Violations in Mutual Fund Houses

What is the issue?

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- The deteriorating governance standard in the mutual fund industry calls for a scrutiny.
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- It is high time that SEBI respond appropriately to the serious violations in mutual fund houses.
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What are the recent incidents?

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- Conflict of interest issues surfaced in HDFC Mutual Fund's shares allotment to its distributors ahead of its IPO (Initial Public Offering).
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- It also occurred in ICICI Mutual Fund's alleged move to bail out ICICI Securities when the latter's IPO was unhealthy.
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- SEBI recently gathered the mutual fund trustees for a meeting, after a series of violations by fund houses.
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- It includes operational violations such as laxity in collection of KYC documents or inappropriate apportioning of advertising expenses.
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- It also includes more serious violations such as
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i. lack of documentation of rationale for inter-scheme transfers
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ii. distribution of dividends without the consent of trustees
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iii. denying investors the correct Net asset value (value per share of a mutual

fund or an exchange-traded fund on a specific date or time)
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- These violations have undoubtedly affected the investor interest.
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What are the concerns?

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- **Response** - SEBI was correct in expressing disapproval of the trustees, as they are the first level regulators in mutual funds.
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- However, there is a concern that SEBI had been too slow to react to the violations.
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- It was less responsive to the violations during an inspection carried out between April 2014 and March 2016.
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- It is to be noted that about 60% of investors in equity funds and 70% in non-equity funds do not stick on beyond two years.
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- So continuous reshuffle of investors necessitates quick actions by the regulators, in case of violations, to protect investors' rights.
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- **Trustees** - Assets under management for mutual funds have trebled to Rs.23 lakh crore in the last five years.
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- Given this, the role of trustees in protecting investor interest is of utmost importance.
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- SEBI (Mutual Fund) Regulations, 1996 endows trustees with the power to take necessary remedial steps for violations in the conduct of the business.
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- SEBI must ensure that trustees take their jobs more seriously in protecting investors’ interests.
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- **Compliance officers** - Trustees are one of the layers of the three-tier

structure under which mutual funds work.
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- The other two are the sponsor and asset management companies (AMC).
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- Compliance officers work inside the asset management companies.
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- They are responsible for monitoring compliance of the Act and other rules and regulations.
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- They are better placed to spot the operational irregularities.
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- So besides trustees, the responsibility of the compliance officers should also be looked into.
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What is the way forward?

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- SEBI needs to take its findings to the logical conclusion by holding fund houses and compliance officers accountable.
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- Where possible, remedial action to protect investor interests needs to be taken.
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- This should be followed by the penal action against the concerned fund houses.
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Source: BusinessLine

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