FPI NAVIGATOR

FPI Framework: An Insight

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FPI REGISTRATION IN INDIA: A REGULATORY EVOLUTION TOWARDS EASE AND EFFICIENCY

Since their entry in the early 1990s, the Foreign Portfolio Investors ("**FPIs**") (or FIIs, as they are sometimes called) have poured in billions of dollars into the Indian stock market (from about USD 302 mn in 1993[1] to about USD 20 bn in 2024[2]).Their appetite and behavior have, on several occasions, dictated market movements, influenced retail participation, and contributed to the increased sophistication of the equities and derivatives market in India.

Acknowledging the above, the Indian Government, the Securities and Exchange Board of India ("**SEBI**") and the Reserve Bank of India ("**RBI**"), from time to time, have endeavored to make the entry process of the FPIs smoother, efficient and less cumbersome, without compromising on the diligence and transparency requirements.

The regime for FPIs (erstwhile 'FIIs') has evolved over a period of time. In this write-up, we have delved into the evolution of the registration process for the FPIs in India since the promulgation of the SEBI (Foreign Portfolio Investors) Regulations, 2019 ("**FPI Regulations**").

Erstwhile Process

For an offshore entity to participate on the Indian stock market, the FPI license procurement consisted of:

(i) filing registration application to the Designated Depository Participant ("**DDP**"), along with depositing the fee prescribed under the SEBI (Foreign Portfolio Investors) Regulations, 2014 ("**Erstwhile Regulations**");

(ii) filing separate application to the Income-tax Department for obtaining a Permanent Account Number ("**PAN**") to file tax returns in India;

(iii) appointing a designated bank to open a foreign currency denominated a/c and a special non-resident rupee a/c, post receipt of the FPI license; and

(iv) opening of the demat a/c by the DDP post ensuring FPI's compliance with the Indian anti-money laundering ("**AML**") laws, FATF standards, and the relevant SEBI circulars and directives.

FPI Regulations, Operational Guidelines & Common Application Form

The FPI Regulations (which repealed the Erstwhile Regulations) and the Operational Guidelines, 2019 ("**Guidelines**") (which were later superseded by the Master Circular, 2022) were issued by SEBI in 2019 which laid out the entire legal framework for the FPIs, along with the registration process and formalities.

Subsequently, in order to provide a single-window clearance to the FPIs, the Common Application Form ("**CAF**") was notified by the Government of India vide a notification dated January 27, 2020.[3] The CAF, jointly prepared by the SEBI, the RBI and the Central Board of Direct Taxes ("**CBDT**"), eliminated the need to make separate applications to different regulatory bodies and consolidated the regulatory, tax (PAN application) and account (bank a/c and demat a/c) opening requisitions at a single place.

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[1] https://www.sebi.gov.in/statistics/fpi-investment/fpi-calendar-year/fpi-investment-details-calendar-year.html
[2] https://www.fpi.nsdl.co.in/web/Reports/Yearwise.aspx?RptType=6
[3] Notification number F. No. 4/15/2016-ECB.

Interestingly, the CAF contained a section wherein the FPIs were required to disclose their Ultimate Beneficial Owner(s) ("UBOs") as per Rule 9 of the Prevention of Money laundering (Maintenance of Records) Rules, 2005 ("PML Rules").

Generation of FPI Registration Number and Hosting of CAF

The FPI Regulations were amended on January 14, 2022, to authorize SEBI to generate FPI registration number which was earlier done by the National Securities Depository Limited ("NSDL"), one of the central securities depositories. Thereafter, SEBI amended CAF to permit NSDL and Central Depository Services (India) Limited ("CDSL") to host CAF on their portal. This led to the DDPs getting access to soft copies of the populated CAF and supporting documents via the online portal.

Further streamlining of onboarding formalities

SEBI, vide its circular dated March 27, 2023[4], made several changes to the FPI onboarding formalities so as to make the process more efficient and less time-consuming. The key changes included:

(i) DDP granting the FPI license basis the scanned copies of CAF and allied documents, provided that the trading activity commences, and the Custodial Participant ("CP") code is applied for post verification of the physical documents;

(ii) permitting FPIs to digitally sign the registration documents;

(iii) allowing document certification using the SWIFT mechanism;

(iv) permitting PAN verification by the DDPs on the depositories' website; and

(v) introducing investor group ID for the FPIs falling within the same investor group.

'Legal entity' verification

SEBI, during the first half of 2023, had sent email communication to the DDPs directing them to procure details of the 'legal entity'[5] of the FPIs and conduct due diligence on them, akin to the FPI applicant. This was to ensure that the identified legal entity, for instance, a bank and not its branch registered as an FPI, or the umbrella entity/fund and not its sub-funds investing as FPIs, become the client of the DDP (i.e. the reporting entity as per the Prevention of Money-Laundering Act, 2002).

Introduction of abridged version of CAF

SEBI, vide its circular dated November 12, 2024[6], introduced an optional abridged version of the CAF to be available in the following instances where data is already captured in the depositories database, thus enabling the FPIs to only fill those fields which are unique to them:

[4] SEBI Circular no. SEBI/HO/AFD/P/CIR/2023/043.
[5] i.e., a bank and not its branch which may be registered as an FPI with SEBI, or an entity and not its sub-funds investing in India as FPIs, would be the legal entity and thus, the client of the DDP.
[6] SEBI Circular no. SEBI/HO/AFD/AFD-PoD-3/P/CIR/2024/156.

(i) fund(s) operated by investing/non-investing IM, wherein such IM or any fund operated by IM, is already registered as FPI;

(ii) sub-fund(s) of a master fund, wherein such master fund or any sub-fund of such master fund, is already registered as FPI;

(iii) sub-fund(s) or separate class(es) of shares or equivalent structure(s) with segregated portfolio of a fund, wherein such fund or any of its sub-fund or separate class of shares or equivalent structure with segregated portfolio, is already registered as FPI; and

(iv) scheme(s) of insurance companies wherein the parent entity or any scheme of insurance company is already registered as FPI.

This further eased off the FPI onboarding process by cutting down on the number of pages to be signed by the FPIs as well as the time consumed in DDP reviewal process.

Status Quo

Owing to the changes and developments described above, the current FPI registration and onboarding process can be a relatively smoother and uncomplicated one, provided it is handled proficiently.

Certain sections of the CAF and Annexure to CAF should be paid specific attention to and reviewed properly in order to ensure smooth onboarding journey, such as:

(i) Selection of the category and/or sub-category of the FPI license (for instance, the category of license suitable for an entity or an unregulated fund having a Category I non-investing FPI IM, or a family office run appropriately regulated fund, etc.);

(ii) UBO identification;

(iii) legal entity verification;

(iv) investor group identification and disclosure; and/or

(v) intermediate material owner entity reporting.

Way Forward

With an uptick in the number of IPOs, a flourishing F&O market, and Indian government bond's inclusion in the JP Morgan, Bloomberg and FTSE Russell emerging market Indices, the augmented interest of foreign players in the Indian listed space is palpable. What is needed from the market regulators is their continued efforts and support in promoting ease of doing business in India for such sophisticated investors, without diluting the market protection standards and norms.

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