Recasting Portfolio Management Services: SEBI's Proposed New Regulatory Framework

INTRODUCTION

On July 23, 2026, the Securities and Exchange Board of India (***SEBI***) released a consultation paper (***Consultation Paper***) proposing to repeal and replace the SEBI (Portfolio Managers) Regulations, 2020 (***PMS Regulations***) in its entirety with a new set of draft regulations set out in Annexure I (***Draft Regulations***). The Consultation Paper states that the proposed reforms shall simplify, consolidate and modernise the regulatory regime applicable to portfolio managers.

KEY PROPOSALS

- **MFs only PMS -** One of the most significant proposals in the Consultation Paper is the inclusion of a new category of portfolio managers, namely 'Mutual Funds only Portfolio Managers' (***MF-PMS***). An MF-PMS can invest only in direct plans of mutual fund schemes (including ETFs and specialised investment funds) and cannot invest directly in securities. The Consultation Paper also details the regulatory framework for such MF-PMS, which will have lower entry thresholds and simplified compliance as compared to regular portfolio managers. Some of the key features of the regulatory framework for MF-PMS are:

  - New applicants would be required to get a separate registration as 'MF-PMS' while existing managers may offer MF-PMS through a different investment approach.
  - A Mutual Fund distributor (MFD) may obtain a MF-PMS license and offer both services (MFD and MF-PMS) through the same entity. However, while the same entity may carry on both businesses, it cannot provide both services to the same client. In addition, the entity offering both services would have to ensure that (i) it maintains an arm's length relationship between activities as an MFD and as a MF-PMS, through a separately identifiable department or division; and (ii) it has client level segregation for its services as an MFD and MF-PMS.
  - MF-PMS would have to maintain a net-worth of INR 2 crores and each client should have a minimum ticket size of INR 25 Lakhs, with simplified applicable certification and educational experience applicable for principal officers and disclosure document requirements, along with other exemptions.

- **Independent fund managers -** The Consultation Paper proposes to permit independent fund managers to operate under a registered portfolio manager. The registered portfolio manager would be responsible for final execution of orders through centralized dealing desk or authorized execution systems, provide the independent managers with infrastructure and other compliance requirements and retain regulatory accountability. In exchange, the registered portfolio manager would be entitled to share the fees/revenue with the independent manager in a mutually agreed ratio pursuant to an agreement between them.

- **Smaller PMS providers -** The Consultation Paper proposes that portfolio managers with less than 10 clients or AUM below INR 100 crores be exempt from the requirement of maintaining a separate dealing room, subject to maintaining appropriate audit trail of communication of order placement with adequate internal controls. Currently, all portfolio managers are required[1] to constitute a dealing team and a specified dealing room for such dealing team to transact business out of in accordance with the guidelines specified by SEBI.

- **Expanding the permissible investment universe -** The Consultation Paper seeks to expand the universe of permitted investments for portfolio managers. The refurbished menu covers:

  - overseas listed equity and debt securities (subject to FEMA norms and explicit client consent);

[1] Paragraph 2.7 of the master circular for portfolio managers issued by SEBI.

- "To-be-listed" securities, defined as "*equity securities available for purchase or application or investment under public issue in an initial public offer, or debt securities under primary market issuance, till its listing on a recognized stock exchange";*
- exchange traded derivatives; and
- investment-grade unlisted debt securities for discretionary portfolio managers' clients, subject to an overall cap of 10% of client assets.

  At present, Regulation 24(3) of the PMS Regulations require portfolio managers to invest only in securities listed or traded on a recognized stock exchange, money market instruments, units of Mutual Funds. Non-discretionary portfolio managers can invest up to 25% of the clients' AUM in unlisted securities. Further, investments in foreign securities are completely prohibited under the PMS Regulations with investments in derivatives permitted only for hedging and portfolio rebalancing.

- **Definition of "net-worth" -** Regulation 9 of the PMS Regulations requires every portfolio manager to have a minimum net worth of INR 5 crores, subject to certain exceptions. Explanation to Regulation 9 of the PMS Regulations defines 'net worth' to mean "*the aggregate value of paid-up equity capital plus free reserves (excluding reserves created out of revaluation) reduced by the aggregate value of accumulated losses and deferred expenditure not written off, including miscellaneous expenses not written off*".

  The Consultation Paper proposes to include securities premium reserve in the definition of net-worth and exclude any loans and advances given by portfolio managers, including to their related parties or associates. It is further proposed that at least ten percent of the portfolio manager's net worth must be deployed in liquid assets which are unencumbered.

- **Commencement of business activity -** The Consultation Paper proposes that a registered portfolio manager would have to "establish its business activities" within 3 years from the date of registration i.e., have a minimum of 10 clients or a total AUM of INR 5 crores, to be entitled to carry on its business beyond the aforementioned period of 3 years.

- **Certification for compliance officer -** Regulation 34(1) of the PMS Regulations requires every portfolio manager to mandatorily have a compliance officer.

  The Consultation Paper proposes that such compliance officers would have to pass the '*NISM Series-III-C: Securities Intermediaries Compliance (Fund) Certification Examination*'. Currently, only the principal officer or employee(s) of the portfolio manager with decision making authority related to fund management are required to pass the '*NISM Series-XXI-B: Portfolio Managers Certification Examination'.*

ANNEXURES TO THE CONSULTATION PAPER

- Annexure I to the Consultation Paper sets out the proposed Draft Regulations, which are intended to replace the existing PMS Regulations. While the Draft Regulations largely consolidates and streamlines the existing regulatory framework, it also includes a chapter dedicated to the new MF-PMS regime. The Draft Regulations in Annexure I are not comprehensive or exhaustive since they do not cover some of the proposals such as the proposal relating to independent fund managers operating under a registered portfolio manager.

- Annexure II provides a comparative table mapping the provisions of the existing PMS Regulations against the corresponding provisions of the Draft Regulations. While this comparative table facilitates navigation between the two frameworks, it does not identify the substantive amendments or new insertions, requiring a side-by-side comparison to fully appreciate the proposed changes.

- As mentioned above, the Consultation Paper also proposes to allow portfolio managers to invest in exchange traded derivatives. Currently, portfolio managers are only allowed to invest in derivates, provided it is for the purpose of hedging and portfolio rebalancing. Annexure-III details the calculation of exposure, offsetting etc. in relation to investments in exchange traded derivatives.

ELP Comments

- *The MF-PMS will bridge the gap between mutual funds and traditional portfolio management services. By reducing the minimum ticket size to INR 25 lakhs and restricting investments to regulated pooled products, SEBI seeks to provide a professionally managed solution for investors who require customised asset allocation but may not meet the investment threshold for conventional portfolio management services. The framework could also create an intermediate product between mutual funds and traditional discretionary portfolio management services.*
- *The introduction of a platform for independent fund managers to operate under a registered portfolio manager could materially reduce entry barriers for experienced investment professionals seeking to establish independent portfolio management practices. However, it is unclear from the Consultation Paper if the independent fund manager would be a person registered with or directly regulated by SEBI.*
- *Proposal (iv) permitting investments in overseas securities responds to increasing investor demand for global diversification while reducing the need for separate offshore investment structures. Similarly, allowing investments in to-be-listed securities enables portfolio managers to participate in IPO opportunities more efficiently and align their investment capabilities with evolving capital market practices. The proposed flexibility to invest in investment-grade unlisted debt could also facilitate more diversified fixed-income strategies for sophisticated investors.*
- *Extending the certification requirement to compliance officers reinforces SEBI's continued emphasis on strengthening governance and compliance standards across regulated intermediaries.*

We hope you have found this information useful. For any queries/clarifications, please write to us at insights@elp-in.com or write to our authors:

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