4 Collective Investment Vehicles

Three distinct categories of collective investment vehicles namely, mutual funds, collective investment schemes and venture capital funds mobilise resources from market for investment purposes. The year 1999-2000 witnessed a major reversal of fortunes of mutual funds (MFs). Major policy initiatives were also taken for collective investment schemes and venture capital funds.

MUTUAL FUNDS

The small investors who generally lack expertise to invest on their own in the securities market have reinforced the saying "*Put not your trust in money, put your money in trust*". They prefer some kind of collective investment vehicle like, MFs, which pool their marginal resources, invest in securities and distribute the returns therefrom among them on co-operative principles. The investors benefit in terms of reduced risk and higher returns arising from professional expertise of fund managers employed by the MFs. This approach was conceived in the USA in the 1930s. In developed financial markets, MFs have almost overtaken bank deposits and total assets of insurance funds.

Experiment with MFs in India began in 1964 with the establishment of Unit Trust of India (UTI), which continues to be market leader even today with a corpus of investible funds of about Rs. 76,547 crore at the end of March 2000, accounting for 68% of total market. UTI lost its monopoly status in 1987 with the entry of other public sector MFs promoted by public sector banks and insurance companies. The industry was opened to private sector, including foreign institutions, in 1993 giving Indian investors a broader choice and increasing competition to public sector funds. From one player till 1987, the number of MFs increased to 8 in 1993 and stood at 38 as on March 31, 2000 (including UTI). Starting with an asset base of Rs. 25 crore in 1964, the industry has grown exponentially at an annual compound growth rate of 27% to Rs. 1,13,005 crore as at end-March 2000.

The MFs in India offer a wide array of schemes that cater to different needs suitable to any age, financial position, risk tolerance and return expectations. These include: *open-ended schemes*, which provide easy liquidity; *close-ended schemes* with a stipulated maturity period; *growth schemes*, which provide capital appreciation over medium to long term; *income schemes*, which provide regular and steady income to investors; *balanced schemes*, which provide both growth and income by periodically distributing a part of income and capital gains they earn; *money market schemes*; which provide easy liquidity, preservation of capital and moderate income; and *tax saving schemes*, which offer tax rebates to investors under tax laws as prescribed from time to time.

Policies and Programmes

The policy and regulatory initiatives during 1999-2000 include:

Union Budget 1999-2000

i) All income from UTI and other MFs received in the hands of the investor were exempted from tax. In addition to reducing incidence of tax, it was expected to eliminate the inconvenience faced by small investors in paying tax and claiming refund in respect of such incomes.

ii) Dividends of open-ended equity schemes including US-64 with more than 50% investment in equities were exempted from dividend tax for three years.

P. K. Kaul Committee

SEBI had constituted a Committee under the Chairmanship of Shri P. K. Kaul, former Cabinet Secretary, to recommend the manner of discharging responsibilities by the trustees as envisaged in the Regulations. Based on the recommendations of the Committee as well as feedback received from public and AMFI, SEBI took the following decisions:

(a) Each trustee shall file the details of his transactions of buy or sell of securities with the trust on a quarterly basis.

(b) All information and documents relating to the compliance process shall be authenticated/adopted by the board of directors of the asset management company (AMC), who are entrusted with the primary responsibility in this regard. In like manner, the board of directors of the trustee company would review all information and documents to be received from the AMC as required under the compliance process.

(c) The manner in which due diligence shall be carried out by the trustees in fulfillment of the various obligations as required under the regulations has been specified.

(d) Uniform management information system shall be adopted and the compliance certificate to be submitted by the AMC to the trustees on periodical basis would contain specific comments. Further, the board of trustees or the trustee company, as the case may be, shall send reports to SEBI in the prescribed format.

(e) The independent directors of the trustees/ AMC shall pay specific attention to certain aspects, e.g. compensation paid under Investment Management Agreement, service contracts with affiliates, selection of the company's independent directors, etc.

(f) With regard to the frequency of the meetings of the trustees/board of directors of the trustee company, there would be at least one meeting every three months and four such meetings to be held in a year. The Trust Deed shall also specify the quorum for such meetings provided that the quorum shall also specify the presence of at least one independent trustee/director.

(g) The minimum number of trustees shall be four and it would be upto the mutual fund to decide the maximum number of trustees.

(h) It shall be left to the discretion of mutual fund whether to appoint independent auditors or to have separate full fledged administrative set up to give support to the trustees in discharging their duties in accordance with SEBI Regulations.

(i) The trustees shall not be held liable for acts done in good faith and if they have exercised adequate due diligence honestly.

Amendments to MF Regulations

SEBI amended MF Regulations to provide for the following:

i. Investment in equity related instruments

Investments in the equity related instruments of a single company is restricted to 10% of the net asset value (NAV) of the scheme. However, this limit shall not be applicable in case of index funds and in case of sector/ industry specific schemes subject to adequate disclosures in the offer documents.

ii. Investment in rated and unrated debt securities

Investments in rated investment grade debt instruments issued by a single issuer is restricted to 15% of NAV of the scheme. This limit may be extended to 20% with the prior approval of the Board of AMC and Board of Trustees.

In case of unrated as well as rated, but below investment grade, debt instruments, the investment in a single issuer shall not exceed 10% of the NAV of the scheme and such investment in all the issuers shall not exceed 25% of NAV subject to approval of board of AMC and trustee company.

However, these restrictions shall not apply to government securities and money market instruments.

iii. Investment in unlisted shares

Investment in unlisted shares is restricted to a maximum of 10% of the NAV of the scheme in case of close-ended scheme and to 5% in case of open-ended schemes.

iv. Investment restrictions in listed group companies

A mutual fund shall not invest more than 25% of NAV of any of its schemes in the listed securities of group companies of the sponsor instead of the present requirement of 25% of NAV of all the schemes put together.

v. Change in control/fundamental attributes in case of an open ended scheme

In case of change in control and fundamental attributes of open-ended schemes, the unitholders shall be informed by way of individual communication and through advertisements in the newspapers and the unitholders shall be given option to exit at the prevailing NAV without any exit load. However, no such change shall be allowed for a period of one year from the date of allotment of units.

vi. Transactions with associates

The MFs shall disclose at the time of declaring half-yearly and yearly results: (i) any underwriting obligations undertaken by the schemes of the MFs with respect to issue of associate companies, (ii) devolvement, if any, (iii) subscription by the schemes in the issues lead managed by associate companies, and (iv) subscription to any issue of equity or debt on private placement basis where the sponsor or its associate companies have acted as arranger/manager.

vii. Advertisement code

Any advertisement on performance should be supported by relevant figures and such figures of NAV, yields or returns should be given for the past three years wherever applicable. Advertisements reproducing selective extracts from the offer document which could be misleading should not be published. Celebrities should not be displayed in advertisements.

viii. Code of conduct

Code of conduct shall include certain clauses pertaining to integrity, due diligence, fairness in dealings etc. which should be adhered to by the AMC and the Trustees.

ix. Portfolio management activities

AMCs are allowed to carry out portfolio management activities subject to certain conditions.

x. Net worth requirement for AMC

The definition of the net worth will be elaborated for the sake of clarity and uniformity.

xi. Disclosure standards

MFs are required to ensure frequent and timely portfolio disclosures by sending a complete statement of their scheme portfolios to all unit-holders within one month from the close of each half-year. However, the requirement of such disclosure shall be dispensed with if the statement of portfolio is published as an advertisement in two newspapers. They are also required to ensure despatch of redemption or repurchase proceeds within 10 working days requiring AMCs to bear interest on delayed payment at such rates as may be specified by SEBI for the period of delay.

xii. Permission to trade in derivatives

MFs can enter into derivatives transactions for the purpose of hedging and portfolio balancing. Detailed guidelines on the procedures to be followed while entering into derivatives trading were also issued.

xiii. Investment in ADRs/GDRs

MFs were permitted to enter global securities market. This facility is initially available in respect of ADRs/GDRs issued by Indian companies with an overall cap of US $ 500 million with a sub-ceiling of 10% of the net assets managed by individual MFs and a maximum limit of US $ 50 million for each MF.

The initiatives undertaken during April-September 2000 include:

Union Budget 2000-2001

The rate of tax on income distributed by debt-oriented mutual funds and UTI was increased from 11% to 22% (including surcharge) in an effort to correct the distortions arising out of differing tax treatment for interest incomes from mutual funds and other instruments, like bank deposits and corporate deposits.

With effect from April 1, 2000, investment in mutual funds will not be exempted from payment of capital gains tax under Sections 54EA and 54EB of the Income Tax Act 1961.

Amendments to MF Regulations

SEBI amended regulations to:

i. Permit investments by mutual funds in the mortgage-backed securities. These securities must, however, have a credit rating of not below investment grade and represent investments in real estate mortgages (i.e. loans secured by real estate collateral) and not directly in real estate. This is expected to augment the availability of funds for housing sector and provide greater investment flexibility to the mutual funds.

ii. Allow mutual funds to invest in unlisted companies. A mutual fund scheme can invest upto 5% of its NAV in the unlisted equity shares or equity related instruments in case of open-ended scheme and upto 10% of its NAV in case of close ended scheme. Within the investment limit of 15% of NAV in debt instruments issued by a single issuer, mutual funds can also invest in mortgage-backed securitised debt, which are rated not below investment grade by a credit rating agency registered with SEBI.

Testing and Certification

AMFI in association with NSE has developed a self study and testing programme for mutual fund employees and distributors to foster professional standards in their services. For the present, this certification is voluntary.

Money Market Mutual Funds

Consequent upon withdrawal of guidelines by RBI on money market mutual funds w.e.f. March 7, 2000, the schemes of such funds, like other mutual fund schemes, would exclusively be governed by the SEBI (Mutual Funds) Regulations, 1996.

Assured Return Schemes

In order to protect the interests of investors, SEBI has been directing sponsors/AMCs of mutual funds to honour their commitment of assured returns. During 1999-2000, SEBI directed Indian Bank and Indian Bank Mutual Fund to meet the shortfall in the returns committed in the offer documents of Ind Prakash and Ind Jyothi Schemes. In case of Magnum Triple Scheme of SBI Mutual Fund, SEBI insisted that the investors of the schemes must be paid three times the face value of units as indicated in the offer document. By the end of March 2000, 7 mutual funds had contributed Rs.1,979 crore to meet the shortfalls in 19 assured return schemes.

Resource Mobilisation

Popularity of the MFs as an investment vehicle may be seen from the RBI data as presented in Table 4-1. The schemes of MFs of the commercial banks and the insurance companies, which entered the market in 1987, were well received. This was further fuelled by the assured returns schemes offered by a few MFs, which created a perception that MFs were as safe as bank deposits. The boom continued into the nineties with liberalisation evoking positive response from the investors. In 1992-93, the MFs mobilised a record Rs.13,021 crore. The resource mobilisations by MFs remained steady with annual gross mobilisation averaging Rs.11,000 crore per annum during the period 1993-95. However, the bearish conditions in the secondary market since October 1994 hit MFs severely. The years 1995-96 and 1996-97 witnessed net outflows of resource from MFs. The market picked up gradually during the next two financial years. During 1999-2000, the mutual fund industry witnessed a sharp turnaround with resource mobilisation by MFs grossing Rs.21,972 crore. The improvement was brought about by tax sops announced in the Union Budget 1999-2000 and emergence of bullish trends in the secondary market.

A comparison of resource mobilisation by MFs vis-à-vis incremental bank deposits indicates increasing investor preference for MFs. While there were net outflows from MFs during 1995-97, the resources mobilised by MFs during 1997-98 were

Table 4-1: Resource Mobilisation by Mutual Funds

(Rs. crore)

Year	Public Sector MFs			Private Sector MFs	Grand Total
	Bank sponsored	FI sponsored	UTI		
1986-87	-	-	1,261	-	1,261
1887-88	250	-	2,060	-	2,310
1988-89	320	-	3,855	-	4,175
1989-90	888	315	5,584	-	6,787
1990-91	2,352	604	4,553	-	7,509
1991-92	2,140	427	8,685	-	11,252
1992-93	1,204	760	11,057	-	13,021
1993-94	148	239	9,297	1,560	11,244
1994-95	765	576	8,611	1,322	11,274
1995-96	113	235	-6,314	133	-5,833
1996-97	6	137	-3,043	864	-2,036
1997-98	243	206	2,875	678	4,002
1998-99	231	691	170	2,519	3,611
1999-00	-141	394	4,548	17,171	21,972

Source: RBI.

equivalent to 4% of incremental bank deposits. Resources mobilised by MFs during 1999-2000 shot up to 22% of total incremental bank deposits. This indicates emergence of MFs as competitors to banks.

The data on resource mobilisation by mutual funds are compiled by a number of agencies including the RBI, SEBI and Association of Mutual Funds in India (AMFI). The following analysis is, however, based on AMFI data.

The MF industry surged ahead during 1999-2000 leaving the average growth of securities market far behind. While Nifty and Sensex registered a growth of 42% and 34% respectively, the gross amount mobilised by MFs during the year was higher by 180% over the previous year. During 1999-2000, 64 new schemes were launched as against 40 new schemes launched during the preceding year. This took the total number of schemes as at end-March 2000 to 337 from 277 at end-March 1999. These schemes together mobilised Rs. 59,748 crore during 1999-2000 as against Rs. 21,377 crore during the preceding year. MFs launched 19 new schemes during April-September 2000. They mobilised a gross amount of Rs. 38,870 crore during April-September 2000. After adjustment of repurchases and redemptions, there was an inflow of funds of Rs. 345 crore, Rs. 18,074 crore and Rs. 5,861 crore during 1998-99, 1999-2000 and April-September 2000, respectively (Table 4-2). The tax reforms effected through Union Budget 2000-2001 seem to have affected inflow of resources to MF industry during April-September, 2000.

The resources mobilised by MFs show a strong correlation with secondary market. The net inflows to MFs moved in the same direction as the movement of market indices, like Nifty.

Public sector MFs (including UTI) mobilised Rs.17,575 crore accounting for 29.4% of total resource mobilisation by MFs during 1999-2000, as against Rs. 13,411 crore with 62.7% share during preceding year. Their share reduced further to 21.5% with Rs. 8,370 crore mobilised during April-September, 2000. UTI alone raised 54.6%, 22.7% and 16.9% of total resources mobilised during 1998-99, 1999-2000 and April-September 2000, respectively. In net terms, the public sector MFs mobilised Rs. 4,304 crore during 1999-2000 and Rs. 536 crore during April-September 2000.

Table 4-2: Accretion of Funds with Mutual Funds

(Rs. crore)

Category	1998-99		1999-00		April-September 2000		Assets under Management as on		
	Sale	Purchase	Sale	Purchase	Sale	Purchase	31.03.99	31.03.00	30.09.00
A. Unit Trust of India	11,679	13,364	13,536	9,663	6,568	3,957	53,320	76,547	64,521
B. Bank Sponsored	420	772	1,828	1,744	1,037	2,908	5,481	7,842	3,819
C. Institution Sponsored	1,312	512	2,211	1,864	765	969	2,811	3,570	2,912
D. Private Sector (I+II+III)	**7,966**	**6,384**	**42,173**	**27,933**	**30,500**	**25,175**	**6,860**	**25,046**	**26,210**
I. Indian	2,739	2,636	6,688	5,718	6,417	5,441	1,016	2,331	3,468
II. Joint Ventures - Predominately Indian	3,019	2,290	15,548	10,641	8,331	7,106	3,040	9,724	8,861
III. Joint Ventures - Predominately Foreign	2,208	1,458	19,937	11,574	15,752	12,628	2,804	12,991	13,881
Grand Total (A+B+C+D)	**21,377**	**21,032**	**59,748**	**41,204**	**38,870**	**33,009**	**68,472**	**113,005**	**97,462**

Source: AMFI Updates.

On the contrary, private sector MFs surged ahead in terms of resource mobilisation. They raised 77% and 91% of net resources mobilised by MF industry during 1999-2000 and April-September, 2000 respectively. While private sector MFs and UTI experienced positive inflows during April-September 2000, the bank/institution sponsored MFs suffered net outflows.

The share of open-ended schemes in total funds raised increased from 67% in 1998-99 to 90.8% in 1999-2000 and further to 97.7% in April-September 2000. The share of assured return schemes in total funds raised declined from 26.1% in 1998-99 to 8.7% in 1999-2000 and further to 1.3% in April-September 2000. The share of close-ended schemes also declined from 7% during 1998-99 to less than 1% during 1999-2000 and April-September, 2000. During 1999-2000, the open-ended schemes and assured return schemes registered net inflows of Rs. 16,627 crore and Rs.4,234 crore respectively, while the close-ended schemes registered outflows of Rs. 2,317 crore. The corresponding inflows for open-ended schemes and assured return schemes were Rs.8,140 crore and Rs. 29 crore respectively during April-September 2000, while close-ended schemes suffered an outflow of Rs. 2,308 crore. Details of funds mobilised and repurchase/redemption by MFs under different schemes are presented in Table 4-3A.

Income schemes raised about one fourth of resources during April-September 2000 as against one-third and two-third in the preceding two years respectively. The gilt schemes gained acceptance during 1999-2000, though it suffered marginal outflows during April-September 2000. The liquid/money market schemes have emerged as the first preference of investors. These schemes accounted for about 50% of net inflows during April-September 2000. Scheme-wise details of inflows/outflows are presented in Table 4-3B.

Assets under Management

During 1999-2000, the assets under management increased by 65% to Rs. 113,005 crore as at end-March 2000 (Table 4-2). The assets under management, however, declined by 14% to Rs. 97,462 crore by end-September 2000. The share of private sector MFs in total assets under management increased from 10% as at end-March 1999 to 22.2% as at end-March 2000 and further to 26.9% as at end-September 2000. UTI continues to be market leader with share of 67.7% as at end-March 2000 and 66.2% as at end-September 2000 though its dominance is decreasing fast. During April-September 2000, the assets under management of public sector MFs declined by Rs. 16,707 crore, while that of private sector MFs increased by Rs.1,164 crore.

As may be observed from Table 4-4, the open-ended schemes accounted for 61.1% of total assets under management of MFs as at

Table 4-3A: Scheme-wise Resource Mobilisation by Mutual Funds

(Rs. crore)

Scheme	1998-99		1999-00		April-September 2000	
	Sale	Purchase	Sale	Purchase	Sale	Purchase
Open-ended	14,314	14,961	54,224	37,597	37,970	29,830
Close-ended	1,490	4,094	337	2,654	377	2,685
Assured Return	5,573	1,977	5,187	953	523	494
Total	**21,377**	**21,032**	**59,748**	**41,204**	**38,870**	**33,009**

Source : AMFI Updates.

Table 4-3B: Scheme-wise Resource Mobilisation by Mutual Funds

(Rs. crore)

Scheme	1998-99		1999-00		April-September 2000	
	Sale	Purchase	Sale	Purchase	Sale	Purchase
Income	13,738	12,904	17,707	9,039	10,014	8,308
Growth	1,923	2,672	15,020	10,170	7,274	7,121
Balanced	161	248	5,717	4,204	3,781	2,284
Liquid/ Money Market	5,307	4,637	15,925	14,177	14,963	12,261
Gilt	240	110	5,132	2,997	2,667	2,936
ELSS	8	461	247	617	171	99
Total	**21,377**	**21,032**	**59,748**	**41,204**	**38,870**	**33,009**

Source: AMFI.

end-September 2000. The close-ended and assured return schemes accounted for about 17.1% and 21.6% respectively of assets under management as at end-September 2000.

The income schemes accounted for 47% of total assets under management of MFs as at end-September 2000, followed by balanced schemes with 23.2%. The growth schemes accounted for 19% of assets under management of MFs as at end-September 2000. The shares of different types of institutions, and categories of schemes in assets under management are presented in Chart 4-1.

About 56% of the total assets under management were invested in equities, while 33% in the debt and 11% in money market instruments as at end-March 2000. Asset-wise classification of total assets under management is presented in Chart 4-2.

Table 4-4: Assets under Management as at end September, 2000

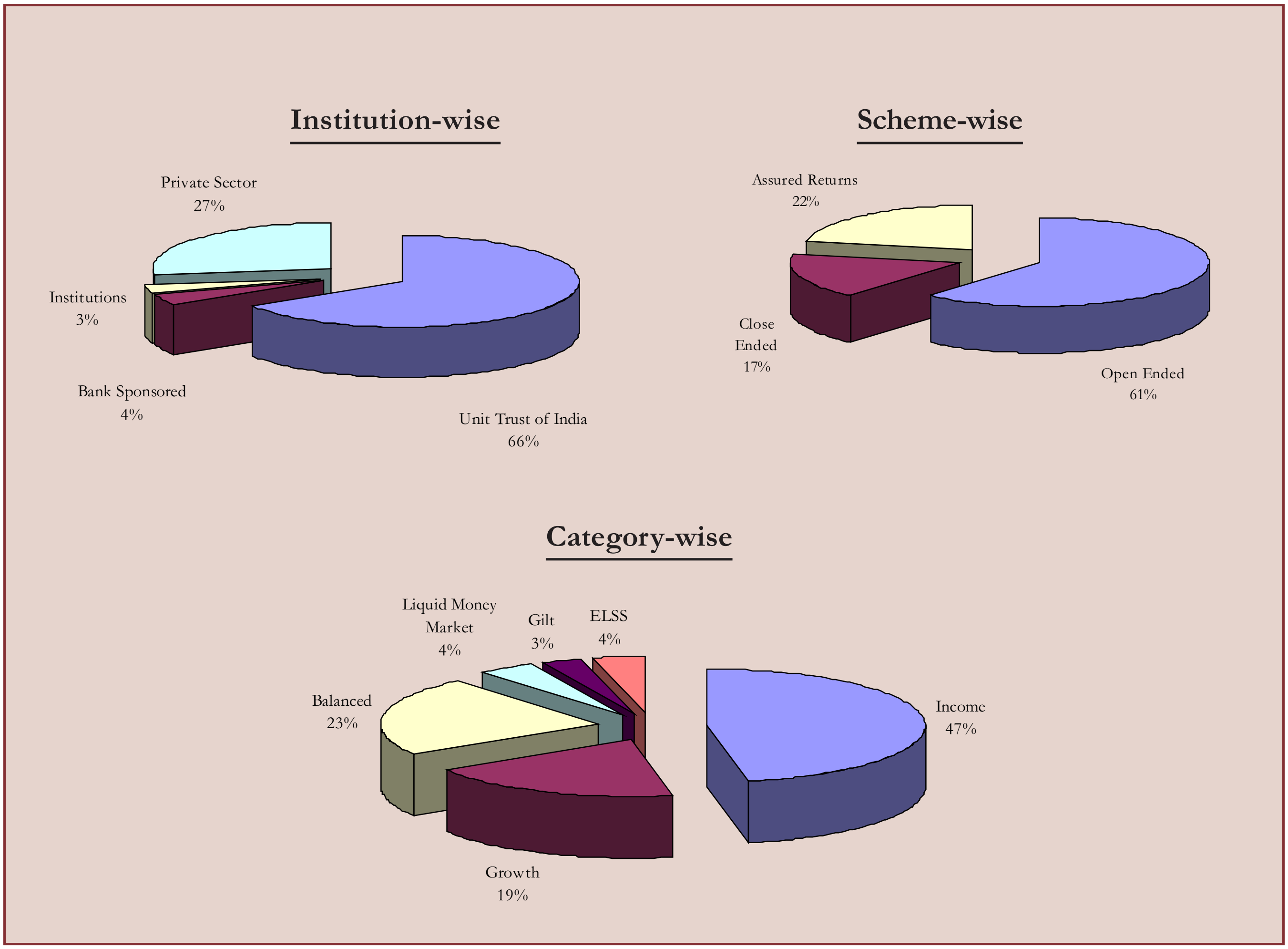
(Rs. crore)

Scheme	Open Ended	Close Ended	Assured Returns	Total
Income	18,513	6,623	21,132	46,268
Growth	12,062	6,630	-	18,692
Balanced	22,416	265	-	22,681
Liquid/Money Market	3,820	-	-	3,820
Gilt	2,399	56	-	2,455
ELSS	392	3,154	-	3,546
Total	**59,602**	**16,728**	**21,132**	**97,462**

Source: AMFI Updates.

Index Funds

A few index funds were launched in the recent past to reduce the bias of fund managers in stock selection and to provide a return at par with the index. For example, UTI launched in February 2000 an open ended Nifty Index Fund, which invests in fifty stocks forming part of the S&P CNX Nifty index in the same weightage as they have in the Nifty with an objective to track the index with minimum error. Similarly, Templeton Asset Management India Pvt. Ltd. launched on June 12, 2000, the Franklin India Index Fund, an open ended passive index fund, to invest in companies whose securities are included in the S&P CNX Nifty Index in the same weightage as they are represented in the index and, subject to tracking errors, endeavour to attain results commensurate with the S&P CNX Nifty Index. There are two other funds, viz. IDBI Principle Index Fund and UTI Master Index Fund which passively invest in Nifty and Sensex respectively. Together, these four funds manage assets worth Rs.700 crore, barely 0.7% of the assets with Indian mutual fund industry. Thus, passive investment approach has not caught fancy of investors partly

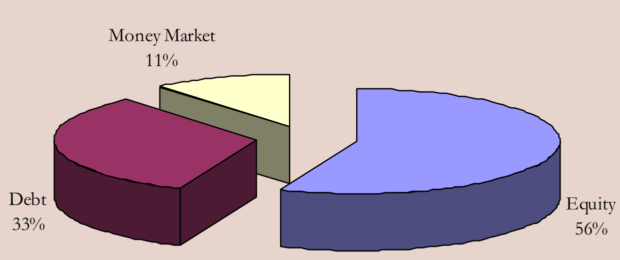


because it is relatively new in India. More importantly, investors do not want to invest in something that simply mirrors the index, while most of the MFs have been beating index by a reasonable margin.

Performance of MFs

There was a perceptible improvement in the overall performance levels and a vast majority of schemes outperformed the market indices. Most of the equity and balanced schemes outperformed the market. According to a Business Standard study, (10th April, 2000), of the 117 equity schemes, 88 provided a return of more than 50% and even 15 of them provided a return of more than 200%. This has been possible due to stock indices hitting roof during the year and investment bias in IT sector. The performance of debt funds, as tracked by CRISIL fund~dx, reveals a similar story.

Chart 4-2: Investment of Assets at the end of March 2000



Unit Scheme 1964 (US-64)

US-64, which is the flagship scheme of UTI, has a corpus of about Rs. 20,000 crore and is subscribed to by about 21 million investors. Following a steep depreciation in its investments, UTI announced negative reserves in the scheme on June 30, 1998, creating a widespread concern among investors. UTI constituted a Committee under the Chairmanship of Mr. Deepak Parekh in October 1998 to undertake a comprehensive review of the functioning of the scheme and recommend measures for sustaining investor confidence and to strengthen the scheme. The Committee submitted its report in February 1999.

Following the recommendations of the Committee, mid-course reorganisation and portfolio rebalancing of US-64 was effected by UTI, which by the end of the year led to positive reserves. A number of measures were also taken by the Government of India. These include tax reliefs granted in the Budget for 1999-2000, as stated earlier. A swap arrangement was worked out whereby the Special Unit Scheme 99 (SUS 99) was created to which PSU stocks of US-64 were transferred on May 1, 1999. Government subscribed to SUS 99 through issue of dated GOI securities worth Rs. 3,300 crore. The GOI securities have five year maturity with a coupon rate of 11.24%. SUS 99 discharged the transfer consideration of PSU stocks by transferring the dated GOI securities to US-64. As a result, the scheme declared a dividend of 13.7% for the year 1999-2000. 4th All India Household Investors Survey, recently conducted by Society for Capital Market Research and Development, reveals that nearly 82% of the respondents surveyed considered US-64 as reasonably safe to very safe.

COLLECTIVE INVESTMENT SCHEMES

CIS Regulations

The SEBI Act prohibits any person from sponsoring or causing to sponsor any CIS without obtaining a certificate of registration from SEBI in accordance with the Regulations. A committee under the Chairmanship of Dr. S. A. Dave was set up by SEBI to frame regulations for such schemes. Based on the recommendations of the Dave Committee, SEBI notified regulations on October 15, 1999. The salient features of the Regulations are set out below:

1. The term “Collective Investment Scheme” has been defined in the Regulations. However, the definition of the term as inserted by the Securities Laws (Amendment) Act 1999 in the SEBI Act, 1992 overrides the definition in the Regulation.
2. CIS can be floated only by public companies registered under the provisions of the Companies Act, 1956. The company floating CIS shall have to seek registration with SEBI as Collective Investment Management Company (CIMC).
3. CIS shall be constituted as a two tiered structure comprising of a trust and a CIMC.
4. At the time of application for Registration as CIMC, these entities should have a minimum networth of Rs. 3 crore, which shall have to be increased to Rs. 5 crore.
5. Every Scheme shall have to compulsorily file offer documents with SEBI containing adequate disclosures to enable investors to take informed investment decisions.
6. Each scheme shall have to obtain rating from a recognised credit rating agency. The projects being undertaken must also be appraised by an empanelled appraising agency.
7. The schemes are prohibited from guaranteeing assured returns. Indicative returns, if any, provided by the scheme shall be based on the projections in the appraisal report.
8. Advertisements in respect of every scheme shall have to conform to the SEBI’s advertisement code.

9. No scheme shall be kept open for subscription for a period of more than 90 days. The schemes shall be close-ended in nature. The schemes must indicate the minimum and maximum amount proposed to be raised over this period.

10. The duration of the schemes shall be for a minimum period of 3 years.

11. Compulsory insurance cover for the assets of the scheme and personal indemnity cover for the CIMC shall be obtained.

12. Units issued under the CISs are to be compulsorily listed on recognised stock exchanges.

13. Accounting/valuation norms as stipulated shall have to be followed by CISs.

14. The initial issue expenses for schemes of duration of upto 8 years shall not exceed 7% of the corpus mobilised and for schemes of duration exceeding 8 years shall not exceed 9% of the corpus mobilised.

15. The management fees payable to CIMC shall consist of basic fee and incentive fee. The 'basic fee' shall not exceed:

    i. 1% each year of the funds raised under the scheme for the first five years of the operation of the scheme.

    ii. 1.25% each year of the funds raised under the scheme for the next five years of the operation of the scheme.

    iii. 1.5% each year of the funds raised under the scheme for the subsequent period thereof till the termination of the scheme.

    The incentive fee shall not exceed 25% of the excess return realised over and above the indicative return as shown in the offer document (excluding the unit capital) at the time of the termination of the scheme. In case, the return at the time of termination of the scheme is less than or equal to the indicative return as shown in the offer document, then no incentive fee shall be paid.

    Existing CISs as on the date of notification of the SEBI regulations would be treated as existing CIS and would need to seek registration from SEBI within a period of 2 months from the date of notification. They would be considered for grant of a provisional registration and given some time to comply with the provisions of the regulations. The existing CIS would also have to abide by the directions of the Honourable Courts in various matters in this regard.

Securities Laws (Amendment) Act, 1999

The Securities Laws (Amendment) Bill, 1999 was introduced in Lok Sabha on October 28, 1999. The Lok Sabha passed the Bill on November 30, and the Rajya Sabha on December 1, 1999. It became the Securities Laws (Amendment) Act 1999 on receiving the assent of the President on December 16, 1999. The Act came into force on February 22, 2000.

In order to strengthen the hands of SEBI to protect interests of investors in plantation companies, the Act has amended the definition of "securities" in the SC(R)A so as to include within its ambit the units or any other instruments issued by any CIS to the investors in such schemes. The Act also inserted a definition of the CIS in the Securities and Exchange Board of India Act, 1992. The CIS has been defined to mean any scheme or arrangement made or offered by any company under which (a) the contributions, or payments made by the investors, by whatever name called, are pooled and utilised solely for the purposes of the scheme or arrangement; (b) the contributions or payments are made to such scheme or arrangement by the investors with a view to receive profits, income, produce or property, whether movable or immovable from such scheme or arrangement; (c) the property, contribution or investment forming part of scheme or arrangement, whether identifiable or not, is managed on behalf of the investors; and (d) the investors do not have day to day control over the management and operation of the scheme or arrangement. The CIS, however, does not include any scheme or arrangement (a) made or offered by a cooperative society, (b) under which deposits are accepted by non banking financial companies, (c) being a contract of insurance, (d) providing for any Scheme, Pension Scheme or the Insurance Scheme framed under the Employees Provident Fund and Miscellaneous Provision Act, 1952, (e) under which deposits are accepted under section 58A of the Companies Act, 1956, (f) under which deposits are accepted by a company declared as Nidhi or a mutual benefit society under section 620A of the Companies Act, 1956, (g) falling within the meaning of Chit business as defined in clause (d) of section 2 of Chit Fund Act, 1982 and (h) under which contributions made are in the nature of subscription to a mutual fund. The Act empowers the Central Government to make rules to provide for the requirements, which shall be complied with by CIS for the purpose of getting their units listed on any stock exchange.

Registration of CIS with SEBI

As per the provisions of SEBI (Collective Investment Schemes) Regulations, 1999, which were notified on October 15, 1999, no existing CIS can launch any new scheme or raise money from the investors even under the existing schemes, unless a certificate of registration is granted to it by SEBI. And for grant of certificate of registration, existing CIS entities were required to make an application within a period of 2 months from the date of notification of the Regulations. Accordingly, the last date for making an application for grant of certificate of registration to SEBI by existing CIS entities was December 14, 1999. However, having regard to the interests of investors who had invested in such existing CISs and requests of CIS for extension of time received as aforesaid, the last date for making an application was extended by SEBI upto March 31, 2000. Under the provisions of the Regulations, an existing CIS, which has failed to make an application or is not desirous of obtaining registration has to compulsory wind up the scheme(s) and make payment to the investors.

Upto March 31, 2000, SEBI has received applications for grant of certificate of registration from 35 existing entities. Besides, 2 entities who had earlier not filed information with SEBI have applied for registration. Therefore, the remaining existing entities, who had earlier filed information with SEBI, have to compulsorily wind up their schemes and make payment to the investors latest by May 28, 2000 failing which they shall face legal and administrative action. The names of 605 entities who were to compulsorily wind up their schemes and make payment to the investors latest by May 28, 2000 are available on SEBI website.

VENTURE CAPITAL FUNDS

Chandrasekhar Committee

Recognising the acute need for higher investment in venture capital activities to promote technology and knowledge-based enterprises, SEBI had appointed a Committee headed by Shri K.B. Chandrasekhar to identify the impediments in the growth of the venture capital industry in India and suggest suitable measures. SEBI considered the report of the Committee and approved the recommendations in principle in January 2000. The recommendations, inter-alia, include harmonisation of multiple regulatory requirements into a nodal regulatory system under SEBI, tax pass-through for VCF, flexibility in investment and exit, facilitating mobilisation of global and domestic resources through hassle-free entry of foreign venture capital investors on the pattern of FIIs and increase in the list of sophisticated institutional investors to invest in VCFs. The recommendations for incentives for employees by providing ESOPs in foreign companies and global opportunities of investment for domestic funds and venture undertakings were also accepted. The matters directly related to SEBI such as relaxation of entry norms for IPOs of venture funded companies to treat the funding by registered VCF for entry eligibility in the lines of banks/financial institutions and exemption from Takeover Code in certain situations were also approved in principle.

Nodal agency for VCFs

To simplify procedures, the Finance Act 2000 has made SEBI the single-point nodal agency for registration and regulation of both domestic and overseas VCFs. No approval of VCFs by tax authorities is required. VCFs shall enjoy a complete pass-through status. There will be no tax on distributed or undistributed income of such funds. The income distributed by the funds will only be taxed in the hands of investors at the rates applicable to the nature of income. This liberalisation is expected to give a strong boost to NRIs in Silicon Valley and elsewhere to invest some of their capital, knowledge and enterprise in ventures in their motherland.

Regulations for VCFs

SEBI amended regulations for VCFs in September 2000. The salient amendments are:

i. VCF is a fund established in the form of a trust/a company including a body corporate and registered with SEBI. It has a dedicated pool of capital, raised in the specified manner and invested in Venture Capital Undertakings (VCUs) in accordance with the regulations. VCU is a domestic company whose shares are not listed on a stock exchange and is engaged in specified business.

ii. The minimum investment in a VCF from any investor will not be less than Rs. 5 lakh and the minimum corpus of the fund before it can start activities shall be at least Rs. 5 crore.

iii. A VCF can not invest in associated companies. The investment in a single VCU can not exceed 25% of the corpus of VCF. At least 75% of the investible funds shall be invested in unlisted equity shares or equity linked instruments. A VCF seeking to avail benefit under the relevant provisions of the Income Tax Act will be required to divest from the investment within a period of one year from the listing of the VCU.

iv. The VCF will be eligible to participate in the IPO through book building route as Qualified Institutional Buyer.

27 VCFs have been granted registration by SEBI by September 2000.