

PORTFOLIO INVESTMENTS

Portfolio Investment Scheme (PIS)

- (i) Foreign institutional Investors (FIIs) registered with SEBI and Non-resident Indians (NRIs) are eligible to purchase shares and convertible debentures issued by Indian companies under the Portfolio Investment Scheme (PIS)
- (ii) The FIIs who have been granted registration by SEBI should approach their designated AD Category - I bank (known as Custodian Bank), for opening a foreign currency account and/or a Non Resident Special Rupee Account.
- (iii) NRIs can approach the designated branch of any AD Category - I Bank authorized by the Reserve Bank to administer the Portfolio Investment Scheme for permission to open a NRE/ NRO account under the Scheme for routing investments.

Investment by FIIs under PIS

Reserve Bank has given general permission to SEBI registered FIIs/sub-account to invest under the PIS

(i) Shareholding

- (a) Total shareholding of each FII/sub-account under this Scheme shall not exceed 10 per cent of the total paid up capital or 10 per cent of the paid up value of each series of convertible debentures issued by the Indian company.
- (b) Total holding of all FIIs/sub-accounts put together shall not exceed 24 per cent of the paid-up capital or paid-up value of each series of convertible debentures. This limit of 24 per cent can be increased to the sectoral cap / statutory limit, as applicable to the Indian company concerned, by passing a resolution of its Board of directors followed by a special

Resolution to that effect by its General Body.

(c) A domestic asset management company or portfolio manager, who is registered with SEBI as an FII for managing the fund of a sub-account can make investments under the Scheme on behalf of

- I. a person resident outside India who is a citizen of a foreign state, or
- ii. a body corporate registered outside India;

Provided such investment is made out of funds raised or collected or brought from outside through normal banking channel. Investments by such entities shall not exceed 5 per cent of the total paid-up equity capital or 5 per cent of the paid-up value of each series of convertible debentures issued by an Indian company, and shall also not exceed the overall ceiling specified for FIIs.

(ii) Prohibition on investments

(a) FIIs are not permitted to invest in equity shares issued by an Asset Reconstruction Company. They are also not allowed to invest in any company which is engaged or proposes to engage in the following activities:

- i). Business of chit fund, or
- ii). Nidhi Company or
- iii). Agriculture or plantation activities or
- iv). Real estate business, or construction of farm houses
- v). Trading in Transferable Development Rights (TDRs)

“Real Estate Business” mentioned above, does not include development of townships, construction of residential/commercial premises, roads or bridges.

Short Selling by FIIs

Foreign Institutional Investors (FIIs) registered with SEBI and sub-accounts of FIIs are permitted to short sell, lend and borrow equity shares of Indian companies. Short selling, lending and borrowing of equity shares of Indian companies shall be subject to such conditions as may be prescribed in that behalf by the Reserve Bank and the SEBI / other regulatory agencies from time to time. The above permission is subject to the following conditions:

- (a) The FII participations in short selling as well as borrowing / lending of equity shares will be subject to the current FDI policy and short selling of equity shares by FIIs shall not be permitted for equity shares which are in the ban list and / or caution list of Reserve Bank.
- (b) Borrowing of equity shares by FIIs shall only for the purpose of delivery into short sales.
- (c) The margin / collateral shall be maintained by FIIs only in the form of cash. No interest shall be paid to the FII on such margin/collateral.

Exchange Traded Derivative Contracts

(i) SEBI registered FIIs are allowed to trade in all exchange traded derivative contracts on recognized Stock Exchanges in India subject to the position limits as prescribed by SEBI from time to time. The SEBI registered FII/sub-account may open a separate account under their Special Non-Resident Rupee Account through which all receipts and payments pertaining to trading/investment in exchange traded derivative contracts will be made (including initial margin and mark to market settlement, transaction charges, brokerage, etc.) further, transfer of funds between the Special Non-

Resident Rupee Account and the separate account maintained for the purpose of trading in exchange traded derivative contracts can be freely made. However, repatriation of the rupee amount will be made only through their Special Non-Resident Rupee Account subject to payment of relevant taxes. The AD Category – I banks have to keep proper records of the above mentioned separate account and submit them to Reserve Bank as and when required. (ii) FIIs are allowed to offer foreign sovereign securities with AAA rating as collateral to the recognized Stock Exchanges in India for their transactions in derivatives segment. SEBI approved clearing corporations of stock exchanges and their clearing members are allowed to undertake the following transactions subject to the guidelines issued from time to time by SEBI in this regard :

- a. to open and maintain demat accounts with foreign depositories and to acquire, hold, pledge and transfer the foreign sovereign securities, offered as collateral by FIIs;
- b. to remit the proceeds arising from corporate action, if any, on such foreign sovereign securities; and
- c. to liquidate such foreign sovereign securities if the need arises.

(iii) Clearing Corporation have to report, on a monthly basis, the balance of foreign sovereign securities, held by them as non-cash collaterals of their clearing members to the Reserve Bank. The report should be submitted by the 10th of the following month to which it relates.

Forward cover & cancellation and rebooking

(i) Designated branches of AD Category-I Banks maintaining accounts of FIIs can provide forward cover with rupee as one of the currencies to such customers subject to the following conditions:

- a. FIIs are allowed to hedge the market value of their entire investment in equity and/or debt in India as on a particular date. If a hedge becomes naked in part or full owing to shrinking of the value of portfolio, for reasons other than sale of securities, the hedge may be allowed to continue to the original maturity, if so desired;
- b. FIIs may be allowed to cancel and rebook forward contracts up to a limit of 2 per cent of the market value of their entire investment in equity and / or debt in India. The limit for calculating the eligibility for rebooking shall be based upon market value of portfolio as at the beginning of the financial year (April – March). The outstanding contracts must be duly supported by underlying exposure at all times. These contracts may be rolled over on or before maturity. The monitoring of forward cover must be done on a fortnightly basis by the AD banks, and reported to the Reserve Bank on a monthly basis, as per the format prescribed.
- c. the cost of hedge is met out of repatriable funds and /or inward remittance through normal banking channel;
- d. all outward remittance incidental to the hedge are net of applicable taxes.

(ii) The eligibility for cover may be determined on the basis of the declaration of the FII. A review may be undertaken on the basis of market price movements, fresh inflows, amounts repatriated and other relevant parameters to ensure that the forward cover outstanding is supported by an underlying exposure. The AD Category – I bank has to ensure that

- (i) total forward contracts outstanding should not exceed the market value of portfolio, and
- (ii) forward contracts permitted to be rebooked should not exceed 2 percent of the market value as determined at the beginning of the financial year.

Margin requirements

SEBI registered FIIs / sub-accounts are allowed to keep with the Trading Member / Clearing Member amount sufficient to cover the margins prescribed by the Exchange / Clearing House and such amounts as may be considered necessary to meet the immediate needs.

Accounts with AD Category – I banks

- (i) FIIs/sub-accounts can open a Foreign Currency denominated Account and / or a Special Non-Resident rupee account with an AD Category – I bank, for the purpose of investment.
- (ii) They can transfer sums from the foreign currency account to the rupee account for making genuine investments in securities in terms of the SEBI (FII) Regulation, 1995.
- (iii) The sums may be transferred from foreign currency account to rupee account at the prevailing market rate and the AD category – I bank may transfer repatriable proceeds (after payment of tax) from the rupee account to the foreign currency account.

(iv) The Special Non-Resident Rupee Account May be credited with the proceeds of sale of shares / debentures, dated government securities, Treasury Bills etc. Such credits are allowed, subject to the condition that the AD category – I bank should obtain confirmation from the investee company / FII concerned that tax at source, wherever necessary, has been deducted from the gross amount of dividend / interest payable / approved income to the share / debenture / Government securities holder at the applicable rate, in accordance with the Income Tax Act.

(v) The Special Non-Resident Rupee Account may be debited for purchase of shares / debentures, dated Government securities, Treasury Bills etc., and for payment of fees to applicant FIIs' local chartered Accountant / Tax Consultant where such fees constitute an integral part of their investment process.

Private placement with FIIs

SEBI registered FIIs have been permitted to purchase shares / convertible debentures of an Indian company through offer/private placement, subject to the ceiling prescribed, i.e. individual FII/sub-account – 10 per cent and all FIIs/sub-account put together -24 per cent of the paid-up capital of the Indian company and to the sectoral limits, as applicable. Indian company is permitted to issue such shares provided that:

- i. in the case of public offer, the price of shares to be issued is not less than the price at which shares are issued to residents; and
- ii. in the case of issue by private placement, the price is not less than the price arrived at in terms of SEBI guidelines or guidelines

Issued by the erstwhile Controller of Capital Issues, as applicable. Purchases can also be made of PCDs / FCDs/ Right Renunciations / Warrants / Units of Domestic Mutual Fund Schemes.

Allocation of funds

The SEBI registered FII shall restrict allocation of its total investment between equities and debt in the Indian capital market in the ratio of 70:30. The FII may form a 100% debt fund and get such fund registered with SEBI. Investment in debt securities by FIIs are subject to limits, if any, stipulated by SEBI in this regard.

Reporting of FII investments

(i) An FII may invest in a particular share issue of an Indian company either under the FDI Scheme or the Portfolio Investment Scheme. The AD Category – I banks have to ensure that the FIIs who are purchasing the shares by shares debit to the special rupee accounts report these details separately in the LEC (FII) returns.

(ii) The Indian company which has issued shares to FIIs under the FDI Scheme (for which the payment has been received directly into company's account) and the portfolio Investment Scheme (for which the payment has been received from FIIs' account maintained with an AD Category – I bank in India) should report these figures separately under item no. 5 of form FC-GPR (Post issue pattern of shareholding) so that the details could be suitably reconciled for statistical / monitoring purposes.

(iii) A daily statement in respect of all transactions (except derivative trade) have to be submitted by the custodian bank in floppy/soft copy in the

prescribed format directly to Reserve Bank to monitor the overall ceiling/ sectoral cap/statutory ceiling.

Investments by Non-Resident Indians (NRIs)

NRIs are allowed to invest in shares of listed Indian companies in recognized Stock Exchange under the PIS. NRIs can invest through designated Ads on repatriation and non-repatriation basis under PIS route upto 5% of the paid up capital/paid-up value of each series of debentures of listed Indian companies. The aggregate paid-up value of shares/ convertible debentures purchased by all NRIs cannot exceed 10% of the paid-up capital of the company. The aggregate ceiling of 10% can be raised to 24%, if the General Body of the Indian company passes a special resolution to that effect.

The NRI investor has to take delivery of the shares purchased and give delivery of shares sold. Short selling is not permitted.

Payment for purchase of shares and/or debentures on repatriation basis has to be made by way of inward remittance of foreign exchange through normal banking channels or out of funds held in NRE/FCNR account maintained in India. If the shares are purchased on non-repatriation basis, the NRIs can also utilize their funds in NRO account in addition to the above.

The link office of the designated branch of an AD Category-I bank shall furnish to the Reserve Bank, a report on a daily basis on PIS transactions undertaken by it, such report can be furnished on-line or on a floppy to RBI.

Shares Purchased by NRIs on the Stock Exchange Under PIS cannot be Transferred by

Way of Sale Under Private Arrangement or By Way of Gift to a Person Resident in India or OUTSIDE India without Prior Approval of RBI.

NRIs are allowed to invest in Exchange Trade Derivative Contracts approved by SEBI from time to time out of Rupee funds held in India on non-repatriation basis subject to the limits prescribed by SEBI.

Monitoring of Investment Position by RBI

Reserve Bank monitors the investment position of NRIs in listed Indian companies, reported by Custodian Banks on a daily basis in Forms LEC (FII) and LEC (NRI).

Caution List

When the total holdings of FIIs/NRIs under the Scheme reach the trigger limit, which is 2% below the applicable limit (for companies with a paid-up capital of Rs. 1000 crores and above, the trigger limit is 0.5% below the applicable limit), Reserve Bank will issue a notice to all designated branches of AD Category-I banks cautioning that any further purchases of shares of the particular Indian company will require prior approval of Reserve Bank. Reserve Bank gives case by case approvals to FIIs for purchase of shares of companies included in the caution list. This is done on a first come first served basis.

Ban List

Once the shareholding by NRIs reaches the overall ceiling / sectoral cap / statutory limit, Reserve Bank puts the company on the Ban List. Once a company is placed on the Ban list, no FII or NRI can purchase the shares of the Company under the Portfolio Investment Scheme.

FREQUENTLY ASKED
QUESTIONS (FAQs)
FOREIGN PORTFOLIO
INVESTMENT

Q. 1. What are the regulations regarding Portfolio Investments by Foreign Institutional Investors (FIIs)?

A.1. Investment by FIIs is regulated under SEBI (FII) Regulations, 1995 and Regulation 5(2) of FEMA Notification No 20 dated May 3, 2000. FIIs include Asset Management Companies, Pension Funds, Mutual Funds, and Investment Trusts as Nominee Companies, Incorporated/Institutional Portfolio Managers or their Power of Attorney holders, University Funds, Endowment Foundations, Charitable Trusts and Charitable Societies.

- SEBI acts as the nodal point in the registration of FIIs. The Reserve Bank of India has granted General Permission to SEBI Registered FIIs to invest in India under the Portfolio Investment Scheme (PIS).
- Investment by individual FIIs cannot exceed 10% of paid up capital. Investment by foreign registered as sub accounts of FIIs cannot exceed 5% of paid up capital. All FIIs and their sub-accounts taken together cannot acquire more than 24% of the paid up capital of an Indian Company. An Indian Company can

Raise the 24% ceiling to the Sectoral Cap / Statutory Ceiling, as applicable, by passing a resolution by its Board of Directors followed by passing a Special Resolution to that effect by their General Body.

Q.2. What are the regulations regarding Portfolio Investments by NRIs/ PIOs?

A.2. Non Resident Indian (NRIs) and Persons of Indian Origin (PIOs) can purchase/ sell shares/convertible debentures of Indian Companies on Stock Exchanges under Portfolio Investment Scheme. For this purpose, the NRI/PIO has to apply to a designated branch of a bank, which deals in Portfolio Investment. All sale/ purchase transactions are to be routed through the designated branch.

- An NRI or a PIO can purchase shares up to 5% of the paid up capital of an Indian company. All NRIs/PIOs taken together cannot purchase more than 10% of the paid up value of the company. (This limit can be increased by the Indian company to 24% by passing a General Body resolution).
- The sale proceeds of the repatriable investments can be credited to the NRE/NRO etc. Accounts of the NRI/PIO, whereas the sale of nonrepatriable investment can be credited only to NRO accounts.

The sale of shares will be subject to payment of applicable taxes.

Investment in Government Securities and Corporate Debt

Q.3. Can a Non-resident Indian invest in Government Securities/Treasury bills and Corporate debt?

A.3. Under the FEMA Regulations only NRIs and SEBI registered FIIs are permitted to purchase Government Securities/ Treasury bills and corporate debt. The details are as under;

- I. A Non-resident Indian can purchase,
- a) Government dated securities (other than bearer securities) or treasury bills or units of domestic mutual funds;
 - b) bonds issued by a public sector undertaking (PSU) in India;
 - c) Shares in Public Sector Enterprises being disinvested by the Government of India.

They can also invest, on non-repatriation basis, in dated Government securities (other than bearer securities), treasury bills, units of domestic mutual funds, units of Money Market Mutual Funds in India, or National Plan/Savings Certificates on non repatriation basis. The guidelines for these schemes are framed by the concerned Government agencies.

- II. A SEBI registered Foreign Institutional Investor may purchase, on repatriation basis, dated

Government securities/treasury bills, non-convertible debentures/ bonds issued by an Indian company and units of domestic mutual funds either directly from such securities or through a registered stockbroker on a recognized stock exchange in India. The FIIs is required to ensure that,

- a) The FII allocation of its total investment between equity and debt instruments (including dated Government Securities and Treasury Bills in the Indian capital market) should not exceed the ratio of 70:30.
- b) In case the FII is set-up as a 100% debt FII, it can invest the entire corpus in dated Government Securities including Treasury Bills,- non-convertible debentures/bonds issued by an Indian company subject to limits, if any, stipulated by SEBI in this regard.

The Investment in Government Securities/Treasury Bills and Corporate debt is subject to a ceiling decided in consultation with the Government of India. Investment limit for the FIIs as a group in Government securities currently is USD 3.2 Billion. The limit for Investment in Corporate debt is USD 1.5 billion. At present, the FIIs can also invest in Innovative instruments such as upper tier-II capital upto a limit of USD 500 million.