

MEMO# 20228

August 1, 2006

ICI Letter to The Securities and Exchange Board of India on Foreign Institutional Investor Issues

©2006 Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice. [20228] August 1, 2006 TO: AML COMPLIANCE WORKING GROUP No. 19-06 INTERNATIONAL INVESTING SUBCOMMITTEE No. 17-06 INTERNATIONAL MEMBERS No. 14-06 INTERNATIONAL OPERATIONS ADVISORY COMMITTEE No. 19-06 RE: ICI LETTER TO THE SECURITIES AND EXCHANGE BOARD OF INDIA ON FOREIGN INSTITUTIONAL INVESTOR ISSUES Earlier this year, staff of the Securities and Exchange Board of India (SEBI) encouraged us to submit a letter describing some of the key issues that foreign institutional investors (FIIs) face investing in India. Our letter to SEBI in response is attached.¹ The ICI's letter continues a dialogue with SEBI that began in late 2002 about ways to streamline and improve the investing environment in India for FIIs. This letter is the third letter to SEBI on the topic since that time. The ICI's letter highlights four areas of continuing concern to FIIs: 1. The application of new anti-money laundering (AML) rules to FIIs. New AML rules in India require banking companies, financial institutions and other "intermediaries" to perform prescribed AML functions, including filing suspicious transaction reports and verifying the identity of clients. The new rules also require firms to designate an officer as "Principal Officer" responsible for ensuring AML compliance. In the letter, we urge SEBI to reconsider direct application of the new AML rules to FIIs, and instead recommend that SEBI treat FIIs as clients of local firms rather than intermediaries for purposes of India's AML rules. 2. The recent increases in the fees for FII licenses and FII subaccounts. On June 26, 2006, SEBI effectively tripled the fees FIIs must pay to invest in India by increasing FII license 1 The letter contains a lengthy set of attachments, which we have omitted here. If you are interested in obtaining a copy of the complete ICI letter with all of its attachments, contact Ruth Tadesse at 202/326-5836 or rtadesse@ici.org. 2 fees and decreasing the renewal cycle to three years. In our letter, we strongly reiterate our long-standing recommendation that FII fees be eliminated or, at the very least, set at a level commensurate with the costs of processing the FII applications. We also reiterate our recommendation that FII licenses be of indefinite duration, eliminating the need for renewals every three years. 3. The daily disclosure of large trades. A SEBI policy that took effect on February 17, 2004 requires brokers to contemporaneously disclose the details of certain large trades to the stock exchanges, and requires the stock exchanges to disseminate those details to the general public on their websites the same day. Disclosure is required if an investor trades more than 0.5% of the number of equity shares of a company listed on the stock exchange in a single trading day, either in a single trade or cumulatively. In our letter, we express our continuing concern that this disclosure has the

potential to harm institutional investors such as FII and reiterate our recommendation that SEBI reconsider the application of the rule to institutional investors and seek a more tailored approach to the disclosure of bulk trades, at least with respect to the transactions executed on an exchange. 4. The high rate of “close-outs” in the clearance and settlement of trades. There are relatively high rates of partial settlement in the Indian markets, resulting in a “close-out” process that presents a number of trading, tax, and recordkeeping problems for institutional investors. To alleviate these problems, we recommend that SEBI require the clearinghouse to facilitate the fulfillment of trade orders through the use of a mandatory securities borrowing and lending program. We will follow up on these issues with SEBI staff over the coming months. Robert C. Grohowski Senior Counsel - International Affairs Attachment (in .pdf format) Note: Not all recipients receive the attachment. To obtain a copy of the attachment, please visit our members website (<http://members.ici.org>) and search for memo 20228, or call the ICI Library at (202) 326-8304 and request the attachment for memo 20228.

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