

SEBI Guidelines - Fintech Startups to Enter Mutual Fund Business

Why in news?

- SEBI (Securities and Exchange Board of India) recently released the amended rules governing the mutual fund industry.
- A key decision is to relax the profitability criteria for entities floating a mutual fund asset management company (AMC).

What is an asset management company?

- Asset management companies (AMCs) are firms pooling investments from various individual and institutional investors.
- The company manages the investment by investing in capital assets such as stocks, real estate, bonds, and so on.
- The asset management companies have professionals called fund managers who decide where the pooled money is invested.
- Fund managers identify the investment options that are in line with the objectives of the investors.
- **Regulation** - An AMC works under the supervision of the board of trustees.
- But, they are answerable to the capital market regulator, the Securities and Exchange Board of India (SEBI).
- While SEBI is a government body, mutual fund companies have formed the AMFI.
 - The Association of Mutual Funds in India (AMFI) is another statutory body that addresses investors' grievances.
- Every fund house must comply with the set of risk management guidelines by SEBI and AMFI.
- RBI also plays an essential role in regulating AMCs, if a bank is one of the sponsors.
- Finally, the Ministry of Finance works as the authority for all these regulators.

What are the recent changes?

- **Profitability criteria** - The SEBI has paved the way for technology startups to enter the mutual fund business by waiving the profitability requirement.
- Sponsors that are not fulfilling profitability criteria at the time of making

application shall also be considered eligible to sponsor a mutual fund.

- This is however subject to having a net-worth of not less than Rs 100 crore for the purpose of contribution towards the net-worth of the AMC.
- It is to be maintained at Rs. 100 crore until the AMC makes profits for 5 consecutive years.
 - This is aimed to encourage start-ups such as Paytm to enter the mutual fund space.
- Until now, regulators required an entrant to have 5 years of experience in the financial services business, demonstrate 3 years of profitability, and maintain a net worth of Rs 50 crore.
- **Other changes** - SEBI has approved a proposal to make it mandatory for all AMCs to maintain the minimum net worth on a continuous basis.
- At present, fund houses were required to maintain it toward the year end.
- Besides, all assets and liabilities of each scheme would have to be segregated and ring-fenced from other schemes of the mutual fund.
- This is in addition to the existing requirement of segregating bank and securities accounts.
- SEBI has also done away with the minimum promoters' contribution and subsequent lock-in requirements for issuers making an FPO (Follow on Public Offer).
- At present, promoters are mandated to contribute 20% toward FPOs.
- SEBI has also relaxed the one-year lock-in requirement for incoming investors.
- It has tweaked rules on minimum public holding norms for companies emerging out of the insolvency process.
 - Such companies would have to have at least 5% public shareholding at the time of their admission to dealing on stock exchange, as against no minimum requirement at present.
 - They would have to achieve 10% public shareholding within 12 months and 25% within three years.
 - This is a welcome move and shareholders will get at least 5% equity share as compared to zero share in a resolution plan.
- Companies undergoing insolvency resolution under the Insolvency and Bankruptcy Code (IBC) would have to make additional disclosures including -
 - i. specific details of resolution plan including details of assets post-CIRP (corporate insolvency resolution plan)
 - ii. details of securities continuing to be imposed on the companies' assets
 - iii. other material liabilities imposed on the company
 - iv. proposed steps to be taken by the incoming investor for achieving the minimum public shareholding

What is the rationale?

- SEBI has been continuously amending the rules governing the mutual fund industry over the last couple of years.
- The recent changes seek to increase penetration of the industry and improve governance at fund houses.
 - The number of mutual fund folios and demat accounts show that just 2% of the population is investing in these instruments.
 - Of the household financial savings, mutual funds account for only 7%.
 - The assets of the fund industry are also concentrated in larger cities with only 16% of these originating beyond the top 30 cities.
- The decision to relax the profitability criteria will allow companies that are constrained by their past profitability record to launch an AMC.
- With improved communication network along with the proliferation of smart phones, a large set of young investors are willing to invest through tech-enabled platforms.
- These platforms can now start an AMC to service their existing customer base.
- But, SEBI has to screen the experience, intent and past record of the promoting entity closely.

Source: The Economic Times, BusinessLine