Frequently Asked Questions (FAQ) - Portfolio Managers

September 20, 2024

1. The document of FAQs is not a legal document.
2. The FAQs are meant for the purpose of providing basic guidance pertaining to Portfolio Managers
3. The document is merely a compilation of questions and is not to be construed as a replacement to any of the provisions contained in the Acts, Regulations, Circulars, PMS Manual, etc. The user is expected to keep abreast of the current provisions of the relevant Acts, Regulations, Circulars and Policy Notes etc.

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1. Who is a Portfolio Manager?

A portfolio manager is a body corporate, which, pursuant to a contract with a client, advises or directs or undertakes on behalf of the client (whether as a discretionary portfolio manager or otherwise) the management or administration of a portfolio of the client.

2. What is the difference between discretionary portfolio management service and non-discretionary portfolio management service?

In **discretionary** portfolio management service, the portfolio manager individually and independently manages the funds and securities of each client in accordance with the needs of the client.

Under the **non-discretionary** portfolio management service, the portfolio manager manages the funds in accordance with the directions of the client.

3. Who is co-investment portfolio manager?

Co-investment portfolio manager is the investment manager of a Category I or II Alternative Investment Fund (AIF) and provides services only to the investors of such AIF.

4. What is the procedure for obtaining portfolio manager registration from SEBI?

An application is to be made in Form-A available at https://siportal.sebi.gov.in along with a non-refundable application fee of INR 1,00,000/- plus applicable taxes. Additionally, application in physical form has to be submitted alongwith self-certified copy of all the documents.

5. **Where can I find the contents of agreement between the portfolio manager and his clients?**

   The contents of the agreement between the portfolio manager and clients are always part of Know Your Client (KYC) documents and terms and conditions of the agreement between Portfolio Manager and his clients should be in accordance with Schedule IV of SEBI (Portfolio Managers) Regulations, 2020.

6. **What is the minimum net worth requirement of a portfolio manager?**

   The portfolio manager is required to have a minimum net worth of INR 5 crore at all times.

7. **What is the period of validity of PMS registration Certificate?**

   The certificate of PMS registration is valid unless it is suspended or cancelled by the Board. A portfolio manager who has been granted a certificate of registration, to keep its registration in force, need to renew every three years by paying the fee, from the date of grant of certificate of registration. A prospective client is always advised to check the registration detail of portfolio manager at SEBI website before entering into any agreement.

8. **What fees can a portfolio manager charge from clients for the services rendered by him?**

   Portfolio manager can charge fee as per the agreement with the client for rendering portfolio management services. The fee so charged may be a fixed amount or a performance-based fee or a combination of both. However, no upfront fee can be charged by the portfolio manager directly or indirectly from the clients.

   The agreement between the portfolio manager and the client is also required to include the quantum and the manner of fees payable by the client for each service rendered by the portfolio manager directly or indirectly.

9. **What are the various securities in which a Portfolio Manager may invest clients' funds?**

   Under Discretionary Portfolio Management Service (DPMS), Portfolio Manager invests funds of his clients in the securities listed or traded on a recognized stock exchange, money market instruments, units of Mutual Funds through direct plan and other securities as specified by the Board from time to time.

   Under Non-Discretionary Portfolio Management Service (NDPMS), Portfolio Managers may invest up to 25% of the AUM of a client in unlisted securities, in addition to the securities permitted for discretionary portfolio management.

   "Unlisted securities" for investment by Portfolio Managers include units of Alternative Investment Funds (AIFs), Real Estate Investment Trusts (REITs), Infrastructure Investment Trusts (InvITs), debt securities, shares, warrants, etc. which are not listed on any recognized stock exchanges in India.

10. **Can a portfolio Manager invest funds of his discretionary client in unlisted bonds?**

    No, a portfolio Manager cannot invest funds of a discretionary client in unlisted bonds.

11. **Can portfolio managers invest in derivatives including commodity derivatives?**

    Portfolio Managers can invest in derivatives for the purpose of hedging and portfolio rebalancing and it has to be as per the terms specified in the portfolio management agreement. Portfolio managers are also permitted to participate in exchange traded commodity derivatives on behalf of their clients subject to certain terms and conditions.

12. **Under Non-Discretionary PMS, Can a Portfolio Manager invest more than 25% in unlisted securities?**

    No, a portfolio Manager cannot invest more than 25% in unlisted securities on behalf of a client registered for non-discretionary PMS services.

13. **Can a portfolio manager invest in the securities of associates / related parties?**

    Portfolio manager can make investments within the prescribed limits in the securities of its related parties or its associate only after obtaining the prior consent of the client in accordance with SEBI Circular dated August 26, 2022.

14. **What is the minimum value of funds or securities that can be accepted by the portfolio manager from the client while opening the PMS account?**

    The portfolio manager is required to accept minimum INR 50 Lacs or securities having a minimum worth of INR 50 Lacs from the client.

15. **Is partial withdrawal of Portfolio permitted, for the existing clients of Portfolio Managers?**

    The client can withdraw partial amounts from his portfolio, while ensuring that requisite minimum investment of INR 50 Lacs is maintained.

16. **Is the client required to top up his account if the portfolio value falls below the minimum investment amount?**

    No, client is not required to maintain minimum investment of INR 50 lacs, if the portfolio value falls below it.

17. **What are the limits on transactions executed through associates of Portfolio Managers?**

    Charges for all transactions in a financial year (Broking, Demat, custody etc.) through self or associates are capped at 20% by value per associate (including self) per service. Such limits are applicable separately for demat services, custodian services etc.

Further, any charges to self/associate should not be at rates more than that paid to the non-associates providing the same service.

For instance, in case of Broking services, the total amount paid to the associate Stock Broker cannot be more than 20% of the total brokerage paid for trades on behalf of its clients during the year.

If Portfolio Manager uses multiple Stock Brokers who are its associates, then transaction through each associate Stock Broker are capped at 20% of the total brokerage paid for trades on behalf of its clients during the year.

18. Is there any restriction on the number of non-associates through which transactions stated in the previous question may be executed?

There is no restriction imposed on the number of non-associate Stock Brokers, Depository Participants or Custodians that may be engaged by a Portfolio Manager, e.g. Portfolio Manager may utilize a single non-associate Stock Broker for executing 100% of the trades on behalf of its clients.

19. How performance of Portfolio Managers is reported to clients?

Portfolio Managers are required to present the Time-weighted Rate of Return ('TWRR') of the Investment Approach (IA) along with the trailing return of the selected benchmark when communicating/ advertising/ publishing/ mentioning performance of an Investment Approach.

Portfolio Manager are required to present the Extended Internal Rate of Return ('XIRR') for each IA the investor invests in, when reporting performance to an investor. This needs to be accompanied by the minimum, maximum and median XIRR return generated across all investors in each of the IA the investor has invested in. The TWRR of the respective IA(s) and the trailing return of the benchmark(s) required to be presented separately. However, the following disclaimer must also follow:

"Please note that performance of your portfolio may vary from that of other investors and that generated by the Investment Approach across all investors because of
1) the timing of inflows and outflows of funds; and
2) differences in the portfolio composition because of restrictions and other constraints."

20. What kind of reports can the client expect from the portfolio manager?

The portfolio manager has to furnish a quarterly report to the client which should contain the following details, namely: -

(a) the composition and the value of the portfolio, description of securities and goods, number of securities, value of each security held in the portfolio, units of goods, value of goods, cash balance and aggregate value of the portfolio as on the date of report;

(b) transactions undertaken during the period of report including date of transaction and details of purchases and sales;

(c) beneficial interest received during that period in the form of interest, dividend, bonus shares, rights shares, etc;

(d) expenses incurred in managing the portfolio of the client;

(e) details of risk foreseen by the portfolio manager and the risk relating to the securities recommended by the portfolio manager for investment or disinvestment;

(f) default in payment of coupons or any other default in payments in the underlying debt security and downgrading to default rating by the rating agencies, if any;

(g) details of commission paid to distributor(s) for the particular client.

21. Where can I find the Disclosure documents of a Portfolio Manager?

Every Portfolio Manager is required to ensure that a copy of Disclosure Document is available on its website at all times.

22. What is the disclosure mechanism of the portfolio managers to their clients?

Every client of a Portfolio Manager need to be provided with a Disclosure Document prior to entering into an agreement.

The Disclosure Document contains the quantum and manner of payment of fees payable by the client for each activity, portfolio risks, complete disclosures in respect of transactions with related parties, the performance of the portfolio manager and the audited financial statements of the portfolio manager for the immediately preceding three years.

23. Does SEBI approve any of the services offered by portfolio managers?

No, SEBI does not approve any of the services offered by the Portfolio Manager.

24. Does SEBI approve the disclosure document of the portfolio manager?

No, SEBI does not certify the accuracy or adequacy of the contents of the Disclosure Document.

25. What are the rules governing services of a Portfolio Manager?

The services of a Portfolio Manager are governed by the agreement between the portfolio manager and the investor. The agreement covers the minimum details as specified in the SEBI Portfolio Manager Regulations. However, additional requirements can be specified by the Portfolio Manager in the agreement with the client. Hence, an investor is advised to read the agreement carefully before signing it.

26. Can a Portfolio Manager impose a lock-in on the investor?

Portfolio managers cannot impose a lock-in on the investment of their clients. However, a portfolio manager can charge applicable exit fee from the client for early exit, as laid down in SEBI PMS Master Circular.

27. Can a Portfolio Manager offer indicative or guaranteed returns?

No, Portfolio Manager cannot offer indicative or guaranteed returns.

28. Where can an investor look out for information on portfolio managers?

Investors can log on to the website of SEBI www.sebi.gov.in for information on SEBI regulations and circulars pertaining to portfolio managers. Addresses of the registered portfolio managers are also available on the SEBI website. Information on monthly reports submitted by Portfolio Managers to SEBI can be accessed at https://www.sebi.gov.in/sebiweb/other/OtherAction.do?doPmr=yes.

29. What is the procedure to seek change in control by a portfolio manager and how long is the validity of prior approval?

A portfolio manager can make online application at https://siportal.sebi.gov.in and validity period of the prior approval granted is six months from the date of approval. A portfolio manager, pursuant to change in control, has to apply for fresh registration within a period of six months from the date of prior approval.

30. Does information about change in control of a portfolio manager required to be informed to the clients?

A portfolio manager has to inform all the existing clients about the proposed changes prior to effecting the same so that the clients can take decision regarding continuing with the changed management or otherwise. A portfolio manager has to provide an option to the investors to exit without any exit load within a period of 30 calendar days from the date of communication.

31. What is eligible investment fund?

"Eligible Investment Fund" have the same meaning as assigned to it in Sub-Section (3) of Section 9A of the Income-tax Act, 1961

Section 9A (3) inter-alia states that a fund established or incorporated or registered outside India, which collects funds from its members for investing it for their benefit and inter-alia fulfils the following conditions;

i. not a person resident in India;
ii. is resident of a country or a specified territory as specified by Central Government;
iii. the aggregate participation or investment in the fund, by persons resident in India does not exceed five per cent of the corpus of the fund;
iv. has a minimum of twenty-five members who are, directly or indirectly, not connected persons;
v. cannot invest more than 25% of its corpus in any entity;
vi. cannot make any investment in its associate entity;
vii. the monthly average of the corpus of the fund should not be less than 100 crore rupees;

viii. cannot carry on or control and manage, directly or indirectly, any business in India;

ix. not to engage in any other activities other than those undertaken by the eligible fund manager on its behalf.

32. Who is eligible fund manager and what is his obligations and responsibilities?

i. Eligible Fund Manager (EFM) is defined under sub-section 4 of Section 9A of the Income Tax Act, 1961 which inter-alia states as follows:

ii. Any person who is engaged in the activity of fund management and fulfils the following conditions;
Not an employee of the eligible investment fund or a connected person of the fund;
Registered as Fund Manager or an investment advisor in accordance with the specific regulations;
Acting in the ordinary course of his business as a fund manager;
Along with his connected persons is not entitled to more than twenty per cent of the profits accruing or arising to the Fund from the transactions carried out by the Fund through the fund manager.

<u>Obligations and responsibilities of Eligible Fund Managers</u>

i. Has to comply with the requirements specified under Section 9A of the Income-tax Act.

ii. Offer discretionary or non-discretionary or advisory services or a combination thereof.

iii. Segregate the funds and securities of eligible investment funds from those of its other eligible funds/ clients.

iv. Maintain and segregate its books and accounts pertaining to its activities as a portfolio manager to eligible investment funds and other clients.

v. Appoint a custodian

33. What is the investor charter and what kind of information it contains?

The investor charter is a brief document which contains detail of different services provided by the portfolio managers to the investors along with estimated timelines, like account opening, agreement with the portfolio manager, periodic statements to the investors, investor grievance redressal mechanism and responsibilities of investors etc. at one single place.

34. Where can an investor file their complaints?

The grievance redressal and dispute mechanism is mentioned in the disclosure document and on the website of respective Portfolio Manager. Investors would also find the name, address and telephone number of the investor relation officer of the portfolio manager (who attends to the investor queries and complaints) in the disclosure document. In case of non redressal of the complaint by the Portfolio Manager, investors can approach SEBI for redressal of their complaints. Investors may lodge their complaints through SCORES (SEBI Complaints Redress System - https://scores.sebi.gov.in) or by sending their complaints on the address given below.

Office of Investor Assistance and Education,
Securities and Exchange Board of India,
SEBI Bhavan II
Plot No. C7, 'G' Block,
Bandra-Kurla Complex, Bandra (E),
Mumbai - 400 051

35. How is TWRR calculated for the purpose of calculating performance of the portfolio manager?

The time-weighted rate of return breaks up the return on an investment portfolio into separate intervals, based on whether money was added or withdrawn from the fund. The detailed calculation and an indicative illustration in this regard is provided in **Annexure 1**.

36. How will the performance fee be calculated considering the high watermark principle?

An indicative illustration for calculation of performance fee, considering high watermark principle, is provided in **Annexure 2**.

Annexure 1: Calculation of Time-Weighted Rate of Return

Steps to Compute Individual Portfolio TWRR:

1. Begin with market value at the beginning of the period.
2. Move forward through time towards the end of the period.
3. Compute the market value of the portfolio immediately before the contribution to / withdrawal from the portfolio.
4. Calculate a sub-period return for the period between the valuation dates i.e. the dates corresponding to the contribution and / or withdrawal dates using the formula:
   (Ending Market Value - Beginning Market Value - Contribution + Withdrawal) ÷ (Beginning Market Value + Contribution - Withdrawal)
5. Repeat steps 3 and 4 for each contribution and / or withdrawals
6. When there are no more contributions and / or withdrawals, calculate a subperiod return for the last period to the end of the period market value.
7. Compound the sub-period returns by taking the product of (1+sub-period returns). This is called geometric linking or chain linking of the sub-period returns.
8. Subtract 1 from the product value as arrived at in step 7 above.
9. Express the result as per 8 above in percentage terms to get the TWRR for the time period under evaluation.

Example:

An account is funded on 1-Jan-2019 by an amount 50,00,000. On 1-Mar-2019, client contributed additional 20,00,000. The market value of the account as on 28-Feb-2019 is 49,00,000. On 1-Oct-2019, the client withdrew an amount of 10,00,000 from the account. The market value of the account on 30-Sep-2019 was 75,00,000. The market value of the account on 31-Dec-2019 was 70,00,000.

Sub-Periods	**Sub-period returns**	**Sub-period returns + 1**
1-Jan-2019 to 28-Feb-2019	(49,00,000 – 50,00,000) ÷ 50,00,000 = -2.00%	(1 – 2.00%) = 0.98
1-Mar-2019 to 30-Sep-2019	(75,00,000 – 49,00,000 – 20,00,000) ÷ (49,00,000 + 20,00,000) = 8.69%	(1 + 8.69%) = 1.08
1-Oct-2019 to 31-Dec-2019	(70,00,000 - 75,00,000 + 10,00,000) ÷ (75,00,000 - 10,00,000) = 7.69%	(1 + 7.69%) = 1.07
TWRR		**((0.98*1.08*1.07) – 1)*100 = 14.7%**

Annexure 2: Illustration - Computation of Performance fee by Portfolio Manager

Particulars	Year 1	Year 2	Year 3	Year 4
Initial Corpus	**50,00,000**	**65 ,92,000**	**47,98,976**	**70 ,92,887**
Hurdle rate of return (A)	**8%**	**8%**	**8%**	**8%**
Performance fee over hurdle rate (B)	**20%**	**20%**	**20%**	**20%**
Fixed Fee (C)	**1.5%**	**1.5%**	**1.5%**	**1.5%**
Brokerage p.a. (D)	**0.20%**	**0.20%**	**0.20%**	**0.20%**
Other Expenses (E)	**0.50%**	**0.50% -**	**0.50%**	**0.50%**
Rate of return on the portfolio (I)	**40%**	**25%**	**50%**	**40%**

Assumptions:

1. Performance linked fee and fixed management fee are calculated on an annual basis (i.e, performance period = 1 year)
2. All figures in the tables have been assumed for the purpose of illustration
3. Other expenses mentioned include Custody & FA charges, RTA fees etc

All amounts in Rs. & all returns are pre-tax

Sl No.	Particulars	Year 1		Year 2		Year 3		Year 4		Year 5
		Amount in Rs.		Amount in Rs.		Amount in Rs.		Amount in Rs.		
1	**Amount invested by client / Opening value**	**50,00,000**		**65 ,92,000**		**47,98,976**		**70 ,92,887**		
2	**Portfolio Returns duing the year (=I * 1)**			-16,48,000		23,99,488		28 ,37,155		
3	Brokerage and Transaction cost @ 20bps **(=D * 1)**	20,00,000	**70 ,00,000**	13,184		9,598		14,186		
4	Other Expenses**(= E*1)**	10,000				23,995				
5	Fixed Management Fee **(= C * 1)**			32,960		71,985		35,464		
6	**Pre-performance fee closing value of portfolio (1+2-3-4-5) Note : If this value exceeds the high water mark, only then shall performance fee be charged to the client**	25,000		98,880	**49 ,44,000**	70,92,887	**71 ,98,464**	1,06,393	**99 ,30,041**	
7	Returns realised by investor (pre-performance fee) over High Water Mark **(= (6-14)/14*100)** [For Year 1, returns over initial corpus would be considered]	75,000		47 ,98,976		2.94%		97 ,73,998		
8	Returns realised by investor over hurdle rate (= **7-A,** and in case of negative returns, it shall be zero)	68,90,000		-30.35%		-5.06%		37.80%		
9	Performance fee levied by PM (in %) **(Perf. Fee = 8*B)**	37.80%	4,08,000	0%		0%				
10			65,92,000 **31.84%**			-				

11	**Amount of performance fee recovered by PM (high-watermark applicable) on Capital Amount (= 9*1)**	29.80%		0%				29.80%		
12		5.96%			1,45,024			5.96%		
13	Total Charges During the year **(=3+4+5+10)**						1,05,577		5,78,779	
	Net Value of the portfolio at the end of year **(=1+2-11)**			-	47,98,976		70 ,92,887		93 ,51,262	
	**Overall Returns to investor in % (=(12-1)/1) ***100	**2,98,000**			**-27.20%**		**47.80%**	**4,22,736**	**31.84%**	
14	**High Water Mark for calculation of performance fee for the next performance period**	**-**		**6890000**		**6890000**		**7092887**		**9773998**