



**A DISTINCT APPROACH TO CAPITAL
INVESTMENT:
ALTERNATIVE INVESTMENT FUNDS (AIF)**

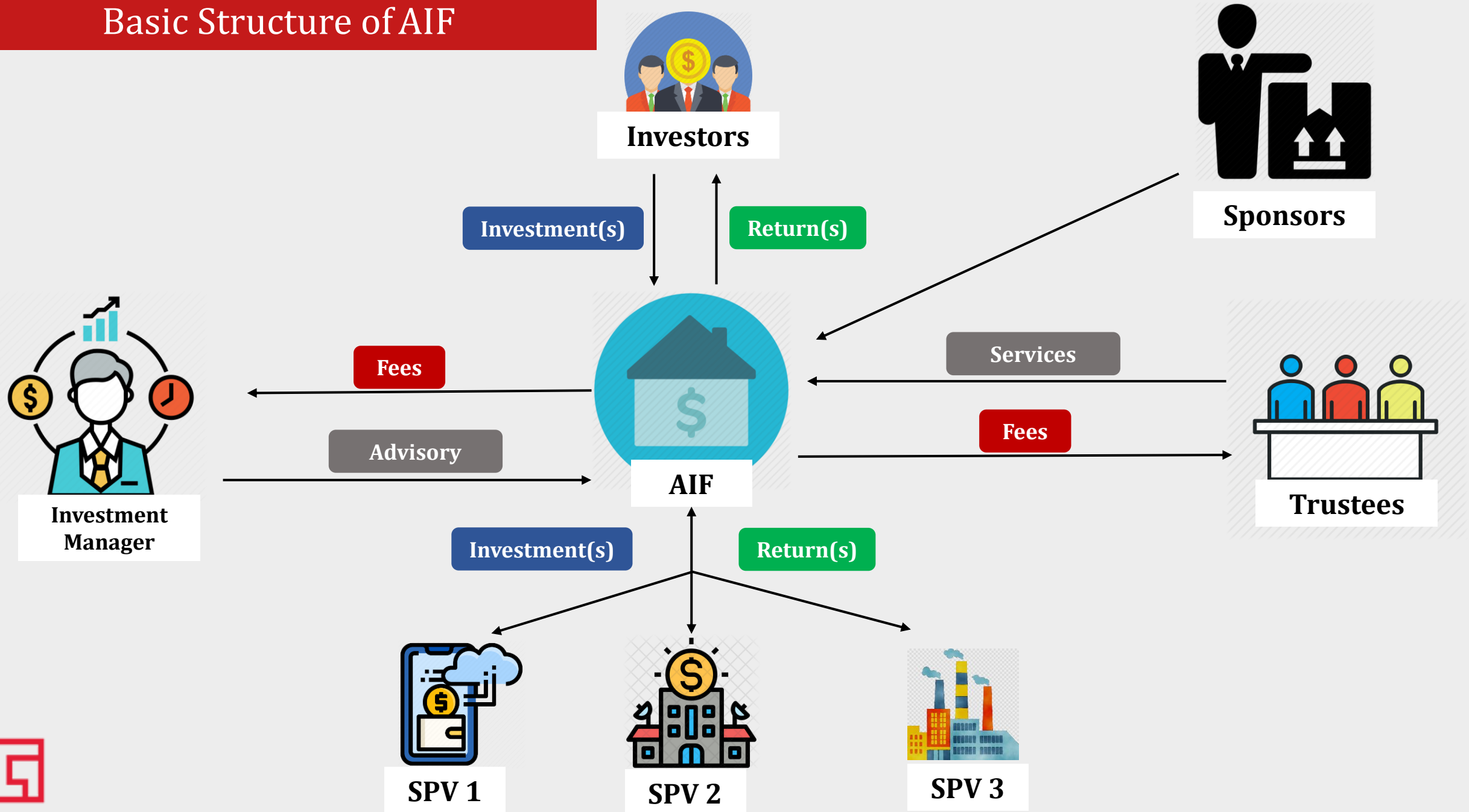




Alternative Investment Fund (AIF)









Basic Structure of AIF



Assessment of Structure Options

Criteria	Trust	Company	LLP
Existing Structures	Maximum AIFs are set up as Trusts	Negligent in number	Few are registered as LLP
Preference of Investors	Most preferred	Least preferred	preferred
Confidentiality	Maximum	Least	Moderate
Legal Compliance	Least	Maximum	Moderate
Ease of Business	Maximum	Least	Moderate

Features and General Conditions

No. of Investors	Investment Amount	Minimum Corpus	Fund Raising	Investor Eligibility	Interest of IM/Sponsor
 <ul style="list-style-type: none">• Max. 1000 investors per scheme (200 for Angel Fund)	 <ul style="list-style-type: none">• Min. INR 1 Crore (only 2 joint holders)• An employee or director of AIF Manager can invest Rs. 25 lakhs or more	 <ul style="list-style-type: none">• INR 20 Crore• INR 5 Crore for Angel Funds	 <ul style="list-style-type: none">• Through private placement only• Can float multiple schemes	 <ul style="list-style-type: none">• Indian• Foreign National• Non Resident	 <ul style="list-style-type: none">• 2.5% of corpus or INR 5 crore (whichever is lower)• 5% of Corpus or INR 10 Crore (lower of two) (only for Cat-III)



General Investment Conditions

Investment in securities of foreign companies allowed subject to conditions imposed by RBI.

Un-invested Investible fund may be invested in liquid mutual funds, or other liquid assets like treasury bills, commercial papers etc.



Terms of co-investment in an investee company by manager or sponsor shall not be favorable than offered to AIF.

No investment in associate entities without approval of 75% of the investor

The Manager or Sponsor shall disclose their investment in the Alternative Investment

Types of AIF



CATEGORY I

Invests in start-up or early stage ventures or social ventures or SMEs or infrastructure or other sectors or areas which the government or regulators consider as socially or economically desirable and shall include venture capital funds (including Angel Funds), SME Funds, social venture funds, infrastructure funds and such other Alternative Investment Funds.



CATEGORY II

Does not fall in category I and does not undertake leverage. This includes PE funds, debt funds, etc.



CATEGORY III

Employ diverse or complex trading strategies and are allowed to employ leverage and to be open ended. This category includes hedge funds, etc. and have stringent reporting requirements.



Alternative Investment Funds (AIF) – CATEGORY - I

Deployment of funds

Primarily invest in **unlisted entities**, start-ups etc. or units of other Cat – I AIFs



Borrowing / leverage

Allowed only for meeting temporary funding for limited period.



Type of scheme

Close ended



Registration Fees

INR 5 Lacs



Broad Sub-categories

- Venture Capital Fund
- Infrastructure Fund
- Angel Fund
- Social Venture Fund



Tenure

3years +
max. 2
years
extension
with
approval of
2/3rd
investors



No. of projects

Maximum 25% in one
projects



CATEGORY – I – Angel Funds

Deployment of funds

- 100% Investment in Venture Undertaking (incorporated not more than 3 years, turnover less than INR. 25 Cr etc.)
- Investment in range of INR 25 Lacs to max INR 10 Crores



Other Conditions

- Min Corpus – INR 5 Crores
- Min Investment by Investor– INR 25 Lacs for max 5 years
- Max 200 Investors
- Approval of Investors before each investment
- Each Investment treated as different scheme
- Instead of filing PPM, filing of Term sheet



Registration Fees

INR 2 Lacs



Tenure

Maximum period of 5 years



Type of scheme

Close ended



No. of projects

Maximum 25% in one projects



Alternative Investment Funds (AIF) – CATEGORY - II

Deployment of funds

Majorly in unlisted entities or units of AIF Cat I or II



Borrowing / leverage

Allowed only for meeting temporary funding for limited period.



Type of scheme

Close ended



Registration Fees

INR 10 Lacs



Broad Sub-categories

- Private Equity (PE) fund
- Debt Fund
- Fund of Funds

Tenure

3years + max. 2 years extension with approval of 2/3rd investors



No. of projects

Maximum 25% in one projects



Alternative Investment Funds (AIF) – CATEGORY - III

Deployment of funds

- Securities of listed or unlisted companies
- Derivatives
- Complex or structured products,
- Units of other Category I or II AIFs



Borrowing / leverage

- Allowed subject to:
- Consent from the investors; &
 - Maximum limit specified by the Board.

Type of scheme

Open or Close ended



Registration Fees

INR 15 Lacs



Other Requirement

Mandatory to have Custodian



Broad Sub-categories

- Hedge Fund
- PIPE Fund

Tenure

Close Ended

Min. 3 yrs.
(2 years ext. by 2/3rd majority)

Open ended
No tenure



No. of projects

Maximum 10% in one project



Eligibility Requirements to be Registered as AIFs

Charter Document* should permit the activity of AIF

Charter Document needs to be registered

Charter Document should prohibit making invitation to the public

Applicant, Sponsor and Manager should be “fit & proper”**

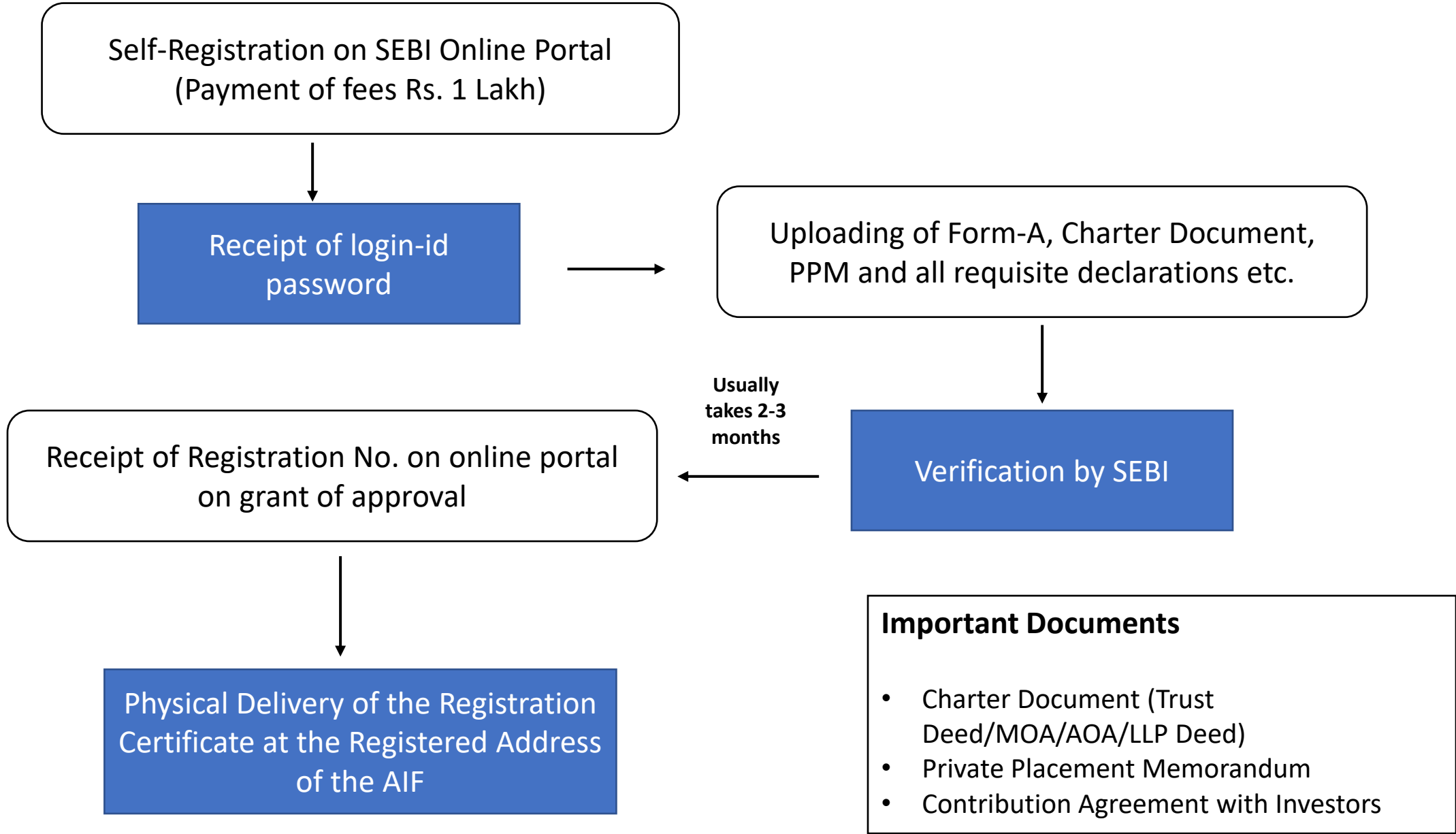
Key Investment Team should have 1 personnel with 5 years of experience

Manager and Sponsor should have necessary manpower

*Trust Deed/AOA/MOA/LLP Deed respectively

**As per SEBI Intermediaries Regulations, 2008

Process of registration:



- Important Documents**
- Charter Document (Trust Deed/MOA/AOA/LLP Deed)
 - Private Placement Memorandum
 - Contribution Agreement with Investors

Key disclosures in Private Placement Memorandum

PART – A: SECTION FOR MINIMUM DISCLOSURES

- Investment Objective, Strategy And Process
- Market Opportunity/ Indian Economy/ Industry Outlook
- Fund/Scheme Structure
- Governance Structure
- Track Record Of Manager
- Principal Terms Of The Fund/Scheme
- Principles Of Portfolio Valuation
- Conflicts Of Interest
- Risk Factors
- Legal, Regulatory, And Tax Considerations
- Illustration Of Fees, Expenses And Other Charges
- Distribution Waterfall (Include Various Possible Scenarios)
- Disciplinary History

PART – B: SUPPLEMENTARY DISCLOSURES AS PER THE INVESTMENT MANAGER

Foreign Investment in AIFs

- 100% FDI is permitted under automatic route in all the Categories of AIFs.
- In terms of FEMA20 Regulations, if the Sponsor and Manager (both) are “Owned and Controlled” by Indian resident citizens, then the AIF does not need to follow FDI downstream investment norms.
- The extent of foreign investment in the corpus of the AIF will not be a factor to determine as to whether downstream investment by the AIF is foreign investment or not although in case of Cat III which has any foreign investment, it shall make portfolio investment in only those securities or instruments in which FPI is allowed to invest under the FEMA 20 Regulations
- Downstream investment by an AIF that which is treated as foreign investment (based upon its management & Control) shall have to conform to the sectoral caps and conditions / restrictions, if any, as applicable to the company in which the downstream investment is made.

Investments in Foreign Securities by AIFs

- RBI, through its circular dated December 09, 2014, has permitted AIFs to invest in equity and equity-linked instruments of off-shore venture capital undertakings, subject to an overall limit of USD 500 million with the prior approval of SEBI
- The said limit was increased to USD 750 million by SEBI Circular dated July 03, 2018.

Matters requiring $\frac{3}{4}$ majority approval of Investors:

- Any material change (i.e. changes in fundamental attributes of the Fund)
- Investment by the Fund in an Associate
- In-specie distribution by the Fund
- Extension of limit for valuation from 6 months to 12 months (For Cat-I & II AIFs)*
- Winding up of the Fund;

Matters requiring 2/3 majority approval of Investors:

- Extension of the Term of the Fund
- Material change in the investment strategy

Reporting Requirements – SEBI and Custodian

Nature of Reporting	Reporting to	Frequency	Details of information sought
Reporting by AIFs	SEBI	<p>Quarterly Reporting: Cat-I, Cat-II and Cat-III AIFs which do not undertake leverage.</p> <p>Monthly Reporting: Category III AIFs which undertake leverage. (7 days from end of quarter/month)</p>	Details of the Fund including target corpus, total corpus, funds raised, investments made, details of investors, industry wise, investments etc.
Reporting on leverage	Custodian	Daily Reporting. Custodian to send to SEBI by 10 A.M. next day	To ensure that the leverage shall not exceed the prescribed limit at all times.
Valuation	SEBI	Cat-I & Cat-II every 6 months	Valuation of their investments by an independent valuer.

Reporting Requirements – Trustees and Investors

Nature of Reporting	Reporting to	Frequency	Details of information sought
Compliance Test Report	Trustee	<ul style="list-style-type: none"> • Within 30 days from the end of the financial year 	Details of compliance with provisions of AIF Regulations and circulars issued thereunder
Performance Report	Investors	<ul style="list-style-type: none"> • Cat I & Cat II within 180 days from year end; • Cat III within 60 days from end of Quarter 	<ul style="list-style-type: none"> • Financial Information of Investee Companies • Material Risks and how they are Managed
NAV	Investors	<ul style="list-style-type: none"> • Cat-III only • Open-ended every month-end • Close-ended every quarter-end 	Calculation of the net asset value

Additional Points in relation to AIFs

Performance Benchmarking

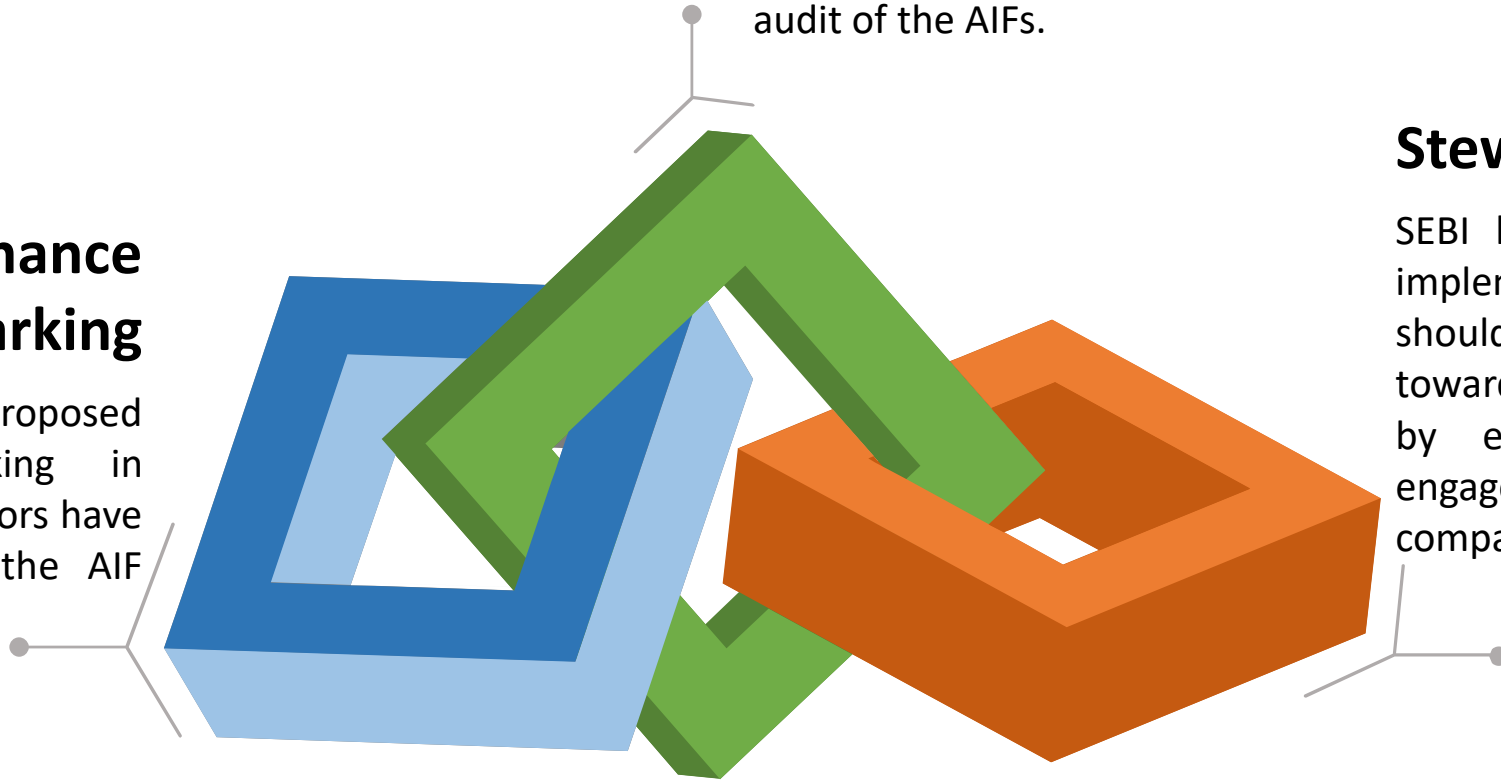
SEBI has recently proposed Performance Benchmarking in order to ensure that investors have a standard to compare the AIF performances

Audit Requirement

SEBI has also made it compulsory for all AIFs to conduct an annual audit of the AIFs.

Stewardship Code

SEBI has also mandated AIFs to implement a Stewardship Code to shoulder greater responsibility towards their clients / beneficiaries by enhancing monitoring and engagement with their investee companies .



Taxation

- The Finance Act, 2015, extended tax pass through status to AIFs that are registered with SEBI as Category I AIFs or Category II AIFs under the AIF Regulations.
- They are governed by a special tax regime as provided under Section 115UB of the Income tax Act, 1961 (the Act)
- Any income (other than business income) earned by a SEBI registered Category I and II AIF, is exempt from tax in the hands of the AIF under Section 10(23FBA) of the Act. Such income shall be taxable directly in the hands of the investors of the AIF under Section 115UB of the Act.
- Any income distributed by investment fund is not liable for DDT u/s 115-0
- Any income distributed by investment fund (except business income), TDS of 10% has to be deducted by inv fund u/s 194 LBB

Taxation

- The investors shall be chargeable to tax in the same manner as if it were the income accruing or arising to, or received by, such investor had the investments, made by the AIF, been made directly by such investor. Income taxable in investors' hands shall be deemed to be of the same nature and proportion as in the hands of the AIF.
- Further, in terms of Section 115UB(2) of the Act, in case there is a loss at the fund level (i.e. current loss or loss which remained to be set off), such loss shall not be allowed to be passed through to the investors but would be carried forward at AIF level to be set off against income of future years in accordance with the provisions of Chapter VI of the Act.
- Investment fund compulsorily required to file return u/s 139(4F)

Taxation – AIF Cat III

Category III AIFs has not yet been accorded a Pass through status, which means that income from such funds will be taxed at the investment fund level and the tax obligation will not pass through to unit holders.

Income under the head, “Profits or gains from business or profession”, the fund would be taxed in respect to such income at marginal rate of tax

In case of Trust structure, taxation will be as per tax provisions applicable to a Trust.



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