CIRCULAR

SEBI/HO/IMD/DF2/CIR/P/2021/683 **December 10, 2021**

All Mutual Funds (MFs)/
Asset Management Companies (AMCs)/
Trustee Companies/ Board of Trustees of Mutual Funds/
Association of Mutual Funds in India (AMFI)

Sir / Madam,

Subject: Circular on Mutual Funds

1. Usage of pool accounts by Mutual Funds

1.1 In terms of Clause (5) of the Fifth Schedule of SEBI (Mutual Funds) Regulations, 1996 (hereinafter referred as "MF Regulations"), it is stipulated that:

"Trustees and asset management companies shall ensure that the assets and liabilities of each scheme are segregated and ring-fenced from other schemes of the mutual fund; and bank accounts and securities accounts of each scheme are segregated and ring-fenced."

1.2 In this regard, representations were received from the industry highlighting the instances where pool accounts are used, as certain transactions are carried out only at Mutual Fund level for operational ease and due to certain regulatory requirements. However, the securities or funds held in the pool accounts at Mutual Fund level are duly segregated scheme-wise and appropriately reflected in the books of the respective schemes, at the end of day.

1.3 The issue was discussed in Mutual Funds Advisory Committee (MFAC). Based on the recommendations of MFAC, the following has been decided:

1.3.1 Mutual Funds may use pool accounts, only for such transactions which are executed at mutual fund level owing to certain operational and regulatory requirements, subject to the following conditions:

a. AMCs shall have internal policies approved by the Board of AMC and Trustees to ensure that adequate operational processes and internal controls are in place to segregate and ring-fence the assets and liabilities of each scheme along with segregation and ring-fencing of securities & bank accounts.

b. In such cases, at the end of day, the assets and liabilities of each scheme shall be segregated and ring-fenced from other schemes of the mutual fund; and bank accounts and securities accounts of each scheme shall be segregated and ring-fenced. The pool accounts for both securities and funds should have nil balance at end of the day.

   Provided that if the funds lying in the pool bank account of the mutual fund are not identified, due to the reasons beyond the control of the AMC, the same shall be transferred to the respective scheme account not later than one business day from the day such transactions are identified.

c. At no point of time, the securities or funds of one schemes shall be used for other scheme(s) and there shall be any conflict of interest amongst investors of various schemes.

d. The responsibility to ensure segregation and ring-fencing of the assets and liabilities of each scheme along with segregation and ring-fencing of bank accounts & securities accounts shall lie with the Board of AMC and Trustees. Trustees in their Half Yearly Trustee Report (HYTR) to SEBI shall confirm that the assets and liabilities of each scheme along with their bank accounts & securities accounts are segregated and ring-fenced on daily basis, except the unidentified transactions of funds as mentioned in sub-para (b) above, during the half-year period.

e. The whole mechanism shall be audited on half yearly basis by the auditor appointed by the trustees.

1.3.2 Further, with regard to the margin or collateral requirement for execution of certain transactions, which are carried out only at Mutual Fund level by various schemes, the following has been stipulated:

a. In terms of Clause (5) of the Fifth Schedule of MF Regulations, the AMC shall ensure that margins or collaterals for such transactions are placed from the assets of the respective schemes only, without co-mingling with the assets of other schemes.

b. In partial modification to SEBI circular no. SEBI/HO/IMD/DF3/CIR/P/2017/114 dated October 6, 2017, overnight funds can deploy, not exceeding, 5% of the net assets of the scheme in G-secs and/or T-bills with a residual maturity of upto 30 days for the purpose of placing the same as margin and collateral for certain transactions.

2. Norms for investment in Bills Re Discounting Scheme (BRDS)

2.1 In terms of Paragraph-B(5) of SEBI circular no. SEBI/HO/IMD/DF2/CIR/P/2019/104 dated October 01, 2019, investments in unrated debt and money market instruments, other than government securities, treasury bills, derivative products such as Interest Rate Swaps (IRS), Interest Rate Futures (IRF), etc. can only be made in instruments like bills re-discounting, usance bills, etc., that are generally not rated and for which separate investment norms are not provided in MF Regulations and various circulars issued thereunder and exposure of mutual fund schemes in such instruments, shall not exceed 5% of the net assets of the schemes.

2.2 In this regard, a representation was received from AMFI to have uniformity across the industry with regard to investment in BRDS. The issue was discussed in MFAC and based on the recommendations, the following has been decided:

a. The single issuer limit and the group exposure limit shall be calculated at the issuing bank level as BRDS are issued with recourse to the issuing bank.

b. Investment in BRDS by debt schemes of mutual funds shall be considered as exposure to financial services sector for the purpose of sector exposure limits.

3. <u>Risk Management Framework (RMF) for Mutual Funds</u>

3.1 SEBI circular no. SEBI/HO/IMD/IMD-1 DOF2/P/CIR/2021/630 dated September 27, 2021 on "Risk Management Framework (RMF) for Mutual Funds" was to be effective from January 01, 2022 along with rescinding of the existing circular no. MFD/CIR/15/19133/2002, dated September 30, 2002 on "Risk Management System" from the same date.

3.2 Based on the request received from AMFI, it has been decided to extend the date of implementation of the circular to April 01, 2022. Till such time, the existing circular no. MFD/CIR/15/19133/2002, dated September 30, 2002 on "Risk Management System" shall remain operational. However, AMCs may choose to adopt the provisions of circular dated September 27, 2021 before April 01, 2022.

4. <u>Guiding Principles for bringing uniformity in Benchmarks of Mutual Fund Schemes</u>

4.1 SEBI, vide circular no. SEBI/HO/IMD/IMD-II DOF3/P/CIR/2021/652 dated October 27, 2021, had specified a two-tiered structure for benchmarking of certain categories of schemes. The circular, *inter-alia*, specified that AMFI shall publish the first tier benchmarks for open ended debt schemes as per the Potential Risk Class and the same shall be implemented by the AMCs with effect from January 1, 2022.

4.2 Based on the request received from AMFI, it has been decided to extend the date of implementation of the above to April 1, 2022.

5. <u>Applicability</u>

5.1 The provisions at paragraph 1.3 & 2.2 above shall be effective from the 30th day from the date of this circular.

6. This circular is issued in exercise of powers conferred under Section 11 (1) of the Securities and Exchange Board of India Act, 1992, read with the provisions of Regulation 77 of SEBI (Mutual Funds) Regulations, 1996, to protect the interests of investors in securities and to promote the development of, and to regulate the securities market.

Yours faithfully,

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