Why are there very few registered investment advisors in India?

SEBI's stringent norms on education and experience, and its zeal to keep givers of stock tips away, have ended up keeping out genuine investment advisors.

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When Indore-based Prashant Chitnis, 64, a retired banking officer, applied to market regulator SEBI for a Registered Investment Adviser (RIA) license, he was in for a rude shock. Chitnis was already selling mutual funds (MFs) and insurance policies, but he wanted to get into goal-based financial planning. SEBI demanded lots of information. It asked for offer letters of all his past employers, copies of bank statements of all accounts that he had ever held, and even bills of his laptop, printer and other office infrastructure. SEBI also asked for all his Form 16 and 26AS income tax documents, in addition to his return filings.

Moneycontrol has a copy of this letter that asked for 16 such details. Frustrated, Chitnis visited the SEBI's local office a few days later. There was a deeper problem.

A SEBI official told him that it has stopped giving RIA licenses there since 2018. Many SEBI-registered investment advisers from Indore, and elsewhere in Madhya Pradesh, were caught giving dubious stock tips under the garb of investment advice and charging fees. Regular police visits at SEBI's Indore office to investigate how such people were given licenses in the first place, deterred the regional office there from issuing fresh ones.

SEBI's refusal to give any RIA licenses in Indore is one part of the problem. The bigger problem is that despite the regulations being nearly nine years old, there are only 1,321 RIAs as per SEBI data as of September 28, 2021. If you weed out those giving just stock tips, there are roughly just 400 financial advisors in the country. And only half of them would be pure fee-based individual advisors. The other half comprises corporate advisors who also earn a distribution commission. On the other hand, there are nearly 4 crore MF investors and another about 2-3 crore demat account holders. It's a yawning gap.

The birth of (licensed) investment advisory in India

Spurred by the many complaints about mis-selling of products over the years, SEBI decided to make investment advisers accountable. It issued the Investment Adviser Regulations in January 2013.

The regulations said that those who give investment advice across products or charge a fee, must register. Mutual fund distributors (MFDs) who give limited advice, incidental to their larger activity of selling MFs, were exempted.
But the regulations threw more questions than answers. For instance, MFDs were allowed to earn commissions from mutual funds by distributing schemes and also charge advisory fees (just for basic advice that they were allowed to render), under one roof. But RIAs were not allowed to earn distribution commission income unless they were non-individuals having a separately-identifiable department.

What RIAs can do and what they can't

As time rolled by, SEBI started deliberations. It asked for feedback on how the regulations could be refined and more people could be nudged to register as investment advisers. The idea was to figure out how to segregate investment advice and distribution, clearly define what MFDs and investment advisers could do, and increase the choice available to investors in terms of intermediaries. That way, investors would have easier choices to make based on whether they just wanted to invest in a mutual fund or if they required financial planning. SEBI also wanted to keep those giving only stock tips away.

After four consultation papers spread over three-and-a-half years, SEBI finally tightened the investor adviser regulations in July 2020. It said that individual advisors can only earn a fee income. They cannot sell mutual funds and earn commission. Non-individual or institutional advisors can offer both (investment advisory and distribution), but not to the same client.

Raising the bar or restricting entry?

SEBI also tightened the qualification norms. All advisors must have a post-graduate qualification and at least five years of relevant work experience. This became an impediment for quite a few.

Chennai-based S.A. Subarajah saw his RIA application rejected by SEBI in June 2021. Subarajah is an IIT Madras graduate, cleared his civil services exam and worked in the Central Board of Indirect Taxes and Customs in Chennai for 13 years. A job abroad for six years and two more investment advisory certifications later, he decided to apply for the investment adviser license earlier this year.

SEBI said that he didn't have work experience in giving investment advice. "As per earlier guidelines, I would have qualified because, at that time, what was required was the necessary education or work experience. Now, the revised guidelines ask both. I have worked for the Government of India under the ministry of finance for 13 years. That too isn't enough. What's worse, there is no way to appeal against SEBI's ruling," he says.

Further, licensed advisors are now mandated to re-take the advisory certification exam every few years. Earlier, they had to show proof of their continuing education credits by attending seminars, conferences, and so on, to keep their licenses valid. Suresh Sadagopan, Founder of Ladder7 Financial Advisories says: "Despite 17 years of financial advisory experience, I still had to take the same, back-to-basics, exam every time I renewed the certification. It's pointless for experienced advisers," he says. That's not all. SEBI also fixed the maximum fees that RIAs can charge.

Also, once individual advisors cross 150 clients, they need to become corporates. Doing so would require a higher networth of Rs 50 lakh.

Problems vs necessity

Renu Maheshwari, a SEBI-registered investment advisor and CEO and principal advisor at Finscholarz Wealth Managers LLP, says that an RIA model is "a complicated one to pursue." She says that the distribution business is easier to practice and makes enough money. RIA is a consulting practice and requires a different orientation. With a higher entry barrier to become an RIA now, it's not uncommon hearing distributors avoiding investor adviser registration. That didn't deter Maheshwari though. She jumped straight into becoming an RIA – she was never a MFD before that. "If you do the right thing and act in clients' best interests, they will pay you," she says.

Sadique Neelgund, founder of Network FP, says that "such high entry barriers have been created to discourage stock tip givers from entering the fray and mis-selling. However, it has impacted ethical financial advisors and planners."

Vishal Dhawan, a certified financial planner and founder-CEO of Plan Ahead Wealth Advisors is a bit more optimistic. He points out that SEBI's four white papers were an evolution journey. SEBI itself went back and forth on a few points, before it came out with Regulations 2.0 in 2020, he says. This, he reminds us, happened just a year back in September 2020. "Technically, it has just been a year since the RIA guidelines were finalised. If distributors take a corporate license, they can advise and distribute. We need to wait and see how distributors and advisors adopt the Regulation 2.0."

Dhawan feels the main reason for very few advisors in the country is SEBI failing to enforce its own regulations of ensuring multi-product advice being available only through RIAs.

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