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SEBI's QFI norms to curb misuse by resident Indians

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MUMBAI: India's regulators have unveiled rules for direct investment in stocks by foreign investors, including individuals, seeking to put curbs on opaque structures to prevent routing of funds by resident Indians through this window.

On January 1, the government decided to allow foreign resident investors to invest directly in the Indian equities market, in a move aimed at boosting capital inflows, reducing market volatility and deepening the markets. QFIs can buy up to 5% of the paid-up capital of a company, with the overall limit capped at 10% in a company.

SEBI said entities having opaque structures, where details of the ultimate beneficiary are not accessible or where the beneficial owners are ring fenced from each other, will not be allowed to open demat account as qualified foreign investor, or QFI.

The regulator has also said that these investors will need to take delivery of shares they purchase on the local bourses. The onus of carrying out full due diligence on an overseas investor is now on depository participants, which includes banks, with other obligations also cast on them.

"The DP (depository participant) shall perform appropriate due diligence at the time of account opening and ensure that such entities are not allowed to open demat account," SEBI said in a statement on Friday. "An express undertaking to this effect shall be obtained by DP from the QFI."

SEBI said foreign investors, who wish to invest directly in Indian shares, will also have to obtain a separate permanent account number or PAN. While this rule has been imposed to prevent money laundering, brokers feel this could be a hurdle as most foreign residents are already compliant with their countries' rules.

"It seems that this route available to foreign investors is not necessarily restricted to individuals. This being distinct to the FII route, investors may prefer this as they don't have to fulfil the broad-based criteria. Also, there is no registration requirement with any authority," said Kishore Joshi of Nishith Desai Associates, a leading law firm.

QFIs have also been barred from issuing offshore derivatives instruments or participatory notes and will also have to give a declaration to this effect to the DP.

The SEBI circular is silent on whether these investors can trade in India's futures and options segment. The regulator said DPs will have to ensure that the same set of end beneficial owners is not allowed to open more than one demat account as QFI.

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