



भारतीय रिज़र्व बैंक  
RESERVE BANK OF INDIA

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All Scheduled Commercial Banks  
(excluding RRBs)

Dear Sir/Madam

**Guidelines on Wealth Management /Marketing/Distribution Services offered by Banks – Draft Guidelines**

Please refer to paragraphs 86, 87 and 88 (extracts enclosed) of the Monetary Policy Statement 2013-14 announcement on May 3, 2013 regarding issue of guidelines on wealth management services and distribution of third party financial products by banks.

2. The draft guidelines on Wealth Management and Marketing/Distribution services have been prepared and are enclosed. Comments on the draft guidelines may be addressed to the Chief General Manager, Department of Banking Operations & Development, RBI, 13<sup>th</sup> floor, Shahid Bhagat Singh Marg, Fort, Mumbai - 400 001 by [e-mail](#) latest by July 31, 2013.

Yours faithfully

(Prakash Chandra Sahoo)  
Chief General Manager

Enc: As above

बैंकिंग परिचालन और विकास विभाग, केंद्रीय कार्यालय, 13 माला, शहीद भगतसिंह मार्ग, मुम्बई 400001

Department of Banking Operations and Development, Central Office, 13<sup>th</sup> floor, NCOB, Shahid Bhagat Singh Marg, Mumbai - 400001  
टेलिफोन /Tel No: 91-22-22601000 फैक्स/Fax No: 91-22-22701241 Email ID:cgmicdbodco@rbi.org.in

हिंदी आसान है, इसका प्रयोग बढ़ाइए

## EXTRACT

Date: May 03, 2013

### Monetary Policy Statement 2013-14

#### Provision of Wealth Management Services and Marketing and Distribution of Third Party Financial Products

86. The Reserve Bank recently undertook investigations in the light of reported allegations that certain banks were involved in structuring transactions to aid tax evasion and fraudulent transfer of funds. The investigations revealed the need for better regulatory compliance by banks. It is proposed to issue guidelines which would include, *inter alia*, the following:

##### *(a) Wealth Management*

87. Wealth management services (WMS) generally include referral services, investment advisory services (IAS) and portfolio management services (PMS). In India, banks with well-developed branch network have access to a large customer base. Banks offering wealth management services are exposed to reputational risks on account of mis-selling of products, conflict of interest, lack of knowledge and clarity about products and frauds. It is, therefore, proposed to:

- issue draft guidelines on wealth management services offered by banks by end-June 2013.

##### *(b) Marketing and Distribution of Third Party Financial Products*

88. As per extant instructions, banks are allowed to market insurance and mutual fund products as agents of other entities on non-risk participation basis. It has been observed that in some cases, banks did not have clear segregation of duties of marketing personnel from other branch functions, and bank employees were directly receiving incentives from third parties such as insurance, mutual fund and other entities for selling their products. Such practices may lead to mis-selling and distortion of the staff incentive structure. It is, therefore, proposed to advise banks to:

- ensure segregation of the marketing function from the approval/transactional process at bank branches;
- ensure that its employees do not receive cash/non-cash incentives directly from insurance companies, mutual funds and other third party product providers; and
- have a board approved policy to avoid mis-selling and conflict of interest in marketing and distribution of own or third party financial products.

Detailed guidelines will be issued by end-June 2013.

## GUIDELINES ON WEALTH MANAGEMENT/MARKETING/DISTRIBUTION SERVICES OFFERED BY BANKS- DRAFT

### **Introduction**

1.1 The term Wealth Management comprises a number of aggregated financial services. The following categories of services offered by banks in India to their customers are generally included in the term 'Wealth Management Services' (WMS):

- i) Referral Services
- ii) Investment Advisory Services (IAS); and
- iii) Portfolio Management Services (PMS).

In addition to the above services, banks also market and distribute third party financial products, which, though not part of WMS, is an allied activity. The particular business model adopted by individual banks may differ in terms of products and services offered, corporate structure, clients targeted and revenue generated,

1.2 Though these services are offered by banks, Investment Advisory as well as Portfolio Management Services are regulated by SEBI. Similarly, in offering referral services for insurance, banks are required to comply with relevant IRDA regulations. While marketing and distributing third party financial products, banks are acting as agents for entities regulated by other regulators. Reserve Bank has also issued guidelines for banks on these matters from time to time from the perspective of permitting entities regulated by RBI to undertake these activities.

1.3 Over time, there has been an expansion of the roles and responsibilities of banks as providers of these services. Concerns arising out of mis-selling, conflict of interest, requirement of grievance redressal, etc, have arisen and after debate in inter-regulatory forums it was decided to issue guidelines addressing the same. Further, in the recent investigations undertaken by RBI in the light of reported allegations that certain banks were involved in structuring transactions to aid tax evasion and fraudulent transfer of funds, it was observed that many of these transactions centered around the WMS provided by banks as well as marketing of third party products. The main regulatory concerns have arisen regarding violation of KYC/AML guidelines, mis-selling of products or selling of products that are

unsuitable for the client, conflict of interest between the marketing and advisory/ financial management function, and lack of robust risk management systems and procedures leading to frauds.

1.4 Mis-selling raises serious consumer protection issues. Further, as observed from the recent allegations, WMS activities as well as marketing third party products can expose banks to serious reputational risks. These Guidelines define the scope of these services.

## **2. Current Regulatory Prescriptions**

### **2.1 Marketing and Distribution of third party products**

2.1.1 Marketing and distribution of financial products are undertaken by banks by acting as agents of the third party financial services provider. Initially, banks were permitted to undertake retailing of government securities, subject to certain conditions, since it was felt that with the large network of branches, banks would be in a position to enlarge the market for Government securities which would, in turn, help in activating the secondary market for Government securities and making the market for such securities deep and broad-based.

2.1.2 Later, banks were permitted to market mutual funds, subject to the following conditions:

- (i) Banks should only act as an agent of the customers, forwarding the investor's applications for purchase/sale of MF units to the Mutual Fund/the Registrars/the transfer agents. The purchase of units should be at the customers' risk and without the bank guaranteeing any assured return.
- (ii) Banks should not acquire units of Mutual Funds from the secondary market.
- (iii) Banks should not buy back units of mutual funds from their customers.
- (iv) If banks propose to extend any credit facility to individuals against the security of shares or units of Mutual Funds, sanction of such facility should be in accordance with the extant instructions on advances against shares, debentures and units of mutual funds.

(v) Banks holding custody of MF units on behalf of their customers should ensure that their own investments and investments belonging to their customers are kept distinct from each other.

(vi) Banks should put in place adequate and effective control mechanisms as detailed in our circular DBOD.No.FSC BC.143A/24.48.001/91-92 dated June 20, 1992. Besides, with a view to ensuring better control, retailing of units of mutual funds may be confined to certain selected branches of a bank.

2.1.3 Subsequently, it was decided to grant banks general permission for engaging in insurance agency business, subject to the following conditions:

(i) The bank should comply with the IRDA regulations for acting as 'composite corporate agent' with insurance companies.

(ii) The bank should not adopt any restrictive practice of forcing its customers to go in only for a particular insurance company in respect of assets financed by the bank. The customers should be allowed to exercise their own choice.

(iii) As the participation by a bank's customer in insurance products is purely on a voluntary basis, it should be stated in all publicity material distributed by the bank in a prominent way. There should be no 'linkage' either direct or indirect between the provision of banking services offered by the bank to its customers and use of the insurance products.

(iv) The risks, if any, involved in insurance agency should not get transferred to the business of the bank.

2.1.4 Banks may be marketing / referring several competing products of various mutual fund / insurance / financial companies to their customers. Keeping in view the need for transparency in the interest of the customers to whom the products are being marketed / referred, banks were advised to disclose to the customers, details of all the commissions / other fees (in any form) received, if any, from the various mutual fund / insurance / other financial companies for marketing / referring their products. This would be required even if the bank is marketing the products of only one mutual fund/company.

## **2.2 Referral Services**

2.2.1 It was envisaged that under the referral arrangement, banks would provide physical infrastructure within their select branch premises to insurance companies for selling their insurance products to the banks' customers with adequate disclosure and transparency, and in turn earn referral fees on the basis of premia collected. Initially, banks were permitted to undertake insurance referral business after obtaining specific permission from RBI and IRDA. It was later decided that banks need not obtain prior approval of RBI for engaging in insurance referral business without any risk participation. Banks were advised to enter into Agreements with the insurance company for allowing use of premises and making use of the existing infrastructure of the bank. They were also advised to comply with the IRDA regulations for referral arrangement with insurance companies, in addition to the stipulations mentioned at para 2.1.3 above, viz, they should not adopt any restrictive practice of forcing its customers to go in only for a particular insurance company in respect of assets financed by the bank. The customers should be allowed to exercise their own choice. As the participation by a bank's customer in insurance products is purely on a voluntary basis, it should be stated in all publicity material distributed by the bank in a prominent way. There should be no 'linkage' either direct or indirect between the provision of banking services offered by the bank to its customers and use of the insurance products.

2.2.2 This permission was later expanded to permit banks to offer referral services to their customers for financial products subject to the following conditions:

- i) The bank/third party issuers of the financial products should strictly adhere to the Know Your Customer (KYC) norms / Anti-Money Laundering (AML) standards/Combating of Financing of Terrorism (CFT)/Obligation of banks under PMLA, 2002 guidelines in respect of the customers who are being referred to the third party issuers of the products. In this context, KYC/AML Guidelines provided inter alia, that since information provided by the customer for KYC compliance while opening an account is confidential and divulging any details thereof for cross selling or any other purpose would be in breach of customer confidentiality obligations, banks were, advised to collect any information about the customer for a purpose other than KYC requirements, separately, purely on a voluntary basis,

after explaining the objectives to the customer and taking express approval for the specific uses to which such information could be put.

ii) The bank should ensure that the selection of third party issuers of the financial products is done in such a manner so as to take care of the reputational risks to which the bank may be exposed in dealing with the third party issuers of the products.

iii) The bank should make it explicitly clear upfront to the customer that it is purely a referral service and strictly on a non-risk participation basis.

iv) The third party issuers should adhere to the relevant regulatory guidelines applicable to them.

v) While offering referral services, the bank should strictly adhere to the relevant RBI guidelines

2.2.3 The instructions at para 2.1.4 regarding transparency and disclosure would also apply to banks offering referral services, viz, they were advised to disclose to the customers, details of all the commissions / other fees (in any form) received, if any, from the various mutual fund / insurance / other financial companies for referring their products. This would be required even if the bank is referring the products of only one mutual fund/company.

### **2.3 Investment Advisory Services (IAS)**

Prior to the issue of SEBI (Investment Advisers) Regulations 2013, the activity of investment advisory services was regulated as per SEBI (Portfolio Managers) Rules and Regulations, 1993. Banks, carrying out investment advisory services, require prior approval of RBI, which is issued on a case -to-case basis, subject to certain conditions.

### **2.4 Portfolio Management Services (PMS)**

2.4.1 The activity of PMS is regulated by SEBI as per SEBI (Portfolio Managers) Rules and Regulations, 1993. Consequent to certain irregularities observed in the

securities transactions of banks, general powers given to banks to operate Portfolio Management Schemes (PMS) and similar schemes were withdrawn and banks were advised not to restart or introduce any new PMS or similar schemes in future without obtaining prior approval of RBI, vide circular No. DBOD.BC.73/27.07.001/94-95 dated June 7, 1994. These instructions were also made applicable to subsidiaries of banks, including bank-sponsored NBFCs.

2.4.2 The conditions under which banks could offer PMS are as under:

- i) Only those banks which can provide such services on their own should undertake the activity. Funds accepted for portfolio management from their clients, should not be entrusted to another bank for management.
- ii) PMS should be in the nature of investment consultancy/management, for a fee, entirely at the customer's risk without guaranteeing, either directly or indirectly, a pre-determined return. The bank should not indemnify the client directly or indirectly in any manner in the event of the bank not being able to achieve the minimum stipulated rate of return specified, if any, in the agreement. The bank should charge definite fee for the services rendered independent of the return to the client (i.e. benefit earned or losses incurred by the client on account of acting on the advice of the bank).
- iii) PMS should be provided to the clients in respect of the latter's long term investable funds. Funds should not be accepted for portfolio management for a period less than one year. In case of placement of funds for portfolio management by the same client on more than one occasion on a continuous basis, each such placement should be treated as a separate account and each such placement should be for a minimum period of one year.
- iv) Portfolio funds should not be deployed for lending in call/notice money; interbank term deposits and bills rediscounting markets and lending to/placement with corporate bodies.
- v) Banks should maintain client wise account/record of funds accepted for management and investments made thereagainst and all credits (including realized interest, dividend etc) and debits relating to the portfolio account should be put through such account. The tax deducted at source in respect of interest/dividend on securities held in the portfolio account should be reflected in



the portfolio account. The account holder should be entitled to get a statement of the portfolio account.

vi) Bank's own investments and investments belonging to PMS clients should be kept distinct from each other, and any transactions between the bank's investment account and client's portfolio account should be strictly at market rates.

vii) In case of transactions relating to PMS clients' account, although the bank could hold the securities belonging to the portfolio account in its own name on behalf of its PMS clients, all the relative records should give a clear indication that the transaction belongs to PMS clients and does not belong to banks' own Investment Account.

viii) In the bank's general ledger, a 'Clients Portfolio Account' should be maintained and all the funds received by it for portfolio management should be reflected in it on a day-to-day basis. The balance lying in this account (i.e the funds undeployed, if any, from this account) should be treated as outside borrowings of the bank and it should maintain Cash Reserve Ratio/Statutory Liquidity Ratio on such funds.

ix) The bank's liability to its clients in respect of funds accepted by it for portfolio management should be properly reflected in the published books of accounts of the bank/subsidiary.

x) There should be a clear functional separation of trading and back office functions relating to banks' own investment accounts and PMS clients' accounts. PMS clients' accounts should be subjected by banks to a separate audit by external auditors.

xi) Violation of these instructions would be viewed seriously and invite deterrent action against the banks, which would include raising of reserve requirements, withdrawal of facility of refinance from the RBI and denial of access to money markets, apart from prohibition from undertaking PMS activity.

xii) These instructions apply, *mutatis mutandis*, to the subsidiaries of banks except where they are contrary to specific regulations of RBI or SEBI governing their operations.

xiii) Banks / subsidiaries of banks operating PMS or similar schemes with the specific prior approval of the RBI are also required to comply with the guidelines contained in the SEBI (Portfolio Managers) Rules and Regulations, 1993 and those issued from time to time.

xiv) Apart from the conditions stipulated above, in the case of bank subsidiaries offering discretionary PMS, banks were advised to ensure that the Board of the bank lays down appropriate risk management policy for the subsidiary which is effectively implemented by the subsidiary.

A list of circulars on the subjects referred to in the above paragraphs is enclosed as Appendix.

### **3. Proposed Guidelines on Wealth Management Services as well as the Marketing/Distribution services offered by Banks**

A comprehensive review of the existing Guidelines has been undertaken in view of the concerns stated in para 1.3 and 1.4 above. As stated therein, the major concerns arise from consumer protection issues involving conflict of interest, mis-selling and lack of adequate grievance resolution mechanism, and exposure to operational risk arising from weak internal control mechanisms.

#### **3.1 Marketing/Distribution of financial products and services**

3.1.1 Although traditionally, the agency model for marketing and distributing third party products is without risk participation since the sales are on behalf of the issuer of the third party financial products, in case of a bank acting as distributor, the customer's expectation from a bank in terms of the bank's credibility is significantly different than that of any other agent of the product issuer. Thus banks are expected to take greater care while undertaking such services, including avoiding mis-selling.

3.1.2 Mis-selling of products and services occurs when products that are unsuitable to the client profile are sold to him, particularly through misrepresentation or by linking it with banks' own products e.g., making purchase of insurance compulsory along with a car loan. Mis-selling can arise either from lack of knowledge of the product being sold, and occurs when untrained staff sell products. It may also arise

from the provisions regarding payment of commissions and incentives which distort the selling structure. In the recent investigations undertaken by RBI referred to above, it was observed that in some cases, banks did not have clear segregation of duties of marketing personnel from other branch functions, and bank employees were directly receiving incentives from third parties such as insurance, mutual fund and other entities for selling their products.

3.1.3 Section 10(1)(b)(ii) of the BR Act, 1949 prohibits a bank from employing or continuing the employment of any person whose remuneration or part of the remuneration takes the form of commission or of a share in the profits of the bank, save as exempted in the Proviso thereto. Accordingly, payment of a portion of the commission earned on marketing and distribution of third party products by the bank to the staff would fall under the said prohibition.

3.1.4 While banks may act as agents of third-party issuers of financial products and services on fee basis, without any risk participation, additional safeguards are necessary. Accordingly, the following conditions are prescribed in addition to the extant instructions:

- i) As mis-selling is a serious issue in terms of consumer protection, the bank should put in place a policy approved by its Board regarding marketing and distribution of third party financial products which should, inter alia specifically consider the issue of addressing mis-selling.
- ii) Banks may only undertake marketing and distribution of financial products and services. The third party product issuer should be a regulated financial entity in India.
- iii) The bank should adhere to the guidelines laid down by the sector specific regulator for its agency business.
- iv) Persons undertaking marketing/distribution services of third party financial products should have suitable professional qualification for carrying out the role. There should be a system of continuous development & training (internal as also external) of such persons so that they may understand the complexity of the product.

- v) The sales process should be transparent with full disclosure as to the details of the product. The selling should be need based and mapped to the customer profile.
- vi) Products should be marketed only in branches having specified trained personnel for the purpose.
- vii) The persons undertaking such marketing/distributions services, should not be entrusted with any other approval/transactional process at bank branches. There should be a clear segregation of functions between marketing and operational staff.
- viii) There should be a Code of Conduct for the sales personnel who should adhere to the same.
- ix) The fact that the bank is acting only as an agent should be clearly brought to the notice of the customer.
- x) The bank should set up robust internal grievance redressal machinery for resolving issues related to mis-selling, agency services, service defaults etc.
- xi) It may be ensured that there is no violation of Section 10(1) (ii) of the BR Act 1949 in payment of commissions/incentives as well as of Guidelines issued by the regulator of the third party issuer. No incentive (cash or non-cash) linked directly or indirectly to the income received from marketing and distribution function should be paid to the staff engaged in marketing/distribution services of third party products. The staff of the bank is also not permitted to receive any incentive (cash or non-cash) directly from the third party issuer. Banks must ensure that there is no violation of the above in the incentive structure to staff.
- xii) The bank should adhere strictly to all KYC/AML Guidelines as issued from time to time on the matter.
- xiii) Transactions above Rs 50000 for these products should only be accepted through debit to customers account with the bank and not in cash/cheque of other banks. There should be no evasion of these regulations by accepting several amounts for lower values from the same client to avoid the stated threshold.
- xiv) Banks should disclose to the customers, details of all the commissions/other fees (in any form) received, if any, from the various mutual fund/insurance/other

financial companies for marketing their products. This disclosure would be required even in cases where the bank is marketing products of only one mutual fund/ insurance company etc.

xv) Banks should disclose in the 'Notes to Accounts' to their Balance Sheet, the details of fees/remuneration received in respect of the marketing and distribution function undertaken by them.

### **3.2 Segregation of WMS activities of the bank by setting up of a Separately Identifiable Department or Division(SIDD)**

3.2.1 Conflict of interest arises mainly from the juxtaposition of the marketing/distribution function and the advisory or funds management function. To address the issue of conflict of interest arising from the single entity conducting both the activities of advisory/fund management as well as marketing, it is proposed to segregate the two functions.

3.2.2 Accordingly, banks may conduct all WMS activities, i.e., referral, IAS and PMS either from a separate subsidiary or through a Separately Identifiable Department or Division (SIDD) set up for the purpose. Banks would require prior approval of RBI before undertaking WMS services whether through a subsidiary or a SIDD and would have to comply with the following requirements in both cases.

The specific prescriptions in this regard are as under:

- i) Such subsidiary/SIDD would require to be registered with SEBI and comply with SEBI Guidelines regarding provision of these services, including code of conduct if any prescribed.
- ii) There should be a strictly defined and clear demarcation between the other departments of the bank and the SIDD. It should be ensured that there is no intermingling of the distribution and advisory role in case a bank is undertaking both the activities.
- iii) There should be an arm's length relationship between the bank and the subsidiary if WMS is being undertaken through the subsidiary.

- iv) Persons manning the SIDD/subsidiary should have suitable professional qualification for carrying out the role of Investment Advisor /Financial Advisor/Portfolio Manager. There should be a system of continuous development & training (internal as also external) of such persons.
- v) While the specific activity of financial advisory services/portfolio management will be regulated by SEBI, the Reserve Bank would continue to supervise the bank for all its activities including those undertaken through the SIDD.
- vi) The bank/subsidiary should set up robust internal grievance redressal machinery for resolving issues related to services offered.
- vii) The bank/subsidiary should formulate a board approved customer compensation policy in case of complaints related to services offered.
- viii) Banks/subsidiaries should disclose to the customers, details of all the commissions/other fees (in any form) received, if any, from the various mutual fund/insurance/other financial companies for marketing their products. This disclosure would be required even in cases where the bank is marketing products of only one mutual fund/ insurance company etc.
- ix) The instructions/ guidelines on KYC/AML/ CFT applicable to banks, issued by RBI from time to time, may be adhered to, in respect of customers to whom the services of referral/IAS/PMS are being provided.
- x) Banks may, through the SIDD/subsidiary, provide services only in respect of financial services and products offered by regulated financial services entities.
- xi) Violation of the instructions regarding undertaking of referral/IAS/PMS business by banks/subsidiaries will be viewed seriously and may invite deterrent action against the banks, which could include raising of reserve requirements, withdrawal of facility of refinance from the RBI and denial of access to money markets, apart from prohibition from undertaking referral/IAS/PMS activity.

### **3.3 Grievance Redressal Mechanism**

Irrespective of the nature of the service offered, i.e., sale of third party products, advisory, referral or fund management, or the form in which it is provided, whether

departmentally or through subsidiary or through SIDD, the bank must put in place a robust customer grievance redressal mechanism which should form part of the Board approved policy.

### **3.4 Operational Risk**

Similarly, banks should put in place sound internal control mechanisms and a system of checks to address risk management.

## **4. Specific Guidelines pertaining to Wealth Management Services**

Apart from the above, guidelines on the specific Wealth Management Services offered by banks are enhanced and detailed as under:

### **4.1 Referral Services**

4.1.1 Referral activities are those where the bank refers its customers to third party issuers of the financial products and services including those offered by bank' subsidiaries/entities who are part of the same group. Under the referral arrangement, banks may also have a specific agreement with the third party issuer for sharing of customer information apart from providing physical infrastructure within select branch premises for selling their products and, in turn, earn referral fees.

4.1.2 In the Report of the Committee on Bancassurance, 2011, IRDA had observed that there were several irregularities in the referral arrangements entered into by insurance companies with banks due to obliteration of the difference between corporate agency and referral business and regulatory arbitrage enabling circumvention of the cap on commissions and training requirements. In some cases, the referral banks were actually soliciting the customers for sale of insurance through untrained staff. As stated in the Report, this had prompted IRDA to permit only those banks which are not eligible to undertake corporate agency business to register as referral companies' in terms of the IRDA (Sharing of database for distribution of insurance products) Regulations, 2010.

4.1.3 As the differences between services provided under referral model and those provided under agency model have blurred in many cases, banks are perceived to be operating as agencies while in reality they may be providing only referral services. There are also instances where customer information has been shared with third-party issuers without obtaining an explicit consent or where the customer was not provided with the option of refusing to give consent for sharing personal information. Such practices have serious consequences leading to reputation risk to the banks. It is therefore proposed that banks shall not be permitted to enter into specific referral agreements with third party issuers of products and services.

4.1.4 However, if a customer requests a bank regarding obtention of financial products/services, there will not be any objection to banks referring them to providers of such services.

## **4.2 Investment Advisory Services (IAS)**

4.2.1 The SEBI(Investment Advisors) Regulations 2013, defines an “investment adviser” as any person, who for consideration, is engaged in the business of providing investment advice to clients or other persons or group of persons and includes any person who holds out himself as an investment adviser, by whatever name called. Further investment advice is defined as advice relating to investing in, purchasing, selling or otherwise dealing in securities or investment products, and advice on investment portfolio containing securities or investment products, whether written, oral or through any other means of communication for the benefit of the client and shall include financial planning. All investment advisors will be required to obtain a certificate of registration from SEBI under these Regulations. Accordingly all banks and bank sponsored subsidiaries offering Investment Advisory Services will require to be registered with SEBI and comply with the provisions of the SEBI Investment Advisors Regulations.

4.2.2 Banks may offer Investment Advisory Services (IAS), after obtaining specific prior approval of RBI (DBOD), subject to the following conditions:



- i) Banks may offer Investment Advisory Services (IAS) only through a Separately Identifiable Department or Division (SIDDD) which will conform to the prescriptions stated at para 3.2.2 above.
- ii) The bank offering IAS (through the SIDDD) should be registered under the SEBI (Investment Advisers) Regulations 2013 and shall adhere to all SEBI prescribed regulations including the code of conduct formulated thereunder.
- iii) The services offered should be purely advisory in nature. The bank should not, under any circumstance, accept funds from the clients for management.
- iv) The bank should not indemnify, directly or indirectly, for any losses incurred by the client as a result of acting on the advice of the bank. The agreement entered into with the client should provide a clause to this effect.
- v) The bank should charge a definite fee for the services rendered independent of any benefit or losses incurred by the client on account of acting on the advice of the bank. The bank should issue a suitable disclaimer in this regard.

#### **4.2.3 Investment Advisory Services (IAS) by bank sponsored subsidiaries**

4.2.3.1 Bank-sponsored subsidiaries offering/desirous of offering IAS, may follow the following guidelines:

- i) The sponsor-bank should obtain specific prior approval of DBOD before offering Investment Advisory Services through an existing subsidiary or for setting up a subsidiary for this purpose. This would also be applicable to a foreign bank, having presence in India as a branch and desirous of offering IAS through its subsidiary. (Setting up of any subsidiary will, as hitherto, be subject to the extant guidelines on para-banking activities of banks).
- ii) The subsidiary offering IAS should be registered under the SEBI (Investment Advisers) Regulations 2013 and shall adhere to all SEBI prescribed regulations including the code of conduct formulated thereunder.
- iii) The subsidiary is permitted to offer IAS to their customers only on products or services which a bank can offer.

iv) The instructions/ guidelines on KYC/AML/ CFT, issued by the regulator of the subsidiary, as amended from time to time, may be adhered to, in respect of customers to whom the service of IAS is being provided.

### **4.3 Portfolio Management Services (PMS)**

4.3.1 The activity of PMS is regulated by SEBI as per SEBI (Portfolio Managers) Rules and Regulations, 1993 wherein a portfolio manager is defined as any person who pursuant to a contract or arrangement 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 the funds of the client, as the case may be. As stated above, banks may undertake PMS only through a Separately Identifiable Department or Division (SIDD) or a subsidiary. PMS can be either discretionary or non-discretionary in nature.

#### **4.3.2 PMS-Non-Discretionary**

4.3.2.1 The non-discretionary portfolio manager manages the funds in accordance with the directions of the client. Thus under Non-Discretionary PMS, the portfolio manager will provide advisory services enabling the client to take decisions with regards to the portfolio. The choice as well as the timings of the investment decisions rest solely with the investor. However the execution of the trade is done by the portfolio manager. Since in non-discretionary PMS, the portfolio manager manages client portfolio/funds in accordance with the specific directions of the client, the PMS Manager cannot act independently.

4.3.2.2 Banks may offer **non-discretionary** portfolio management services, after obtaining specific prior approval of RBI (DBOD), subject to the following conditions:

- i) All banks offering Portfolio Management Services (PMS) will be registered with SEBI and regulated as per SEBI (Portfolio Managers) Rules and Regulations, 1993 and shall adhere to all SEBI prescribed regulations including the code of conduct formulated thereunder.
- ii) Banks may undertake PMS only through a Separately Identifiable Department or Division (SIDD) and will comply with all prescriptions regarding the SIDD as stated in para 3.1 above.

- iii) Only those banks which can provide such services on their own should undertake the activity. Funds accepted for portfolio management from their clients should not be entrusted to another bank for management.
- iv) PMS should be in the nature of investment consultancy / management, for a fee, entirely at the customer's risk without guaranteeing, either directly or indirectly, a pre-determined return. The bank should not indemnify the client directly or indirectly in any manner in the event of the bank not being able to achieve the minimum stipulated rate of return specified, if any, in the agreement. The bank should charge definite fee for the services rendered independent of the return to the client (i.e. benefit earned or losses incurred by the client on account of acting on the advice of the bank).
- vii) PMS should be provided to the clients in respect of the latter's long term investable funds. Funds should not be accepted for portfolio management for a period less than one year. In case of placement of funds for portfolio management by the same client on more than one occasion on a continuous basis, each such placement should be treated as a separate account and each such placement should be for a minimum period of one year. There will, however, be no objection to shuffling of relative investments during this period.
- viii) Portfolio funds should not be deployed for lending in call/notice money; inter-bank term deposits and bills rediscounting markets and lending to/placement with corporate bodies.
- ix) Banks should maintain client wise account/record of funds accepted for management and investments made there against and all credits (including realized interest, dividend etc) and debits relating to the portfolio account should be put through such account. The tax deducted at source in respect of interest/dividend on securities held in the portfolio account should be reflected in the portfolio account. The account holder should be entitled to get a statement of the portfolio account.
- x) Bank's own investments and investments belonging to PMS clients should be kept distinct from each other, and any transactions between the bank's investment account and client's portfolio account should be strictly at market rates.
- xi) In case of transactions relating to PMS clients' Account, although the bank could hold the securities belonging to the portfolio account in its own name on behalf

of its PMS clients, all the relative records should give a clear indication that the transaction belongs to PMS clients and does not belong to banks' own Investment Account.

xii) In the bank's general ledger, a 'Clients Portfolio Account' should be maintained and all the funds received by it for portfolio management should be reflected in it on a day-to-day basis. The balance lying in this account (i.e the funds un-deployed, if any, from this account) should be treated as 'outside borrowings' of the bank and should be reckoned for calculation of Cash Reserve Ration/Statutory Liquidity Ratio.

xiii) The bank's liability to its clients in respect of funds accepted by it for portfolio management should be properly reflected in the published books of accounts of the bank.

xiv) There should be a clear functional separation of trading and back office functions relating to banks' own investment accounts and PMS clients' accounts. PMS clients' accounts should be subjected by banks to a separate audit by external auditors.

xv) Acceptance of funds by banks from their clients for management, by whatever scheme/name, other than deposits for specific periods which are subject to RBI's interest rate directives, should be subject to the RBI's guidelines on PMS. In other words, apart from deposit taking, the banks should accept funds from their clients for management only under the terms and conditions stipulated for the PMS and not under any other scheme.

#### **4..3.2.3 Portfolio Management Services (PMS)- Discretionary:**

The discretionary portfolio manager individually and independently manages the funds of each client in accordance with the needs of the client. Under discretionary PMS, independent charge is given by the client to the portfolio manager to manage the portfolio/funds. The discretionary Portfolio Management Service also includes portfolios broadly directed by the customer or those wherein the customer gives a negative list of investment products at the time of opening the account so that the Fund Manager ensures that such investment products are not included in the portfolio.

Banks are **prohibited** from offering discretionary portfolio management services.

#### **4.3.2.4 Portfolio Management Services (PMS) by bank sponsored subsidiaries**

Bank sponsored subsidiaries (domestic and overseas) may offer discretionary PMS, subject to the following conditions in addition to the conditions stated at 4.3.2.2. above for banks which will apply to their subsidiaries also :

- i) The sponsor-bank should obtain specific prior approval of DBOD before offering Portfolio Management Services through an existing subsidiary or for setting up a subsidiary for this purpose. This would also be applicable to a foreign bank, having presence in India as a branch and desirous of offering PMS through its subsidiary. (Setting up of any subsidiary will, as hitherto, be subject to the extant guidelines on para-banking activities of banks).
- ii) All bank sponsored subsidiaries offering Portfolio Management Services (PMS) will be registered with SEBI and regulated as per SEBI (Portfolio Managers) Rules and Regulations, 1993 and shall adhere to all SEBI prescribed regulations including the code of conduct formulated thereunder.
- iii) There should be an arms' length relationship between the bank and the subsidiary.
- v) The instructions/ guidelines on KYC/AML/ CFT applicable to the subsidiary, issued by the concerned regulator, as amended from time to time, may be adhered to, in respect of customers to whom the service of PMS is being provided.

#### **5. Timeline for re-organization**

Banks, including their subsidiaries, who are already undertaking the above activities, may reorganize their structure in accordance with the final guidelines within a period of one year from the date of issue of final Guidelines on the subject.

**APPENDIX****List of Circulars consolidated in the draft guidelines on Wealth Management /Marketing /Distribution Services Offered by banks**

<b>No</b>	<b>Circular No.</b>	<b>Date</b>	<b>Subject</b>
1.	Mailbox clarification	March 25, 2006	Marketing / Distribution of Mutual Fund / Insurance etc. products by Banks
2.	DBOD.No.FSD.BC.60/24.01.001/2009-10	November 16, 2009	Marketing/Distribution of Mutual Fund/ Insurance etc., Products by Banks
3.	DBOD.No.FSC.BC.74/24.76.002/95-96	June 13, 1996	Marketing of Mutual Fund Units by banks
4.	DBOD.No.FSC.BC.129/24.76.002/97	October 22, 1997	Retailing of Government Securities
5.	DBOD.No.FSC.BC.129/24.76.002/97	June 8, 1996	Retailing of Government Securities
6.	DBOD .No. FSD. BC.67/24.0 1.001/2009-10	January 07, 2010	Disclosure in Balance Sheet-Bancassurance Business
7.	DBOD.FSC.BC.27/24.01.018/ 2003-2004	September 22, 2003	Entry of banks into Insurance business
8.	DBOD.FSC.BC/16/24.01.018/ 2000-2001	August 9, 2000	Entry of banks into Insurance business
9.	DBOD.No.FSC.BC.118/24.76.002/98	December 26, 1998	Information System for Portfolio Management Services (PMS)
10.	DBOD.No.BC.73/27.07.001/94-95	June 7, 1994	Acceptance of deposits under Portfolio Management Scheme (PMS)
11.	DBOD.No.BC.183/27.07.003/93-94	October 18, 1993	Information System for Portfolio Management Services (PMS)
12.	DBOD.No.BC.11/24.01.009/92-93	July 30, 1992	Portfolio Management on behalf of banks
13.	DBOD.No.FSC.BC.69/469-90/91	January 18, 1991	Portfolio Management on behalf of clients
14.	DBOD.No.BP.(FSC)BC.120/C.469-89	May 2, 1989	Portfolio Management on behalf of clients
15.	DBOD.No.Dir.BC.43/C.347-87	April 15, 1987	Portfolio Management on behalf of clients