# CONSULTATION PAPER ON HANDLING OF CLIENT FUNDS FOR PORTFOLIO MANAGEMENT SERVICES IN IFSC

## A. Background of Portfolio Management Services in IFSC

1. The IFSCA (Fund Management) Regulations, 2022, inter alia, provide that a Fund Management Entity (FME) registered with IFSCA as a Registered FME (Non-Retail) or as a Registered FME (Retail) may provide Portfolio Management Services (PMS) in IFSC.

2. PMS were previously governed under IFSCA (Capital Market Intermediaries) Regulations, 2021, wherein any entity desirous of offering PMS in IFSC was required to seek registration as a Portfolio Manager from IFSCA. However, with a view to dispense with the requirement of seeking multiple registrations for undertaking different types of fund management related activities in IFSC, PMS were subsumed under IFSCA (Fund Management) Regulations, 2022.

3. Chapter VI of IFSCA (Fund Management) Regulations, 2022 ("Regulations") provides for the regulatory framework for PMS in IFSC.

## B. Present requirement for handling of client funds for PMS in IFSC

1. Among the other requirements prescribed for PMS, Regulation 77, titled – "Dealing with Client Funds", provides the following under sub-regulation (2):

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

2. The said regulation requires the FME to pool its PMS clients' funds in a bank account maintained by it in an IFSC Banking Unit and therefrom make the investments on behalf of the PMS clients.

3. The ability to pool clients' funds in a dedicated bank account offers operational convenience to the FME as it is required to manage only a single bank account for all investments and maintain the records thereof. While operationally convenient, certain limitations of the present requirement have been observed, as discussed in subsequent paragraphs.

## C. Limitations of present requirement

1. The limitations or challenges of the present requirement are listed below:

**a. Requirement of pooling of funds**

Some clients, while desirous of availing PMS of an IFSC based FME, are reluctant to part with their money until an order is placed by the FME for deployment of funds. While this reluctance has been highlighted for the institutional clients, individual clients could also be unwilling to transfer their funds to a FME's pool account for the purpose of availing PMS from the FME.

**b. Jurisdiction-specific restrictions for investments**

Foreign investors investing in India are generally required to open a separate bank account for investments in India. Therefore, such investors, if desirous of availing PMS of an IFSC based FME, would be constrained as they would not be able to pool their funds in the FME's bank account in IFSC, as per the present requirement. The presence of similar requirement of having a bank account in the same jurisdiction for investment may be pertinent for other foreign jurisdictions as well.

2. The possible solution to the limitation posed by the present requirement is to clarify that the clients may maintain separate bank accounts and the FME may obtain authorisation from clients on their bank accounts. This shall not only align with the requirement of segregating each clients' funds from the FME's own funds as required under regulation 78(5) but shall also facilitate segregation of funds of each client and, thereby, bring more visibility to the client of his/her funds.

3. However, even if it is clarified that client availing the PMS of a FME may maintain a bank account in IFSC Banking Unit and authorise the FME to operate the same, it may still pose certain challenges / inconvenience. In many cases, opening a new bank account in a foreign jurisdiction such as GIFT-IFSC may require large institutional clients to obtain internal approvals, which may be challenging especially if the clients have a pre-approved banking relationship with certain banks only and such banks are not present in IFSC. Further, for the clients which intend to invest in India or foreign jurisdictions, the funds from IFSC bank account of the client would largely be destined for investments into these jurisdictions. In such cases, the IFSC bank account of the investor would simply become an additional layer for routing the funds to the destination bank account, without adding any value to the client in the overall transaction.

## D. Proposal

1. In view of the limitations and challenges seen above, it is proposed to amend Regulation 77 (2) to permit client(s) availing the PMS to maintain a bank account in IFSC, India or foreign jurisdictions and authorise the FME to operate the same.

2. However, maintenance of bank accounts outside IFSC may have some supervisory concerns regarding transactions in these accounts. Therefore, some additional safeguards may be warranted to ensure that IFSCA continues to have access to the information of the bank accounts, even if they are outside of IFSC.

3. Accordingly, amendment to IFSCA (Fund Management) Regulations, 2022 is proposed. The text of the proposed amendment is placed at **Annexure – I** to this paper.

## E. Public Comments

1. Comments and suggestions from public are invited on the proposed amendments to IFSCA (Fund Management) Regulations, 2022 contained in **Annexure - I** to this paper.

2. Comments may be sent by email to Mr. Aditya Sarda, Assistant General Manager, IFSCA at aditya.sarda@ifsca.gov.in with a copy to Mr. Pavan Shah, Deputy General Manager, IFSCA at pavan.shah@ifsca.gov.in latest by March 8, 2023.

3. The comments may be provided in the following format (MS Word or MS Excel only):

| **Name of Person / Entity**<br>(Name of Organisation & Designation (if applicable), Contact No., Email ID) | | | | |
|---|---|---|---|---|
| **S. No.** | **Regulation No.** | **Sub-Regulation No.** | **Comments / Suggestion** | **Detailed Rationale** |
| | | | | |

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## Annexure – I: Amendments proposed to Fund Management Regulations

**Existing text of regulation**

77(2). A portfolio manager shall keep the funds of all clients in a separate account to be maintained by it in a Banking Unit.

**Proposed text of regulation**

77(2). The funds of clients of portfolio management services may be maintained in-

(a) a specific account of the FME in a Banking Unit;
(b) a specific account of client(s) in Banking Unit, banks in India or a Foreign Jurisdiction; or
(c) any other manner as may be specified by the Authority.

Provided that when the funds are maintained in the bank account of a client, the FME shall ensure that it is duly authorised to operate the said bank account and shall provide the details of all such accounts including transactions carried out thereunder, to the Authority, whenever directed to do so.