

**EXECUTIVE DIRECTOR
INVESTMENT MANAGEMENT DEPARTMENT**

SEBI/IMD/CIR No.7/73202/06
August 2, 2006

**All Mutual Funds Registered with SEBI
Association of Mutual Funds in India (AMFI)**

Dear Sirs,

**Re: Investment in ADRs/GDRs/Foreign Securities and overseas ETFs by
Mutual Funds**

1. Please refer to SEBI Circulars MFD/CIR No. 4/052/99 dated September 1, 1999, MFD/CIR No. 5/062/99 dated September 30, 1999, MFD/CIR/17/419/02 dated March 30, 2002, MFD/CIR/18/21826/2002 dated November 7, 2002, SEBI/MFD/CIR No.02/6855/03 dated April 4, 2003, SEBI/MFD/CIR No.07/5573/04 dated March 19, 2004 and SEBI/IMD/CIR No.3/50241/05 dated September 26, 2005 pertaining to investment by mutual funds in ADRs/GDRs/foreign securities.
2. The aggregate ceiling for the mutual fund industry to invest in ADRs/GDRs issued by Indian companies, equity of overseas companies listed on recognized stock exchanges overseas and rated debt securities (subsequently referred to as "foreign securities") has been raised from US \$ 1 billion to US \$ 2 billion in the Finance Bill 2006 – 07.
3. **Conditions for investments in ADRs/GDRs/Foreign Securities**
 - a. The mutual funds can make investments in
 - i. ADRs/GDRs issued by Indian companies
 - ii. equity of overseas companies listed on recognized stock exchanges overseas
 - iii. foreign debt securities in the countries with fully convertible currencies, short term as well as long term debt instruments with highest rating (foreign currency credit rating) by accredited/registered credit rating agencies, say A-1/AAA by Standard & Poor, P-1/AAA by Moody's, F1/AAA by Fitch IBCA, etc.
 - iv. government securities where the countries are AAA rated.
 - v. units/securities issued by overseas mutual funds or unit trusts which invest in the aforesaid securities or are rated as mentioned above and are registered with overseas regulators.
 - b. The mutual funds can invest in ADRs/GDRs/Foreign Securities within overall limit of US\$2 bn. with a sub-ceiling for individual mutual funds which should not exceed 10% of the net assets managed by them as on March 31 of each relevant year, subject to a maximum of US \$100 mn. per mutual fund.

4. **Conditions for Investment in Overseas exchange traded funds(ETFs):**

Finance Bill for the year 2006-2007 permits a limited number of qualified Indian mutual funds to invest, cumulatively up to \$ 1 billion, in overseas exchange traded funds.

a. **Eligibility** : To be eligible to invest in overseas ETFs, either of the two conditions shall be satisfied:

- i. The Mutual Fund shall be in existence for a minimum period of 10 years as on July 31, 2006 and managing schemes.
- ii. The Mutual Fund or its Sponsors shall have experience, to be certified by the Trustees, of investing in foreign securities, and an appropriate disclosure regarding the nature of experience shall be made in the offer document.

b. **Limits**: The mutual funds can invest in overseas ETFs within overall limit of US\$ 1 bn. with a sub-ceiling for individual mutual fund which should not exceed 10% of the net assets managed by them as on March 31 of each relevant year, subject to a maximum of US \$50 mn. per mutual fund.

5. **Other Conditions:**

Apart from applicability of SEBI (Mutual Funds) Regulations, 1996 and guidelines issued from time to time, the mutual funds shall adhere to the following specific guidelines for making investments in ADRs/GDRs/Foreign Securities and overseas ETFs by the Mutual Fund schemes:

a. **Appointment of dedicated Fund Manager**

The Mutual Fund shall appoint a dedicated Fund Manager for making investments in ADRs/GDRs/Foreign Securities and overseas ETFs. However, the existing schemes which have already invested in ADRs/GDRs/Foreign Securities shall ensure compliance with the said requirement within a period of six months from the date of this circular.

b. **Due Diligence**

Boards of Asset Management Companies (AMCs) and trustees shall exercise due diligence in making investment decisions as required under Regulation 25 (2). They shall make a detailed analysis of risks and returns of investment in foreign securities and overseas ETFs, comparing them with likely yields of the securities available in domestic markets and how these investments

would be in the interest of investors. Investment must be made in liquid actively traded securities.

Boards of AMCs and trustees may prescribe detailed parameters for making such investments which may include identification of countries, country rating, country limits, etc. They shall satisfy themselves that the AMC has experienced key personnel, research facilities and infrastructure for making such investments. Other specialised agencies and service providers associated with such investments e.g. custodian, bank, advisors, etc should also have adequate expertise and infrastructure facilities. Their past track record of performance and regulatory compliance record, if they are registered with foreign regulators, may also be considered. Necessary agreements may be entered into with them as considered necessary.

All investment decisions shall be recorded in accordance with SEBI circular dated July 27, 2000.

c. Disclosure Requirements

The following disclosure requirements shall be mandatory for mutual fund schemes proposing to invest in foreign securities.

- i. Intention to invest in foreign securities/ ETFs shall be disclosed in the offer documents of the schemes. The attendant risk factors and returns ensuing from such investments shall be explained clearly in offer documents. The mutual funds shall also disclose as to how such investments will help in the furtherance of the investment objectives of the schemes. Such disclosures shall be in a language comprehensible to an average investor in mutual funds.
- ii. The mutual funds shall disclose the name of the dedicated Fund Manager for making investments in ADRs/GDRs/Foreign Securities and Overseas ETFs.
- iii. In case of schemes investing in ETFs the nature of experience of mutual fund or its Sponsors of having invested in foreign securities shall be disclosed shall be appropriately disclosed in the offer document.
- iv. The mutual funds shall disclose exposure limits i.e. the percentage of assets of the scheme they would invest in foreign securities/ ETFs.
- v. Such investments shall be disclosed while disclosing half-yearly portfolios in the prescribed format by making a separate heading "Foreign Securities/overseas ETFs." Scheme-wise percentage of investments made in such securities shall be disclosed while publishing half-yearly results in the prescribed format, as a footnote.

d. Investment by Existing Schemes:

Existing schemes of mutual funds where the offer document provides for investment in foreign securities and attendant risk factors but which have

not yet invested, may invest in foreign securities, consistent with the investment objectives of the schemes, provided a dedicated fund manager

has been appointed for making investments in ADRs/GDRs/Foreign Securities. Any additional disclosure as specified above shall be informed to unitholders by way of addendum.

In case the offer document of an existing scheme does not provide for investment in ADRs/GDRs /foreign securities and overseas ETFs, the scheme, if it so desires, may make such investments in accordance with these guidelines, provided that: prior to investment in ADRs/GDRs /foreign securities and overseas ETFs for the first time, the AMC shall ensure that a written communication about the proposed investment is sent to each unitholder and an advertisement is given in one English daily newspaper having nationwide circulation as well as in a newspaper published in the language of the region where the Head Office of the mutual fund is situated. The communication to unitholders shall also disclose the risk factors associated with such investments.

e. Reporting to Trustees :

The AMCs shall send detailed periodical reports to the trustees which shall include the following aspects:

- i. Performance of investments made in foreign securities and overseas ETFs in various countries.
- ii. Amount invested in various schemes and any breach of the exposure limit laid down in the scheme offer documents.

f. Review of Performance

Boards of AMCs and trustees shall review the performance of investments made in foreign securities/overseas ETFs in their meetings by comparing the yield with that of investment opportunities available in domestic markets and shall decide further course of action. In case of schemes investing exclusively in foreign securities/overseas ETFs, performance may also be compared with appropriate benchmark(s).

g. Reporting to SEBI

The AMCs and trustees shall offer their comments on the compliance of these guidelines in the quarterly and half-yearly reports filed with SEBI.

h. Clause 4 of Seventh Schedule of the SEBI (Mutual Funds) Regulations 1996

It is clarified that Clause 4 of Seventh Schedule of the SEBI (Mutual Funds) Regulations 1996 which restricts investments in mutual fund units upto 5% of net assets and prohibits charging of fees, shall not be applicable to investments in mutual funds in foreign countries made in accordance with guidelines as per aforesaid circular. However, please

note that the management fees and other expenses charged by the mutual fund(s) in foreign countries along with the management fee and recurring expenses charged to the domestic mutual fund scheme shall not

exceed the total limits on expenses as prescribed under Regulation 52(6). Where the scheme is investing only a part of the net assets in the foreign mutual fund(s), the same principle shall be applicable for that part of investment. The details of calculation for charging such expenses shall be reported to the Boards of AMC and trustees and shall also be disclosed in the Annual Report of the scheme.

6. SEBI Circulars MFD/CIR No. 4/052/99 dated September 1, 1999, MFD/CIR No. 5/062/99 dated September 30, 1999, MFD/CIR/17/419/02 dated March 30, 2002, MFD/CIR/18/21826/2002 dated November 7, 2002, SEBI/MFD/CIR No.02/6855/03 dated April 4, 2003, SEBI/MFD/CIR No.07/5573/04 dated March 19, 2004 and SEBI/IMD/CIR No.3/50241/05 dated September 26, 2005 pertaining to investment by mutual funds in ADRs/GDRs/foreign securities stand withdrawn.
7. The procedure for applying to SEBI for making investments in ADRs/GDRs/foreign securities and overseas ETFs is given in the Annexure.
8. These guidelines are issued in exercise of powers conferred under Section 11(1) of the Securities and Exchange Board of India Act, 1992 read with the provisions of Regulation 77 of SEBI (Mutual Funds) Regulations, 1996 to protect the interests of investors in securities and to promote the development of, and to regulate the securities market.

Yours faithfully,

R. K. Nair

Encl: a/a

PROPOSAL FOR INVESTMENTS IN ADRs/GDRs/ FOREIGN SECURITIES / OVERSEAS ETFs

Name of the Mutual Fund:	
SEBI Registration No.:	
Amount Proposed to be Invested in ADRs /GDRs /Foreign Securities / Overseas ETFs (Rs. crores)	
Net Assets of the Fund as on March 31 (Rs crores)	
Schemes of the Mutual Fund through which investment is proposed:	Name and Type of scheme(s)
Whether the investment is consistent with the Investment Objectives of the Scheme (s);	
Whether the offer document(s) provides for Overseas Investments and discloses the attendant risks	
Name and Address of the branch of the bank through which Foreign Currency Transactions are to be routed:	
Details of all overseas service providers proposed to be engaged including custodians, specialised agencies etc. (Details must include name & address, services to be rendered, details of fee arrangement proposed, whether their track record of performance and regulatory compliance considered, their valid registration with overseas regulators, details of experience/expertise, assets under management/custody, etc.)	

Declaration

1. Boards of AMC and trustees have exercised due diligence as required under Regulation 25(2) and Guidelines issued in this regard.
2. Board of AMC and trustees are satisfied that
 - i. The proposed investments in ADRs/GDRs issued by Indian companies or foreign securities or overseas ETFs are consistent with the investment objectives of the above mentioned scheme(s) and are in the interest of investors.
 - ii. The systems and procedures adopted by the AMC including the arrangements made with the overseas service providers are adequate to support such investments and to safeguard the interest of investors.
 - iii. The overseas service providers have sufficient experience, competence and a satisfactory track record of performance and regulatory compliance.

A resolution to the above effect has been passed by the Boards of AMC and trustees on.....
(dates)

Place:

Signatures

Name:

Designation:

(Authorised by Trustees)

Date: