars	Retail Schemes (Retail Funds)	Restricted Schemes (Non-Retail Funds)
	Cap on investment in a single sector – 25% of the AUM of the Fund or scheme. However, cap on investment in financial services sector – 50% of the AUM of the Fund or scheme	
Cap on investment in unlisted securities	Open-ended: Maximum investment in unlisted–15% with no cap on minimum investment Close-ended: Maximum investment in unlisted – 50%, subject to minimum investment limit of USD10,000.	VCF: At least 80% of the investible funds should be deployed in companies incorporated for less than seven years. Open-ended Schemes other than VCF: Maximum investment in unlisted– 25% Close-ended scheme: No such restriction
Leverage	Permissible only for meeting temporary liquidity requirement (for meeting redemptions or dividend payments) up to a limit as disclosed in the offer document	Permissible subject to disclosure in the offer document.

Other Activities of FME

PMS

A Registered FME shall be able to offer PMS to clients. Apart from satisfying the eligibility criteria applicable for FME as mentioned above, an FME providing portfolio management services to its clients would also be required to satisfy additional conditions similar to the one prescribed under the current IFSCA (Capital Market Intermediaries) Regulations, 2021 which amongst others provides for a minimum ticket size of USD 70,000, segregation of client's holdings in securities or assets in a separate account, maintenance of client's fund in a separate account in a Banking Unit in IFSC, etc.

Investment Advisory by a Registered FME

A Registered FME may provide stand-alone investment advisory services, including investment advisory services to offshore funds, subject to ensuring the interest of investors in IFSC are adequately protected. This may be subjected to such other conditions/ relaxations, as may be prescribed.

REITs and InvITs

The IFSCA has issued circulars[1] specifying therein the framework for REITs and InvITs. The framework should be incorporated in the fund regime for such funds. Further, private placement of REITs should be permitted in IFSC. Also, given the similarities in the asset class and the regulatory framework, it may be easier to consolidate the regimes for REITs and InvITs into one Investment Trusts' regime. The Registered FME may act as Investment Manager to such Investment Trusts.

Family Offices

IFSC, with its world class infrastructure has the potential to be the first-port-of-call for Family Offices around the globe.

Family offices can be classified into two categories as under:

[1] F. No. 41/IFSCA/SEBI/REITs-InvITs/2020-21 dated 21 October 2020

i) SFO - SFO (hereinafter referred to as Family Investment Fund) manages the wealth of a private family with no public money or any third-party funds being solicited. Such SFOs are generally not regulated or governed with a light touch regulatory regime; and
ii) MFO - MFO can manage funds of multiple families. MFOs may be governed by a more comprehensive set of regulations as compared to SFOs and can be considered under portfolio management.

The following broad framework could be adopted for Family Investment Funds in IFSC:

Legal Structure	Family Investment Funds could be set-up in form of a Company, LLP or Contributory Trusts
Pooling of funds	Family Investment Funds should pool funds from a single family only and not from any third party. Further, they should be allowed to raise debt/ loans, subject to approval of all members.
Net Worth	An entity registering as a Family Investment Fund should have and maintain a minimum net worth of USD 10 million
Investment Personnel	The Family Investment Fund should have at least one investment professional with prescribed qualifications and with minimum experience of at least 5 years.
Eligible Investments	i) Family Investment Funds should be eligible to invest across all asset classes ii) Family Investment Funds whose majority of members are resident outside India should be permitted to invest in India under the FPI, FVCI and FDI route; and abroad in accordance with laws of the jurisdiction iii) Family Investment Funds with majority resident Indians should be permitted to invest abroad

The regime should also prescribe a list of permissible activities, which could be undertaken by a Family Investment Fund.

Focus Areas

ETFs

Growth in both active and passive fund management is continuing with blurring of boundaries between the two. Also, there is a growing demand for ETFs including active ETFs. ETFs are baskets of securities that are traded on an exchange. Availability of ETFs will lead to development of asset managers as well as investor community at the IFSC. Only a Registered FME – Retail should be able to launch ETFs in IFSC.

The following broad framework could be adopted for ETFs in IFSC:

Types of ETFs	Equity Index oriented ETFs, Debt Index oriented ETFs, Commodity oriented ETFs (Gold ETF, Silver ETF), Currency oriented ETFs, Balanced ETFs, Other ETFs
Issuance of ETFs	- To be offered as a part of new fund offer (NFO) at IFSC - All investors are permitted by IFSCA to transact on exchanges in IFSC
Listing of ETFs	- FMEs shall seek approval from IFSCA for listing of its ETFs - Dual listing of an existing ETF listed on other global Exchanges be permitted on IFSC exchanges
NAV disclosure	- FMEs shall disclose the NAV of the ETF scheme at periodic intervals - Computation of NAV should be as per the methodology specified by IFSCA including method followed for valuation

Market Makers	- FME shall appoint a market maker who shall be responsible for liquidity in the trading of ETF and for providing two-way quotes - Recognised Stock Exchanges in IFSC may provide a simplified framework for registration of IFSCA registered entities as market makers

Environmental, Social and Governance (ESG) focused Funds

In today's context, it has become imperative to build a business that is resilient and sustainable with a positive impact towards the environment and society at large. Growing number of investors expect fund managers to make ESG issues integral to their investment strategies. Regulators and policymakers worldwide have been examining issues relating to sustainable finance in their regulatory and supervisory roles to address ESG related challenges.

IFSC should consider introducing a framework for ESG focused Funds in IFSC.

Entity level disclosures with respect to governance, risk management and investment strategy should be mandated where a FME is managing AUM greater than a significant threshold. Additionally, an ESG Fund should be required to make Fund level disclosures of considerations such as investment objectives, investment policy, material risks, periodic portfolio etc. as may be prescribed by IFSCA. Further, all scheme documents filed with IFSCA should disclose whether sustainability related risk are incorporated in the decision making.

Stressed Assets

The Government introduced the Insolvency and Bankruptcy Code 2016 (IBC) regime to address concerns relating to Non-Performing Assets (NPA) faced by the banking sector. IFSCA can play an important role in the Government initiative of addressing this issue. To attract Funds under the distressed space to the IFSC, IFSC should consider permitting a Fund managed by an FME set up in the IFSC to become a sponsor and set up a stressed loans SPV (organised as a trust) in India.

IFSCA has constituted a separate committee on framework for transfer of stressed loans from domestic lenders to permitted financial institutions in IFSC. Based on the recommendations to be received from this committee, appropriate regulatory regime may be finalised by IFSCA.

Supporting innovations

Fund Lab

The Indian market is still under penetrated and has plethora of investments opportunities. At the same time, the Asset Management industry is constantly evolving with new innovations in terms of new products with new features, investment in new asset classes, etc.

The IFSCA should consider providing a platform to aspirational Fund Managers in the form of a "Fund Lab". Fund Lab as a concept will be akin to regulatory sandbox, which allows FMEs to create and develop asset management/ Fund products and strategies in a controlled manner with limited AUM/ number of investors.

The Fund Lab would raise moneys only from the FME or FME's group entities. Such a Fund Lab should be close ended with a predefined experimentation period of not more than 18 months. Certain criteria could be laid down for Fund Labs such as minimum investment corpus of USD 1 million, maximum investment corpus of USD 3 million, no investment restrictions/ divestment norms, no minimum criteria with respect to educational qualification or experience of the investment team, etc.

Post the experimentation period, the IFSCA could either require winding up of the Fund in case the results are not satisfactory, or the Fund migrates into the full Fund regime in appropriate categorisation under the proposed Fund regime.

Special Purpose Vehicles as a co-investment structure

Internationally, co-investment is popular and has been in existence for long. In this context, FMEs should be allowed to create SPVs under the main Fund to enable undertaking large investment with the help of their existing investors or other investors to co-invest along with the Fund/ scheme. The Fund may also make use of SPV to take leverage at SPV level. Such SPVs should be deemed to be 'Fund' for all practical purposes. Certain additional conditions or dispensations (such as the Fund to hold minimum of 50% of shares and voting power in the SPV, no skin in the game contribution required by the FME at SPV level, etc.) could be considered as detailed later in the report.

Public participation in private markets

With growing interest of retail investors in private markets, there is a case to enable Funds with retail investors to participate in private markets, albeit in a limited way as one cannot undermine the risks of investing in private markets. To enable the same, it is proposed to allow open-ended or close-ended schemes with retail investors to invest less than 15% in unlisted securities. Where concentration of investments in unlisted securities is higher (more than 15% but capped to 50%), the schemes would need to be close-ended and the minimum investment from a single investor should be USD 10,000, on the presumption that such investors would have the necessary capital/experience to appreciate the risks of investing in private markets.

Supporting Ecosystem

Framework for Accredited Investors

Investors who understand risks associated with complex financial products and a certain minimum income/ net worth are recognised as 'Accredited Investors'. Accredited Investors are reckoned to not require extensive regulatory protection. Therefore, such investors should be given certain regulatory concessions.

The IFSCA can prescribe eligibility criteria with respect to income/ net worth requirements which would need to be met for an investor to qualify as an Accredited Investor.

The Accredited Investor could be classified in the following two categories:

<u>Recognised Accredited Investor:</u> Financial criteria can be the grounds for classification under this category.

<u>Deemed Accredited Investors:</u> Certain classes of investors e.g., Government and Government related investors, any Fund/ FME regulated by IFSCA, Market Infrastructure Institutions in IFSC, capital market intermediaries in IFSC, an investment fund (mutual fund, insurance fund, pension fund, university endowment fund etc. by whatever name called),commercial banks, asset management companies, insurance, and reinsurance companies from a FATF compliant jurisdiction and regulated by a Financial sector regulator, Professional / Accredited / Qualified Investors from FATF member countries could be deemed to be accredited investors.

A recognized stock exchange or a depository ("**Specified Agency**") could be authorised to certify eligible investors as accredited. Also, a FME or the concerned intermediary could be permitted to certify accreditation. Depending upon the preference of investor, an investor may opt to seek an accreditation from the Specified Agency, which would then be valid vis-à-vis each intermediary the investor deals with or may choose to represent/ confirm its accredited status directly/ each time to every concerned intermediary with whom it may deal with from time to time. Such concerned intermediary dealing with Accredited Investors should obtain the relevant investor's consent to be treated as an Accredited Investor and maintain the relevant documentation to confirm the status of investor as accredited investors.

Accredited Investors should be granted certain relaxations including no minimum investment limit with respect to availing PMS or investing in restricted schemes. This would, however, be subject to such conditions/ restrictions detailed later in the report.

Framework for distributors

Distribution activities should be covered under the regulatory regime prescribed for ancillary services to *inter alia* ensure protection of investor's interests and promote a wider distribution network by enabling a streamlined process for distribution activity.

Any person, domiciled or established in the IFSC, desirous of acting as a distributor of

- financial products or services regulated by the IFSCA;
- financial products or services subscribed/ availed by any person domiciled or established in the IFSC; or
- financial products or services regulated by financial sector regulator of such jurisdictions (including India) as may be specified by IFSCA

should be required to seek authorisation as a distributor from IFSCA.

Certain exemptions from authorisations e.g., in the case of IBUs, investment advisers, stockbrokers, any other entities approved by the IFSCA may be provided. However, such exempted entities should be required to follow the Code of Conduct for distributors as may be prescribed by IFSCA[2].

Any person distributing any financial product under the regulatory ambit of IFSCA shall also comply with the code of conduct. Further, persons engaged in providing investment management, portfolio management, investment advisory and other related financial products and services shall only utilise services of such distributor/s who hold registrations with the IFSCA or are exempted from authorisation requirement.

Passporting of Funds

Ideally, regional fund managers should be able to freely offer their local products to investors in other countries on a level playing field. However, different countries have different regulatory regimes, due to which financial centres often grapple with multiple standards across jurisdictions making it difficult to facilitate cross-border marketing/ distribution of such products.

One way to facilitate such cross-border marketing/ distribution of financial products could be through introducing a regime that allows for passporting of funds.

The IFSCA may consider the following suggestions/ recommendations for passporting of funds:

- IFSCA may participate in reciprocal passporting arrangements/ mutual recognition frameworks with regulators of other prominent overseas jurisdictions having fund management such as European Union, Singapore, USA, Mauritius, Cayman Islands etc. The IFSCA Regulations on Fund Management could have equivalent rules as compared to these jurisdictions.

- Additionally, the IFSCA should recognise third-country regimes under such arrangements, subject to appropriate equivalence requirements.

Increasing presence in the IFSC by requiring appointment of local representative can also be considered.

Taxation framework

The tax regime available to Specified Funds in IFSC has been welcomed by the foreign investor community. It should be extended to all the Funds in IFSC. Accordingly, the existing taxation framework could be revisited and realigned as follows:

Principles for proposed tax framework	
Levy of Tax	• There should be levy of tax at one level. • In case of inbound funds with investments from non-resident investors, tax could be levied and collected at Fund level. • In case of outbound funds with investment from resident investors, income of the Fund should be exempted, and income distributed by the Fund should be taxable in the hands of resident investors.

[2] Detailed Code of Conduct has been provided in section 11.2 of this report

Principles for proposed tax framework	
Attribution of income for inbound funds	• Vis-à-vis non-resident investors, the Fund should pay tax in India only on income earned from Indian securities. • No tax should be levied on income accruing or arising from investments in assets or securities outside India (including IFSC). • Vis-à-vis Indian securities, gains on securities other than equities should be exempted from tax in India. • Gains on equities should be chargeable to tax as per the provisions of the domestic tax law. • Exemptions should be provided for gains with respect to certain non-resident investors that are exempt with respect to their entire income or on certain streams of income under the Tax Treaty that India has with such other country. • Dividend and interest income should be taxed at lower rate of 5% (plus applicable surcharge and cess).
Outbound Funds	The income of the Fund should be exempted from tax and the income distributed by the Fund should be taxable in the hands of resident investors. A lower rate of tax could be considered for resident investors.
Family Investment Fund	**Non-residents setting up Family Investment Funds** The current tax regime available to non-resident investors who invest in a specified fund in IFSC should be extended to non-residents setting-up family offices/ Family Investment Fund in IFSC. In case of share of resident family members, the same should be taxed at applicable rates in the hands of the Fund on accrual of any income to Family Investment Fund, in proportion to their contribution. The income being taxed at the Fund level should be exempt in the hands of the family members. **Residents setting up Family Investment Funds** In case of family office being set-up in IFSC by Indian residents, the above principle of taxation applicable to outbound funds should be extended to Family Investment Fund in IFSC.
Tax on dividends distributed by FME	There should be no tax on dividends distributed by an IFSC FME to non-resident shareholders and dividend distributed to resident shareholders should be taxed at lower rates.

Proposed changes in other regulations and ask from Authorities other than IFSCA

Certain changes in other laws and regulations would also be required so as to enable and align the proposed Fund regime in IFSC. These have been discussed in detail in the section 13 of this report.

6. Need for a unified regime in IFSC

Currently, in the IFSC, there is a framework for AIFs which largely regulates “Funds” and through Funds, there is some oversight exercised over Fund Managers. These regulations are largely adopted from the AIF regulations notified by the Securities and Exchange Board of India. Additional dispensation for AIFs in IFSC includes no mandates on diversification, possibility of co-investments, enabling funds to undertake leverage, transfer in case of re-location being tax exempt, no mandate of sponsor contribution in case of re-location of funds, contribution by Indian sponsors under the automatic route, etc. However, there is no regulatory framework for mutual fund type products though there are regulations with respect to REITs and InvITs. With respect to “separate accounts”, there is a regulatory framework for portfolio managers and investment advisers in IFSC.

As evident from the above, there are multiple regimes governing the Investment Funds industry which are prescribed under different regulations issued by different regulators. There is a pressing need to consolidate these regulations in one unified regime. Also, there are gaps in the regulatory framework, which need to be addressed while considering the new framework for Investment Funds.

The hallmarks of any “good” regulatory frameworks are:

- It should be comprehensive;
- It should be simple and easy to understand;
- It should be easy to implement;
- It should be benchmarked to the best-in-class practices prevalent overseas;
- It should be dynamic to cover the emerging business scenarios;
- It should foster innovation while protecting the consumer (i.e., the investors); and
- It should foster ease of doing business for the manufacturer (i.e. the fund manager).

With the above backdrop, the Committee deliberated on the following:

Regulating “Funds” v “Fund Managers”

One of the key aspects to consider as one evaluates the regulatory framework for Investment Funds is determining “who should be regulated” – i.e., the Fund or the Fund Manager or both. Drawing an analogy from the manufacturing sector, it is like determining who should be regulated i.e., the product (the Fund) or the manufacturer (the Fund Manager) or both?

There are pros and cons of each of the alternative approaches. Regulating Fund Managers provides direct oversight to the Regulator over the “manufacturer” whereas regulating Funds implies prescribing more rules for the “product” and less for the “manufacturer”. Internationally, most jurisdictions prefer to regulate Fund Managers with certain oversight over Funds as well.

After much deliberation, the committee was of the view that a comprehensive investment funds regime that is based on regulating the fund managers, with uncomplicated registration and on-going requirements to facilitate smooth fund launch and fund raising along with an overlay of specific requirements for certain funds (such as mutual funds, AIFs, REITs, InvITs and Exchange-Traded Funds [ETFs]), would be the right approach for the IFSC. This is intended to ease the onboarding process of Funds or Schemes, thereby facilitating quicker launch, and allowing the Fund Managers to suitably time the launch of the Funds or Schemes. This will also ensure ease of doing business for the fund managers as a single registration would facilitate multiple activities which hitherto required multiple registrations at different point of time. This would give comfort to investors as well.

Thus, it was concluded that it may be more appropriate to exercise regulatory oversight through regulation of Fund Managers as compared to regulation of Funds. Some form of regulation or registration may, nonetheless, be required for Funds as well.

With a view to assess the regulatory landscape that could be made applicable to Funds in the IFSC, this report summarises the committee’s recommendations for the new unified fund regime in IFSC which will allow fund managers to seek authorisation/ registration from the IFSCA and launch funds/ schemes much faster than possible under the current regulatory regime available in India.

7. Global Practices

The evolution of the Asset Management industry across the globe has followed an interesting path. The genesis of certain jurisdictions emerging as prominent Asset Management hubs can be traced to the following reasons –

- "Pro-business" policies combined with talented and experienced Asset Managers (as seen in Singapore)
- Market access and passporting functionality (as seen in Luxembourg and Ireland).
- Proximity to a large investment pool and large investment markets (as seen in New York, London, Tokyo, and Shanghai)
- Enabling regulatory and tax regimes which are not onerous for Investment Managers and investors (as seen in Cayman Islands and Mauritius).

A jurisdiction that accommodates the diverse needs of the different stakeholders enables development of a sustainable Fund management Industry.

Determination of jurisdiction for an investor would amongst others involve consideration of varied factors such as supportive legal and regulatory framework, stable tax neutral regime, engaged government/ regulators, political and economic stability, availability of first-class infrastructure and talent pool, reasonable operational costs, and investor protection norms.

As a part of its mandate, the Committee examined fund regimes across popular fund jurisdictions such as Singapore, Mauritius, and Luxembourg and how they have evolved over time. The Committee invited external experts to get their perspective as well.

These jurisdictions have been analysed on key attributes applicable to the Fund Management entity as well as the Funds viz. the type of funds, legal structure, capital requirements, category of underlying investors and so on. A comparative analysis of the key aspects of the Fund regime in various jurisdictions and the proposed IFSC Fund regime is provided as **Annexure A**

A brief overview of the Fund regimes across popular fund jurisdictions such as Singapore, Mauritius and Luxembourg are outlined below:

Singapore

Singapore, as a jurisdiction, offers four categories of fund management licenses: Retail Licensed Fund Management Companies (Retail LFMCs), Accredited/ Institutional Licensed Fund Management Companies (A/I LFMCs), Venture Capital Fund Managers (VCFMs), and Registered Fund Management Companies (RFMCs).

The first three categories refer to FMCs that hold capital markets services (CMS) license for fund management, which are issued by MAS. The licenses differ in the types of investors which the FMC may manage funds for and the type of funds which the FMC manages. The last category, the RFMC, is not licensed by the MAS, but only registered. Not only this requires fewer regulations to be adhered to by the FMC but also shrinks the permissible scope of fund management activities.

A summary table outlining the types of funds which the FMC manages, and the underlying investor class is provided as under:

Category		Type of Investors
Licensed Fund Management Company	Retail LFMC	All types of investors
	A/I LFMC	Qualified investors only, without restriction on the number of qualified investors
	VCFM	Venture capital fund with qualified investors only, without restriction on the number of qualified investors.
Registered Fund Management Company (RFMC)		No more than 30 qualified investors (of which no more than 15 may be funds or limited partnership fund structures) and the total value of the assets managed does not exceed USD 250 million

Mauritius

The regulatory framework in Mauritius caters to investors in both retail and AIFs space. Retail funds are offered to the public and are regulated as open-ended (collective investment schemes) or closed-ended funds (CEFs). An AIF, on the other hand, can further be classified as a Professional collective investment scheme (CIS), Specialised CIS or an Expert fund. In comparison with a retail fund, an AIF is exempt from the stricter regulations that govern the retail funds.

In respect of the type of investors, nature of investments and regulatory requirements, a CIS can be classified as follows:

- Retail scheme: A scheme which involves capital invested primarily by individual investors. This includes mutual funds, ETFs, etc.
- Professional CIS: A scheme which involves issuance of shares solely to Sophisticated Investors or via private placements.
- Specialised CIS: A scheme that invests in real estate, derivatives, commodities, or any other product authorised by the Financial Services Commission.
- Expert Fund: A Fund that is restricted to investments from Expert Investors or Sophisticated Investors.
- Global Scheme: A CIS that holds a Global Business Company (GBC) license whose primary objective is to investment outside Mauritius with the purpose of expedite and streamline operations outside Mauritius.

Luxembourg

- Luxembourg, as a jurisdiction, caters to both retail and non-retail investors. These can either be regulated funds, (i.e., authorised and supervised by the Financial Sector Supervisory Commission) or unregulated funds.
- Retail funds include Undertaking for Collective Investment in Transferable Securities (UCITS) and are governed by the Undertakings for Collective Investment (UCI) Law.
- Non-Retail Funds are organised as Specialised Investment Funds (SIFs), Reserved Alternative Investment Funds (RAIFs), Investment companies in risk capital (SICAR) and Unregulated AIFs.
- AIFs are managed by an alternative investment funds manager (AIFM) and are governed by the Alternative Investment Funds Manager Directive 2011/ 61/ EU (AIFMD)
- UCITS are available to all type of investors. Further, only well-informed investors are eligible to invest in SIF, SICAR and RAIFs.

Globalisation of Family offices

The concept of family office has been in existence for over a century in developed nations such as USA and across Western Europe and in parts of Asia. However, the same has been gaining prominence across the world with various jurisdictions encouraging setting-up of family offices in their territory.

Further, a family office set-up in a particular jurisdiction may wish to 'detach its roots' or redomicile from its original base as succeeding generations settle around the world. This may spread the family office set-up across different jurisdictions. For example, the administrative functions may be located in a particular jurisdiction while the investment function may be undertaken from a different jurisdiction such as a major financial hub.

A brief overview of the regulations prescribed under select jurisdictions has been summarised below:

Singapore

Singapore, as a jurisdiction, does not have a specific regime for family offices. SFO structures are typically exempted from local securities regulations either through a) exemption provided under the local regulations (i.e., for an entity which manages assets for or on behalf of only one family and is wholly owned or controlled by members of the same family); or b) by way of an application to the local regulator (where the entity does not fall under the exemption bucket but is under common control of SFO).

Multi-family offices are subject to regulatory oversight as any other Fund Manager managing third party monies though there is no separate regime for them.

Dubai

The Dubai International Financial Centre Authority (DIFCA) has prescribed regulations, which govern family offices under which every person seeking to form a family office needs to obtain a specific license from the regulator.

Each SFO should have minimum investable/ liquid assets of USD 10 million[3]. The regulations prescribe criteria for determining investible/ liquid assets, wherein only those assets which are realisable in a 180-day period should be considered.

Mauritius

Any person rendering family office services (single or multiple) in Mauritius is required to obtain a license from the Financial Services Commission. Each family under SFO or MFO management needs to have assets and/ or investments of more than USD 5 million. The regulations in Mauritius prescribe minimum capital requirements, which need to be maintained at all times. The minimum capital requirements prescribed are USD 35,000 for a SFO and USD 70,000 for an MFO.

Cayman Islands

Until August 2020, the local regulations in Cayman Islands provided an exemption for SFO to be registered or holding a license for dealing in securities. However, to monitor and exercise effective supervision over SFO, the regulations were amended to bring the SFO within the purview of Securities Investment Business law. By virtue of the amendment carried out in the regulations, a person including SFO carrying on securities investment business is required to hold a license or registration as required under SIBL.

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[3] The limit as per the proposed regulations is minimum net assets of USD 50 million

Separately, the regulatory framework for family offices in DIFC Dubai, Mauritius and Cayman Islands also require appointment of authorized person for ensuring compliance with prescribed regulations and requirements and acting as a point of contact between the family office and the regulator.

Global practices with regard to Passporting of Investment Funds

With the growth of capital mobility and the development of financial markets, there has been a strong desire to see more financial linkages within the region which led to the development of the framework of passporting of investment funds. This provides the investors with uninhibited access to investments and expertise across the territories at a reduced cost. The key principle of a passport regime is to allow the marketing of funds formed in a particular jurisdiction into another jurisdiction with minimal regulatory hurdles.

Passporting of Funds in the European Union

The EU Directive 2011/ 61/ EU on Alternative Investment Fund Managers (AIFMD) created a single marketplace within the European Union (EU) for marketing of AIFs.

Presently, AIFMD allows for the marketing of AIFs in the EU by alternative investment fund managers (AIFMs) to professional investors. Retail funds marketed to retail investors are governed by the Undertakings for Collective Investment in Transferable Securities Directive 2009/ 65/ EC (UCITS Directive).

The AIFMD applies to all EU AIFMs managing EU AIFs or non-EU AIFs, irrespective of whether or not they are marketed in the Union. Secondly to non-EU AIFMs managing EU AIFs, irrespective of whether or not they are marketed in the Union and lastly to non-EU AIFMs marketing EU AIFs or non-EU AIFs in the Union.

From the perspective of marketing of funds, the Directive gives the non-EU AIFMs two different options to access the EU market: (1) first, with the EU passport; or (2) through the national private placement regimes specific to each member state.

<u>Non-EU authorised AIFMs marketing non-EU AIFs in the EU</u>

The AIFMD allows each EU member state to decide whether or not to allow non-EU AIFMs to market in its jurisdiction and to determine the rules that should apply and provides for certain conditions to be met. Certain equivalence requirements and role of ESMA has also been prescribed.

<u>EU authorised AIFMs marketing EU AIFs in the EU</u>

Under the AIFMD, an EU authorised AIFM has a passport to freely market its EU domiciled AIFs to professional investors in its own Member State and in other EU Member States, subject to a notification process.

Mutual Recognition Framework between Hong Kong and mainland China

The Securities and Futures Commission (SFC) HK and the China Securities Regulatory Commission (CSRC) launched the initiative of Mutual Recognition of Funds (MRF) between Mainland China and Hong Kong, allowing eligible Mainland and Hong Kong funds to be distributed in each other's market through a streamlined vetting process.

If a Mainland fund complies with the relevant Mainland laws and regulations, it is generally deemed to have complied in substance with the relevant SFC requirements and will enjoy a streamlined process for the purpose of authorisation for offering to Hong Kong public and vice-versa.

The two regulators have set out eligibility requirements, application procedures, operational and regulatory arrangements of the MRF.

Asian Regional Funds Passport

The Asia Region Funds Passport (ARFP) is an international initiative led by Asia-Pacific Economic Cooperation (APEC) that aims to facilitate cross-border offerings of eligible collective investment schemes among APEC member economies while ensuring investor protection in the economies participating in the ARFP.

The Memorandum of Cooperation (MOC) is the internationally agreed framework which sets out the rules and conditions for offerings of cross-border mutual funds under the ARFP.

There are currently 5 participating economies who are signatories to these frameworks, namely, Australia, Japan, the Republic of Korea, New Zealand, and Thailand.

Singapore

Singapore allows for two ways in which investment funds may be distributed.

- Firstly, through the recognized schemes which involves a recognition process with Monetary Authority of Singapore (MAS) where recognition is required for foreign funds targeting retail investors.

- Secondly, through restricted foreign schemes offered only to accredited investors involving a notification to the MAS.

To obtain recognition, the foreign fund's home legislation and market practices must provide equivalent protection to Singapore investors as they would get from Singapore domiciled funds.

Funds passporting framework under ASEAN (CIS) Framework

The ASEAN Collective Investment Scheme (CIS) Framework allows fund managers based in Singapore, Malaysia, and Thailand to offer CIS constituted and authorised in their home jurisdiction directly to retail investors in the other two ASEAN countries under a streamlined authorisation process.

For this purpose, a set of common ASEAN standards has been established to ensure that participating fund managers have the necessary experience and track record in managing retail funds offered under the framework.

8. Fund Regime

8.1. Registration of Fund Manager

All FMEs operating in the IFSC should be required to seek prior authorisation / registration from the IFSCA.

One of the key tenets of a good regulatory regime should be to keep it simple and simultaneously flexible to accommodate evolving scenarios. Furthermore, the regulatory regime should follow a 'risk based' approach for regulatory oversight. The supervision over such Fund Managers may vary depending upon the category of investors whose funds are sought to be managed, type of product or Fund (asset class) and the amount of AUM sought to be managed.

Categories of FMEs

With the above considerations, the FME could be segregated into two broad categories: **Authorised FME** with 'least oversight' and **Registered FME** with 'higher oversight' for institutional investors and retail investors.

Broadly, the following types of registrations could be considered:

Type of registration	Description
Authorised FME	• FMEs that pool money from accredited investors or investors investing above the USD 250,000 by way of private placement and invest in start-up or early-stage ventures through Venture Capital Fund/ Scheme. • Single Family office investing in securities, financial products and such other permitted asset class may also seek approval under this category.
Registered FME	**Registered FME – Institutional (Non-Retail)** • FMEs that pool money from accredited investors or investors investing above USD 250,000 by way of private placement for investing in securities, financial products, and such other permitted asset class through one or more restricted schemes. • Such FMEs shall also be able undertake Portfolio Management Services (including for multi-family office) and act as investment manager for private placement of REIT and InvIT. Such FMEs shall also be able to undertake all activities as permitted to Authorised FMEs.
	Registered FME – Retail • FMEs that pool money from retail and non-retail investors under one or more schemes for investing in securities, financial products, and such other permitted asset class through retail or restricted schemes. • Registered FME – Retail may act as investment manager for public offer of REIT and InvIT.

Type of registration	Description
	• Such FMEs shall also be able to launch ETFs. Further, such FMEs shall also be able to undertake all activities as permitted to Authorised FMEs and Registered FMEs – Institutional (Non-Retail).

*Accredited investors subsequently discussed in the report.

A FME with a higher category of FME registration say 'Registered FME – Retail' can undertake activities permitted to other FMEs such as 'Registered FME – Institutional'. Similarly, a 'Registered FME – Institutional' can undertake activities permitted to an 'Authorised FME'. However, the reverse should not be permitted.

Procedure for grant of registration

A Fund Manager who wishes to apply for a fund management registration would be required to submit to the IFSCA the relevant prescribed forms, accompanied by an application fee and all supporting documents.

Eligibility criteria

1. Legal structure

- The entities obtaining approval under **Authorised FME** and **Registered FME-Institutional** category could be established or incorporated in IFSC in the form of a company or its subsidiary, LLP, LP structure or a branch thereof of the existing intermediaries in any of the **Financial Action Task Force** (FATF)-compliant jurisdictions. In case of branch, the parent entity should be regulated by the capital market regulator of such jurisdiction for conducting similar activities.

- The entity obtaining approval under **Registered FME-Retail** category could be in the form of a company incorporated in the IFSC or a branch set up in the IFSC of any company in any of the FATF- compliant jurisdictions. In case of branch, the parent entity should be regulated by the capital market regulator of such jurisdiction for conducting similar activities.

2. Net Worth

Depending upon the category of registration obtained, the entities shall, at all times, fulfil the net worth requirements tabulated as follows:

Category of registration	Net worth requirement
Authorised FME	USD 75,000
Registered FME	Institutional - USD 500,000 Retail - USD 1,000,000

For this purpose, 'net worth' means the aggregate value of the paid-up share capital (or capital contribution) and all reserves created out of the profits, securities premium account and debit or credit balance of profit and loss account, after deducting the aggregate value of the accumulated losses, deferred expenditure and miscellaneous expenditure not written off, as per the balance sheet, but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation.

In case the FME is in the form of a branch, the parent entity may fulfil the net worth requirements. In case the FME is a subsidiary, the subsidiary shall fulfil the net worth requirements.

Furthermore, the FME shall be required to fulfil the net worth requirements, separately and independently, of the capital adequacy requirements, if any, for each activity undertaken by it under the relevant regulations.

3. Staffing and competency requirements

A FME who has been delegated with investment management is expected to meet certain minimum staffing and competency requirements. These relate to relevant professionals and their requisite qualification and experience in the activities relating to fund management, the number of directors, appointment of compliance officer, etc. Depending upon the category of registration proposed to be obtained, the staffing and competency requirements may differ.

The experience and qualification requirements for each of the FME categories is stated below. This is broadly in line with the IFSC (Capital Market Intermediaries) Regulations, 2021.

Particulars	Authorised FME	Registered FME	
		Institutional	Retail
FME Experience	FME or its holding company and/ or its key managerial personnel shall have relevant experience. Key managerial personnel(s) within the FME are mandatorily required to have relevant professional qualification and experience. (detailed later)		FME or its holding company to have not less than five years of experience in managing AUM of at least USD 200m with more than 25,000 investors; or At least one person in control holding more than 25% shareholding or share of profits in the FME to have at least five years of experience in financial markets.
Minimum number of key managerial personnel	**1** To be designated with the overall responsibility of the FME (including fund management, risk management and compliance function)	**2** One key personnel to be designated with the overall responsibility of the FME; and One key personnel to be designated as a compliance and risk manager.	**3** One key personnel to be designated with the overall responsibility of the FME; One key personnel to be designated as a compliance and risk manager; and One key personnel to be in charge of the fund management function.
Experience and professional qualification of key personnel	**Experience**: One Key personnel to have minimum five years of experience in related activities in the securities market or dealing in financial products such as a portfolio manager,	**Experience**: Two Key personnel to have minimum five years of experience in related activities in the securities market or dealing in financial products such as a portfolio manager,	**Experience**: Three Key personnel to have minimum five years of experience in related activities in the securities market or dealing in financial products such as a portfolio manager, broker dealer, investment advisor, research analyst or fund management.

Particulars	Authorised FME	Registered FME	
		Institutional	Retail
	broker dealer, investment advisor, research analyst or fund management.	broker dealer, investment advisor, research analyst or fund management.	
	Professional qualification: Professional qualification (such as Chartered Accountant, Chartered Financial Analyst, Company Secretary or equivalent) or post-graduate degree or post-graduate diploma in finance, accountancy, business management, commerce, economics, capital markets, banking, law, insurance, or actuarial science from a recognised institution or any other qualification as may be specified by the IFSCA.		
Minimum number of Directors or Partners in FME	-	-	Four (At least 50% of the Directors to be independent)

Note: The personnel exercising influence or control over the management of the investment portfolio and who initiates the proposal on the portfolio composition shall be based in the IFSC.

4. Fund management activity from IFSC

The key management and commercial decisions relating to investment management and trade execution that are necessary for the conduct of the business of the FME should in substance be undertaken from the IFSC.

5. Criteria for fit and proper person

FME shall ensure that its principal officers[4], directors/ partners/ designated partners, key managerial personnel[5] and controlling shareholders are fit and proper persons. For this purpose, a person shall be deemed to be a fit and proper person if,

a. Such person has a record of fairness and integrity, including but not limited to — (i) financial integrity; (ii) good reputation and character; and (iii) honesty.

b. Such person has not incurred any of the following disqualifications —

    i. The person has been convicted by a Court of competent jurisdiction for any offence involving moral turpitude or any economic offence or any offence under securities laws;

    ii. A recovery proceeding has been initiated against the person by a financial regulatory authority and is pending;

    iii. An order for winding up or liquidation has been passed against the person for malfeasance, and in case of an individual, the person has been declared insolvent and not discharged;

[4] Principal officer should include a person who is responsible for the overall activities of the FME in the IFSC and should include any designated partner, in the case of an LLP; whole time/ executive / managing director, in the case of a Company; and any other person designated as a principal officer.
[5] Key managerial personnel should include the officers or personnel of the FME who are members of its core management team and also the members of the management one level below the executive directors of the FME, functional heads and should also include Chief Executive Officer, Company Secretary and Chief Financial Officer or any other person whom the FME may declare as key managerial personnel.

iv. An order, restraining, prohibiting or debarring the person from accessing or dealing in securities or financial products or financial services has been passed by any regulatory authority, and a period of three years from the date of the expiry of the period specified in the order has not elapsed;

v. Any other order against the person, which has a bearing on the securities market, has been passed by the IFSCA or any other regulatory authority, and a period of three years from the date of the order has not elapsed;

vi. The person has been found to be of unsound mind by a Court of competent jurisdiction, and the finding is in force;

vii. The person is financially not sound or has been categorised as a wilful defaulter;

viii. The person has been declared a fugitive economic offender; or

ix. any other disqualification as may be specified by the IFSCA.

6. Infrastructure and office space

- The FME should have a physical office in the IFSC.
- The office should be dedicated, secure and accessible only by authorised person(s).
- FME should have the necessary infrastructure, manpower, risk management policies (to identify, address and monitor the risks associated with the funds' assets that it manages), etc. to effectively discharge the activities of the FME. This should be commensurate to the size of its operations.
- FME should ensure compliance with the Anti-Money Laundering (AML) or Combating the Financing of Terrorism norms as applicable.

7. Period of validity of certificate

The certificate of registration granted by the IFSCA shall be perpetual, unless suspended or withdrawn or cancelled by the IFSCA or surrendered by the FME.

8.2. Type of Schemes (inclusive of Investment conditions and restrictions)

While the FME would obtain registration with the IFSCA, to ensure appropriate oversight, it is important for the Funds or schemes to be registered or regulated with the IFSCA as well.

FME should be permitted to set up different schemes depending upon its investment objectives. The schemes can be close-ended or open-ended. A close-ended scheme means any scheme in which the period of maturity of the scheme is specified in the Private Placement Memorandum (PPM) or the offer document. In a close-ended scheme, redemption would be offered to investors only at the closure/ maturity of the scheme or on a periodic basis post initial lock-in period as may be disclosed in the PPM or offer document. An open-ended scheme means a scheme that offers units for sale without specifying any duration for the redemption or maturity of the scheme.

Type of schemes (retail schemes and restricted schemes)

Depending upon the nature of the fund (retail or non-retail) and the size of the fund or scheme, various documentation or information would be required to be filed with the IFSCA for launching new Funds or schemes. The Funds or schemes are accordingly divided into the following two categories:

Type of Funds or schemes	Description
Retail schemes (i.e. retail funds)	• Retail schemes are schemes that can be offered to all investors, including retail investors. • Given the potential reach of such retail schemes, there would be higher oversight and certain restrictions on such retail schemes, including the need for filing with the IFSCA, and the manager of the Fund or schemes must be a Registered FME-Retail.
Restricted schemes (i.e. non-retail funds)	• Restricted schemes are the schemes offered only to 'relevant persons' on a private placement basis, being accredited investors or other investors investing above the prescribed threshold. • Restricted schemes would include funds investing in start-ups or early-stage ventures (VCFs) and other non-retail funds • Since the potential pool of investors is smaller and presumably more sophisticated or financially literate, the requirements for restricted schemes would be less stringent. • Restricted schemes are subject to lessor restrictions. • They can be launched by any FME category.

Conditions for setting up the Fund or Schemes

Particulars	Retail Schemes	Restricted Schemes
Legal structure	Trust/ Company/ VCC	Trust/ Company/ LLP/ VCC
Minimum and maximum number of investors	• Minimum – 20* • Maximum – no cap * This condition to be fulfilled within six months from the date of launch.	• VCF No requirement on minimum number of investors Maximum – 50

<table>
<tr><th>Particulars</th><th>Retail Schemes</th><th>Restricted Schemes</th></tr>
<tr><td rowspan="2"></td><td></td><td>Funds other than VCF
Minimum – 2
Maximum – 1000 or such higher limit as may be prescribed by the IFSCA</td></tr>
<tr><td colspan="2">In the context of master-feeder structures, this limit should be applied on a look-through basis.</td></tr>
<tr><td>Minimum contribution/ capital commitment from an investor in the Fund/ Scheme</td><td>Open-ended – No minimum contribution requirement. FME can decide the ticket size for investment in these Schemes.
Close-ended – Minimum investment to be USD 10,000
For close-ended schemes investing less than 15% in unlisted securities, there shall be no restriction on the minimum ticket size.</td><td>Accredited investors – none
VCF investors – USD 250,000
Other investors – USD 150,000</td></tr>
<tr><td>Maximum holding by a single investor in the Fund or Scheme, to be tested only at final closing</td><td>Maximum holding by a single investor to be capped at 25%. The cap of 25% should not be applicable for skin-in-the-game contribution from an FME or its group entity.</td><td>VCF – No maximum holding requirement
Other than VCF – Maximum holding by a single investor to be capped at 50%. The cap of 50% should not be applicable for skin-in-the game contribution from the FME or its group entity.</td></tr>
<tr><td rowspan="2">Filing of Fund/ Scheme documents with IFSCA</td><td>The FME, prior to launching of new schemes, should be required to file the scheme documents with the IFSCA in the prescribed format along with necessary documentation.
Schemes to be launched after receipt of communication or comments from the IFSCA. This would be subject to the FME commencing operations of the Fund or Scheme within 12 months from the date of approval.</td><td>FME may launch scheme after intimating to IFSCA and providing the necessary documentation at least 21 days prior to launching of the Fund or Schemes.
FME must commence the operations of the Fund within six months from the date of filing.</td></tr>
<tr><td colspan="2">Between the date of filing of the scheme documents and the commencement date, in case of any change in the terms of the offering or any material change such as change in the disclosures of the FME, its directors, key managerial persons, etc., the same should be promptly notified to the IFSCA.</td></tr>
<tr><td>Disclosures in the Scheme document</td><td>Regulations should prescribe detailed disclosures for retail funds so that investors are able to make informed decisions.
Principles may be prescribed for disclosures in Scheme documents to put onus on the FME to disclose all material information to the investors.</td><td>Broad criteria and principles of Fund or Scheme in the offer documents or PPM to be specified to ensure FME makes adequate disclosures of material information.</td></tr>
</table>

<table>
<tr><th>Particulars</th><th>Retail Schemes</th><th>Restricted Schemes</th></tr>
<tr><td>Tenure</td><td>Open-ended – No fixed tenure.
Closed-ended – The maximum tenure should be decided upfront*, and disclosed in the offer or placement document, at the time of launch of the Fund or scheme.
*Can be extended with the consent of two-third (by value) majority of investors and approval from the IFSCA.</td><td>Open-ended – No fixed tenure.
Closed-ended – the maximum tenure should be decided upfront*, and disclosed in the offer or placement document, at the time of launch of the Fund or scheme.
*Can be extended with the consent of the two-thirds (by value) majority of investors.</td></tr>
<tr><td rowspan="2">Skin in the game contribution from FME or its group entity</td><td>Lower of 1% of the corpus of the Fund or USD 200,000 to be brought in within six months from launch of the Fund or Scheme and maintained on an ongoing basis.
Such contribution would be separately required for each scheme of the fund.
The contribution from each entity should be capped at 10% of the corpus.
Such contribution should form a part of the net worth calculation.</td><td>Close-ended – lower of 2.5% of the corpus of the Fund or USD 750,000 to be brought in within six months from the launch of the Fund and maintained on an ongoing basis.
Open-ended – lower of 5% of the corpus of the Fund or USD 1,500,000 to be brought in within six months from the launch of the Fund and maintained on an ongoing basis.
Such contribution would be separately required for each scheme of the fund.
The contribution from each entity should be capped at 10% of the corpus.
Such contribution should form a part of the net worth calculation.</td></tr>
<tr><td colspan="2">Internationally, there is no mandatory requirement for such contribution, including in jurisdictions such as Singapore, Ireland, and Mauritius. This is usually a matter of commercial negotiation between the Fund Manager and the investors.

On the other hand, under the domestic regulatory regime, such contribution does have a role to play to have ‘skin in the game’ so that the interests of the Fund Manager and the investors are aligned.

Considering that the IFSC is likely to compete against several leading international financial centres, having a balanced approach is suggested, wherein there is a requirement to have a minimum mandatory contribution that could be waived off subject to fulfilling certain conditions.

For example, contribution from FME or its group entity could be waived if investors contributing more than 50% of the Restricted fund’s capital permit the waiver of such contribution. Additionally, Funds with more than 50% accredited investors shall not be mandated with such mandatory contribution. Furthermore, for fund of fund set up in the IFSC investing in funds in India or overseas that require such contribution, the need for such contribution can be made at any one level at the discretion of the FME.

The contribution should come from FME or its group entities.

IFSCA may review the need for skin in game from time to time and based on market practices, investor, and industry requirements, may also consider not putting any regulatory requirement towards skin in the game.</td></tr>
</table>

Particulars	Retail Schemes	Restricted Schemes
Infrastructure and office space	The Funds/ schemes are not required to have any physical office in the IFSC separately.	

Investment conditions and restrictions

There should be enough flexibility for Fund Managers to invest, especially while raising funds from non-retail investors. Hence, there should be minimal investment conditions or restrictions for such Funds. The basic principle to follow for non-retail funds should be 'invest as disclosed', i.e., the investment conditions should largely be governed by the offer document.

For retail funds, the IFSCA may prescribe 'boundary conditions' to protect the interest of the investors.

Based on the above, the following investment conditions or restrictions is recommended for retail or non-retail funds:

Investment strategy or objective

The Funds should state the investment strategy, investment purpose and its investment methodology in the offer documents to the investors, and any material deviation or alteration to the fund strategy should be made with the consent of at least two-thirds of unit holders by value.

Retail as well as Restricted Schemes should be permitted to invest in all types of securities or financial products (in IFSC, India and outside India), subject to appropriate disclosure in the Offer documents. The intention of the IFSCA should be to permit all types of products, whether in India or overseas, through the IFSC Funds. To illustrate, the Funds should be permitted to invest, among others, in the following:

- Securities listed or traded on recognised stock exchanges in India including IFSC stock exchanges and recognised stock exchanges outside India including:
    - Investments in collective investment vehicles or funds in India, IFSC and overseas jurisdictions
    - Derivatives including commodity derivatives subject to conditions as may be specified by the IFSCA
- Unlisted securities issued by the entities set up in India, IFSC and overseas jurisdictions subject to suitable restrictions. However, there should be no restriction in terms of the amount or percentage of investments that can be made in the overseas jurisdiction from the IFSC AIF.
- Money Market Instruments
- Debt securities
- Securitised debt instruments, which are either asset backed or mortgage-backed securities
- Units of other AIFs set up in the IFSC, subject to conditions and appropriate disclosure in the offer documents;
- Other physical assets such as real estate, bullion, and art, subject to certain limits and under close ended schemes only; and
- Such other securities or instruments or assets (such as commodities and digital currency or token) as prescribed by the IFSCA.

Investment in Indian securities or assets shall be subject to exchange control regulations as prescribed by the RBI from time to time.

Fund or scheme related restrictions and conditions

Particulars	Retail Schemes	Restricted Schemes
Diversification Conditions	• Investment in single investee company should not exceed 10% of the AUM. • In case of Index Funds investment cap in a single investee company to be aligned as per Index weights. • Cap on investment in a single sector – 25% of the AUM of the Fund or scheme. • However, cap on investment in financial services sector – 50% of the AUM of the Fund or scheme	• No diversification conditions should be applicable. • If required, the IFSCA may specify such conditions applicable for non-retail funds from time to time. In case of physical assets, investment limits may be specified by the IFSCA.
Cap on investment in unlisted securities	• Open-ended: Investment in unlisted securities should not exceed 15% of its total investible funds; with no cap on minimum investment • Close-ended: Investment in unlisted securities should not exceed 50% of its total investible funds; subject to minimum investment limit of USD10,000	• VCF: At least 80% of the investible funds should be deployed in companies incorporated for less than seven years. • Open-ended Schemes other than VCF: Investment in unlisted securities should not exceed 25% of its total investible funds. (Akin to current Category III AIFs) • Close-ended Schemes other than VCF: No specific restriction as regards investment in securities so long as appropriate disclosures are provided in the offer document of the funds or schemes.
Investment in entities associated to the FME	• Permissible with a cap of 25% of the AUM of the Scheme.	• Permissible with written consent of at least 75% of the unitholders of the Scheme
Fund of Fund structure	• Investment in other Retail Schemes should be permitted subject to appropriate disclosure in the offer documents.	• Investment in units of other Retail schemes as well as Restricted Schemes should be permitted, subject to applicable investment conditions and appropriate disclosure in the offer documents. • Investment in units of Schemes managed or sponsored by same manager, or associates of the same manager should be permitted only with the written consent of at least 75% of the unitholders of the Scheme or if stated upfront in the offer document.

<table>
<tr><th>Particulars</th><th>Retail Schemes</th><th>Restricted Schemes</th></tr>
<tr><td rowspan="2">Leverage</td><td>Permissible only to meet temporary liquidity requirements for payment of redemption or dividend by the fund or schemes up to a limit as disclosed in the offer document (please note that there would be specific requirements as regards leverage for REITs or InvITs or distressed funds).</td><td>Permissible subject to disclosure* in the offer document.
Comprehensive risk management framework appropriate to the size, complexity, and risk profile of the fund to be in place.</td></tr>
<tr><td colspan="2">*Appropriate disclosure to be provided regarding the overall level of leverage employed, the level of leverage arising from borrowing of cash, the level of leverage arising from position held in derivatives or in any complex product and the main source of leverage, in their fund to the investors and to the IFSCA periodically.</td></tr>
<tr><td rowspan="2">Net Asset Value (NAV) calculation, Disclosure</td><td>Open-ended – daily
Close-ended – weekly</td><td>VCFs – annually
Open-ended Schemes other than VCFs – monthly
Close-ended Schemes other than VCFs – half yearly</td></tr>
<tr><td colspan="2">• The NAV of each scheme to be computed by dividing the net assets of the scheme by the number of units outstanding on the valuation date.
• The procedure and methodology for calculating the NAV should be fully documented, and such documentation should be regularly verified and amended.</td></tr>
<tr><td rowspan="2">Valuation of the Scheme Portfolio</td><td>• Scheme portfolio to be independently valued by a third-party service provider such as a fund administrator or a custodian or such other person as specified by the IFSCA to perform such valuation.</td><td>• Open-ended:
Same as Retail Schemes
• Close-ended:
Scheme portfolio may be valued by an in-house fund valuation team that is independent from the fund management function or a third-party service provider, such as a fund administrator or custodian or such other person as specified by the IFSCA.</td></tr>
<tr><td colspan="2">The IFSCA may prescribe certain valuation principles or norms to ensure that the valuation of the Fund portfolio is reflective of the realisable value of assets.</td></tr>
</table>

Other general investment conditions or restrictions for all categories of Schemes

- In case the FME is making co-investment along with the fund or scheme, the terms offered to the FME should not be more favourable than those offered to the fund or scheme.

- Schemes should be permitted to raise monies from investors whether residents of India or a foreign country by way of issue of units. However, investment from Indian resident person would be subject to exchange control regulations as prescribed by the RBI from time to time.

- Restricted Schemes should not be permitted to solicit funds except by way of private placement by issue of information memorandum or placement memorandum, by whatever name called. However, to provide greater flexibility, the IFSCA should not prescribe any specific format for the information or placement memorandum. IFSCA may, however, require disclosure of specified information in the information or placement memorandum.

- All the investment conditions or restrictions applicable shall be adhered to at each scheme level.

Fees and expenses

Fees and expenses may vary depending upon the Scheme's investment strategy. The FME shall ensure appropriate disclosure in the offer document of the maximum fees and expenses that it may charge. Each expense such as set up or establishment expenses, operating expenses or management fees shall be disclosed separately as a specific line item in the offer document. This shall facilitate the investors contemplating to invest in a fund to have access to comparable information about competing funds.

Listing of Funds/ Scheme

Listing of open-ended funds/ scheme (retail and non-retail)

Units of open-ended funds/ schemes may be listed on the IFSC exchanges.

Listing of close-ended funds/ scheme (retail and non-retail)

Units of close-ended retail funds/ schemes are mandatorily required to be listed on the IFSC exchange. Units of non-retail funds/ schemes may, at the discretion of the FME, be listed on the IFSC exchange. Listing of close-ended funds/ schemes should be only after the completion of the final closing of the funds/ scheme.

Delisting of close-ended funds/ scheme

Delisting of the units of the funds/ scheme should be permissible. IFSCA may levy conditions to be satisfied prior to delisting, as it may deem appropriate.

Other provisions

Prior to listing of the funds/ schemes, the funds/ schemes should be required to make appropriate filings, including the offer document, with the IFSCA and the relevant stock exchange. The funds or schemes should be permitted to list only after receiving approval from the IFSCA and the relevant stock exchange.

Merger/ demerger/ restructuring of Funds or schemes

Merger/ demerger/ restructuring of Funds or schemes should be permissible, subject to the guidelines to be issued by the IFSCA.

Winding up of the Fund

The Fund managed by the FME may be wound up either voluntarily (i.e., if all the schemes within the Fund managed by the FME are wound up) or as per the direction of the IFSCA, if the IFSCA believes that it would be in the interest of the investors. Furthermore, a Fund can also be wound up:

i. When the tenure of the Fund or scheme as mentioned in the placement memorandum is over;

ii. If it is the opinion of the trustees or the trustee company that the Fund be wound up in the interests of investors in the units;

iii. If 75% of the investors, by value of their investment in the Fund, pass a resolution at a meeting of unitholders that the Fund be wound up.

8.3. Other activities of FME

8.3.1. PMS

A Registered FME shall be able to offer PMS to clients. Apart from satisfying the eligibility criteria applicable for FME as mentioned above, an FME providing portfolio management services to its clients would be required to satisfy the following conditions:

i. A portfolio manager can invest in securities or assets and financial products in an IFSC, India or Overseas Jurisdictions. However, a discretionary portfolio manager should be permitted to invest only in securities or assets listed or traded on the stock exchanges, money market instruments, units of mutual funds and other financial products as specified by the IFSCA. Portfolio Manager may be permitted to invest in unlisted securities if the client is an Accredited Investor investing more than USD 2 Million.

ii. A portfolio manager can provide investment advisory (along with portfolio management) services or standalone investment advisory services to the clients subject to appropriate disclosures in the fund / scheme document and the terms agreed between the client and the portfolio manager.

iii. A portfolio manager (including the portfolio manager providing investment advisory services) should not accept from the client, funds, or securities worth less than USD 70,000. No such restriction should apply in case the clients are accredited investors.

iv. A portfolio manager should provide a disclosure document (containing requisite particulars such as services offered and risk factors), prior to entering into an agreement with the client. The portfolio manager should ensure that a copy of disclosure document is available on its website.

v. A portfolio manager should be required to enter into a written agreement with the client that clearly defines the inter se relationship and sets out their mutual rights, liabilities and obligations relating to the management of portfolio including details pertaining to investment objectives, risk factors, terms of fees, period of the contract, etc.

vi. The portfolio manager shall charge an agreed fee from the clients for rendering portfolio management services without guaranteeing or assuring, either directly or indirectly, that any return and the fee so charged may be a fixed fee or a return-based fee or a combination of both.

vii. A portfolio manager should keep the funds of all clients in a separate account to be maintained by it in a Banking Unit.

viii. A portfolio manager should segregate each client’s holding in securities or assets in separate accounts.

ix. A portfolio manager shall periodically furnish a report to the client in terms of the agreement between the portfolio manager and the client, which shall, inter alia, contain details relating to composition and value of the portfolio, transactions undertaken during the period of the report, beneficial interest received during the period of the report, expenses incurred in managing the portfolio and details of risk relating to the securities or assets recommended by the portfolio manager for investment or disinvestment

x. A portfolio manager (except those providing only advisory services) should appoint a custodian in respect of the securities or assets managed or administered by it.

xi. The portfolio accounts of a portfolio manager should be audited annually, and a copy of the certificate should be given to the client.

xii. The portfolio manager should not leverage the portfolio of its clients for investment in derivatives unless express consent has been obtained from its clients. A portfolio manager should not borrow funds or securities on behalf of the client.

Other conditions as applicable to a Portfolio Manager as specified in IFSCA (Capital Market Intermediaries) Regulations, 2021 shall also be made applicable.

Investment Advisory by a Registered FME

A Registered FME may provide stand-alone investment advisory services, including investment advisory services to offshore funds, subject to ensuring the interest of investors in IFSC are adequately protected. This may be subjected to such other conditions/ relaxations such as no requirement to appoint a custodian, no requirement to maintain a separate account with a banking unit in IFSC, etc. as may be prescribed.

Other conditions as applicable to an Investment Adviser as specified in IFSCA (Capital Market Intermediaries) Regulations, 2021 shall also be made applicable.

8.3.2. REITs/ InvITs

Globally, REITs and InvITs are regarded as a separate asset class. Given the different nature or structure of investments and different requirements, a special framework for REITs and InvITs merit consideration. While the overarching framework applicable for FMEs managing restricted and retail funds or schemes can continue to be the same, some aspects of the framework could be customised for REITs and InvITs.

IFSCA has issued Circulars[6] specifying therein the framework for REITs and InvITs. We suggest subsuming the framework in the proposed fund regime. Having said so, it is advisable to have a unified chapter for both the Investment trusts i.e., REITs and InvITs as there are a lot of similarities in the activities. The differences on account of asset class restrictions, minimum ticket size, leverage, etc. could be detailed separately.

Also, as per the current framework applicable for REITs in IFSC, only public issue of units of REITs is permissible. We suggest permitting issue of units of REITs on a private placement basis as well. The Registered FME may act as Investment Manager to such Investment Trusts.

8.3.3. Family office

India is witnessing a significant rise in the wealth of HNIs and UHNIs. Further, as per the twelfth edition of the Global Wealth Report, published by the Credit Suisse Research Institute[7] in June 2021, the number of dollar millionaires in India is expected to increase by 80% from 698,000 to 1.26 million in the next five years.

As per an estimate by Fortune India[8], family offices in India have invested over USD 5 billion in the last five to six years, in listed/ unlisted companies as well as in startups, in the country as well as abroad.

While the increase in wealth of individuals acts as a catalyst for growth of family offices, the recent reforms introduced by the Indian government such as Digital India, Make in India, introduction of various profit linked incentive schemes, etc. provide opportunities to innovate and increase the economic output which could lead to a virtuous cycle of generating higher income and creating more wealth.

The growth in family offices in India has been accentuated by the rise in start-ups and first-generation entrepreneurs and has been proliferated by the growth in financial services and the alternative investments' landscape.

Consequently, there is an increasing need for having a formal structure for managing and preserving the wealth of the HNIs and UHNIs and their families. This has paved a need for conceptualisation of a regime for family offices in India.

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[6] F. No. 41/IFSCA/SEBI/REITs-InvITs/2020-21 dated 21 October 2020
[7] https://www.credit-suisse.com/about-us/en/reports-research/global-wealth-report.html
[8] https://www.fortuneindia.com/enterprise/family-offices-thrive-in-tech-savvy-startup-world/105590

Further, in a globalised world, many families, especially first-generation promoters and entrepreneurs of start-ups and families whose children have immigrated abroad, evaluate, and invest in opportunities across the world.

The Government has conceptualised IFSC as a regime to bring onshore, financial services/ activities that are currently carried on outside India by overseas financial institutions. IFSC could emerge as a perfect solution to facilitate growth of Indian family offices which are looking at diversifying abroad and to encourage domiciling of family offices promoted by Indians or persons of Indian origin residing abroad.

The IFSC should, therefore, aspire to be a hub for Indian family offices who are desirous of having exposure to global assets. These family offices would have otherwise set-up a presence in say, Singapore or Dubai to get such global exposure. The IFSC should aspire to be their 'first-port-of-call'.

Similarly, the IFSC should aspire to become a preferred destination for Indian families settled outside India or non-Indian families, wanting an exposure to emerging markets or intending to invest in EMEA and Asia Pacific, who would consider establishing their family office set-up in IFSC.

This will obviously foster the development of IFSC. The Asset Under Management will increase leading to overall growth and development in IFSC. The increase in family offices in IFSC will also create employment opportunities for professionals, portfolio managers, other service providers, etc.

Introduction of a separate regulatory regime, which is "tailor-made" for family offices in IFSC may attract HNIs and UHNIs of the world to set-up their family offices in IFSC and also aid the onshoring of offshore Fund Managers.

Proposed regulatory Framework for Family Office

To provide an enabling regime for setting up of family offices in IFSC, the following regulatory framework could be considered.

Types and Structures

Family offices to be classified in two broad segments:

- SFO – which are more "in-house" and manage the assets and wealth of a single-family group; and
- MFO – which are akin to "third party" fund managers and manage the assets and wealth of more than one family group.

SFO's typically manage the wealth of a private family with no public money, or any third-party funds being solicited. Following a "risk based" approach, in light of lower risk/ exposure to "public money", SFOs are generally not regulated or, alternatively, governed with a very light touch regulatory regime, which is neither compliance-heavy nor burdensome.

On the other hand, MFOs raise/ manage funds of multiple families. Accordingly, these may be governed by a different set of regulations which could be, comparatively, more comprehensive, and akin to the set of regulations which apply to advising or managing "third party monies".

Authorisation/ Registration requirement

The family offices need to have regulatory oversight by the IFSCA. SFO should be "authorised" by the IFSCA in the form of a "self-managed" Fund Management Entity (hereinafter referred to as Family Investment Fund, which should include any SPVs set-up by the Fund). MFOs may be governed by a more comprehensive set of regulations as compared to SFOs and can be considered under portfolio management.

Scope/ Coverage

The regulations governing family offices in various jurisdictions have generally defined the term 'Single Family' to mean a group of individuals who are the lineal descendants of a common ancestor and includes their spouses (including widows and widowers, whether remarried or not) and children (including stepchildren, adopted children, ex nuptial children). These regulations generally consider a common ancestor no more than three generations away from the youngest generation of the family member. Certain regulations also provide an exhaustive list of connected persons/ family members who shall constitute a single-family office. The IFSCA could consider adopting a wide definition of the term 'family' to include lineal descendants from a common ancestor along with their spouses and children referred above without any restriction on the number of generations as such.

Applicability

The regulations should apply to all Family Investment Funds, being SFOs, set-up in IFSC engaged in one or more permissible activities. The regulations should prescribe a list of permissible activities, which could be undertaken by a Family Investment Fund. The permissible activities under the regulations could include:

- management and administration of investments, assets and/ or estate(s);
- advising and educating on various investment avenues;
- advising on wealth planning and preservation;
- management of accounting and reporting;
- administration and management of philanthropic services;
- administration and management of disaster recovery planning;
- administration of risk management;
- provision of administrative support;
- ensuring compliance with domestic and international legislations;
- establishing family governance, succession planning, wealth strategies, family board(s) including family charter(s); and
- any other activities as may be approved by the IFSCA.

Eligibility Conditions

Some of the eligibility conditions in this regard could include -

a. The Family Investment Fund must pool funds from a single family only and no monies from any third party should be solicited by or pooled in a Family Investment Fund.

   Further, a Family Investment Fund should be permitted to raise debt or loans. The raising of any debt or loan by a Family Investment Fund should however require approval of all the family members.

b. The Family Investment Fund could be set up in the IFSC as a Company, Trust (Contributory Trust only) or Limited Liability Partnership or any other form as may be permitted by the authority from time to time. It should be set-up as a contributory vehicle and where, the Fund is in the form of a Trust, a contributory Trust i.e.

- A Trust where the beneficiaries are identifiable based on the provisions of the Trust deed, though not specifically named in the trust deed.

- The share of each beneficiary should be capable of being determined based on the provision/ formula prescribed in the trust deed and should not be at the discretion of the Trustee.

- If the Trust deed authorises addition of further contributors to the Trust at different points in time in addition to the initial contributors, the same would not make the beneficiaries unknown or their shares indeterminate.

The above suggestion has been motivated for better alignment of tax treatment of the Fund, as explained in subsequent paras.

c. To institutionalise the set-up, the Family Investment Fund should have at least one investment professional with prescribed qualifications[9] and with minimum experience of at least five years in the field of securities market or dealing in financial products such as a portfolio manager, broker dealer, investment adviser, research analyst or fund management.

d. An entity registering as a Family Investment Fund should have and maintain a minimum net worth of USD 10 million.

e. The Fund Investment Fund could be open-ended or close-ended, depending upon the requirements of the family.

Ownership and Control

The Family Investment Fund should be owned and controlled by family members and other persons as appointed by the family.

Eligible Investments

This is a very important aspect. Given the “low risk/ exposure to “public money”” nature of SFOs, the regulatory regime should not stifle or restrict investments and allow them full flexibility. Illustratively, the Family Investment Fund should be eligible to invest across all asset classes and securities including unlisted shares, real estate/ property, debt securities (including money market instruments/ securitized debt instruments)/ loans, commodity derivatives, bullion, art, tokens etc. If required, IFSCA may consider amending the definition/ coverage of “financial products” considering the wide spectrum of asset classes available for investments to a Family Investment Fund.

Similarly, there should not be any diversification or concentration norms so long as investments are in accordance with the investment policy of the Fund.

<u>Family Investment Funds from residents outside India</u>

Family Investment Funds whose majority of the members are resident outside India should:

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[9] Professional Qualification (such as Chartered Accountant, Chartered Financial Analyst, Company Secretary or equivalent) or post-graduate degree or post graduate diploma in finance, accountancy, business management, commerce, economics, capital markets, banking, law, insurance, or actuarial science from a recognized institution or any other qualification as may be specified by the IFSCA.

- be permitted to invest in India under the FPI, FVCI and FDI route in accordance with the applicable regulations;
- be permitted to invest abroad in accordance with local laws of the jurisdiction in which the investment is being made.

To encourage setting-up of family offices in IFSC by Non-Resident Indians living abroad, appropriate relaxations of FPI norms for NRI/ OCI investments could be considered. To address any concerns in dilution of FPI norms, suitable safeguards or mitigants in the form of disclosure of beneficial ownership, etc., which are not burdensome, could be prescribed.

Family Investment Funds from residents in India

Family Investment Funds whose members are resident in India should:

- be permitted to invest abroad;
- be restricted to invest in India

Reporting and Compliance Requirements

There may be general reporting requirements prescribed for the Family Investment Funds in IFSC to ensure compliance and enable the IFSC to have an oversight of the family offices established in IFSC. This could be by way of an annual compliance report along with a copy of audited financial statements. The compliance report could include details such as summary of total assets under management along with any changes to the family structure, any information requirements from say, AML perspective, etc.

8.4. General obligations and responsibilities of the FME

Code of Conduct

FMEs and key management personnel of FMEs should abide by the Code of Conduct while managing the Fund or while providing portfolio manager services to the clients. They should maintain the highest level of integrity, ethical and professional standards and ensure that an effective risk management process and appropriate internal controls are in place.

The responsibility to abide by the Act, rules, regulations, guidelines, and circulars issued by the IFSCA would rest with the FME. FME will also be responsible for ensuring that all the decisions of the Funds are in compliance with the law, terms of the placement memorandum, agreements made with investors or clients and other fund documents.

Appointment of Investment Committee

FME may, at its discretion, constitute an Investment Committee to make investment decisions for the Fund or schemes. In case an investment committee is appointed, their responsibilities would be similar to those of the FME.

Appointment of Trustee

In case the Fund is set up as trust, the FME shall be required to appoint a trustee who shall hold the assets of the scheme for the benefit of the investors. The Trustee should be authorised by the IFSCA to act as a trustee.

All individual trustees in the trustee company should be independent from the FME. Furthermore, in case a group company of the FME is acting as trustee for the Funds managed by such FME, then the same should be regarded as independent.

Appointment of Fund Administrator

All FMEs are required to appoint a Fund Administrator to ensure adequate segregation of duties, particularly in the performance of functions such as valuation or fund accounting, acting as a fund register and client reporting. (e.g., sending of monthly account statements).

Appointment of Custodian of securities

A Registered FME is required to appoint a custodian in the investment jurisdiction to ensure that assets under management are subject to independent custody.

Appointment of Compliance Officer

A Registered FME shall designate a compliance officer who shall be responsible for monitoring the compliance of the Act, rules and regulations, notifications, guidelines, instructions etc., issued by the IFSCA or the Central Government and for redressal of investors' grievances.

Appointment of an Auditor to audit scheme accounts

All FMEs shall ensure that the books of accounts or records of the Fund or schemes are appropriately maintained and are in compliance with the requirements specified by the IFSCA. These books of accounts are required to be audited by an independent auditor.

Change in control in FME

FMEs should obtain prior approval of IFSCA in case of any change in control of the FME. ‘Control’ (including, with correlative meaning, the terms ‘controlled by’ and ‘under common control with’) of a Person means (a) ownership of more than 51% (Fifty-one per cent) of the equity shares, voting rights or other ownership interests of such Person, whether directly or indirectly; or (b) the power to appoint more than half of the members of the board of directors, whether directly or indirectly. In case of internal reorganisation, there should be no approval required from the IFSCA, and merely an intimation to the IFSCA should be sufficient.

Conflict of interest

FME to establish and implement written policies and procedures to identify, monitor and appropriately mitigate conflicts of interest throughout the scope of business.

Other aspects

- FME is required to ensure the segregation of assets and liabilities of each of its schemes and clients.
- FME to maintain adequate books of accounts for its activities as well as for all the funds that it manages.
- A Registered FME should ensure that funds under management are subject to independent valuation.
- FME should ensure that there is adequate disclosure to its investors or clients in respect of the respective fund or scheme or account.
- FME shall maintain the requisite net worth and furnish a net worth certificate to the IFSCA issued by a practicing-chartered accountant, as and when required by the IFSCA.

Disclosures and filings with the IFSCA

FMEs would be required to periodically furnish details regarding the quantum of AUM managed, net worth certificate, annual compliance report, annual (audited) report (within six months from the end of the relevant financial year) or such other reports as may be required by the IFSCA. FME would be required to file returns with the IFSCA on a quarterly (unaudited) basis providing details as may be required by the IFSCA, within 14 days from the end of the quarter.

IFSCA may also call upon the FME to submit such reports as the IFSCA may desire with respect to the activities of the FME of the Fund. It may also call upon the FME to provide a list of the clients whose portfolios are managed by them.

Scheme Annual Report

The FMEs are required to file a scheme-wise annual report with the IFSCA on a yearly basis. While Authorised FME and Registered FME with accredited or institutional investors may submit an abridged summary of the scheme-wise annual report Registered FME with retail investors are required to submit a detailed annual report to the IFSCA. The same should also be sent to the investors via email or any other mechanism.

9. Focus Areas

9.1. Exchange Traded Funds

Introduction to ETFs

ETFs as the name implies is baskets of securities that are traded on an exchange. Unlike regular open-end mutual funds, ETFs can be bought and sold throughout the trading day like any stock.

As per one of the global research providers, the Global Exchange Traded Funds/ Exchange Traded Products' (ETP) industry had 9,700 products, with 19,606 listings, assets of USD 9.92 trillion, from 596 providers listed on 79 exchanges in 62 countries at the end of November 2021. The most liquid stock on the NYSE is an ETF based on the US S&P500 Index called "SPY" and it trades approximately $20billion a day vs the most liquid stock Bank of America which trades approximately $4 billion a day.

In India, ETFs assets under management is just over USD 51 billion with 116 ETFs listed on the stock exchanges. ETFs have been in existence in India for over 15 years. The first ETF, Nifty BeES was launched in December 2001. Currently, ETF's AUM is less than 3% of the total assets of the Indian Mutual Fund industry but it has the potential to grow significantly. Today, the largest mutual fund scheme in India is the SBI Nifty ETF. Further, the Government of India has used the ETF route for disinvestment through the CPSE ETF and recently Bharat 22. Therefore, ETFs have come a long way in India with Institutional participation.

The mutual fund schemes in India investing in international market through fund of funds has assets under management at around USD 3.2 billion as of November 2021, a 3.5 times growth as compared to USD 0.9 billion as of October 2020 indicating a high demand for international assets amongst Indian investors.

This Chapter emphasises why ETFs need to be introduced at IFSC and some of the facilitations that would be required such as providing regulatory framework for asset management companies and framework/ operating guidelines for ETFs.

Why ETFs are critical for IFSC?

World Federation of Exchanges in its report[10] titled "Enhancing Liquidity in Emerging Market Exchanges" has inferred that "Increasing the pool of securities and associated financial products by increasing the number of local or foreign listings, launching derivative and ETF products, or creating market linkages" is one of the core areas which exchanges, and regulators should focus on to grow liquidity. The same has been highlighted by sighting few case studies such as The Stock Exchange of Thailand where availability of investment products such as ETFs and derivatives are noted as the key drivers for developing the exchange.

Globally, ETFs as an instrument account for a sizeable portion of the equity segment. The volumes are more prominent in America where ETF volumes account for 30%~40% of the equity volumes, in Europe - Africa - Middle East ETFs account for 6%~9% and Asia sees 4%~6%.

Availability of ETFs will lead to development of asset managers as well as investor community at the IFSC, thereby creating an attractive proposition for fund raising for asset managers and corporates in the long run.

Rationale for Global ETFs succeeding at IFSC

IFSC offers trading and settlement in US Dollars eliminating the currency risk in general as compared to global ETFs being offered on any local exchange.

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[10] https://www.world-exchanges.org/storage/app/media/research/Studies_Reports/liquidity-in-emerging-market-exchanges-wfe-amp-ow-report.pdf

- **Investor's perspective –**

    - **Unified Stable Regime –** A uniform regime regulating the FME and permitting the FME to launch various types of ETFs would ensure ease of launch, builds investor confidence, and provide opportunity to participate in $ denominated Global ETFs.

    - **Investment opportunities -** ETFs offer a means to gain exposure to specific markets or asset classes that otherwise could be difficult or impossible to attain. Investor demand for index-linked investments has been strong for the past several years.

    - **Higher returns due to lower taxes in hands of investors** – An ETF bought by investor at an exchange in IFSC, will be able to generate relatively better returns due to tax exemptions at the transaction level (no STT, GST on brokerage/ Exchange fees), tighter bids by market maker and exemption on other taxes such as capital gains and dividend tax there by increasing the yields for the investor as compared to any other jurisdictions/ venues.

    - **Lower expense ratio of IFSC domiciled ETFs –** A ETF in IFSC by an asset manager domiciled in IFSC, will be able to charge lower expense ratios on account of tax advantages enjoyed by the Asset manager as well the authorised person/ market maker.

- **Asset manager's perspective –** A FME with single registration shall be able to launch ETFs and attract capital from a variety of investors. A FME domiciled in IFSC is likely to be more efficient in terms of returns on investors from the trustee's/ sponsors perspective as compared to other jurisdictions due to tax advantages such as income tax holiday.

The above key drivers will attract asset managers as well as foreign investors to IFSC.

Framework for issuance and trading of ETFs

IFSCA may consider prescribing a principle-based operating framework, to facilitate the issuance, listing (including dual listing) and trading of ETFs. ETFs may be launched by Registered FME with retail investors only.

The principle-based framework may be based upon the IOSCO principles for regulation of ETFs[11]. The principles are provided in the **Annexure B**.

- **ETFs as permissible securities at IFSC**

    SEBI circular SEBI/ HO/ MRD/ DSA/ CIR/ P/ 2016/ 125 dated November 28, 2016 for IFSC, permits all categories of exchange-traded products as available for trading in stock exchanges in FATF/ IOSCO compliant jurisdictions shall be eligible for trading, subject to prior approval of SEBI.

    As per WFE statistics ETFs are available on 56 member exchanges including domestic exchange in India. Some of the top global exchanges based on turnover include Nasdaq, CBOE, Shanghai Stock Exchange, Korea Exchange, and Japan Exchange. As these exchanges are FATF compliant jurisdictions, ETFs can be made available on exchanges at the IFSC, and no separate circular/ notification is required by the IFSCA.

    IFSCA may issue a framework/operating guideline to facilitate other provisions for issuers, issuance, listing (including dual listing), trading and clearing & settlement.

- **Types of ETFs**

    The ETF can be an open-ended ETF where new units can be created on need basis and trading in secondary market or a closed ended ETF with limited number of units and trading in secondary market.

    The following broad categories of ETFs may be permitted

[11] https://www.iosco.org/library/pubdocs/pdf/IOSCOPD414.pdf

- **Equity Index oriented ETFs**
  - The selected benchmark index should have the underlying securities or the securities related instruments from a FATF/ IOSCO compliant jurisdiction.
  - FME may appropriately select any of the equity-oriented indices available as a benchmark index published by a reputed index provider or a publishing agency depending on the investment objective and portfolio.
  - FME may choose to invest in the underlying securities or securities related instruments such as the depository receipts, ETFs, derivative instruments, etc.
  - The related instruments will be required to be specified by FME with prior permission of its board and subject to approval from Exchanges and/ or IFSCA.
  - Accordingly, any ETF/ Index Fund that seeks to replicate a particular Index shall ensure that such index complies with the aforesaid norms.
  - Further, an Equity based Index ETF that seeks to replicate a particular Index shall ensure that such index complies with the following norms:
    - Equity based Index ETF shall replicate the underlying Index to the extent of at least 90% of total assets.
    - The index shall have a minimum of 10 stocks as its constituents.
    - For a sectoral/ thematic Index, no single stock shall have more than 35% weight in the index. For other than sectoral/ thematic indices, no single stock shall have more than 25% weight in the index.
- **Debt Index oriented ETFs**
  - The selected benchmark index should have the underlying securities or the securities related instruments from a FATF/ IOSCO compliant jurisdiction.
  - Asset management companies may appropriately select any of the debt-oriented indices available as a benchmark index published by a reputed index provider or a publishing agency depending on the investment objective and portfolio
    - The rating of the constituents of the index shall be of investment grade
    - The selected benchmark should have a minimum of 5 issuers or 1 issuer in case of Sovereign rating
    - No single issuer shall have more than 25% weight in the index.
  - Accordingly, any ETF that seeks to replicate a particular Index shall ensure that such index complies with the aforesaid norms.
  - The ETF should be able to always replicate at least 90% of the index
  - In the event, if ETF is not able to replicate the index due to non-availability of issuances of the issuer forming part of the index, the ETFs shall specify the deviations in an order that would be executed to seek the least tracking error possible.
- **Commodity oriented ETFs**
  - A commodity ETF shall invest primarily in the specified commodity/ commodities. Additionally, investment in the specified commodity related instruments will also be permitted.

- The related instruments will be required to be specified by asset manager with prior permission of its board and subject to approval from Exchanges and/ or IFSCA.

- **Gold ETF**

  - In case of a Gold ETF, at least 90% of the AUM should be invested in Gold or bullion instruments such as Bullion Depository Receipts and Exchange Traded Commodity Derivatives with gold as the underlying.

  - Provided that the exposure to ETCDs having gold as the underlying shall not exceed 10% of AUM of the scheme. However, the above limit of 10% shall not be applicable to Gold ETFs where the intention is to take delivery of the physical Gold and not to rollover its position to next contract cycle.

  - Gold ETFs shall be benchmarked against the price of Gold at the International Bullion Exchange and Registered FME with retail investors should endevour to have tracking error as low as possible.

  - Physical verification of gold underlying the Gold ETF units shall be carried out by an independent agency capable of undertaking such activities and reported to the Board of FME on half yearly basis

- **Silver ETF**

  - In case of a Silver ETF, at least 90% of the AUM should be invested in Silver or bullion instruments such as Bullion Depository Receipts and Exchange Traded Commodity Derivatives with silver as the underlying.

  - Provided that the exposure to ETCDs having silver as the underlying shall not exceed 10% of AUM of the scheme. However, the limit of 10% shall not be applicable to Silver ETFs where the intention is to take delivery of the physical silver and not to rollover its position to next contract cycle.

  - Silver ETFs shall be benchmarked against the price of Silver at the International Bullion Exchange and Registered FME with retail investors should endevour to have tracking error as low as possible.

  - Physical verification of silver underlying the Silver ETF units shall be carried out by an independent agency capable of undertaking such activities and reported to the Board of FME on half yearly basis.

  - For participation in commodity-based ETF, FME shall ensure a KMP with 5 years of experience in dealing with commodities is designated as a Fund Manager.

- **Currency oriented ETFs**

  - A currency ETF shall invest primarily in the specified currencies. Additionally, investment in the specified currency related instruments will also be permitted.

  - The related instruments will be required to be specified by asset manager with prior permission of its board and subject to approval from Exchanges and/ or IFSCA.

- **Asset allocation/Combination of asset class/ balanced ETFs**

  - The selected benchmark index should have the underlying securities or the securities related instruments from a FATF/ IOSCO compliant jurisdiction.

  - Asset management companies may appropriately select any of the indices available as a benchmark index published by a reputed index provider or a publishing agency depending on the investment objective and portfolio.

  - Additionally, investment in the specified related instruments will also be permitted.

  - The related instruments will be required to be specified by asset manager with prior permission of its board and subject to approval from Exchanges and/ or IFSCA.

- **Other ETFs**

  Any other ETF which does not form part of the 2.1 to 2.5 shall be with prior permission of its board and subject to approval from Exchanges and/ or IFSCA.

- **Issuance of ETFs**

  - Asset managers may decide to initially offer the ETF as part of new fund offer (NFO) at IFSC
  - Exchanges may offer a facility to asset managers for order collection mechanism during the NFO period.
  - Eligible investors – All investors permitted by IFSCA to transact on Exchanges based in IFSC from time to time.

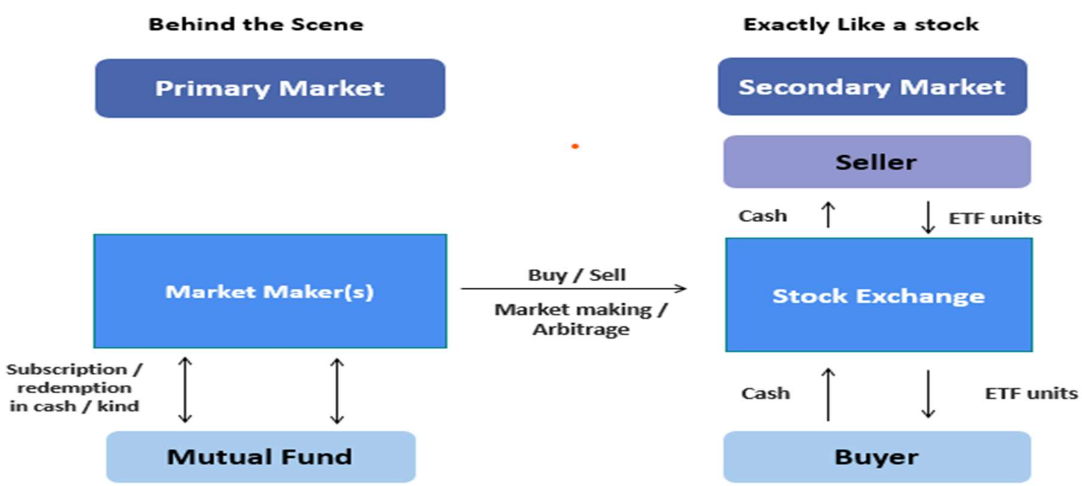
- **Listing of ETFs on stock exchange**

  - FMEs may seek approval from IFSCA for listing of its ETF at an IFSC exchange.
  - Listing may be done initially through a new fund offer (NFO) at IFSC or directly list the ETF on an exchange at IFSC. This may also include the dual listing of an existing ETF which is listed on other global exchanges on the IFSC exchanges12.

- **Trading of ETFs in secondary market**

  A broad process of trading an ETF in secondary market at IFSC is given below

Working Mechanism of ETFs in India



  Trading on the stock exchange will be on an anonymous order matching platform.

- **Net Asset Value (NAV)**

  - Asset manager shall disclose the NAV of the ETF scheme at periodic interval depending on the type of scheme.

[12] The framework for such dual listing could follow the norms similar to secondary listing as referred to in the IFSCA listing regulations. Operational details could be separately included after seeking inputs from relevant stakeholders.

- The NAV of the Units of the Scheme will be computed by dividing the net assets of the Scheme by the number of Units outstanding on the valuation date.

- It is advised to publish the NAV on daily basis. In case the same is not possible due to issues in arriving at the valuations then the NAV must be published periodically as specified by IFSCA from time to time. The same may be published on the asset managers website as well as sent to the exchanges where it can be published.

- To ensure uniformity, NAV shall be rounded up to four decimal places for all ETFs.

- Computation of NAV will be as per the methodology specified by IFSCA including method followed for valuation.

- **Redemption of ETFs**

  Investors other than market makers can directly approach the Fund for redemption of units, and no exit load will be charged if

  a) Traded price of the ETF units is at discount of more than 5% of NAV for continuous 30 trading days, or

  b) Discount of bid price to NAV over a period of 15 consecutive trading days is greater than 5%, or

  c) No quotes are available on exchange for 5 consecutive trading days, or

  d) Total bid size on the exchange is less than higher of 1% of the total units valued at NAV in ETF or USD 2,500 in value, averaged over a period of 7 consecutive trading days. In case, NAV is not published on daily basis then the last available NAV will be considered till availability of new NAV.

  In such a scenario existing ETF unitholder shall be eligible to avail the redemption request directly from the Fund on the basis the closing NAV of the day. In case, NAV is not published on daily basis then the last available NAV will be considered till availability of new NAV.

Market Makers

FME shall appoint a market maker who shall be responsible for liquidity in the trading of ETF. Market makers shall be responsible for providing two-way quotes.

Recognised Stock Exchanges in IFSC may provide a simplified framework for registration of IFSCA registered entities as market makers. Existing Broker Dealers or IBUs in IFSC may act as market makers.

Recognised Stock Exchanges shall also provide detailed rules for market makers viz. maximum spread, minimum quantity, etc. Stock Exchanges may also provide certain benefits to the market makers. For the market maker, certain exemptions as mentioned in **Annexure C** may be considered for building a liquid ETF market in IFSC.

Disclosures

An IFSC ETF should disclose clearly in its prospectus and all marketing communications the policy regarding portfolio transparency and where information on the portfolio may be obtained, including where the indicative net asset value, if applicable, is published.

An IFSC ETF should also disclose clearly in its prospectus how the indicative net asset value is calculated, if applicable, and the frequency of calculation.

9.2. ESG

There has been a growing recognition of the significant economic and financial impact of climate change and ESG risks. The recently concluded United Nations Climate Change Conference of Parties (COP26) held in Glasgow paved the way for participating nations agreeing to achieve the ambitious target to contain global warming to 1.5 degrees. This has led to participating nations accepting targets for achieving net-zero over a period. India has agreed to achieve a net-zero target by 2070.

The Principles of Responsible Investing define responsible investing as a strategy and practice to incorporate ESG factors in investment decisions and active ownership. Taking care of E, S and G factors, and the adoption of these responsible investment principles is becoming a ‘way of doing business’. The narrative from an investor’s perspective is shifting towards ‘how’ the profits are being earned over the traditional approach of ‘how much’ profits are generated. In today’s context, it is imperative to build a business that is resilient and sustainable with a positive impact towards the environment and society at large. To achieve this, the investor community is uniquely positioned, considering their strengths, market position and capabilities to generate positive returns for society in specific areas, as it generates returns for investors.

Another important aspect where the investor community can play a role is ‘impact investing’. It is an investment strategy that seeks to generate financial returns while also creating a positive and measurable social or environmental impact. Such investing strategy also positively contributes to achieving the aspirational goals set by the United Nations in the form of Sustainable Development Goals.

ESG - focused investing and sustainability-related products entail a number of challenges. The most important challenge is the need for consistent, comparable, and decision-useful information and the risk of greenwashing. Regulators and policymakers worldwide have been examining issues relating to sustainable finance in their regulatory and supervisory roles to address these challenges. This includes how asset managers take sustainability-related risks and opportunities into consideration. Internationally, industry participants, investors, regulators, and policy makers are working to address sustainability-related risks, opportunities and impacts and to help improve sustainability-related disclosures.

Along with that, there has been increased interest and focus on investments in the ESG space globally. AMCs in India have also been launching equity schemes in the ESG space under the thematic category. The AMCs are also launching ETFs and ETF Fund of Funds in India in the ESG space.

In this regard, International Organization of Securities Commissions (IOSCO) had published a final report on ‘Recommendations on Sustainability-Related Practices, Policies, Procedures and Disclosure in Asset Management’ in November 2021. The recommendations relate to the improvement of practices, policies, procedures, and disclosures by encouraging asset managers to take sustainability-related risks and opportunities into account in their investment decision-making and risk management processes. Securities and Exchange Board of India (SEBI) has also launched a consultation paper on introducing disclosure norms for ESG Mutual Fund schemes.

IOSCO reports have provided recommendations on the following matters:

i. Asset manager practices, policies, procedures, and disclosure (entity-level disclosure)

   In respect to sustainability-related requirements relating to practices and disclosures by asset managers at the entity level, the requirements can be broadly categorised into the following areas:

   a. Governance: Management’s role in managing climate-related risks and opportunities

   b. Investment strategy: To describe climate-related risks and opportunities, its impact on the organisation and resilience of the organisation’s strategy due to climate risks

c. Risk management: To describe the organisation's process for identifying, assessing, and managing climate-related risks and how these processes are integrated into overall risk management

d. Metrics and targets: To disclose metrics for assessing climate risks; scope 1, 2 and 3 (if possible) Green House Gas (GHG) emissions and related risks; and targets used by organisation to manage climate-related risks

ii. Product disclosure

a. Disclosures on sustainability risks

b. Detailed information on sustainable characteristics of index

c. Large Fund managers to disclose portfolio carbon footprints of Scope 1 and 2 GHG emissions data.

Regulatory requirements or guidance relating to product-level disclosure for sustainability-related products are intended to promote consistency, comparability, and reliability in disclosure, which will help prevent greenwashing at the product level.

iii. Supervision and enforcement

Securities regulators and/ or policymakers, as applicable, should have supervisory tools to monitor and assess whether asset managers and sustainability-related products follow regulatory requirements and enforcement tools to address any breaches of such requirements.

iv. Terminology

Securities regulators and/ or policymakers, as applicable, should consider encouraging industry participants to develop common sustainable finance-related terms and definitions, including relating to ESG approaches, to ensure consistency throughout the global asset management industry.

v. Financial and investor education

Securities regulators and/ or policymakers, as applicable, should consider promoting financial and investor education initiatives relating to sustainability, or where applicable, enhance existing sustainability-related initiatives.

Similarly, the European Union (EU) has introduced the Sustainable Finance Disclosure Regulations (SFDR), which are designed to drive capital toward sustainably oriented investments. As part of the disclosures, all EU asset managers (regardless of whether they are focused on sustainability) are now required to publicly disclose, (a) their approach to incorporate sustainability considerations in their investment decisions, (b) any adverse impacts on environmental or social factors and (c) any sustainability risks that may impact performance. Furthermore, the Financial Conduct Authority of the UK require Authorised Fund Managers of funds that focus or claim to focus on sustainability and ESG as per the following guiding principles:

- Design of responsible or sustainable investment funds and disclosure of key design elements in the fund documentation
- Achievement of stated objectives and ongoing monitoring of holdings
- Pre-contractual and ongoing periodic disclosures on responsible or sustainable investment funds should be easily available to consumers and contain information that helps them make investment decisions.

Keeping the above facts and progress in mind, three important aspects need consideration:

I. General Climate Disclosure Requirements

All the asset managers and funds, irrespective of their composition and classification, may be required to disclose certain climate-related disclosures that should be consistent and comparable.

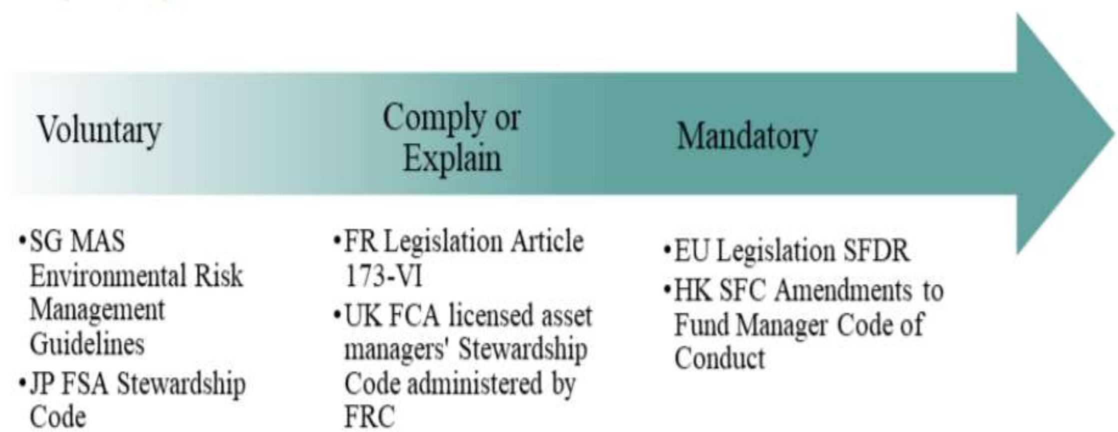
II. ESG classification

There is a need to create an ESG classification system or taxonomy that is open, transparent, and objective. For example, in Germany, a fund is considered an ESG fund if it invests in sustainable assets or if it follows sustainable investment strategy as its core in identifying the companies to invest or if it follows any sustainable index.

III. Mandatory disclosure requirements for certain funds

There should be mandatory disclosure requirements for certain funds either on the bases of total AUM as in the UK or on the bases of work force size as it exists in Europe. It could also be on the basis of funds strategy as followed in Germany.

The following diagram illustrates the range of approaches available to regulators contemplating their policy options:



References:

1. ‘Consultation paper on introducing disclosure norms for ESG Mutual Fund schemes’ by SEBI

2. ‘Recommendations on Sustainability-Related Practices, Policies, Procedures and Disclosure in Asset Management’ report by IOSCO

3. ‘ESG in Asset Management: A Global Perspective’, report by Latham & Watkins

Upon examination of the same, the committee recommend disclosures at 3 levels:

A. Entity (FME) Level Disclosures:

The entity level disclosures could be made mandatory if the FME is managing AUM greater than a significant threshold.

Particulars	Remarks
(i) Governance	FME to establish and disclose policy on governance around material sustainability-related risks and opportunities. For Example: board's oversight mechanism and role of management in managing climate related risks and opportunities.
(ii) Risk management	FME to disclose how it identifies, assesses and manages material sustainability-related risks across funds and portfolio companies.
(iii) Investment Strategy	FME to establish and disclose the process of factoring sustainability-related risks and opportunities into it's investment strategies and processes, including, where relevant, data and methodologies used.

B. Fund Level Disclosures in case of ESG related Schemes

Particulars	Remarks
(i) Name of the scheme	The name of the scheme should accurately reflect the nature and extent of the scheme's sustainability focus and investment objective and strategy.
(ii) Investment objectives	The scheme disclosure documents should provide transparency about the nature and extent of the scheme's sustainability ESG-related investment objectives.
(iii) **Investment policy**	The investment policy of FMEs should encompass processes to review the investments during a certain period and the strategy pursued. The investments should be designed to generate a beneficial impact alongside a financial return. The Investment Policy of FME should disclose the list of invested entities, that have sustainability-related disclosures and their alignment with national or international standards.
(iv) **Investment strategy**	Disclose the type of strategy followed by the scheme, with regards to sustainability or ESG characteristics that merit the nomenclature of an ESG fund, including.: 1) Investment Universe, and Investment Selection Process 2) Usage of indices, ESG Scores/ Ratings, Criteria Used for Inclusion/ Exclusion 3) Extent of portfolio's focus on sustainability

Particulars	Remarks
	The following are some examples of sustainability-related strategies: a) **Exclusions:** Exclude securities based on certain ESG-related activities, business practices, or business segments. b) **Integration:** Explicitly consider ESG-related factors that are material to the risk and return of the investment, alongside traditional financial factors, when making investment decisions. c) **Best-in-class and Positive Screening:** Aim to invest in companies and issuers that perform better than peers on one or more performance metrics related to ESG matters. d) **Impact investing:** Seeks to generate a positive, measurable social or environmental impact alongside a financial return and how the Fund Manager intends to achieve the impact objective. e) **Sustainable objectives:** Aim to invest in sectors, industries or companies that are expected to benefit from long-term macro or structural ESG-related trends. f) Any other clearly defined ESG investment strategy g) **Decision-making process for investing:** Decision-making process for investing should include disclosure on use of proprietary or third-party ESG scoring process or methodology.
(v) **Disclosure of material risks**	Disclosure of unique risks that arise from a scheme's focus on sustainability. Examples include 1) Risk of concentration in certain type of investments 2) Risk of reliance on third party providers for ESG ratings/ scores. 3) Risk of climate-related issues on investments Disclosure of measures taken to mitigate risks related to green washing.
(vi) **Benchmark**	The benchmark should be continuously aligned with each of the environmental, governance and social characteristics followed by the scheme. The website of the respective Fund or scheme should also provide a link to the index methodology.
(vii) **Monitor and evaluate**	FMEs should monitor and evaluate the investments in terms of KPIs, active engagement and stewardship activities with investee companies. In case of Impact, Funds should assess, measure and monitor: (a) it's compliance with investment objectives, (b) the sustainability impact of its portfolio to the extent possible; and (c) its sustainability-related performance.
(ii) **Stewardship and shareholder engagement disclosure**	Disclosures of Stewardship policy reflecting that the exercise of voting rights is in accordance with the objectives of the scheme.

Particulars	Remarks
(iii) **Periodic Portfolio Disclosures**	FMEs shall periodically disclose (to the IFSCA and investors), using quantitative metrics, where available, and qualitative information on a) The various ESG engagement and stewardship activities carried out during the FY b) Periodic reporting relating to achieving sustainability-related investment objectives including sustainability-related performance and holdings. This should also include specific metrics identified as part of investment objectives. c) Climate related scope 1, scope 2 and scope 3 (optional) GHG emissions associated with fund's underlying investments. This may be backed by third-party validation, as may be applicable.
(iv) **Maintenance of ESG policy related to investments**	FMEs should disclose on their website the following information covering various aspects of sustainability-related investments such as: a) Source of ESG information of underlying investments b) Investment process and philosophy c) Key ESG factors to be considered in decision making d) Due diligence process and methodology e) Engagement policies including stewardship f) Monitoring of investments and evaluation. The above disclosures should be made by retail funds. For non-retail funds, the disclosures may be made to the extent possible.
General obligations	(i) The Board or any authorised persons (such as CEO/ COO) of the FME should submit a declaration to the Trustees that the scheme is following its disclosed strategy and is in compliance with its Investment Policies on a quarterly basis. This may be backed by third-party validation, as applicable. (ii) FMEs to engage suitably qualified and/ or experience personnel resources and implement processes to take into account the ESG philosophy of schemes in this space. (iii) FMEs should ensure that the marketing materials and website disclosures are fair, balanced, and consistent with the regulatory filings.

C. All Scheme Documents to be filed with IFSCA

All scheme documents filed by FME shall disclose whether sustainability related risk is incorporated in the decision making. If yes, details thereof may be provided. If no, a negative statement to that effect may be included for retail funds.

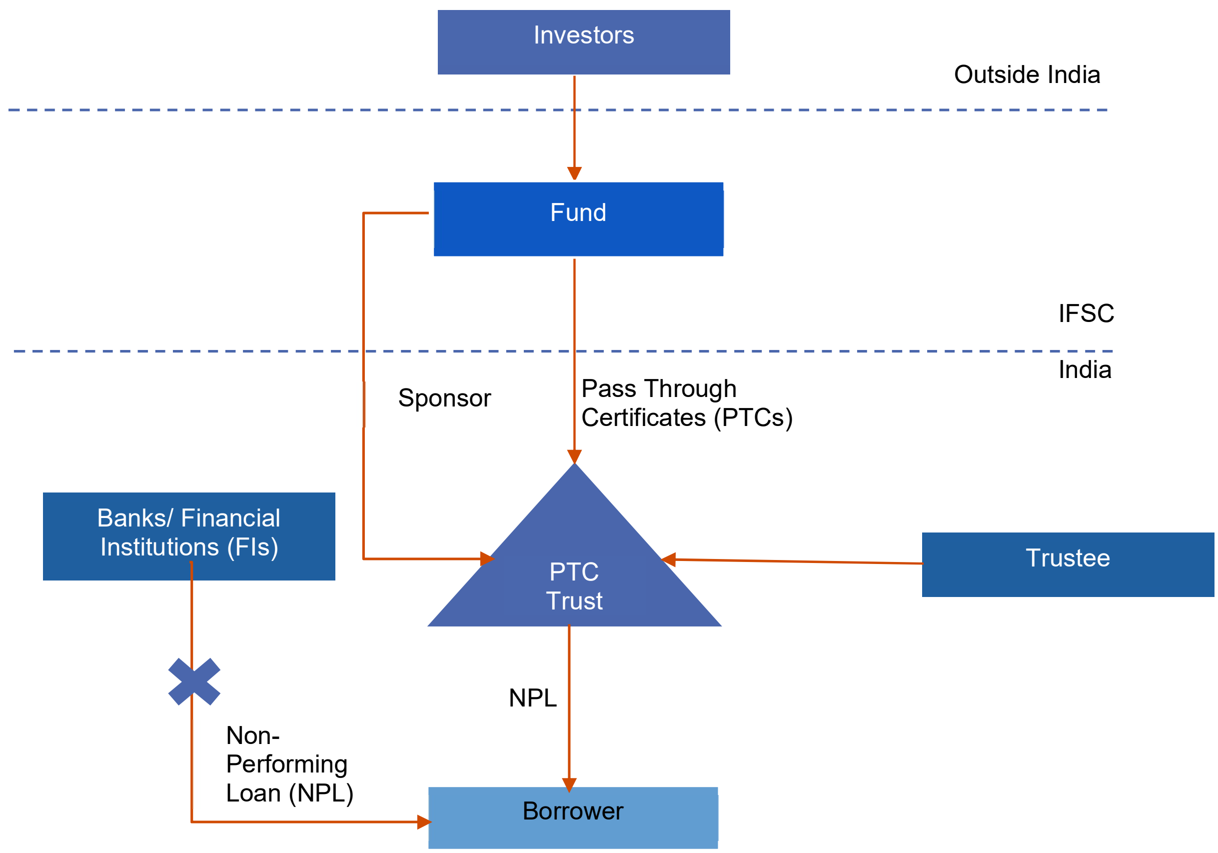
9.3. Stressed Assets

The Government introduced the Insolvency and Bankruptcy Code 2016 (IBC) regime to address Non-Performing Assets (NPA) issues faced by the banking sector. There is a significant interest among offshore distressed Funds to invest in India. The Funds are, in fact, already investing in India through the Foreign Portfolio Investors (FPI) or Security Receipts (SRs) route. The RBI has and continues to progressively liberalise the regime for onshore Asset Reconstruction Companies (ARCs) or securitisation trusts to attract more foreign investment. IFSCA can also play an important role in this Government initiative.

To attract distressed Funds to the IFSC and to facilitate FMEs in the IFSC to raise monies from such investors, the following could be considered:

A Fund managed by an FME set up in the IFSC can be permitted to become a sponsor and set up a stressed loans SPV (organised as a trust) in India.

Structure Chart



Mechanics

- Fund in the IFSC to be the sponsor of the PTC Trust.
- SEBI-registered trustee to be appointed as a trustee of the PTC Trust.
- PTC Trust issues PTCs to the IFSC Fund (under the FPI route).
- PTC Trust to acquire NPLs from banks or FIs.

Eligible investors

- Investors in the Fund in the IFSC shall be either persons resident outside India or non-resident Indians (NRIs) – this condition shall not apply to the mandatory investment by the sponsor or manager of the Fund.
- The FME shall ensure that the investors in the Fund are not disqualified in terms of section 29A of the IBC vis-a-vis any investments made by the Fund on an ongoing basis.

Leverage

The Fund shall not avail any borrowings from Indian banks or FIs (including their branches or subsidiaries in IFSC or outside India) for the acquisition of PTCs.

Other requirements/ conditionalities/ guidelines

Subject to the above, all the other conditions, guidelines, and reporting requirements applicable to the Funds or FME set up in the IFSC shall continue to apply.

- IFSCA has constituted a separate committee on framework for transfer of stressed loans from domestic lenders to permitted financial institutions in IFSC. Based on the recommendations to be received from this committee, appropriate regulatory regime may be considered by IFSCA.

10. Supporting Innovations

10.1.Funds Lab

India is one of the most prominent emerging markets for foreign investors. The Indian market is still under penetrated and has plethora of investments opportunities. During initial periods many Fund Managers and investors prefer to experiment with new investment strategies as they build their portfolios/ track record, etc.

At the same time, globally, the Asset Management world is constantly evolving with new innovations in terms of new products with new features, investment in new asset classes, etc. The adage “change is the only constant” truly applies to the Asset Management industry. This phenomenon is magnified with fintech players venturing into asset management.

The IFSCA, as a global financial hub, should consider providing a platform to such aspirational Fund Managers in the form of a “Fund Lab” as explained below. This is also in sync with the Government’s and the IFSCA’s vision to develop fintech industry in IFSC.

Fund Lab as a regulatory sandbox

Regulatory Sandboxes are becoming more common in India and globally as regulators promote innovation in a controlled manner by providing a safe space to businesses wanting to test new products/ services/ business models.

Fund Lab as a concept will be akin to regulatory sandbox, which allows FMEs to create and develop asset management/ Fund products and strategies in a controlled manner with limited Asset Under Management (AUM)/ number of investors.

The broad features of the Fund Lab framework for FMEs are described below:

Eligibility Criteria

The IFSCA could allow FMEs to operate within its Fund Lab framework with the following criteria:

Particulars	Applicability
Type of Fund/ period	• In the Fund Lab, the Fund should be close ended. The period for which the FME wants to ‘experiment’ should be defined upfront and should not exceed 18 months. • Once the ‘experiment’/ investment strategy is successful and the Fund ‘migrates’ to the normal Fund regime, it could be made open-ended or open to additional investors while remaining close-ended in accordance with the Fund regime.
Investors	• The Fund will be floated by the Fund Manager or its group entity. The Fund would not accept money from external entities/ persons.
Investment team	• To foster an element of “out-of-the-box” thinking and encourage “start-ups” like set-up, the IFSCA could permit FMEs to operate in the Fund Lab without any minimum criteria with respect to educational qualification or experience or investment team size. • Once the ‘experiment’ is successful, the FME should comply with such criteria as applicable to relevant FME regime.
AUM	• Minimum investment corpus - USD 1 million.

Particulars	Applicability
	• Minimum investment corpus - USD 3 million.
Investment restrictions/ diversification norms	• To encourage innovation, investments shall be allowed in any asset class or security, subject to the discretion of the IFSCA. If such asset class or security is not expressly permitted in the Fund regime, the IFSCA should notify the same upon successful completion of the 'experiment'. • To start with, there should be no restriction on diversification and investment concentration. Once the Fund migrates to the normal regime, restrictions relevant to the regime could be made applicable.
Leverage	• Leverage should generally not be permitted while the Fund is in the "Fund Lab".
Applicability of KYC and AML conditions	• The Fund should be required to comply with the KYC and AML norms and requirements; there should not be any exception.

FMEs desirous of operating in the Fund Lab framework should approach the IFSCA with the relevant details including investment team profile, the proposed investment strategy, risks involved, profile of investors, reasons for use of the Fund Lab regime, etc.

Criteria for Approval

On receipt of any application for setting up a Fund Lab testing entity, IFSCA may either accept or reject the application based on criteria such as:

- The importance/ benefits that the product/ service/ business model being tested would have for IFSC and public at large.
- The capability of the applicant to pull through the Fund Lab testing: and
- The impact/ consequences of the failure on the financial environment in IFSC.

During the period while the Fund is in the 'Fund Lab', IFSCA may define timelines/ reporting requirements as considered appropriate.

Also, to encourage growth of such innovative FMEs, the IFSCA/ Government could announce a "seed funding" program to invest in some of these "start-up Funds" in the Fund Lab at its discretion.

Way forward on the completion of the 'experimentation' period

On completion of the Fund Lab period (including the extended period, if any), the FME should be required to submit a detailed report on the findings/ outcome of the proposed strategy and the way forward to launch the product and the plan for compliance with the relevant Fund regime conditions.

The IFSCA may work with the FME to understand the detailed dynamics of the tested product/ services/ business models etc. for introducing it in the larger market.

The IFSCA post evaluation of the report submitted could undertake either of the following:

- Wind up the Fund in case the results are not satisfactory; or
- The Fund migrates into the full Fund regime in appropriate categorisation under the proposed Fund regime.

10.2.SPV structure

Globally co-investment structure and leverage has been in existence for long and have been extensively used by the Investment Funds for making investments. This provides the fund industry the flexibility in structuring their investments. To facilitate co-investments jurisdictions such as Singapore has VCC, and Mauritius has Protected Cell Company (PCC).

FMEs should be allowed to create Special Purpose Vehicle (SPV) under the main Fund/ scheme, to enable undertaking large investment with the help of their existing investors or other investors to co-invest along with the Fund/ scheme. This would provide the Fund Managers an alternative option for co-investment along with other investors in a particular underlying security. The Fund may also make use of SPV to take leverage at SPV level. The leverage taken at the SPV level will enable the Fund to have leverage for a specific investment and safeguard the investors of the main Fund. Key features of the same could be as under:

- Such SPV should be deemed to be a Fund. Thus, all the benefits, conditions, restrictions, etc. under the Fund regime should also be applicable to the SPV with suitable modifications wherever required.
- The Fund/ scheme should hold a minimum of 50% of shares and voting power in the SPV formed for co-investment purposes.
- From a priority perspective, co-investment opportunities through the SPV should be offered first to the existing investors in the Fund and if they are unable to fully participate, then, it should be offered to external investors. The terms offered to external investors should not be more favourable than those offered to the Fund/ scheme/ existing investors.
- The tax regime of the SPV should also be similar to the tax regime applicable to Funds.
- No separate investment manager should be required at the SPV level. Further, no separate sponsor commitment should be required at the SPV level.
- Co-investment by creating a separate SPV can be made by the FME at various times, even subsequent to the formation of the Fund/ scheme.
- Appropriate disclosures should be made to the investors of the Fund/ scheme with respect to the setting-up of a separate SPV for co-investment.
- The term sheet of the SPV is to be filed with IFSCA.
- SPV would have to comply with reporting requirements as may be prescribed by IFSCA.
- The SPV structure will also be available to Family Office funds.
- The SPV will bear its pro rata portion of all investment-related expenses and also bear its own expenses.

10.3.Public participation in private markets

There is growing interest in retail investors to have access to the “market as a whole” i.e., both, public and private markets. This is evident from the successes of initial public offerings of some of the “new age” companies which were subscribed manifold and “secondary” transfers of shares in some of the large unlisted companies to retail investors.

At the same time, one cannot undermine the risks of investing in private markets.

One could evolve a solution to balance both the above aspects i.e., permit retail investors to participate in private markets but in a limited way. The IFSCA should consider this as it fosters growth of capital markets and encourages retail participation. Such similar participation has already been enabled in jurisdictions such as Ireland.

This can be achieved by permitting the retail schemes to invest in private companies along with investment in public markets.

While such investments are permitted, to mitigate risks, it is proposed to cap investment in unlisted securities for open-ended retail scheme to 15% and that of close-ended retail schemes to 50%.

Further, to enable more retail participation, it is proposed that there should be no minimum investment criteria for investors in open-ended retail scheme or in close-ended retail schemes investing less than 15% in unlisted securities. For other close-ended retail schemes, the minimum investment from a single investor should be retained at say USD10,000 on the presumption that such investors would have the necessary capital/ experience to undertake risks of investing in private markets.

11. Supporting Ecosystem

11.1.Framework for accredited investor

- As understood across jurisdictions, a class of investors who understand various financial products, have the ability to make well-informed investment decisions and have a certain minimum income or net worth or assets are recognized as 'Accredited Investors'. The concept is recognized by many securities and financial market regulators around the globe. These investors are typically termed as Accredited Investors or Qualified Investors or Professional Investors.

- It is observed that most jurisdictions use financial information of the investor to determine such category of investors, however, certain jurisdictions also consider other criteria such as knowledge, investment experience, etc.

- In the jurisdictions which recognize such class of investors, it is reckoned that these investors are sophisticated enough to not require extensive regulatory protection, and therefore, issuers of securities and providers of financial products/ services are offered a light touch regulatory regime regulation-light regime, to offer their products/ services to such class of investors. This sometimes implies relaxation with respect to disclosure requirements, filing of offer document/ prospectus etc., and flexibility in respect of investor reporting. It is understood that certain jurisdictions also permit issuers/ providers of financial/ securities market products/ services to design and offer products/ services exclusively to such class of investors.

- In the United States, an Accredited Investor is someone who meets income, professional and/ or net-worth criteria. The placement document meant for investments by Accredited Investors do not require detailed disclosures and the document is not required to be registered. Accredited Investors may invest an unlimited amount in an offering under Regulation Crowdfunding under the Regulation Crowdfunding (JOBS Act) subject to the maximum amount a company can raise each year. In the recent past, Securities and Exchange Commission (SEC) has amended the norms for Accredited Investors to enable institutional and individual investors that have the knowledge and expertise to participate in the private markets.

- Similar to USA, in Singapore under the Securities and Futures Act (SFA), Accredited Investors have been defined based on income and personal assets. A brief comparative table prepared for Singapore and USA which provides provisions with respect to specified class of persons and applicable relaxations, is set out in **Annexure D**.

- In line with the global best practices, SEBI vide recent amendments to the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012 (AIF Regulations), Securities and Exchange Board of India (Portfolio Managers) Regulations, 2020 (PMS Regulations) and Securities and Exchange Board of India (Investment Advisers) Regulations, 2013 introduced the concept of 'Accredited Investors' for the Indian securities market.

- SEBI has laid down the eligibility criteria for different category of investors (viz. individual, Hindu undivided family, family trust, sole proprietorship, body corporate, trust, partnership firm) depending on their annual income, net worth etc. and has also provided the requirement for such qualifying investors to be accredited pursuant to an accreditation process by an 'Accreditation Agency'.

- IFSCA has recently notified the IFSCA (Capital Market Intermediaries) Regulations, 2021 which includes Portfolio Managers and Investment Advisers as capital market intermediaries for which registration has been sought. While the SEBI AIF Regulations are applicable in IFSC, the regime for Investment Funds in IFSC also envisage certain Investment limits and restrictions.

- Accordingly, it is proposed that a framework for Accredited Investors may be introduced in IFSC to permit such investors to:

    - Invest in various securities and financial products without any minimum size restriction.

- Invest in certain securities and financial products designed exclusively for such investors.
- Relax certain regulatory restrictions (disclosures/ investment restrictions, etc.,) for products and services offered to Accredited Investors only.

Introduction of concept of Accredited Investor

Accredited Investors are assumed to be better informed, experienced, and having access to resources to protect their own interests, and therefore require less regulatory protection. It is pertinent to note that less stringent authorisation requirements, disclosures and procedural requirements for privately placed funds would provide wider access to investment opportunities. The definition of "Accredited Investor" can be introduced based on quantitative criteria across the Financial Products' and services (*defined below*). Once the regime stabilizes, IFSCA may also consider qualitative criteria such as qualifications and professional experience. Certain relaxations can be provided with respect to the Accredited Investors under various regulations for such investors.

A. Certification process for Accredited Investors by Specified Agency

a. Eligibility criteria for Specified Agency

A recognized stock exchange or a depository (Specified Agency) can be authorized to certify eligible investors as "Accredited Investors" based on the laid-out criteria. For Specified Agency in IFSC, only those agencies may be appointed who have necessary infrastructure (including manpower) in place to carry out functions of Specified Agency and has been granted approval from IFSCA to act as Specified Agency.

Entities desirous of being reckoned as Accredited Investors may approach an Accreditation Agency for accreditation. The same may be routed through any entity registered or authorised by IFSCA. Accreditation Agencies shall be responsible for:

i. verification of documents submitted by applicants for accreditation,

ii. timely processing of applications for accreditation and issuance of accreditation certificate,

iii. maintaining data of Accredited Investors,

iv. verification of accreditation status,

v. maintaining confidentiality of investor information at all times, except where such disclosures are required to be made in compliance with any law,

vi. providing access to entities to verify the accreditation status of investors, and

vii. any other responsibilities as may be specified by IFSCA from time to time.

b. Pros and Cons (if accreditation process is completed by Specified Agency)

Pros

- Streamlined process for accredited certification.
- Protects investor sensitive personal information from third parties (multiple financial advisers) since the information would not be repeatedly shared with different financial advisers.
- Centralized database will save crucial time by completing the accreditation process in one-go instead of repeating the process every time as and when investors invest in a new opportunity.

Cons

- May result in a delayed on-boarding process of investor with the concerned intermediary in case the accreditation certification is not received from the Specified Agency in timely manner.

- Implementation of additional regulatory framework in terms of registration process and eligibility criteria for Specified Agency.

To provide flexibility to the investors, it is proposed to permit accreditation by both, i.e., by the Specified Agency or by the concerned intermediary, depending upon the preference of the investor. Accordingly, an investor may opt to seek an accreditation from the Specified Agency, which would then be valid vis-à-vis each intermediary the investor deals with or may choose to represent/ confirm its accredited status directly/ each time to every concerned intermediary with whom it may deal with from time to time.

B. Process prevalent in jurisdictions like Singapore and USA for accreditation

In certain countries like USA and Singapore, the financial adviser maintains a screening process to confirm status of investor as accredited investors. They provide assessment form to investors seeking details of monthly income, details of the assets along with list of supporting documents required to and declaration by the investor stating that information provided is true with an undertaking that the investor will immediately inform about any subsequent change/ s in circumstance that may cause any of the personal or financial information provided by the investor to become incorrect or incomplete to meet certain qualifications of accredited investor.

C. Classification of Accredited Investors:

The Accredited Investor can be classified based on the quantitative criteria or based on deemed recognition principle for certain investors. Accredited Investor can be categorized in two categories viz. (a) Recognized Accredited Investor; (b) Deemed Accredited Investor:

a. Recognized Accredited Investor

The financial criteria (including annual income and net worth) can be the grounds for classification of Accredited Investors. As is practiced in various jurisdictions, the criteria can be linked to financial assets, net-worth and/ or income thresholds.

b. Deemed Accredited Investors

The following class of investors - may be considered as deemed Accredited Investor/ s:

i. Government and Government related investors such as central banks, sovereign wealth funds, international or multilateral organizations or agencies including entities controlled or at least 75% directly or indirectly owned by such Government and Government related investor(s),

ii. Any Fund/ Fund Manager regulated by IFSCA,

iii. Market Infrastructure Institutions in IFSC,

iv. Capital Market Intermediaries in IFSC,

v. Banking Units, Finance Companies, Insurance Companies set up in IFSC,

vi. An Investment Fund (mutual fund, insurance fund, pension fund, university endowment fund etc. by whatever name called), commercial banks, asset management companies, insurance, and reinsurance companies from a Financial Action Task Force (FATF) compliant jurisdiction and regulated by a Financial sector regulator,

vii. Professional/ Accredited/ Qualified Investors from FATF compliant jurisdiction.

D. Proposed Definition for Recognized Accredited Investor

a. <u>Natural Person: An Accredited Investor, in context of a natural person, means any person who:</u>

i. has annual income of at least USD 3,00,000 or equivalent amount in applicable foreign currency; or

ii. has net worth of at least USD 1 Million with not less than USD 500,000 of financial assets or equivalent amount in applicable foreign currency (excluding the value of primary residence); or

iii. has annual income of at least USD 150,000 and + has net worth of at least USD 750,000 with not less than USD 375,000 of financial assets or equivalent amount in applicable foreign currency (excluding the value of primary residence).

A sole proprietorship and a Hindu Undivided Family (HUF) may comply for the provisions as applicable to natural person. In case of Partnership firm, each of the individual partner may comply for the aforesaid rules or the partnership firm comply with the net-worth criteria as applicable to non-individuals.

In case of accreditation of individual investors, HUFs and Sole Proprietorships, the value of the primary residence of the individual, Karta of HUF, and the Sole Proprietor respectively, shall not be considered for calculation of net worth.

In case of investments held jointly by more than one individual, the following conditions may apply for eligibility:

i. Where the joint holders are parent(s) and child(ren), at least one person should independently fulfill the eligibility criteria for Professional Investors;

ii. Where the joint holders are spouses, their combined income/ net worth should meet the eligibility criteria for Accredited Investors.

b. **Non - Individuals:** An Accredited Investor, in case of non-individual (other than natural person), means any person who has net worth of at least USD 7.5 Million or equivalent amount in applicable foreign currency.

E. Consent/ Opt-in regime

The intermediary dealing with Accredited Investors should obtain the relevant investors' opt-in (i.e., consent) to be treated as Accredited Investor, and maintain the relevant opt-in documentation (in terms of declarations) from such investors. Thus, a person that meets the criteria to be an Accredited Investor may only be treated as an Accredited Investor if he/ she opts to be onboarded as such.

11.2. Framework for distributors

a. IFSCA vide circular dated February 10, 2021 titled “Framework for enabling Ancillary services at International Financial Services Centres” (Circular) issued a framework for ancillary service providers to enable one or more of the following activities from the IFSC:

- Legal, Compliance and Secretarial;
- Auditing, Accounting, Bookkeeping and Taxation Services;
- Professional & Management Consulting Services;
- Administration, Asset Management Support Services and Trusteeship Services.

b. The above services based out of the IFSC helps in establishing professional service providers in the IFSC and they act as the interface between the various financial service providers and the client/ regulator, etc.

c. Similarly, there is a need to ensure that distributors of financial products are set up in the IFSC to ensure wider distribution of financial products of the IFSC and to bridge the gap between the manufacture of financial products such as Investment Funds, Portfolio Managers, etc., and the investors under a regulated framework.

d. Accordingly, it is proposed that any person, domiciled or established in the IFSC, desirous of acting as a distributor of: (i) financial products or services regulated by the IFSCA; and/ or (ii) financial products or services subscribed/ availed by any person domiciled or established in the IFSC; and/ or (iii) financial products or services regulated by financial sector regulator of such jurisdictions (including India) as may be specified by IFSCA, shall obtain an authorisation from the IFSCA for the same (in terms of the Circular) and shall comply with the code of conduct, as provided below in Exhibit – I.

   Provided that, if any person is not domiciled or established in the IFSC, then such person may act as a distributor with respect to (i) & (ii) above without an authorisation from the IFSCA but subject to its compliance with the code of conduct, as provided below in Exhibit – I.

   Further provided that, an IFSC Banking Unit (IBU), Investment Advisers, stockbroker, insurance broker or such other entities as approved by the IFSCA may act as distributor, without a separate authorisation from the IFSCA, however such entities as approved by the IFSCA will have to comply with the code of conduct, as provided below in Exhibit – I.

e. The distributor shall not take client assets (including money), directly or indirectly in its custody and shall only provide distribution services. Further, the entities intending to undertake activities such as Investment Adviser, Stockbroker, etc., shall seek IFSCA registration separately under the appropriate framework.

f. Persons engaged in providing investment management, portfolio management and investment advisory and other related financial products and services (Financial Service Provider) shall:

- utilize services of only such distributor/ s (whether known as channel partner, agent, referral interface or by any other name) who meet the requirements laid down in clause (d) above.
- ensure that prospective investors are informed about the fees or commission to be paid to the distributor/ its affiliates (directly or indirectly) by the Financial Service Provider/ its affiliates.
- ensure that distributors abide by the code of conduct as outlined below. IFSCA may take appropriate action in case of any violation of the provision/ s of the Code of Conduct.

- ensure that, within 15 days from the end of every financial year, a self-certification is also received from distributors with regard to compliance with the code of conduct.

Exhibit I: Code of Conduct

i. Maintain high standards of integrity, promptitude and fairness in the conduct of all business transactions.

ii. Act with due skill, care, and diligence in the conduct of all their business.

iii. Avoid mis-selling by considering investor's interest and suitability to their financial needs.

iv. Act in the best interests of the investors, the Financial Service Providers, and the integrity of the market.

v. Be fully conversant with the terms of the private placement memorandum, disclosure document and other agreement, as the case may be, entered between the investor and the Financial Service Provider.

vi. Urge investors to go through the private placement memorandum, disclosure document and other applicable document/ agreement, as the case may be, to be entered between the investor and the Financial Service Provider before deciding to make investments.

vii. Disclose to the investor all material information including the details of all the fees or commission (in the form of trail or any other mode, if any), received (directly or indirectly) from Financial Service Provider/ its affiliates for rendering distribution services.

viii. Assist the investor in completing KYC and other related procedures and assist in compliance with relevant PMLA guidelines under the Prevention of Money Laundering Act, 2002 to the extent applicable with respect to the on-boarding of such investors.

ix. Abstain from tampering with the application form and other details submitted by the investor, including inserting, deleting, or changing any information in the application form provided by the investor.

x. Provide full and latest information about the financial products and services offered by the Financial Service Provider and highlight the assumptions made in performance calculations, risk assessments, performance projections etc., if any, for such financial products and services offered.

xi. Abstain from assuring returns and from any kind of misrepresentation.

xii. Abstain from attracting investors through unethical means such as offer of rebate/ gifts etc.

xiii. Maintain necessary infrastructure to provide support to investors and Financial Service Provider in timely receipt of statement of portfolio and performance, statement of fees, audit report, etc.

xiv. Ensure that all investor related statutory communications as applicable (such as changes in fundamental attributes, fees, and expenses, exit options, reports, and other material aspects) are sent to investors reliably and on time.

xv. Clearly disclose the general nature or sources of conflicts of interest to the investor and the Financial Service Provider before undertaking business.

xvi. Take all reasonable steps to avoid conflicts of interest (whether actual or perceived) and develop appropriate policies and procedures to identify, manage, monitor and, where applicable, disclose, those conflicts of interest in order to prevent them from adversely affecting the interests of the Financial Service Provider and the investor.

xvii. Ensure segregation of the activities and proper disclosures about segregation to the Financial Service Provider and the investors to avoid conflict of interest arising due to multiple activities.

xviii. Maintain and protect confidentiality of investor's and the Financial Service Provider's details, deals and transactions, investment strategies and ideas which the distributor comes to know in the course of its business relationship.

xix. Abstain from encouraging over transacting and churning of portfolio of the investor to earn higher commissions.

xx. When distributing various financial products and services, ensure that investors' interest and suitability to their financial needs is paramount and that extra commission or incentive earned should never form the basis for distributing any financial product or services to the investor.

xxi. Not indulge in any manipulative, fraudulent or deceptive practices.

xxii. Hold valid authorisation, as applicable/ specified by the IFSCA, at all times. Comply with all marketing and distribution related norms as may be specified by the IFSCA.

11.3. Passporting of funds

- The IFSCA is making concerted efforts towards raising and developing IFSC that is globally competitive to achieve the end of increased exchange of cross-border financial products and global financial integration.

- In a perfect world, regional fund managers would be able to freely offer their local products to investors in other countries on a level playing field. However, since different countries have different regulatory regimes, financial centres often grapple with multiple standards across jurisdictions which makes it difficult to facilitate cross-border marketing/ distribution of such products. But having said that, many economies have been able to do this successfully and have reaped immense benefits from the influx of investments into their territories.

- Since the desire is to bring IFSC at par with major financial centres around the world, adopting a regime that promotes ease of business through coordination and cooperation between multiple regulators would be crucial for its sustained growth and development. One way this can be facilitated is through introducing a regime that allows for funds passporting in a manner similar to that adopted in the European Union and several Asian economies.

- In 2017, the International Advisory Board (IAB) of SEBI had examined the framework of passporting of investment funds and concluded that SEBI may also explore some alternative framework like mutual recognition and regulatory equivalence for cross-jurisdictional investment flow.

Benefits of adopting a regime that allows Passporting of Funds

There are several benefits that may be realised by adopting a regulatory regime that allows for passporting of investment funds. Some of them have been listed below and categorised as under.

A. Advantages for investors

i. Uninhibited access to investments and expertise across the territories.

ii. Tailored investment products with varying strategies across geographies.

iii. Reduced costs for investors owing to lesser compliance burden on investment funds and lower number of fund structures.

iv. Increased transparency and protection ensuring investors have investment products that they understand and are appropriate to their needs.

B. Advantages for investment manager

i. Increase in accumulation of assets under management owing to access to larger cohort of investors across different geographies.

ii. More cost efficient as lower number of fund structures to be floated to raise money from different geographies.

iii. Reduced compliance burden if member jurisdictions offer comparable regulation and market sophistication.

C. Advantages for the IFSC

i. Deepening of financial markets and availability of a wide variety of investment products.

ii. Establishment of a regulatory regime that is at par with major global financial centres.

iii. Enhanced interest from market participants owing to expansion of opportunities for the investment management industry.

iv. Greater inflow of investments from investors across geographies.

v. Tapping into regulatory and commercial expertise of more developed financial hubs such as Singapore, Japan, Australia which may further boost development of local regulatory standards and frameworks at IFSC.

Concerns surrounding feasibility of passporting of investment funds

- Pronounced differences in market sophistication and economic development of constituent jurisdictions.
- Variations in taxation, regulation, and other structural factors among constituent jurisdictions.
- Absence of a common currency.
- Competition amongst countries, cities, and regulators to become a financial hub.

Global Practices with Regard to Passporting of Investment Funds

A. Passporting of Funds in the European Union

i. The EU Directive 2011/ 61/ EU on Alternative Investment Fund Managers (AIFMD) created a single marketplace within the European Union (EU) for marketing of AIFs.

Scope of AIFMD

ii. Presently, AIFMD allows for the marketing of AIFs in the EU by alternative investment fund managers (AIFMs) to professional investors. Retail funds marketed to retail investors are governed by the Undertakings for Collective Investment in Transferable Securities Directive 2009/ 65/ EC (UCITS Directive).

iii. Firstly, the AIFMD applies to all EU AIFMs managing EU AIFs or non-EU AIFs, irrespective of whether or not they are marketed in the Union. Secondly to non-EU AIFMs managing EU AIFs, irrespective of whether or not they are marketed in the Union and lastly to non-EU AIFMs marketing EU AIFs or non-EU AIFs in the Union.

iv. From the perspective of marketing of funds, the Directive gives the non-EU AIFMs two different options to access the EU market: (1) first, with the EU passport; or (2) through the national private placement regimes specific to each member state.

EU authorised AIFM marketing EU AIFs in the EU

v. Under the AIFMD, an EU authorised AIFM has a passport to freely market its EU domiciled AIFs to professional investors in its own Member State and in other EU Member States, subject to a straightforward notification process.

vi. The home EU Member State regulator may only prevent marketing of shares in EU AIFs where the information provided in the notification demonstrates that the AIF concerned will not be managed in accordance with the Directive.

Non-EU authorised AIFMs marketing non-EU AIFs in the EU

vii. The AIFMD allows each EU member state to decide whether or not to allow non-EU AIFMs to market in its jurisdiction and to determine the rules that should apply provided that:

   a. there is a cooperation agreement in place between the regulatory authorities in the member state and in the jurisdictions in which the non-EU AIFM and the AIF are established,

   b. neither of those jurisdictions is listed as a Non-Cooperative Country and Territory by the FATF, and

c. the non-EU AIFM complies with the transparency and reporting requirements set out in the AIFMD.

Equivalence requirement

viii. The AIFM must comply with all the requirements set forth in the Directive which includes additional disclosure to investors in the fund's offering documents. In cases where compliance with a provision is incompatible with provisions of another mandatory law, there is no obligation on the fund manager to comply with the relevant AIFMD provision.

ix. The AIFM will then however be required to provide any such list of conflicting provisions and provide evidence that it is subject to and complies with equivalent rules with the same regulatory purpose and level of investor protection.

x. The European Securities and Markets Authority (ESMA) provides advice to the European Commission (EC) with regard to which passports to non-EU jurisdictions may be extended to. Such advice is rendered after thorough analysis of factors which may impede the application of the AIFMD (such as obstacles to investor protection, competition, market disruption, monitoring of systemic risk).

B. Mutual Recognition Framework between Hong Kong and mainland China

i. The Securities and Futures Commission (SFC) and the China Securities Regulatory Commission (CSRC) launched the initiative of Mutual Recognition of Funds (MRF) between Mainland China and Hong Kong, allowing eligible Mainland and Hong Kong funds to be distributed in each other's market through a streamlined vetting process. If a Mainland fund complies with the relevant Mainland laws and regulations, it is generally deemed to have complied in substance with the relevant SFC requirements and will enjoy a streamlined process for the purpose of authorisation for offering to Hong Kong public and vice-versa.

ii. The two regulators have set out eligibility requirements, application procedures, operational and regulatory arrangements of the MRF. They have also established a cooperation mechanism for cross-border regulation and enforcement as well as a framework for exchange of information and regulatory cooperation to ensure that Mainland and Hong Kong investors will have equal protection.

iii. At the initial stage, only regular equity funds, bond funds, mixed funds, unlisted index funds and physical index-tracking ETFs are eligible for MRF. This list may be expanded to include other financial products in the future.

iv. Mainland fund managers that wish to apply for SFC authorisation of their funds for distribution in Hong Kong have to meet certain eligibility requirements.

v. The distribution arrangements of Recognised Mainland Funds in Hong Kong are the same as those of other retail funds. It must be conducted by intermediaries that are properly licensed by the SFC and comply with all applicable Hong Kong laws and regulations.

vi. Hong Kong has reached similar agreements with Thailand, Switzerland, the UK, Luxembourg, and France.

C. Asian Regional Funds Passport

i. The Asia Region Funds Passport (ARFP) is an international initiative led by Asia-Pacific Economic Cooperation (APEC) that aims to facilitate cross-border offerings of eligible collective investment schemes among APEC member economies while ensuring investor protection in the economies participating in the ARFP.

ii. The ARFP allows units of funds authorized in a participating country (home economy) to be offered in other participating countries (host economies) through locally licensed or regulated distributors upon approval as an ARFP fund and host jurisdiction authorisation.

iii. Under the ARFP framework, efforts are made to unify the mutual entry processes for funds that are managed in accordance with the ARFP rules agreed upon among the relevant regulators of the participating economies.

iv. The Memorandum of Cooperation (MOC) is the internationally agreed framework which sets out the rules and conditions for offerings of cross-border mutual funds under the ARFP. There are currently 5 participating economies who are signatories to these frameworks, namely, Australia, Japan, the Republic of Korea, New Zealand, and Thailand.

D. Singapore

i. Similarly, Singapore allows for two ways in which investment funds may be distributed. Firstly, through the recognized schemes which involves a recognition process with Monetary Authority of Singapore (MAS) where recognition is required for foreign funds targeting retail investors. Secondly, through restricted foreign schemes offered only to accredited investors involving a notification to the MAS.

ii. To obtain recognition, the foreign fund's home legislation and market practices must provide equivalent protection to Singapore investors as they would get from Singapore domiciled funds. A foreign fund would have to be subject to similar investments guidelines in its home jurisdiction that would apply to those applicable to Singapore domiciled funds.

E. Funds passporting framework under ASEAN (CIS) Framework

i. Similarly, the ASEAN Collective Investment Scheme (CIS) Framework allows fund managers based in Singapore, Malaysia, and Thailand to offer CIS constituted and authorised in their home jurisdiction directly to retail investors in the other two ASEAN countries under a streamlined authorisation process.

ii. For this purpose, a set of common ASEAN standards has been established to ensure that participating fund managers have the necessary experience and track record in managing retail funds offered under the framework. These standards are as follows:

a. the CIS has been assessed by the relevant local regulator as being suitable as a "Qualifying CIS";

b. investments may only be made in transferable securities, money market instruments, deposits, units of other CIS and financial derivatives;

c. the CIS may not engage in certain specified activities, such as securities lending or repurchase agreements; and

d. the CIS is operated by a locally licensed CIS operator (that has a minimum five-year track record and at least USD 500 million under management globally).

F. Some of the key highlights of the regulatory regimes discussed above are elaborated in **Annexure E** of this Note. **Annexure E** provides a high-level comparative analysis of the passporting regime in EU and Asia and brings out certain key differences, similarities and points of convergence in each framework.

SUGGESTIONS/ RECOMMENDATIONS

I. Proposed Regimes

A. <u>Promoting greater coordination and cooperation between multiple regulators through mutual recognition or passporting arrangements</u>

As discussed in earlier paragraphs, a number of regulatory innovations have facilitated distribution, administration, and marketability of funds across border – for example, the UCITs and the AIFMD (Europe), and the MRF, the ARFP and the ASEAN CIS (Asia). The common theme underlying each of these frameworks is the decision reached between the host economy and the home economy to mutually recognise laws of the other. In Asia, this decision has manifested in the form of multilateral agreements between various economies (pursuant to which domestic laws in each economy has been appropriately amended) – for example, the agreement between Hong Kong and China, the

Memorandum of Cooperation between Australia, Japan, Thailand, South Korea, and New Zealand – whereas, in Europe a pan-EU Directive has been enacted by the European Commission. The effect of these agreements has been to foster economic growth and strengthen the investment management industry in these regions.

It is recommended that the IFSCA may participate in reciprocal passporting arrangements/ mutual recognition frameworks similar to ones described above. Participating in such arrangements will showcase to the world that the regulatory regime of the IFSCA is at par with global standards and will have the effect of cementing the reputation of the IFSC in India as a renowned financial services centre. Additionally, the IFSCA should recognize third-country regimes under such arrangements, subject to appropriate equivalence requirement (discussed below).

B. Deemed compliance/ Substituted Compliance with foreign jurisdiction having equivalent laws

The AIFMD provides for 'third country' regimes which allow non-EU based firms to offer services into the EU. As a rule, a non-EU AIFM must comply with all the requirements set forth in the AIFMD. However, where compliance with an AIFMD provision is incompatible with provisions of another mandatory law of the home jurisdiction, there is no obligation on the non-EU AIFM to comply with the relevant AIFMD provision. The non-EU AIFM will then however be required to provide evidence that it is subject to and complies with equivalent rules with the same regulatory purpose and level of investor protection and the non-EU AIFM or the non-EU AIF complies with that equivalent rule. Whether a particular law is equivalent to stipulations of the AIFMD is determined after a system of peer review by the ESMA.

It is recommended that the IFSCA may have similar arrangements (deemed compliance/ substituted compliance) with prominent overseas jurisdictions having fund management such as EU (Luxembourg, Ireland etc.), Singapore, USA, Mauritius, Cayman Islands etc. The IFSCA Regulations on Fund Management may have equivalent rules as compared to these jurisdictions. The reason behind the recommendation of the equivalence principle is that the adoption of the equivalence principle is anticipated to avoid a one-size-fits-all market access regime and provide a dynamic system of regulation. Having such a system in place has the potential to rule out the many inconsistencies that are bound to arise while integrating laws of different jurisdictions and allow for seamless regulatory framework for cross-border distribution of funds.

II. Increasing presence in the IFSC under any of the aforesaid proposed regimes by requiring appointment of local representative

As a flourishing destination for cross-border financial products, it is understandable that the IFSCA intends to maximize the presence of financial intermediaries within its geographical territory. However, requiring the physical presence of such financial intermediaries is an onerous demand – one that financial intermediaries may be reluctant to meet. Therefore, it is proposed the IFSCA may require the appointment of a legal person (or a natural person) as a local representative who may be appropriately regulated by the IFSCA. The local representative, together with the fund manager, will act as a point of contact of the passport fund, the investors of the relevant funds, and the IFSCA with regard to the activities which the fund manager is authorised to perform in the IFSC. The local representative may be tasked with performing compliance functions of the financial intermediary which may include maintaining a register of unitholders, sending of reports to unitholders, filing reports with the host regulator etc. Appointing a local representative makes it that much easier for a financial intermediary to streamline the process of getting authorized and it will also be preferable to setting up services in the IFSC owing to decreased consumption of resources and time. The appointment of local representatives may thus be explored by the Committee. Similar mechanism to some extent exists under the AIFMD, the ASEAN CIS and HK MRF frameworks.

The passporting regime may be considered as a medium to long term goal by IFSCA as there are many external factors/ dependencies involved.

12. Taxation

- A well-founded regulatory regime for investors needs to be supplemented by an equally well-founded tax regime. Both work in tandem, and without each other's support, the Fund regime may get stalled.

Basic principles of taxation

- Globally, Funds operate on the principle of 'one' level of taxation in a Fund structure that is usually levied in the hands of investors with no effective taxation in the hands of the Fund (commonly referred to as a tax pass through). The taxation in the hands of the investors could be either on an accrual basis (as and when income is earned by the Fund) or at the time of distribution of income by the Fund.

- Mutual funds in India operate on the basis of 'one' level of taxation, with the income of the Fund being exempt from tax and investors now liable to tax at the time of distribution or exit from the Fund. Domestic Category I and II AIFs have a tax pass through with largely no tax in the hands of the AIF, and investors paying taxes on income earned by the AIF on a flow-through basis. There is no separate tax regime for Category III AIFs.

- Offshore funds investing in India pay tax at the Fund level (India does not extend the pass-through principles to such offshore Funds). There is a separate tax regime for FPIs that broadly provides for the following:

  - Tax on listed shares at the rate of 10% or 15% (depending upon long term or short term) and at the rate of 10% or 30% for other securities

  - Tax on dividends and interest at the rate of 20% (except for interest on certain securities that is taxable @ 5%)

Where FPIs are investing from jurisdictions with whom India has signed Double Taxation Avoidance Agreements (DTAAs), such FPIs may be eligible for lower rates of taxation such as the following:

  - DTAAs with certain countries such as the Netherlands, France and Sweden provide for exemption on capital gains on sale of shares in Indian companies.

  - DTAAs with more common Fund jurisdictions such as Singapore, Ireland and Mauritius provide for tax exemption on capital gains on the sale of securities other than shares including debt securities, mutual fund units, etc.

  - Most DTAAs provide for concessional tax rate of 10%/ 7.5%/ 5% on dividend and interest income.

- With respect to tax residency, the ITA seeks to tax Indian residents on global income and non-residents on India-sourced income. This principle needs to be slightly modified in the context of the IFSC. While the IFSC is regarded as an offshore jurisdiction from an exchange control perspective, from a tax perspective, it is still regarded as a part of India. This necessitates a requirement for providing tax concessions in the ITA through separate exemption provisions to compete with prominent international jurisdictions.

- The current tax regime has several concessions for IFSC constituents, including the following:

  - Tax exemption for gains earned by non-residents from trading in securities on IFSC exchanges;

  - Concessional tax regime for non-resident investors in a Category III AIF in the IFSC that prescribes tax rates at par with the rates in the DTAAs that India has signed with key countries and that extends the benefits available to FPIs to such AIFs;

  - Pass through tax regime for investors in Category I and II AIFs;

- 10-year ‘tax holiday’ for the investment manager in the IFSC.

IFSC’s taxation framework

- Consistent with the above principles, there has to be ‘one’ level of taxation for IFSC Funds. The manner of taxation, including timing thereof, needs a little fine-tuning as explained below.

- In the proposed regulatory framework, no distinction is sought to be made among different categories of IFSC Funds. The regime contemplates raising monies from retail investors as well. To that extent, the existing taxation framework needs to be revisited and realigned.

- The regime contemplates raising monies from both Indian residents and non-residents. It is likely that the Funds having pre-dominantly non-resident investors would be investing primarily in India and that Funds having pre-dominantly resident investors would be investing primarily outside India.

- With the above variations or scenarios, the following principles could be considered while formulating the tax regime for non-retail as well as retail funds:

  Levy and collection of tax

  - There should be one level of taxation.

  - Given the challenges in collecting tax from investors, particularly non-residents, tax could be levied and collected at the Fund level. With taxes being collected at the Fund level, there should be no further tax in the hands of investors at the time of distribution of income or redemption or transfer of units.

  Attribution of income and exemption from taxes for certain non-resident investors or income streams

  - Since the Funds would be contributory Funds, it should be possible to attribute income earned by the Fund to its investors.

  - Vis-à-vis non-resident investors, the Fund should be liable to tax in India only on income earned from Indian securities.

  - Any income accruing or arising from investment in assets and securities outside India (including in the IFSC), which would have been otherwise not taxable in India for non-resident investors but for the Fund being set up in India, should be exempted from India taxation. To that extent, the regime should be aligned to the current Category III AIF or Specified Fund taxation regime.

  - Vis-à-vis Indian securities, gains on securities other than equities, i.e., debt, derivative instruments, and SRs attributable to non-residents, should be exempted from tax in India. This is in line with the Category III AIF or Specified Fund taxation regime. Gains on equities should be chargeable to tax as per the provisions of the domestic law, though a marginally lower tax rate could be a great ‘pull’ factor.

  - Furthermore, there are certain non-resident investors that are exempt on their entire income or on certain streams of income under the DTAA that India has with such other country (such as subsidiary of Abu Dhabi Investment Authority, sovereign wealth fund, etc.). Thus, provisions to exempt gains attributable to exempt non-resident investors should also be provided under the ITA. For this purpose, reference could be drawn from the definition of ‘specified person’ as provided in Explanation 1 of section 10(23FE) of the ITA, which includes a wholly owned subsidiary of Abu Dhabi Investment Authority, sovereign wealth fund and pension fund satisfying certain conditions. A similar exemption should be provided to encourage such investors to invest in IFSC Funds. Furthermore, in case investment is made in sectors (to be specified) intended to be promoted by the IFSCA, then the gains arising on investments in such sectors should also be exempted from tax.

- Separately, income such as dividends and interest are taxed at the rate of 10% for Funds investing in India through popular Fund jurisdictions such as Luxembourg, Ireland, and Japan under the respective DTAA between India and these countries. Furthermore, interest income on REITs, InvITs, government securities and rupee-denominated bonds of an Indian company are chargeable to tax at the rate of 5% (plus applicable surcharge and cess). To keep the taxation regime for the IFSC Fund comparable with the tax regime for the Funds investing from these jurisdictions into India, the dividend and interest income could be taxable at a lower rate of 5% (plus applicable surcharge and cess), resulting in tax rates on the dividend and interest in line with the tax rates for interest on REITs, InvITs, government securities and rupee-denominated bonds of the Indian company and maintaining an effective tax rate of lower than 10%.

- Current relaxations with respect to obtaining Permanent Account Number (PAN) and filing tax returns for non-resident investors should continue.

Outbound Funds

Global income of a resident is taxable in India. Resident investors investing in offshore Funds are liable to tax only on income distributed by such Funds. To encourage the IFSC becoming a hub for overseas investments by RIs, the following variations in taxation could be considered:

- There should be only one level of tax.

- The income of the Fund should be exempted from tax, and the income distributed by the Fund should be taxable in the hands of resident investors.

- To provide an impetus to such Funds, a lower tax rate of 15% could be considered. For example, where such Funds are equity Funds, similar to the tax regime for mutual funds in India, capital gains on sale or redemption of units could be taxable @10% or 15% for long- and short-term capital gains, respectively.

- Income distributed by the Fund should be taxable at the rate of 20%.

Family Offices

To attract family offices to IFSC, the following tax concessions could be considered:

For Non-residents setting up Family office in IFSC -

The current tax regime available to non-resident investors who invest in an AIF in IFSC should be extended to non-residents setting-up family offices/ Family Investment Fund in IFSC. Any income accruing or arising or deemed to accrue or arise to a Family Investment Fund from investment in assets and securities outside India (including in the IFSC), which would have been otherwise not taxable in India but for the Family Investment Fund being set-up in India, should be exempted from India taxation. Vis-à-vis Indian securities, the tax treatment for various income streams as provided in the tax regime for Specified Funds should apply, as indicated above. The share of resident family members should be taxed at applicable rates in the hands of the Fund on accrual of any income to Family Investment Fund, in proportion to their contribution.

The income being taxed at the Fund level should be exempt in the hands of the family members.

The restriction on resident Indians (other than Sponsor/ Investment Manager) being investors in a Specified Fund should not apply to a Family Investment Fund.

Similar to the current provisions, transfer of portfolio from an offshore jurisdiction to an IFSC Family Investment Fund should be made tax neutral.

For Residents setting up Family office in IFSC

To encourage family office being set-up in IFSC by Indian residents, the above principle of taxation applicable to outbound funds should be extended to Family Investment Fund in IFSC.

Transition provisions

The tax framework for Inbound Funds discussed above (Fund level taxation) varies from the current framework prescribed for Category I and II AIFs (pass through taxation). Even for Category III AIFs, the current framework, which provides certain exemptions to Specified Funds, will require significant amendments/ updates to the tax law given the changes proposed in the regulatory framework. As regards Outbound Funds, the tax framework would have to be newly incorporated in the law.

Given the significant changes proposed to the regulatory framework, it would be important to align the existing tax regime to the new framework without creating any ambiguity or disruption for existing Funds. Also, since regulations and tax law are so intertwined, it would be imperative to have the tax regime ready i.e., enacted/ notified so that new regime can be operationalised without any delay and FME/ Funds can be authorised as soon as the regulations are notified. Towards that end, the following suggestions could be considered:

- The IFSCA and the Revenue authorities need to work in tandem for the new Fund regime to be successfully notified and operationalised.
- Once the regulatory framework is being finalised by the IFSCA, it would be advisable to discuss the proposed changes with the Revenue authorities upfront so that their inputs can be obtained and the ball on the tax legislation can set rolling.
- The Revenue authorities should announce the tax framework, including the contours of the amendments to the tax law, provisions for grandfathering of existing funds, referencing changes, etc. along with the roadmap for enactment thereof.
- Depending upon the timing of the notification of the new Fund regime, tax laws should be amended at the first available opportunity to enact them (either through amendment Bills or an ordinance, if required as adopted for enactment of the Specified Fund regime).

Taxation of dividends distributed by FME

There should not be any tax on dividends distributed by an IFSC FME, especially to their non-resident shareholders. This is similar to the tax regime in popular Fund jurisdictions such as Singapore. Resident shareholders should be taxed on such dividends @15%, at par with the regime for taxation of dividends from offshore subsidiaries.

13. Proposed changes in other Regulations

For the Fund regime to be successful, certain amendments are required to ensure ease of set up or doing business in IFSC and to ensure that the tax and regulatory regime in the IFSC is comparable to the global asset management hubs. Some of the 'asks' have been provided hereunder:

RBI

1. **Outbound approvals for Indian Fund Managers to set up IFSC entities or make skin-in-the-game contribution**

   Any FI or branch of a FI set up in the IFSC is treated as a 'person resident outside India' for foreign exchange control purposes. Accordingly, setting up a Manager in the IFSC requires compliance with the FEMA (Transfer or Issue of any Foreign Security) Regulations, 2004 (ODI Regulations). Where an Indian party does not satisfy the conditions stipulated under regulation 7(1) of the ODI regulations, an approval is required from the RBI under regulation 9 of the ODI regulations.

   Such approvals may cause delay in commencing operations in the IFSC. While the IFSC entities are treated as persons resident outside India, for all practical purposes, the entities in the IFSC are situated within India only.

   Recommendation

   Setting up of the FME and investment of skin-in-the-game contribution should be brought under the automatic route, irrespective of meeting any conditions, to improve 'ease of doing business' and to reduce the time frame to set up investment structures in the IFSC. These should also not require SEBI approval.

2. **Enhancement of limit under Liberalised Remittance Scheme ('LRS')**

   Resident individuals can invest outside India under the LRS. Under the LRS, a resident individual could invest up to USD 250,000 outside India in a financial year in permissible investment avenues under the scheme.

   Recommendation:

   A "game-changing" provision to attract family offices in IFSC should be to increase the limit to say, USD 5 million. The rationale for the same is as follows:

   Currently, India's foreign exchange reserves position is quite strong. In fact, there are discussions happening on capital account convertibility. Indians remitting funds to intermediate jurisdictions abroad increase the economic activities of such offshore jurisdictions. Funds remitted to family offices set-up in IFSC increase economic activity in India which, after considering a multiplier effect, could greatly benefit both, the Indian economy, and the exchequer. Further, family offices in IFSC are within the purview of an Indian regulator. Thus, there is merit in allowing an enhanced LRS limit. Also, higher remittances (> USD 5 million per person) may be allowed by the RBI on a case-by-case basis with conditions prescribed.

3. **Amendment in Outbound Investment regulations**

   Establishing a Family Investment Fund in IFSC by a resident entity (other than an individual) would fall within the ambit of 'Financial Services Sector' under the Direct Investment by Residents in Joint Venture/ Wholly Owned Subsidiary Abroad - Master direction issued by RBI (ODI guidelines).

   ODI guidelines prescribe certain conditions which need to be satisfied by an Indian entity to make outbound investment under automatic route i.e., without obtaining an approval from RBI. These include three-year profitability track record, obtaining approval from the Financial Services regulator in both, India and abroad, etc.

Recommendation:

To encourage setting-up of family offices in IFSC, the same should be brought within the ambit of "automatic route" requiring approval of the IFSCA only as the regulator. As mentioned above, remittances under LRS in excess of certain limits should require prior approval from the RBI.

SEBI

4. Higher limits for allowing NRIs to invest in IFSC Funds registered as FPIs

As per the FPI operating guidelines, contribution of a single NRI or Overseas Citizen of India (OCI) or RI shall be below 25% of the total contribution in the corpus of a Fund, and the aggregate contribution of all NRIs or OCIs shall be below 50% of the total contribution in the corpus. These restrictions are applicable for Funds investing in India from abroad or from the IFSC.

NRI or OCI investment could constitute a significant pool of money for capital markets. NRIs or Person of Indian Origin (PIO) have shown great interest in investing monies through the IFSC. Furthermore, NRIs or PIOs are allowed to invest in domestic Category III AIFs without any investment caps. Placing such restrictions on NRI or OCI investments would restrict the overall capital-raising capabilities of a Fund investing in India.

Recommendation

Single or aggregate investment limits by the NRI or OCI into Funds in the IFSC should be relaxed.

5. Relaxation for managing IFSC Funds under Regulation 24(b) of SEBI (Mutual Fund) Regulations, 1996

Regulation 24(b) of the SEBI (Mutual Fund) Regulations, 1996, read with clause 2(i)(b) of the SEBI circular dated 16 December 2019, permits an asset management company to manage or advise only the specified categories of FPIs. The specified categories do not include domestic AIFs investing from the IFSC.

Fund set up in the IFSC would also be registered as an FPI. As a result, an asset management company will not be able to advise or manage a Fund set up in the IFSC, unless the Fund ensures, on a continuous basis, that more than 50% of its units are held by the prescribed category of investors such as Government or Government-related entities, pension funds, insurance or reinsurance entities, banks, and mutual funds. This would be very unlikely and would require the FPI to restrict their investor base to the above specified category of investors that will keep out large investors such as family offices, endowments, and university funds.

Recommendation

Specific exemption or relaxation from the above condition would be required for the Fund set up in the IFSC registered as an FPI.

CBDT

6. Section 9A of the ITA (safe harbour provisions) amendments for IFSC

Many jurisdictions such as London, Singapore and Hong Kong have a safe harbour regime, which basically provides that the Fund will not be subject to tax in that country merely because the Fund Manager is located there.

The Indian tax regime also provides safe harbour regime in the form of section 9A of the ITA. The said section was introduced to encourage management of offshore funds from India. The Portfolio manager in the IFSC would also be required to seek an approval under the safe harbour regime to manage offshore funds to avoid tax residency or business connection risk in India for such funds.

However, no such conditions are applicable if offshore funds are managed overseas by the overseas fund manager. Additionally, the safe harbour conditions assume that only Funds are managed from India and not corporate entities; hence, the conditions laid down under the regime may not be satisfied by a corporate entity. Furthermore, the conditions applicable for availing the safe harbour regime are very stringent and onerous.

Recommendation

There should a separate safe harbour regime for IFSC Fund Managers that are managing offshore funds directly from the IFSC, comparable to the Funds managed in overseas jurisdictions. The benefits of the safe harbour regime should be available without satisfying any conditions.

Also, Family Investment Funds which are set-up by non-residents should be permitted to invest in India in accordance with FDI and FPI norms. Considering that some family members could be residents of India, a “safe harbour” should be provided to such Funds from a regulatory/ round-tripping perspective so long as the total contribution of resident Indians is not more than 5% of the corpus of the Fund

Government of India

7. Exemption from applicability of stamp duty for Funds/ Schemes in IFSC

As per the Indian Stamp Act, 1899 and the Amendments made to it thereafter, stamp duty is applicable on the issuance or transfer of privately placed AIF units (including for an AIF in the IFSC) at prescribed rates.

A specific exemption from stamp duty has been provided for transactions undertaken on the IFSC exchange and depositories established in the IFSC. However, there is no specific exemption from stamp duty for units issued and transferred by an AIF in the IFSC.

It is pertinent to note that in similar International Financial Centres in Dubai or Hong Kong, there is no stamp duty. Furthermore, as per the FAQs on the Indian Stamp Act, 1899, redemption of mutual fund units is not subject to stamp duty on the basis that the same is not a transfer or an issue or a sale. However, the FAQs are silent on the non-applicability of stamp duty on the redemption of units of Fund in the IFSC.

Recommendation:

To provide parity with transactions undertaken on the IFSC exchange and other foreign jurisdictions, stamp duty should not be applicable on unlisted securities, inter alia, privately placed Fund units, upon issue or transfer or redemption in the IFSC.

8. Other recommendations: relevant regulator

- **Domestic FIs such as insurance companies to be permitted to invest by IRDA**

  To promote Investment Funds in IFSC, Domestic FIs should be permitted to invest in the units of an such schemes in the IFSC without any limits and without obtaining any prior approval from any Regulator. For instance, insurance companies should be permitted to invest in the units of such schemes, without obtaining any approval from the Insurance Regulatory and Development Authority (IRDA).

- **EPFO to recognise and permit investments in IFSC Funds**

To promote Investment Funds in IFSC, Employees' Provident Fund Organisation (EPFO) should recognise and permit investments in the units of a scheme launched by FME in the IFSC without any limits and without obtaining any prior approval from any regulator.

- **Indian banks and their subsidiaries to be permitted to invest in IFSC Funds**

  To promote Investment Funds in IFSC, Indian banks and their subsidiaries should be permitted to invest in the units of Investment Funds in the IFSC without any limits and without obtaining any prior approval from any regulator.

- **Funds registered in the IFSC to obtain the same benefits as extended to mainland funds**

  Funds/ Schemes registered with the IFSCA should be entitled to all the benefits available to the AIFs/ MFs set up in mainland India and are registered with the SEBI. For instance, the exemption available to the AIFs/ MFs in mainland India from Significant Beneficial Ownership filings under the Companies Act, 2013 should be extended to IFSC funds as well. Similarly, exemption available to the mainland AIFs from the pre-IPO lock-in period should be extended to the AIFs in the IFSC as well

14. Other Fund structure

Variable Capital Company

A VCC form of a structure is now widely accepted as the preferred form of entity to raise monies from investors. A Committee constituted by the IFSCA has already submitted its report on the VCC regime. Consistent with its aspirations for a 'best-in-class' regime, the IFSCA should actively work towards implementing the suggestions of that Committee.

Limited Partnership

Furthermore, the LP structure is also a widely recognised structure and has several benefits as compared to an LLP structure. An LP structure is a partnership made up of two types of partners — General Partner and Limited Partner. The General Partner oversees and runs the business while the Limited Partners do not partake in managing the business. Usually, the General Partner of a limited partnership has unlimited liability, and Limited Partners have limited liability up to the amount of their investment. The IFSC should also consider the LP form of structure, as it is a widely known and accepted structure across the globe.

15. Annexures

Annexure A

A comparative analysis of key aspects of the Fund regime in various jurisdictions and the proposed IFSC Fund regime is tabulated below:

Particulars	Retail/ non-retail	Jurisdictional analysis			
		Singapore	Luxembourg	Mauritius	Proposed regime in IFSC
Is the Fund Manager registered with the Regulator		Yes	Yes	Yes	Yes
Types of Funds managed by FMEs	Retail	Authorised Scheme	• Regulated Retail Fund covering UCITS governed by the UCI Law • Unregulated Retail Funds covering unregulated AIFs fulfilling certain specific conditions	• Retail CIS	Retail Schemes offered to all investors (including retail investors)
	Non-Retail	• Restricted Scheme • Exempted Scheme	• Specialised Investment Funds • Reserved Alternative Investment Funds • Investment companies in risk capital • Unregulated AIFs	• Professional CIS • Expert CIS • Specialised CIS	Restricted Schemes offered on a private placement basis to accredited investors or investors investing above a specified threshold
Underlying Investors	Retail	All types of investors including retail investors	All types of investors including retail investors	All types of investors including retail investors	All investors (retail as well as non-retail)
	Non-Retail	Accredited or qualified investors	Professional investor	• Sophisticated Investors • Investors making an initial investment for	Accredited investors or investors investing above the specified threshold

Particulars	Retail/ non-retail	Jurisdictional analysis			
		Singapore	Luxembourg	Mauritius	Proposed regime in IFSC
				their own account exceeding USD100,000	
Minimum net worth for FME	Retail	CIS: ~USD 740,000 (SGD 1,000,000) Non-CIS: ~USD 370,000 (SGD 500,000)	~USD 145,000 (Euro 125,000)	~USD 23,000 (Mauritian rupee 1m)	Registered FME – Retail USD 1,000,000
	Non-Retail	~USD 185,000 (SGD 250,000)	~USD 350,000 (Euro 300,000)		Authorised FME USD 75,000 Registered FME – Institutional USD 500,000
Legal Structure of the FME	Retail	Company or Branch (also permitted)	Company, LP	Company	Company or Branch
	Non-Retail				Company or its subsidiary, LLP, LP structure or branch thereof
Sponsor contribution	Retail/ Non-Retail	No such condition	No such condition	No such condition	Close-ended Fund – lower of 2.5% of the corpus of the Fund or USD750,000 Open-ended Fund – lower of 5% of the corpus of the Fund or USD1,500,000 (waiver subject to fulfilling certain conditions)
Appointment of a custodian	Retail	Required	Required	Required	Required
	Non-Retail	Required (except in case of a VCF)	Required (except in case of an Unregulated AIF managed by		Optional for Funds/ schemes managed by Authorised FME

Particulars	Retail/ non-retail	Jurisdictional analysis			
		Singapore	Luxembourg	Mauritius	Proposed regime in IFSC
			a registered AIFM)		
Leverage	Retail	Permissible to the extent permitted by the investment mandate. The definition and measurement of leverage as well as the circumstances under which leverage may be used to be disclosed.	Permissible (a) on a temporary basis – For an investment company - not more than 10% of its assets, or - For a common fund, not more than 10% of the value of the fund; or (b) to enable the acquisition of immovable property essential for the direct pursuit of business - For an investment company - not more than 10% of its assets, Borrowings under (a) and (b) to not exceed 15% of total assets.	Permissible on temporary basis to accommodate requests for the redemption of CIS securities. Maximum borrowing to not exceed 5% of the net assets of the CIS.	Permissible only for meeting temporary liquidity requirement up to a limit as disclosed in the offer document
	Non-Retail	Permissible to the extent permitted by the investment mandate. The definition and measurement of leverage as well as the circumstances under which leverage may be used to be disclosed.	No restrictions on borrowings by AIFs.		Permissible subject to disclosure in the offer document
Appointment of an	Retail	Required To be performed by:	Valuation of assets is made on the basis of realisable value	Optional to appoint a separate independent	Required To be performed by a

Particulars	Retail/ non-retail	Jurisdictional analysis			
		Singapore	Luxembourg	Mauritius	Proposed regime in IFSC
independent valuer		• a third-party service provider, such as a fund administrator or custodian; or • an in-house fund valuation team independent from the FME.	estimated in good faith.	valuer. However, valuation needs to be done.	• third-party service provider, such as a fund administrator or custodian; or • an in-house fund valuation team independent from the FME.
	Non-Retail	Required (except in case of a VCF) To be performed by: • a third-party service provider, such as a fund administrator or custodian; or • an in-house fund valuation team independent from the FME.	Required To be performed by: • an external valuer, that must be a legal or natural person independent from the AIF. • the AIFM itself, (subject to it being functionally independent from the portfolio management)		Required for funds managed by Registered FME - Institutional To be performed by a • third-party service provider, such as a fund administrator or custodian; or • an in-house fund valuation team independent from the FME. Optional for funds managed by Authorised FME
Investment D-diversification norms	Retail/ Non-Retail	Applicable depending on the category of fund viz. money market fund, hedge funds, capital	Applicable, depending on the category of fund	Applicable	Applicable depending on the category of the Fund/ scheme

Particulars	Retail/ non-retail	Jurisdictional analysis			
		Singapore	Luxembourg	Mauritius	Proposed regime in IFSC
		guaranteed funds, index funds, VCF and property funds			

Annexure B

IOSCO Principles for Exchange Traded Funds

Principles Related to ETF Classification and Disclosure

Principle 1: Regulators should encourage disclosure that helps investors to clearly differentiate ETFs from other ETPs.

Principle 2: Regulators should seek to ensure a clear differentiation between ETFs and other CIS, as well as appropriate disclosure for index-based and non-index-based ETFs.

Disclosure regarding ETF portfolios

Principle 3: Regulators should require appropriate disclosure with respect to the manner in which an index-based ETF will track the index it references.

Principle 4: Regulators should consider imposing requirements regarding the transparency of an ETF's portfolio and/ or other appropriate measures in order to provide adequate information concerning:

i) any index referenced and its composition; and

ii) the operation of performance tracking

Disclosure regarding ETF costs, expenses, and offsets

Principle 5: Regulators should encourage the disclosure of fees and expenses for investing in ETFs in a way that allows investors to make informed decisions about whether they wish to invest in an ETF and thereby accept a particular level of costs.

Principle 6: Regulators should encourage disclosure requirements that would enhance the transparency of information available with respect to the material lending and borrowing of securities (e.g., on related costs).

Disclosure regarding ETF strategies

Principle 7: Regulators should encourage all ETFs, in particular those that use or intend to use more complex investment strategies to assess the accuracy and completeness of their disclosure, including whether the disclosure is presented in an understandable manner and whether it addresses the nature of risks associated with the ETFs' strategies.

Principles Related to the Structuring of ETFs

Principle 8: Regulators should assess whether the securities laws and applicable rules of securities exchanges within their jurisdiction appropriately address potential conflicts of interests raised by ETFs.

Principle 9: Regulators should consider imposing requirements to ensure that ETFs appropriately address risks raised by counterparty exposure and collateral management.

Annexure C

Market Maker

A market maker, sometimes called an Authorised Participant (AP), is a broker, dealer or investment firm that plays an essential role in how an ETF trades and ensures the continued liquidity and efficient pricing of the ETFs between buyers and sellers on the exchange. Internationally, APs have an agreement with an ETF sponsor that gives it the right to create and redeem ETF shares. Market makers are tasked with providing ETF liquidity to a given market. They do so by providing units for sale on the stock exchange at asking prices, and then posting bid prices they will purchase units at, for investors wishing to sell. The bids and asks are themselves calculated based upon the underlying asset values, and the costs and fees associated with buying or selling all the underlying securities in ETF.

Global Markets mandate market maker registrations for ETFs and special category products. These registered market makers get special benefits. To avail these benefits, they must abide by the guidelines of market making in terms of liquidity, spreads, and volumes.

As in global markets, IFSC should also look at creating a separate category for Market Makers. Recognised Stock Exchanges in IFSC may provide a simplified framework for registration of IFSCA registered entities as market makers. Existing Broker Dealers or IBUs in IFSC may act as market makers. Registered Market makers must abide by the spread and volume guidelines to avail special benefits. FME can also be categorised as a Market Maker by default.

License of registered Market Makers to be renewed based on review of performance at certain predefined intervals.

Special Privileges for registered market makers:

Only market makers should be allowed to execute Direct Creation/ Redemption with the Fund.

The role of Market Makers (MMs)/ Authorized Participants (APs) in the ETF segment is capital intensive, whereas ideally the MMs role should be to provide liquidity and risk management only. As an example, against a short position for delivery of ETFs, the market maker pays cash upfront to the Fund who in turn places the order for the underlying securities against the units of ETF and effectively, the capital of the market maker is blocked for 2 working days. Hence it is recommended to allow the following:

i. Market Maker can transfer its open positions in ETF market to the Fund or any other means of netting of settlement between underlying and ETF maybe explored.

ii. Benefit of cross margining maybe extended to hedging positions taken between units of ETF and underlying basket of securities or units of ETFs and derivatives on the underlying Index

iii. Short selling in ETFs may be allowed, which is necessary to carry out market making activity

iv. Use of collateral with the Fund for direct creations/ redemptions.

Annexure D

COMPARATIVE STUDY OF INVESTOR QUALIFICATIONS IN SINGAPORE AND UNITED STATES AND KEY EXEMPTIONS AVAILABLE

I. TYPES OF NON-RETAIL INVESTORS IN SINGAPORE

Under the laws of Singapore, there are 2 main categories of non-retail investors: (1) Accredited Investors (AI) and (2) Institutional Investors. Expert investors are a special category of investors who fall in the intersection of retail investors and accredited investors owing to their specialized knowledge. The following table captures the regulatory treatment of accredited investors/ institutional investors/ expert investors. It is to be noted that the table is not an exhaustive depiction of the exemptions applicable to the following classes of investors and reference should be read in conjunction with the Securities and Futures Act, the Securities and Futures (Prescribed Specific Classes of Investors) Regulations 2005 and the Financial Advisers Regulations. Also, please note that the exemptions have been incorporated based on the data available in public domain, basis the limited research done. The Singapore legal counsel may have to be consulted for detail analysis and further discussion.

	Accredited Investors	Institutional investors	Expert Investors
1) Statutory definition	Under the Securities and Futures Act (SFA), "accredited investor"[13] has been defined as – i. An individual with: A. net personal assets exceed in value $2 million; B. whose financial assets (net of any related liabilities) exceed in value $1 million; C. whose income in the preceding 12 months is not less than $300,000. ii. A corporation with net assets exceeding $10million in value; iii. The trustee of a prescribed trust.	Among other entities, SFA defines "institutional investor"[14] to include – i. the Government; ii. a statutory board as may be prescribed; iii. an entity that is wholly and beneficially owned; iv. a central bank in a jurisdiction other than Singapore; v. the central government of a country other than Singapore; vi. a person (other than an individual) who carries on the business of dealing in bonds with accredited investors or expert investors; The definition of "institutional investor" under the SFA was amended on October 8, 2018. The definition now includes persons professionally active in the capital markets such as FIs regulated by foreign regulators and sovereign wealth funds. Statutory boards, other than prescribed statutory boards	"Expert investor"[15] includes – i. a person whose business involves the acquisition and disposal, or the holding, of capital markets products, whether as principal or agent; ii. the trustee of such trust as the Authority may prescribe, when acting in that capacity; or iii. such other person as the Authority may prescribe;

[13] Section 4A(1)(a) of the Securities and Futures Act read with regulation 2 of the Securities and Futures (Prescribed Specific Classes of Investors) Regulations 2005 and regulation 2 of the Financial Advisers Regulations.
[14] Section 4A(1)(c) of the Securities and Futures Act read with regulation 3 of the Securities and Futures (Prescribed Specific Classes of Investors) Regulations 2005 and regulation 2 of the Financial Advisers Regulations.
[15] Section 4A(1)(b) of the Securities and Futures Act read with regulation 2 of the Financial Advisers Regulations.

	Accredited Investors	Institutional investors	Expert Investors
		under the Second Schedule of the SFA, are no longer deemed to be institutional investors.	
2) Exemptions available under regulatory regime	**Securities and Futures Act** • Accredited investors are not entitled to be compensated from the fidelity fund[16], even if the Accredited investor has suffered pecuniary loss in the manner contemplated under Section 186(1)[17] of the SFC. • The issuer and/ or offeror who offers securities to an Accredited investor is exempt from the prospectus requirements under Part XIII of the SFA pursuant to the exemptions under Sections 275 and 305 of the SFA. • An accredited investor is not protected by the requirements of Section 99H(1)(c) of the SFA read with Regulations 3A(5)(C), (d) and (e) of the SFR. A conjunctive reading provides that where a principal wishes to appoint an individual as a provisional or temporary representative in respect of any SFA regulated activity, the principal is required to lodge an	Under the SFA, an institutional investor is also eligible for the similar exemptions available to accredited investors specifically under Section 274.[18] (Offer made to institutional investors) and Section 304.[19] (Offer made to institutional investors) of the Securities and Futures Act. (the exemptions are identical in their purport)	Same as accredited investors. Exemptions envisaged under both Regulations 33 & 34 are also available in the case of 'expert investors', but the scope is limited to "when making a recommendation in respect of any capital markets product".

[16] Under Part XI of the SFA, each approved securities exchange / approved futures exchange is required to establish a fidelity fund for the purpose of compensating investors who suffer losses as a result of defalcation, bankruptcy or insolvency of the members of the exchange.
[17] Section 186 sets out the circumstances under which claims can be made on the fidelity fund.
[18] Provides exemptions vis-a-vis offer of securities or securities-based derivatives contracts.
[19] Provides exemptions vis-a-vis offer of units in a collective investment scheme.

	Accredited Investors	Institutional investors	Expert Investors
	undertaking to ensure that (i) the provisional or temporary representative is accompanied at all times by an authorized person when meeting any client or member of the public, (ii) he sends concurrently to an authorized person all electronic mail that he sends to any client or member of the public and (iii) he does not communicate by telephone with any client or member of the public other than by telephone conference in the presence of an authorized person. **Securities and Futures (Licensing and Conduct of Business) Regulations** • An Accredited Investor may receive advertisements or publications referring to an offer of securities. Restrictions on advertisements under Section 251, 300 SFA do not apply to an accredited investor. • AIs are exempted from treatment as a retail investor; therefore, they can enter into "principal-agent" relationship with financial intermediaries. • An accredited investor is not entitled to statutory disclosures in the manner provided under Regulation 47E of the SFR.		

	[Accredited Investors]()	[Institutional investors]()	[Expert Investors]()
	Under Financial Adviser Act Regulations • Offerors of investment product are not under any statutory obligation to provide accredited investors with all material information on any designated investment product in the prescribed manner. (Regulation 33) • Financial Adviser is not under any statutory obligation to ensure they have regard to the AI's investment objectives, financial situation, and particular needs. (Regulation 34)		

[**Note**: The exemptions discussed above apply to persons dealing with accredited investors/ institutional investors/ expert investors. Accordingly, an exempt person is required to conduct its own due diligence to verify that its clients are of accredited/ expert/ institutional status. In addition, an exempt person dealing with accredited investors (AIs) needs to obtain the investors' opt-in (i.e., consent) to be treated as an AI, and maintain the relevant opt-in documentation for such investors. Exempt persons are also expected to monitor if an investor continues to meet thresholds for accredited/ expert/ institutional investors.]

II. QUALIFIED INVESTOR IN SINGAPORE

A Qualified Investor generally refers to an accredited investor, a collective investment scheme (CIS) offered in Singapore only to accredited and/ or institutional investors, a closed-end fund offered to an accredited and/ or institutional investors, an institutional investor, or a limited partnership comprising solely of partners who are accredited and/ or institutional investors.

Qualified investor has been defined under Regulation 5(3) of the Securities and Futures (Licensing and Conduct of Business) Regulations, 2018 –

“qualified investor” means —

(*a*)			an accredited investor, other than —
	(i)		one who is a participant in a collective investment scheme
	(ii)		one who is a holder of a unit in a closed-end fund or in an arrangement
	(iii)		one which is a corporation –
		(A)	which is related to or controlled by a person exempted from the requirement to hold a capital markets services license to carry on business in fund management under paragraph 5(1)(*i*), or a key officer or substantial shareholder of such person; and
		(B)	the shares or debentures of which are, after 28 May 2008, the subject of an offer or invitation for subscription or purchase made to any person who is not an accredited investor; or
	(iv)		a corporation or an entity which is a collective investment scheme or a closed-end fund the units of which are, the subject of an offer or invitation made to any person who is not an accredited investor;
(*b*)			a collective investment scheme the units of which are the subject of an offer or invitation for subscription or purchase made —
	(i)		in Singapore only to accredited investors, to institutional investors, or to both accredited investors and institutional investors; or
	(ii)		such offer or invitation is made only to accredited investors (or investors in an equivalent class under the laws of the country or territory in which the offer or invitation is made), to institutional investors, or to both accredited investors and institutional investors;
(*c*)			a closed-end fund or an arrangement the units of which are the subject of an offer or invitation for subscription or purchase made only to accredited investors, to institutional investors, or to both accredited investors and institutional investors;
(*d*)			an institutional investor, other than a collective investment scheme; or
(*e*)			a limited partnership, where the limited partners comprise solely of accredited investors, of institutional investors, or of both accredited investors and institutional investors;

Relaxation Persons carrying on business in fund management on behalf of qualified investors are exempted from the requirement to hold capital markets services license to deal in capital markets products that are securities, units in a collective investment scheme or specified exchange-traded derivatives contracts, provided that there are at least 30 such qualified investors, and of which not more than 15 are collective investment schemes, closed-end funds, or limited partnerships and which is registered with the MAS as registered fund management company and the registration is and continues to be published on the MAS's website.

III. TYPES OF NON-RETAIL INVESTORS IN UNITED STATES

The following table captures the differing regulatory treatment of accredited investors, qualified purchasers, and qualified client. For a full and complete understanding, please refer to relevant statutes mentioned below as all of these definitions have been summarized for the sake of brevity. Please note that the exemptions have been incorporated based on the data available in public domain, basis the limited research done. The US legal counsel may have to be consulted for detail analysis and further discussion.

	Accredited Investor	***Qualified Purchaser***	***Qualified Client***
1) Statutory definition	According to Rule 501(a), Rule 215 and Rule 144A of the Securities Act, accredited investor also includes: • Natural persons qualified as Accredited Investor based on certain professional certifications, designation or credentials or credentials issued by an accredited educational institution; • With respect to investments in a private fund, natural persons who are knowledgeable employees of the fund; • LLCs with $5 million in assets may be AI, SEC- and state registered investment advisers, exempt reporting advisers, RBICs; • Family offices with at least $5 million AUM and family clients, as defined under Investment Advisers Act; • Spousal equivalents.[20] An individual will qualify as 'accredited' if they meet the Rule's joint income or net worth thresholds together with their "spousal equivalent".	For purposes of the Investment Company Act of 1940, Qualified Purchaser generally includes: • Any natural person who owns not less than $5 million in investments; • Any company that owns not less than $5 million in investments; • Any person, who in the aggregate owns and invests on a discretionary basis, not less than $25 million in investments; • Any qualified institutional buyer; • Any company, if each beneficial owner of the company's securities is a qualified purchaser; • Any natural person who is deemed to be a "knowledgeable employee" of a Section 3(c)(7) fund; • Certain persons who receive securities in a Section 3(c)(7) fund from a qualified purchaser as a gift, bequest, or due to certain other involuntary events.	For the purposes of the Investment Advisers Act, a client is considered a qualified client if (i) it has at least $1.1 million in assets under management with the applicable investment adviser immediately after the time of its initial investment (**Assets-Under-Management Test**) or (ii) the investment adviser reasonably believes, immediately prior to the time of the client's initial investment, that the investor has a net worth of more than $2.2 million (**Net Worth Test**). ***A qualified client also includes both a "qualified purchaser", and an investment adviser's "knowledgeable employees." Since the net worth threshold for a qualified client is higher than for an accredited investor, all qualified clients are, by definition, also accredited investors.***

[20] The spouse of an 'accredited investor' is permitted to pool his/her finances in order to qualify as accredited investors.

	Accredited Investor	*Qualified Purchaser*	*Qualified Client*
		A qualified purchaser is also an accredited investor. However, not all accredited investors are qualified purchasers as it is much difficult to meet fulfil the thresholds under ICA to be an eligible qualified purchaser.	
2) Exemptions	**Offers, sale and resale of securities** **Section 4(a)(2)** Securities being offered to Accredited Investor (not being a public offering), do not need to be registered nor does it require circulation of a prospectus. **Exemption for non-SEC Reporting companies - Rule 506(b) of Regulation D** Companies conducting an offering under Rule 506(b) can raise an unlimited amount of money and can sell securities to an unlimited number of accredited investors and up to 35 non-accredited as long as they meet certain sophistication requirements. **General Solicitation of restricted securities – Rule 506 (c)** Issuers of restricted securities[21] are permitted to broadly solicit and generally advertise to accredited investors, subject to certain conditions mentioned in Regulation D. "Restricted securities" are previously-issued securities held by security holders that are not freely	**Exemption for Funds with Qualified Purchasers** A private fund, hedge fund, or VCF that exclusively accepts qualified purchasers as investors and does not plan to make an initial public offering qualifies for the 3(c)(7) exemption under the Investment Company Act of 1940 (the "ICA"). (i) Exemption from on-going disclosure requirements; (ii) Exemption from issuing prospectus; ***An accredited investor will be eligible for the above exemption if it also qualifies as a qualified purchaser.***	**Exemptions under Advisers Act** Rule 205-3 of the Advisers Act provides a limited exemption from the performance compensation prohibition and permits investment advisers to receive performance-based compensation (incentive allocations, carry, carried interest, performance fee etc.) from "qualified clients." ***Accredited investors qualifying as qualified purchasers will also be able to avail the exemption under Advisers Act.***

[21] Rule 144(a)(3) identifies what sales produce restricted securities.

	Accredited Investor	Qualified Purchaser	Qualified Client
	tradable. They are acquired in unregistered, private sales from the issuing company or from an affiliate of the issuer. Investors typically receive restricted securities through private placement offerings, Regulation D offerings, employee stock benefit plans, as compensation for professional services, or in exchange for providing "seed money" or start-up capital to the company. **Regulation Crowdfunding (JOBS Act)** Accredited investors may invest an unlimited amount in an offering under Regulation Crowdfunding subject to the maximum amount a company can raise each year.[22] **Exemption from registration of public offerings– Regulation A** Regulation A has two offering tiers: Tier 1, for offerings of up to \$20 million in a 12-month period; and Tier 2, for offerings of up to \$75 million in a 12-month period. For offerings of up to \$20 million, companies can elect to proceed under the requirements for either Tier 1 or Tier 2. There are investment limitations for offerings under Tier 2 if the securities offered are not going to be listed on a national securities exchange upon qualification.		

[22] 12 month fund-raising limit – $5 million; For Reg A+ exemption companies – $75 million. (Reg A+ refers to an exemption that allows small companies to sell their shares to the general public, making it possible for almost anyone to invest in a business through crowdfunding. It enables startups and crowdfunding platforms to raise money from both accredited and non-accredited investors – for the public to invest in private companies.)

	Accredited Investor	Qualified Purchaser	Qualified Client
	Investors either must be an accredited investor or are limited in how much they can invest to no more than 10% of the greater of the person's annual income or net worth.[23]		

[23] Companies relying on a Regulation An exemption can offer and sell their securities to the public under two different Tiers – Tier I & Tier II. There are investment limitations for offerings under Tier 2 if the securities offered are not going to be listed on a national securities exchange upon SEC qualification. If not 'accredited investors', there is a limit imposed on the amount of investment

Annexure E

BROAD PARAMETERS GOVERNING PASSPORTING ACROSS CERTAIN KEY REGIMES

A) ELIGIBILITY CRITERIA FOR OBTAINING PASSPORT				
	AIFMD	**HK MRF**	**ASEAN CIS**	**ARFP**
1) Regulating operators	Managers of alternative investment fund (*Article 1*), with fund being appropriately regulated at national level (*Para 10, Recitals*).	Management firms of compliant funds in mainland China ('Recognised Mainland Funds') *Para 1 r/ w para 7(b) of the Circular on Mutual Recognition of Funds (MRF) between the Mainland and Hong Kong* (Circular)	Qualifying CIS operators from Singapore, Malaysia and Thailand. (*Section 1 of Part I of the Standards of Qualifying CIS*)	Qualifying fund operators from Australia, Japan, South Korea, New Zealand, Thailand. *Para 4.1(k) r/ w para 10 of the Memorandum of Cooperation (*MOC*)*
2) Retail investors	The focus of AIFMD is regulating the marketing of AIFs to professional investors[24] in the EU.[25] *(Article 32, 43 r/ w Para 71 of Recitals)*	Retail SFC-authorized Approved Pooled Investment Funds offered to the public in Hong Kong (APIFs) are qualified as Recognised Mainland Funds. (Response of Securities and Futures Commission to *FAQs on Mainland-Hong Kong Mutual Recognition Framework*)	Both institutional and retail investors are allowed to invest in ASEAN CIS without limitation imposed at personnel/ individual level. (*Handbook for CIS Operators of ASEAN CISs*)	Fund managers are permitted to make offerings to retail investors. *(Para 4.1(k) of MOC)*
B) APPLICATION PROCESS FOR OBTAINING PASSPORT				
1) Involvement of domestic regulator/ regulation	EU AIFM, unless exempted, will need to obtain authorisation from	Fund offered in the public markets of Hong Kong, while being	Home regulator assesses suitability for cross-border	Fund must be registered in home country as a passport fund. (*Part 6 of Annex*

[24] Under the AIFMD, a 'professional investor' means an investor which is considered to be a professional client or may, on request, be treated as a professional client within the meaning of Annex II to Directive 2004/39/EC Markets in Financial Instruments Directive 2 (MIFID II). A Professional Client under MIFID II generally covers professionals in the finance industry, large corporate undertakings, government bodies and those that are eligible to elect to be considered a Professional Client.

[25] However, each member state may, at its discretion, permit marketing of AIFs to retail investors in accordance with local laws.

	home regulator. (*Article 6*)	established, managed, and operated in accordance with laws of mainland China. (*Para 2(b) r/ w 7(a) of the Circular*)	distribution. (*Section 4, Assessment of Qualifying CIS*)	*2 "Modification & Exemptions" in MOC*)
2) Process of authorisation	• Streamlined authorisation process, OR • Notification of national competent authorities.[26] (*Article 7*)	A Recognised Mainland Fund is generally deemed to have complied in substance with the relevant SFC requirements and will enjoy a streamlined process for the purpose of authorisation in HK. (*Para 3 of the Circular)*	Streamlined authorisation process: (i) Obtaining approval of Home Regulator, (ii) submitting approval of Home Regulator along with offering documents to Host Regulator for assessment, and (iii) lastly, appointing local intermediaries for distribution of the ASEAN CIS to the public. (*Handbook for CIS Operators of ASEAN CISs*)	Streamlined authorisation process. (i) Eligible fund manager makes an application to Home Regulator to register a passport fund, (ii) Home Regulator verifies compliance with domestic laws, (iii) Manager forwards its original application together with disclosure documents to Host Regulator (iv) Upon clearance by Host Regulator, the fund manager activates distribution channels. (*Paragraphs 4, 5, 6 – Annex 2, Common Regulatory Arrangements, MOC*)
3) Exemptions	• Intra-group exemption for AIFMs managing funds whose investors are the same AIFMs/ their parent or subsidiary entities (*Article 3(1)*) • De-minimis exemption for managers of small funds (small AIFM) (*Article 3(2)*)	No specific list of exemptions has been identified.	No specific list of exemptions has been identified.	Passport regulator endowed with wide discretion to exempt passport fund from passport rules.

[26] The marketing passport allows AIFs, which have been authorised by the NCA in an EU Member State, to be marketed in other EU Member States on a cross-border basis without the need for full authorisation. See, "*Notification frameworks and home-host responsibilities under UCITS and AIFMD*," ESMA Thematic Study among National Competent Authorities. Available on: https://www.esma.europa.eu/sites/default/files/library/esma34-43-340_final_report_on_thematic_study_on_notification_frameworks.pdf.

<table>
<tr><th colspan="5">C) <u>REQUIREMENTS OF THE FUND AND/ OR THE MANAGEMENT FIRM</u></th></tr>
<tr>
<td>1) .</td>
<td>• Ability of the AIFM to comply with the requirements of AIFMD
• Ability to meet initial capital requirements
• Persons conducting the business of the AIFM are of sufficiently good repute and experience
• Qualifying Shareholders[27] are suitable, taking into account the need to ensure sound and prudent management of the AIFM
the head and registered offices of the AIFM are located in the same EU Member State. (Article 8)</td>
<td>• Fund must have been established for more than 1 year
• Fund size not less than RMB 200 million (or equivalent in a different currency)
• Fund must not invest primarily in HK
• Value of shares/ units sold to investors in HK shall not exceed 50% of total assets of the fund.
• Investment management function remains on home country
• Must appoint a host country representative (Para 7, 8, 12, 13 of the Circular).
<u>Management firms</u> must qualify following requirements be:
(i) registration with CSRC,
(ii) must not have been subject to regulatory action in the past 3 years, and
(iii) should not delegate management functions</td>
<td>• Trustee/ fund supervisor must meet certain qualification requirements relating to prudential regulation, capital adequacy, independence from CIS Operator, etc.
• CIS Operator must have track record of min. 5 years.
• CIS Operator must have min. USD 500M of assets under management globally.
• CIS Operator is subject to capital adequacy requirement of up to USD 1M.
CIS Operator licensed/ registered with Home Regulator seeking to offer Qualifying CIS –
• Must have sufficient infrastructure, technical human resources, risk management tools, internal control system, conflict of interest resolution policy, etc.</td>
<td>• Operator of a passport fund must have officers with relevant qualifications and a track record of 5 years.
• Operator of a passport must meet financial resources test
• Operator must be licensed with Home Regulator
(Para 6, Part 3 of Annex 3. Qualifications of Officers under "The Operator of a Fund")</td>
</tr>
</table>

[27] Shareholders who have 10% or more of the capital or voting rights in the AIFM or the ability to exercise a significant influence over management of the AIFM ("Qualifying Shareholders").

		outside mainland China (*Para 8, 9, 10 of the Circular).*	• CIS Operator as well as its directors, chief executive officer (CEO), key executive officers, fund managers, and substantial shareholders must be "fit and proper." (*Section 1 - Qualifications of CIS Operator/ Manager/ Management Company, Standards of Qualifying CIS*).	
2) Appointment of representative in host jurisdiction	• Non-EU AIFMs selling funds in Europe are required to appoint a ***legal representative*** in the member state where the fund is being marketed. *(Article 37(3))* • The legal representative is a natural person who acts on behalf of such non-EU AIFM vis-à-vis the authorities, clients, bodies and counterparties to the non-EU AIFM in the Union with regard to the	Each Recognised Mainland Fund must appoint a firm in HK as its representative. (*Para 12, Circular on MRF*)	• Qualifying CIS Operator must make arrangements to distribute the ASEAN CIS through local intermediaries licensed or regulated in the Host Jurisdiction. • Although not compulsory, Host Regulator may require the Qualifying CIS Operator of the ASEAN CIS to appoint a local representative who is regulated by or acceptable to the Host	• The Host Economy may or may not require appointment of a local representative.28 (MOC, Annex 1, Para 2(1)(e))

[28] Under Thai law, in order to offer the ARFP Passport Fund in a host jurisdiction, the foreign Operator of a passport fund is required to appoint a local licensed intermediary(ies) who is authorised by the regulator of the host jurisdiction. Local licensed intermediaries/distributors and local representative can be the same entity. Responsibilities of the local representative are to facilitate the following in the host jurisdiction: disclosing and delivering the ARFP Passport Fund's disclosure documents; liaising with the registrar of the ARFP Passport Fund on behalf of the unit holders; and receiving notices, orders, summons or any other documents on behalf of the operator or its ARFP Passport Fund. (*See*, SEC Ann. No. Tor Thor. 8/2561 SEC Ann. No. Tor Thor. 8/2561)

	non-EU AIFM's obligations under this Directive. *(Article 4(u))*		Regulator. (*ASEAN CIS Handbook*)	
D) ONGOING REQUIREMENTS				
Operating conditions, reporting obligations	• Home regulator rules generally apply • Ongoing reporting requirement in home jurisdiction (for authorised AIFMs) (*Article 22*) • Ongoing reporting in host jurisdiction for unauthorised, registered AIFMs. (*Article 22*)	• Home jurisdiction rules generally apply unless it relates to sale and distribution. • Breach of mainland laws of CSRC to be reported to SFC by management firm *(Para 20, 21 – Circular on MRF)*	• Home regulator rules generally apply • Ongoing reporting in host jurisdiction by home regulator: (i) monitoring portfolio, (ii) risk assessment, etc. • Breach of investment restrictions prescribed under regulations of Home Regulator to be reported to Host Regulator	• Assets are managed in accordance with home economy laws, unless it relates to disclosure and distribution. (*Para 3, Part 2 of Annex 2 Common Regulatory Arrangements*) • Ongoing reporting to both economies. • Breach of law of another economy has to be reported (*Para 12, Part 4 – Accountability (Annex 3))*