

Accredited investors in Indian securities market

SEBI consultation paper

March 2021



Background

Accredited investors (AIs)/qualified investors/professional investors are the class of investors that possesses an understanding of various financial products and risks/returns associated with them.

These investors are considered as well informed/advised investors on the premise that their financial capacity enables them to hire expert managers/advisers and provides them an ability to absorb loss. This makes the products with relatively higher risk suitable for them.

In the jurisdictions where such investors are recognised, relaxation is provided to them with respect to several regulatory requirements as they do not require extensive regulatory protection.

Additionally, certain jurisdictions also permit issuers or providers of financial products/services or securities market products/services (herein referred as 'Issuers and Providers'), to design and offer products/services exclusively to accredited investors.

Based on the feedback of several market participants, Securities and Exchange Board of India (SEBI) understood there is a case to consider the introduction of AIs in the Indian securities market.

In this backdrop, on 24 February 2021, SEBI placed a draft framework for introduction of the concept of AIs in Indian securities market for public comments.



Benefits to stakeholders and ecosystem

Concept of AIs accompanied with a flexible regulatory framework will provide the following benefits to Indian securities market

Stakeholders	Benefits
Investors	<p>Availability of portfolio diversification by encouraging access to:</p> <ul style="list-style-type: none">• Customised investment products (e.g. structured products)• Customised contractual arrangements with product or service providers• More investment products due to low entry barriers, such as minimum investment size
Issuers and providers	<ul style="list-style-type: none">• Better risk labeling and product classification• Increased transparency with reduced compliances• Lesser compliance costs• Flexibility in designing investment products• Ease of launching new innovative and customised financial products
Market ecosystem	<p>Limited regulatory framework for products/services meant for AI shall lead to:</p> <ul style="list-style-type: none">• better utilisation of regulatory resources for protection of investors other than AI• development of securities market through more participation and more products

Eligibility criteria under proposed framework (1/2)

For resident Indians

Category of investor	Eligibility criteria
Individuals, HUFs and Family Trusts	<ul style="list-style-type: none">• Annual income \geq INR 2 crore; OR• Net worth \geq INR 7.5 crore with financial assets having worth \geq INR 3.75 crore; OR• Annual income \geq INR 1 crore, Net worth \geq INR 5 Crore; with financial assets having worth \geq INR 2.5 crore
Trusts (other than Family Trusts)	Assets under management (AUM) \geq INR 50 crore
Body Corporates	Net worth \geq INR 50 crore
Others	<ul style="list-style-type: none">• Central and state governments;• Developmental agencies (such as SIDBI, NABARD, etc.) set up by government(s);• Funds set up by government(s);• Qualified institutional buyers as defined

Eligibility criteria under proposed framework (2/2)

For non-resident Indians and foreign entities

Category of investor	Eligibility criteria
Individuals, HUFs and Family Trusts	<ul style="list-style-type: none">• Annual income \geq USD 300,000; or• Net worth \geq USD 1 million with financial assets having worth \geq USD 500,000; or• Annual income \geq USD 150,000, Net worth \geq USD 750,000 with financial assets having \geq USD 375,000
Trusts (other than Family Trusts)	AUM \geq USD 7.5 million
Body corporates	Net worth \geq USD 7.5 million
Others	<ul style="list-style-type: none">• Multilateral agencies• Sovereign wealth funds• International financial institutions• Category I Foreign Portfolio Investors

Eligibility criteria – Other key aspects

In case of joint account held by individuals, the account shall be considered AI subject to following conditions:

- The first holder of the account is an AI
- In case joint holders are parents and children, at least one person is independently an AI
- In case joint holders are spouses, their combined income/net worth meets eligibility criteria

In case of body corporates and trusts, latest audited information as on the date of application to be considered.

Accreditation of investors may be carried out through 'Accreditation Agencies' - Market Infrastructure Institutions (MIIs) i.e., stock exchanges and depositories and/ or subsidiaries of MIIs. Modalities of accreditation to be determined separately.

The accreditation shall be valid for a maximum period of one year from the date of accreditation.

In case of individuals,

- The income/asset details considered for assessment of eligibility criteria, to be as per the income tax returns.
- For calculation of net worth, value of the primary residence of the investor shall not be included.
- In case the assets of investor are in the form of real estate, 'ready reckoner rate' as published by the respective local bodies shall be considered for assessment of eligibility criteria.

Investors to submit necessary data and documents to accreditation agency, for ascertaining eligibility to be an AI. If found eligible, accreditation agency to provide a certificate to this effect, indicating the period of validity of the same. Each certificate of accreditation shall have a unique certificate number.

Investors in the category 'Others' shall not be required to obtain an accreditation certificate from accreditation agencies.

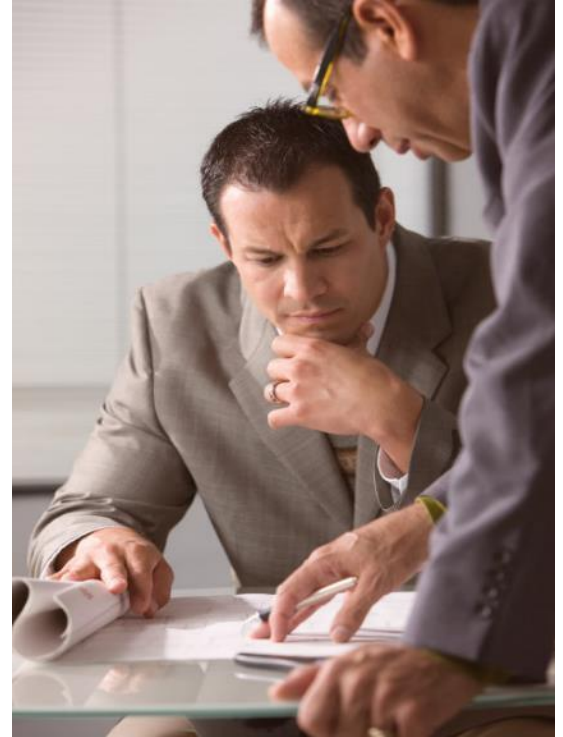
Application of AI across financial services

- The framework offers benefits to investors and issuers and providers broadly classified as under:
 - **Flexibility in minimum investment amount**
 - **Flexibility and relaxation in regulatory requirements**
 - **Access to products/services offered exclusively to AI**
- The AI participating in existing financial products/services shall have the option to choose the benefit of lower ticket size or flexible regulatory framework, as may be appropriate for them.
- We have discussed the benefits in detail in the ensuing slides



A. Flexibility in minimum investment amount

- It is proposed that the AI may participate in an existing investment product/service at a lower threshold as compared to the minimum amount mandated in the respective regulation, subject to the terms of agreement with the product/service provider.
- However, no relaxation shall be available with regard to the other aspects of the regulatory framework.



Illustration

- A Ltd. enters into an agreement with a portfolio manager to avail customised asset management service with a minimum capital of INR 50 lakh. Such capital may be made available to the portfolio manager in the form of cash or securities. In case of a client who is an AI, the portfolio manager may accept capital and manage a portfolio of less than INR 50 lakh.
- Similarly, the minimum capital commitment required to participate in alternative investment funds (AIFs) is INR 1 crore. In case of an AI, the portfolio manager may accept a capital commitment less than INR 1 crore.

B. Flexibility in regulatory requirements (Contd.)

- It is proposed that a relaxed regulatory framework be provided for existing investment products/services. The AI shall be required to invest a certain minimum amount (higher than the minimum amount applicable for regular investor), which shall be specified in the respective regulations.
- Such relaxation may be with respect to the
 - regulations/circulars governing prudential norms;
 - investment conditions;
 - filings with SEBI;
 - frequency of audit or valuation or reporting, etc.
- Further, each provider of investment product/service shall have the flexibility to stipulate additional criteria or conditions, over and above the eligibility criteria specified by SEBI, to avail regulatory relaxations.



B. Flexibility in regulatory requirements (Contd.)

Illustration 1:

Under the SEBI (Alternative Investment Funds) Regulations, 2012, AIFs are required to comply, inter-alia, with the following :

- Maximum investment by Category I/II AIFs in an investee company cannot exceed 25% of its net investible funds. Similarly, a Category III AIF may not invest more than 10% of its net investible funds in a single investee company.
- Schemes may be launched, subject to filing of placement memorandum with SEBI at least 30 days prior to launch of scheme. Comments of SEBI, if any, shall be incorporated in the placement memorandum prior to launch of scheme.
- Category III AIFs may undertake leverage up to two times the net asset value of the scheme.

An AIF (or scheme of AIF) in which all investors (other than manager/sponsor and employees/directors/partners of manager/sponsor) are AIs and each such investor has committed a minimum capital of INR 70 crore (or USD 10 million or its equivalent), subject to contractual agreements with the investors, may have flexibility in respect of norms listed earlier.

B. Flexibility in regulatory requirements (Contd.)

Illustration 2:

Under the SEBI (Portfolio Managers) Regulations, 2020, Portfolio Managers are required to comply, inter-alia, with the following:

- Manner and periodicity of disclosures, exit load, fees charged etc. shall be as specified by SEBI from time to time.
- Portfolio manager offering non-discretionary or advisory services is allowed to invest or provide advice for investment in unlisted securities, only up to 25% of the assets under management (AUM) of the clients. A portfolio manager offering discretionary service may invest the client funds only in listed securities, money market instruments or units of mutual funds.



Subject to the terms of the client agreement, portfolio management service (PMS) availed by an AI client for a portfolio at least INR 10 crore with the following flexibility.

- The terms of agreement between the portfolio manager and client including terms of termination of contract, type and periodicity of client reporting, frequency of audit of client account, exit load, fees, etc. may determined mutually.
- The portfolio of the client (discretionary/non-discretionary) may be invested up to 100% in unlisted securities.

B. Flexibility in regulatory requirements (Contd.)

Illustration 3:

Under SEBI (Investment Advisers) Regulations, 2013 there is no requirement of minimum Asset under Advice (AUA) for availing the services of investment advisers (IAs). The regulatory framework provides extensive norms for client level segregation, fees, risk profiling, suitability, agreements with client incorporating the terms and conditions as specified by SEBI, etc.



In case the client of the investment adviser is an AI, subject to the terms of the client agreement, the following regulatory exemptions/ relaxations may be availed:

- The terms of the agreement may be determined mutually between the IA and the client, without diluting the fiduciary responsibility cast on IAs under SEBI (Investment Advisers) Regulations
- Limits and modes of fees may be governed in its entirety through bilaterally negotiated contractual terms

C. New products exclusively for AI

Jurisdictions across the globe have witnessed a demand for tailor made investment products (i.e. products designed to meet required profile and needs of investor(s))

Keeping this in mind, in addition to participation of AIs in existing products/services, a framework for introduction of new products (exclusively for offering to AIs) may be enabled.

One of the key requirements for a thriving market for such investors is a light touch regulatory regime.

If such products are to be offered only to AIs, there is scope for regulating them with minimal prudential norms.

While such products may not be readily available in the Indian securities market at this juncture, putting in place the required enabling framework may lead to introduction of such products

This step will help in innovation and in development of the Indian securities market.



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