CFA Society India

India Insights

March 2023

EDITORIAL

It is our great pleasure to bring to you our ninth edition of India Insights. We started this e-zine in April 2021 to share CFA Society India's contribution to local advocacy efforts in ESG, Sustainable Investing, ethics, corporate disclosures, and other development areas of finance and investing in India. With our readers and volunteers support and guidance our advocacy e-zine is now entering into its third year.

This was an eventful quarter for The Research, Advocacy and Standards committee of CFA Society India. While SEBI issued several consultation papers in the last few months, we managed to respond on Standardised Approach to Valuation of Investment Portfolio of AIF, AIF Dematerialisation, AIF Direct Plan, AIF Investment Manager Qualification, Regulatory Framework for Index Providers, Strengthening Corporate Governance at Listed Entities by Empowering Shareholders, Streamlining Disclosures by Listed Entities and Strengthening Compliance with SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and Exposure Draft of the CFA Institute Code of Ethics and Standards of Professional Conduct.

On ESG front, apart from responding to the Exposure Draft of the CFA Institute Code of Ethics and Standards of Professional Conduct and SEBI's Consultation Paper on ESG Disclosures, Ratings and Investing, we conducted a half-day workshop on "ESG Investing for Industry Professionals". The workshop focused on Incorporating ESG Ratings in Investment Analysis and Incorporating Climate Changes Risks & Opportunities in Investment Analysis.

CFA Society India has joined hands with C-Kinetics to establish a forum on 'Sustainability'. We held a closed-door roundtable with the invitees from SEBI's ESG advisory committee and a few senior investment management & ESG professionals to discuss the potential formation of an India SIF.

To celebrated "International Women's Day" the Society held an essay writing competition for women in finance, organized a workshop on entrepreneurship for women members which was followed by a powerful keynote address by Rakhee Lalvani and an insightful panel discussion with industry stalwarts.

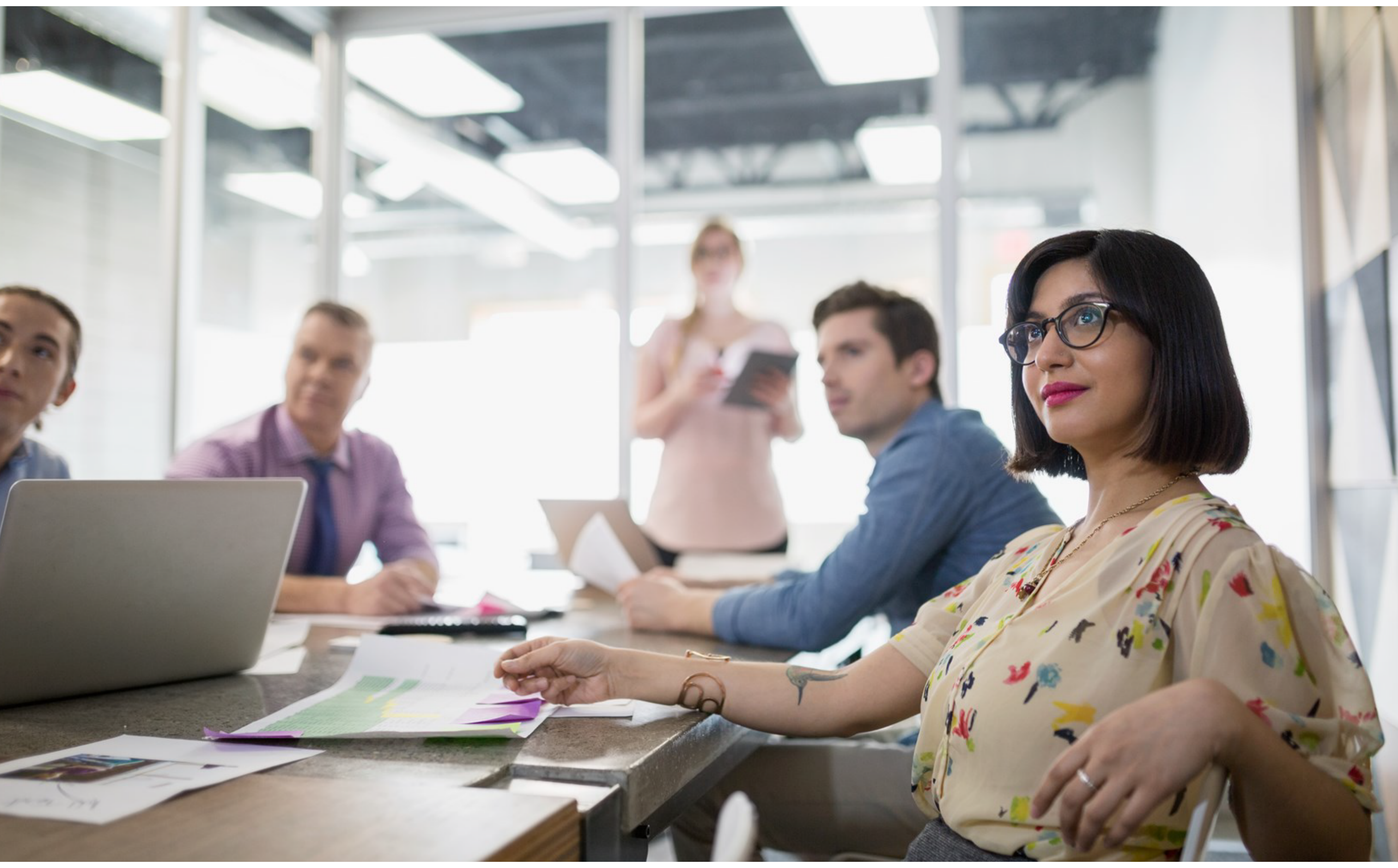
The Society in collaboration with CFA Institute released "Mind the Gender Gap" report highlighting the persistent gender gap across the field of finance in India.

Hope you find this edition of India Insights useful. We will be happy to hear and discuss your suggestions and opinions related to advocacy initiatives.

If you are a member of CFA Society India and wish to participate in any of these advocacy initiatives as volunteers, please drop a message on any of CFA Society India's social media handles and some one from the staff will get in touch with you.

Best Regards,
Volunteer Editors
Nimisha Pandit, CFA

CONSULTATION PAPER ON STANDARDISED APPROACH TO VALUATION OF INVESTMENT PORTFOLIO OF ALTERNATIVE INVESTMENT FUNDS.



As regards valuation of investment portfolio of AIFs, presently, AIF Regulations only focus on disclosures to investors and do not prescribe any guidelines on the principles to be adopted. As such, managers of AIFs have flexibility to adopt any valuation methodology.

The recommendations put forth in the consultation paper for standardizing valuation of investment portfolio of AIF is a positive step and we realize the need for such regulation considering the growth of AIF industry in the last few years.

Following are our key comments on the proposed mechanism:

- Standardization of portfolio valuation as per as IPEV guidelines would allow better comparison of NAV of various AIFs. It also reduces chances of valuation being disjointed from reality. We agree that the IPEV guidelines are a global standard and is followed for valuing Private Equity/Venture capital funds across various jurisdictions.
- We recommended that as the large portion of an investment portfolio for Category III AIFs is in listed security, SEBI may look to give a carve-out to Category III AIFs where the unlisted portion of the investments is limited to 5-10%. If the unlisted portion of the investment portfolio is not large, the independent valuer appointment may lead to operational hassle without significant benefit.
- Proposal of requiring investee companies to provide audited accounts in a specific timeframe to AIF manager so that they can report valuation based on audited data to performance benchmarking agencies within the specified timeline of 6 months has a sound basis

Our complete response to SEBI can be accessed here.

but may not be practically implementable. The audit infrastructure in India may not be ready for both listed and unlisted companies being audited at the same time.

- The recommendation of having same deadline for the company submission of accounts and the valuation submission by AIF is not practically possible in many cases. Valuation process itself can take anywhere from 3 weeks to 3 months, depending upon the size of the portfolio. Therefore, we recommended that AIFs should be permitted to publish their valuation basis unaudited data from unlisted companies, with valuers having the responsibility to true up the results later when audited financials are obtained.
- We believe that the requirement of reporting of variation in valuation of more than 20% between two valuation dates and 33% within a year maybe too restrictive. The investments in unlisted companies especially early-stage startups are more volatile. Repeated reporting of a common occurrence in valuation variance may increase noise for investors and lead to increase in operational burden for managers without having the desired results. Our recommendation was as long as there is no variation in valuation approach, no specific reporting may be required.

To read SEBI's proposal, please click here.

OTHER CONSULTATION PAPERS RELATING TO ALTERNATIVE INVESTMENT FUNDS.

In February 2023, SEBI invited comments on five consultation papers concerning AIFs. The proposals covered key matters like mandatory dematerialization of units of AIFs, mandating direct plan for AIF, adopting trail model of distribution commission, review of eligibility criteria for the key investment team and prescribing qualification for compliance officer and providing an option to AIFs and their investors to carry forward unliquidated investments of a scheme upon expiry of its tenure.

We appreciate SEBI's initiatives for bringing transparency & protecting investors in AIFs. Following are our key comments on the proposals.

- The mandatory introduction of the Direct Plan by AIFs is a welcome step, and we support the same. Investors should not be charged by the Investment Manager as well as the Intermediary. This will lead to higher costs for the investors. By routing all direct and fee-paying investors via the direct plan, the double charging of fees to investors can be avoided.
- We are in favour of adopting trail model of distribution commission in AIFs. However, we have reservations against allowing upfront payment of certain higher amount of distribution fee (viz: one third of the present value of the total distribution fee) for Category I & II AIFs. Up-front fees tend to distort the decision making of distributors. Further, investments will be routed to funds which are close ended and hence ill-liquid. Hence, we suggested that the trail fee model be followed for all category of AIFs.

Our complete response to SEBI can be accessed here.

- We do not agree with the proposal of replacing experience criteria for key members of the investment management team with a requirement for obtaining a relevant certification form an institution notified by Sebi. The proposal assumes that experience is not a necessary qualification for competence, but an educational qualification is. Therefore, one can expect that only qualified individuals would venture into the fund management area. Currently many fund managers already have specialised investment management qualifications. Therefore, requiring the fund management team to have another qualification may not be required and should not be introduced. Further, since no such requirement has been specified in mutual fund regulations, making it mandatory in AIF regulations where investors are supposed to be more sophisticated, does not appear to be consistent.
- We do not agree with the proposal of mandatory dematerialisation of units of AIF. As investors themselves are not in favour of investing in AIFs in demat form. There are other practical issues relating to KYC of new investors, signing of contributions agreements with them, etc.

CONSULTATION PAPER ON 'REGULATORY FRAMEWORK FOR INDEX PROVIDERS'

We appreciate the SEBI's effort to regulate the index providers considering the increased interest in passive investing in the last few years. The recommendations put forth in the proposed regulatory framework for index providers is a positive step as part of efforts to enhance transparency as well as accountability in governance and administration of the indices in the Indian securities market.

Following are our key comments on the proposed mechanism:

- We support that Index providers should be mandated to adhere to global standards i.e. IOSCO Principles. Further, we recommended SEBI to outline guidelines on characteristics of a benchmark. CFA curriculum cover the characteristics of a valid benchmark in detail. To name a few, a valid benchmark should be unambiguous, investable, measurable, accountable etc.
- We support the proposal to have the index providers register with SEBI. This will give SEBI the oversight over the index providers. However, making the same rule applicable for index providers who are based out of India and the securities market is outside India may be counterproductive. This may stifle innovation and may cause difficulty in accessing the international market at low cost to the Indian investor. Further, the rule of having adherence to IOSCO principles should suffice in such cases.
- Instead, we suggested having a minimum threshold for AUM following the index for mandating registration. Alternatively, SEBI can restrict the access of unregistered Index only to Accredited investors.

Our complete response to SEBI can be accessed here.

- We believe the proposed regulation of data sourcing from only regulated entities is restrictive. We recommended that SEBI should allow index providers to source data from unregulated entities also. We believe that SEBI should mandate that there should be a framework if data sourcing is being done by an unregulated entity, like as prescribed in IOSCO principle.

To read SEBI's proposal, please click here.

OTHER ADVOCACY INITIATIVES

CONSULTATION PAPERS

- Regulatory Framework for Index Providers – **Link**
- Standardized Approach to Valuation of Investment Portfolio of Alternative Investment Funds - **Link**
- AIF Investment Manger Qualification – **Link**
- AIF Direct Plan – **Link**
- AIF Dematerialization of Units – **Link**
- Exposure Draft of the CFA Institute Code of Ethics and Standards of Professional Conduct - **Link**
- Streamlining Disclosures by Listed Entities and Strengthening Compliance with SEBI - **Link**
- ESG Disclosures, Ratings and Investing – **Link**

EVENTS, PROGRAMS & COMPETITIONS

- Program: Celebrating the #WOWomen – **Link**

RESEARCH PUBLICATIONS & BLOGS

- Report: Mind the Gender Gap - **Link**
- Blog: Boosting Climate Finance - **Link**
- Blog: Climate-Tech Investments in India- Big Opportunity, Bigger Returns – **Link**

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