Frequently Asked Questions (FAQ) - Portfolio Managers

August 25, 2020

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 securities or funds 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. **What is the procedure of making an application for obtaining registration as a portfolio manager from SEBI?**

   For obtaining registration as a portfolio manager, an applicant is required to make an online application through the SEBI Intermediaries Portal along with a non-refundable application fee of INR1,00,000/- by way of direct credit in the bank account of SEBI through NEFT/RTGS/IMPS or any other mode allowed by RBI. Alternatively, the application fee can also be paid by way of demand draft drawn in favor of 'Securities and Exchange Board of India', payable at Mumbai or at the place where respective regional office is located.

   Any applicant desirous of seeking registration as a Portfolio Manager under PMS Regulations shall file their applications in Form A on the online system at https://siportal.sebi.gov.in

4. **What is the minimum networth requirement of a portfolio manager?**

   The portfolio manager is required to have a minimum networth of INR 5 crore.

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

   SEBI (Portfolio Managers) Regulations, 2020 provide that the portfolio manager shall charge a 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 fees shall be charged by the portfolio manager directly or indirectly to the clients.

The agreement between the portfolio manager and the client shall, *inter-alia,* also include the quantum and the manner of fees payable by the client for each activity for which service is rendered by the portfolio manager directly or indirectly.

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

Under Discretionary Portfolio Management Service (DPMS), Portfolio Managers shall invest 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 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 shall 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.

7. Whether the funds of clients availing discretionary PMS may be invested in unlisted bonds, which are traded over the counter but settled and reported to the Stock Exchanges?

No.

8. Will a portfolio manager be required to take prior approval from SEBI in case of change in status or constitution or control?

No.

However, the Portfolio Manager shall inform SEBI of any proposed material change, including change in status or constitution or control, which may have a bearing on the registration.

Portfolio Manager shall submit such information to SEBI at least 30 days prior to the change or as and when the decision for such change is approved by the directors/partners, whichever is earlier.

9. An existing client of Non-Discretionary PMS, who has already invested in certain unlisted securities, wants to subscribe to rights issue of such unlisted securities, which may result in breach of the 25% limit. Is this permitted?

An active breach due to investor action, subsequent to corporate actions like subscription to rights issue, which results in breach of 25% limit applicable to Non-Discretionary portfolios, shall be considered as non-compliance.

However, a passive breach due to corporate actions like bonus with respect to value of unlisted securities will not be considered as non-compliance.

10. 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.

11. Clients on-boarded by the Portfolio Manager prior to January 21, 2020 were required to bring in minimum of INR 25 Lacs as their initial investment. What is the minimum amount that may be further invested (top-up) by such clients on or after January 21, 2020?

Clients of Portfolio Managers on-boarded before January 21, 2020 shall, in case of any top-up, comply with the requirement of new minimum investment amount and top up their accounts to minimum INR 50 Lacs.

12. Is Partial withdrawal of Portfolio permitted, for the existing clients of Portfolio Managers?

The client may withdraw partial amounts from his portfolio, in accordance with the terms of the agreement between the client and the Portfolio Manager. However, the value of investment in the portfolio after such withdrawal shall not be less than the applicable minimum investment amount.

13. Is the client required to top up his account if the portfolio value falls below the minimum investment amount as provided in the SEBI (Portfolio Managers) Regulations, 2020 as a result of valuation of portfolio?

No.

14. How are the limits on transactions executed through associates of Portfolio Managers applicable?

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

Further, any charges to self/associate shall 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 shall be capped at 20% of the total brokerage paid for trades on behalf of its clients during the year.

15. 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. For e.g. The Portfolio Manager may utilize a single non-associate Stock Broker for executing 100% of the trades on behalf of its clients.

16. On what basis is the performance of the portfolio manager calculated?

The performance of a discretionary portfolio manager is calculated using time weighted rate of return (TWRR) method for the immediately preceding three years or period of operation, whichever is lesser.

SEBI Circular No. SEBI/HO/IMD/DF1/CIR/P/2020/26 dated February 13, 2020, *inter-alia*, provides information on reporting of performance by Portfolio Managers and also a client reporting format which includes information on the performance of the client account, portfolio manager and the appropriate benchmark.

17. 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**.

18. 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**.

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

The portfolio manager shall furnish periodically a report to the client, as per the agreement, but not exceeding a period of three months and such report shall 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.

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

The portfolio manager provides to the client the Disclosure Document prior to entering into an agreement with the client.

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.

21. 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. An investor has to invest in the services based on the terms and conditions laid out in the disclosure document and the agreement between the portfolio manager and the investor.

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

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

23. 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 should cover 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.

24. 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 fees from the client for early exit, as laid down in the agreement subject to provision of SEBI Circular No. SEBI/HO/IMD/DF1/CIR/P/2020/26.

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

No.

26. 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.

27. Where can an investor file their complaints?

Investors would 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. The grievance redressal and dispute mechanism is also mentioned 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.gov.in/scores/Welcome.html) 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

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 sub-period 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**	**66,12,989**
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%**	**40%**	**12%**

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**		**66,12,989**		
2	**Portfolio Returns duing the year (=I * 1)**	20,00,000		-16,48,000		19,19,590		7,93,559		
3	Brokerage and Transaction cost @ 20bps **(=D * 1)**	10,000		13,184		9,598		13,226		
4	Other Expenses **(= E*1)**	25,000		32,960		23,995		33,065		
5	Fixed Management Fee **(= C * 1)**	75,000		98,880		71,985		99,195		
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**	68,90,000	**70,00,000**	47,98,976	**49,44,000**	66,12,989	**67,18,566**	72,61,062	**74,06,548**	
7	Returns realised by investor (pre-performance fee) **(= (6-1)/1***100)	37.80%		-27.20%		37.80%		9.80%		
8	Returns realised by investor over hurdle rate (= **7-A,** and in case of negative returns, it shall be zero)	29.80%		0.00%		29.80%		1.80%		
9	Performance fee levied by PM (in %) **(Perf. Fee = 8*B)**	5.96%		0.00%		0.00%		0.36%		
10	**Amount of performance fee recovered by PM (high-watermark applicable) on Capital Amount (= 9*1)**	**2,98,000**		-		-		**23,807**		
11	Total Charges During the year **(=3+4+5+10)**		4,08,000		1,45,024		1,05,577		1,69,293	
12	Net Value of the portfolio at the end of year **(=1+2-11)**		65,92,000		47,98,976		66,12,989		72,37,255	
13	**Overall Returns to investor in % (=(12-1)/1) ***100		**31.84%**		**-27.20%**		**37.80%**		**9.44%**	
14	**High Water Mark for calculation of performance fee for the next performance period**	-		**6890000**		**6890000**		**6890000**		**7261062**