ET Markets

FPIs bring back age-old PCC model to ringfence liability under new regulation

In a PCC the liability or losses of one cell does not spill over to other cells.

By *Sugata Ghosh* ET Bureau| May 10, 2019, 08.09 AM IST

ThinkStock Photos

Compare it with a mutual fund with multiple schemes under the trust structure.

MUMBAI: In the years after the Ketan Parekh scam in 2001, the Indian capital market regulator had clamped down on foreign funds that ran protected cell companies or PCCs, which were bankruptcy remote special vehicles catering to many rich international investors betting on Indian shares.

These cells had then sparked regulatory concerns because of their opaque nature which masked the identities of actual investors.

After more than a decade, PCCs may make a comeback, thanks to Sebi's new rule that require foreign portfolio investors (FPIs) to disclose the names of ultimate beneficial owners or, the last natural persons who have put money in a fund.

The Sebi-constituted panel, led by former RBI deputy governor HR Khan, is understood to be in favour of allowing PCCs in the present regulatory environment, two persons familiar with the subject told ET.

"Post-Lehman crisis, more and more foreign investors insist on investing into PCCs which ringfence liabilities. Earlier, there were strong suspicion that many PCCs may have been used to manipulate stocks. But following the new know-your-customer rules that apply to FPIs, there is a growing feeling that PCCs should be allowed to attract investments," said a source.

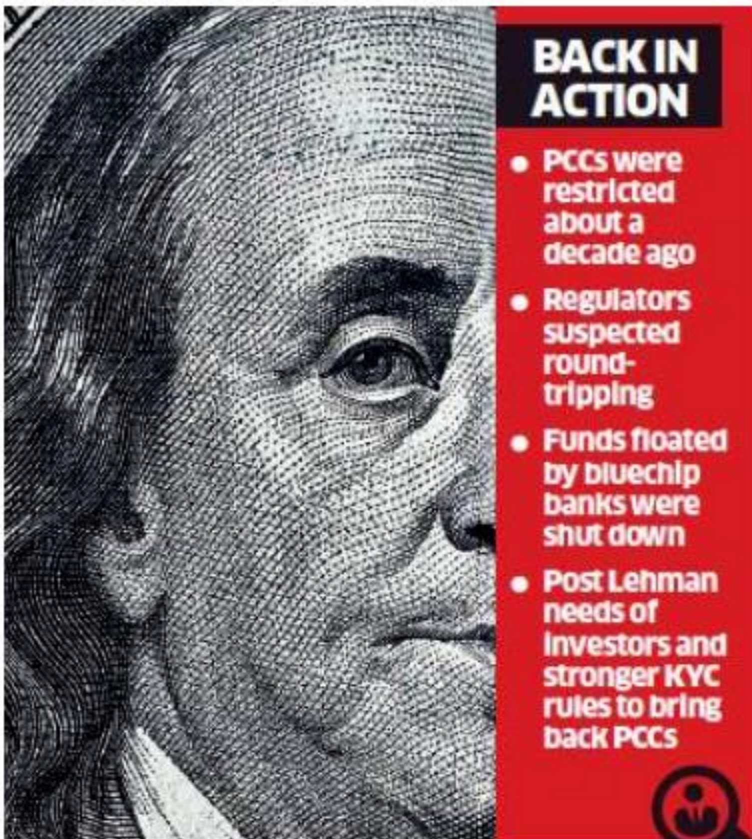
In a PCC, each cell is a legal entity, and the liability or losses of one cell does not spill over to other cells.

“Compare it with a mutual fund with multiple schemes under the trust structure. A PCC has an umbrella asset management company with multiple cells. What makes it different is if an investor sues the trust, the liability would be confined to the cell in which the person concerned has invested,” said an official with a custodian bank.

At present FPIs registered with the Indian regulator are required to give an undertaking that their funds are not structured as PCCs or segregated portfolio companies. This is part of the regulation that aims to minimise round-tripping of funds.

“PCCs allow cellular assets to be legally ring-fenced. All modern fund jurisdictions, including Singapore and Hong Kong, have recently launched fund regimes centred around bankruptcy remote structures like PCC,” said Richie Sancheti, head of Investment Funds at law firm Nishith Desai Associates.

Sebi, according to Sancheti, has selectively re-recognised PCCs when the issue came up for UK-based FPI funds that were asked by their home regulator to roll over to protected cell regime. “The key ask from Sebi has been around KYC disclosures and ‘broad investor base’ criteria at cellular level,” he said.



The Khan committee, which comprises experts on securities market and law, was set up to explore ways the regulations for FPIs — the dominant club in the country’s capital market — could be recast to make it easier for these offshore funds to trade

in India. The committee is expected to release its report soon. According to sources, it could recommend easier participation by NRIs in broad-based funds (with 20 or more investors) and allowing overseas corporate bodies (which are dominantly controlled by NRIs) to invest directly in India.