

**Consultation Paper**  
**on**  
**Performance Validation Agency**

**MIRSD – PoD-2**

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## **1. Objective**

1.1. The objective of this consultation paper is to seek comments from public on the proposal for creation of Performance Validation Agency (PVA) to validate any claims of performance by SEBI registered intermediaries and other entities, thereby facilitating these intermediaries/ entities to showcase their validated performance to investors to grow the reach of their services.

## **2. Background**

2.1. Intermediaries/ other entities need to showcase their performance to attract more clients and grow and continue to do business. However, in the rush for more clients some of these entities may indulge in making inflated claims of their performance or recommendations to investors, thereby misleading the investors.

2.2. Currently, Asset Management Companies (AMCs) calculate the performance of mutual fund schemes. Similarly, portfolio managers have been permitted to report their performance vis-à-vis certain benchmarks. The claims made by these intermediaries/entities are mostly self-verified and currently there is no dedicated agency to validate such claims.

2.3. Investment Advisers (IAs) and Research Analysts (RAs) are also inherently involved in giving investment advice and 'buy/sell/hold' recommendation respectively. In terms of the advertisement code for IAs and RA issued by SEBI, IAs and RAs are currently not allowed to make any reference to past performance.

2.4. Stock brokers providing services relating to algorithmic trading may need to demonstrate the performance of the algorithms provided by them so that investors are better able to understand the algorithms and deploy them towards their investment objectives. Currently, stock brokers are not allowed to make any reference to the past or expected future return/ performance of algorithms or associate with any platform providing reference to the past or expected future return/ performance of algorithms.

## **3. Need for Performance Validation Agency**

3.1. There has been a demand from registered intermediaries to showcase their performance to investors so as to establish/ enhance their credibility in the eyes of

investors and to help grow the reach of their services to investors. In order to address this demand, it is proposed to facilitate registered intermediaries to disclose their performance to investors, while at the same time having checks and balances to protect the interest of investors against unverified claims/ performance.

- 3.2. Accordingly, it is proposed to create an independent body called Performance Validation Agency ('PVA') to validate the claims/ performance related to investment advice, 'buy/sell/hold' recommendation, mutual fund scheme, portfolio management service, algorithm, etc. by SEBI registered intermediaries/ other entities such as IA, RA, portfolio manager, AMC, stock brokers, etc.

#### **4. Criteria for grant of recognition**

- 4.1. As PVA would require to process the data and claims/ performance of intermediaries/ other entities, with attendant privacy of customer data on strategies, it is crucial that the entity that handles the data is able to shoulder the responsibility to gather, process and validate the huge amount of data. Currently, Market Infrastructure Institutions ('MIIs') in securities market handle enormous amount of data on a daily basis especially related to securities market.
- 4.2. Given the above, it is a natural fit for PVA to be a wholly-owned subsidiary of MII or a jointly supported entity by multiple MIIs, whose purpose would be to enable intermediaries/ other entities to market their products based on validations made by the PVA.
- 4.3. Recognition of PVA shall be based on the eligibility of the parent entity, for which the eligibility criteria shall be prescribed by SEBI.

#### **5. Setting up of requisite systems**

- 5.1. In order to ensure smooth functioning, PVA shall be required to put in place systems/ processes for maintaining data, grievance redressal and sharing of information with SEBI.
- 5.2. PVA shall also be required to have necessary infrastructure such as adequate office space, equipment and human resource to effectively discharge its functions.

## 6. Role and responsibility of PVA

- 6.1. Performance claims shall be validated by PVA based on specified parameters such as returns, risk, volatility and other suitable parameters as may be decided by industry forum in consultation with PVA and SEBI. PVA shall be responsible to maintain confidentiality of the information received by it during this process.
- 6.2. For this purpose, PVA may partner with other knowledge partners such as Credit Rating Agencies.
- 6.3. SEBI registered intermediaries/ other entities will be enabled to seek the services of PVA for validating all their security/ portfolio recommendations or claims.

## 7. Charging of fees by PVA

- 7.1. PVA shall be permitted to charge a reasonable fee for its services.

## 8. Types of claims permitted to be validated by PVA

- 8.1. PVA shall validate the following types of claims:

### 8.1.1. Claim of 'Actual profit' made by clients:

PVA shall validate the claims by SEBI registered intermediaries/ other entities of the actual profit made by their clients on the basis of advice/ recommendation/ services provided by them.

Such validation shall be carried out by the PVA for all clients of the registered intermediary/ other entity and shall not be carried out for selective clients. Validation shall be made on the basis of trading/ investment details using PAN of the clients.

### 8.1.2. Performance claim of SEBI registered intermediaries/ other entities and algorithms:

PVA shall validate the performance claims of SEBI registered intermediaries/ other entities.

PVA shall validate the performance of algorithms by testing the algorithms during a prospective reasonable test period. Performance of all the algorithms

shared with PVA for validation shall be disclosed and displayed on the website of PVA.

**8.1.3. Performance of recommended stock/ portfolio:**

For validation of performance of recommended stock/ portfolio, SEBI registered intermediaries shall be required to share with PVA, the actual recommendation given to their client on the day of recommendation. Such recommendation shall be accompanied by recommended holding period of the stock/ portfolio.

**8.1.4. Any other performance claims:**

Apart from the above, any other performance claim may be validated by PVA, subject to the core principle that there will be no selective cherry-picking of favourable events/ strategies/ client and other results. Further, any claim should be independently verifiable from sources other than the entity making the claim.

**9. Display of recommendations by intermediaries and PVA**

- 9.1. SEBI registered intermediaries seeking performance validation for client-specific security/ portfolio recommendations shall display such recommendations and their validation by PVA on their respective websites with restricted access to the concerned clients only.
- 9.2. Where SEBI registered intermediaries seek performance validation for recommendations made publicly, such recommendations shall be displayed on the websites of the intermediaries and PVA on the same day.
- 9.3. Where SEBI registered intermediaries seek performance validation of a recommended security/ portfolio, the performance of such recommended security/ portfolio shall be appropriately displayed on the website of the intermediary and PVA in the format as may be decided by industry forum in consultation with PVA and SEBI. Such validation shall be done for a reasonable period prior to and after the date of the recommendation.

## 10. Public comments

10.1. Comments may be provided on the following:

- (i) Whether SEBI registered intermediaries/ other entities should validate their claims/ performance before disclosing them to clients/ investors.
- (ii) Whether there is a need to have a separate entity (PVA) to validate the claims/ performance of SEBI registered intermediaries/other entities.
- (iii) Whether PVA should be a subsidiary of MII or a jointly supported entity by multiple MIIs.
- (iv) Suggestions on any other types of claims that should be validated by PVA.

10.2. Public comments are invited on the proposals at paragraph numbers 3 to 10.1 above. Comments may be forwarded by email to [consultationMIRSD@sebi.gov.in](mailto:consultationMIRSD@sebi.gov.in) latest by September 21, 2023. While sending the email, kindly mention the subject as “Comments on Consultation Paper on Performance Validation Agency”.

10.3. The comments should be sent by email in MS Excel File only in the format given below. The [link to download the format](#) is given here.

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