



## IFSC AIF - SEBI Operational Guidelines

The Securities Exchange Board of India (SEBI) vide circular dated 26 November 2018, issued Operating Guidelines for Alternative Investment Funds (AIFs) in International Financial Services Centre (IFSC). The IFSC guidelines (issued in March 2015) provided for broad framework for setting up of AIF in IFSC. These Operating Guidelines have been issued based on deliberation in Alternative Investment Policy Advisory Committee and in consultation with other stakeholders.

Traditionally, fund structuring for offshore and onshore investors involved evaluation of various investment routes such as foreign direct investment (primarily used for investment in unlisted entities), foreign portfolio investment (primarily used for investment in listed entities and non-convertible debentures), foreign venture capital investment (investment in specific sectors with benefits), domestic alternative investment fund (pooling along with domestic investors), etc.

An AIF registered with SEBI and set up in IFSC has the potential to encompass all the above investment routes in to one regulated SEBI registered vehicle. Thus, eliminating the need for multiple entities, registrations and other administrative burdens.

The operational guidelines issued by SEBI have been summarized in the table below.

Key Aspects	Key Points
<b>Registration conditions</b>	<ul style="list-style-type: none"><li>• AIF to be formed as a trust or company or LLP or body corporate</li><li>• AIF to seek registration as per categories specified in AIF regulations i.e., Category I, II or III</li><li>• SEBI to provide approval only on satisfaction of fulfilment of conditions under AIF regulations</li></ul>
<b>Eligible investors</b>	<ol style="list-style-type: none"><li>1) Person resident outside India</li><li>2) NRI</li></ol>



	<p>3) Resident Institutional investor who is eligible under FEMA to invest funds offshore (to the extent of outward investment permitted)</p> <p>4) Person resident in India (having net-worth of at least USD 1 million during the preceding financial year) eligible under FEMA to invest offshore, subject to LRS limit (i.e., USD 2,50,000)</p> <p><i>(for persons mentioned in 2-4, investment shall be subject to RBI guidelines)</i></p>
<b>Permissible investments</b>	<ul style="list-style-type: none"> <li>• Securities which are listed in IFSC;</li> <li>• Securities issued by companies incorporated in IFSC;</li> <li>• Securities issued by companies belonging to foreign jurisdiction;</li> <li>• Securities issued by companies incorporated in India provided the investment is under FDI or FPI or FVCI route <b>(Earlier only FPI route was allowed)</b></li> <li>• AIF in IFSC can invest in AIF in IFSC/India subject to AIF regulations (i.e., Fund of AIFs can invest in another AIF (which is not a Fund of Fund))</li> </ul>
<b>Minimum corpus requirement</b>	<ul style="list-style-type: none"> <li>• USD 3 million (approx. INR 21 Crores)</li> </ul>
<b>Minimum investor contribution</b>	<ul style="list-style-type: none"> <li>• USD 150,000 per investor (approx. INR 1.06 Crores)</li> <li>• For employees/ directors of AIF or Manager – USD 40,000 per employee/director (approx. INR 0.28 Crores)</li> </ul>
<b>Sponsor / Manager Criteria</b>	<ul style="list-style-type: none"> <li>• Sponsor / Manager of existing AIF in India may act as Sponsor / Manager of AIF set-up in IFSC either by i) setting up branch or ii) incorporating a company or LLP in IFSC</li> <li>• Sponsor / Manager to be set-up in IFSC however, shall need to incorporate a company or LLP in IFSC</li> </ul>
<b>Minimum Sponsor / Manager commitment</b>	<ul style="list-style-type: none"> <li>• Cat I and II - Manager or Sponsor shall have a continuing interest of not less than 2.5% of the corpus or USD 750,000 (approx. INR 5.32 Crores), whichever is lower</li> <li>• Cat - III AIF, the continuing interest shall be not less than 5% of the corpus or USD 1.5 million (approx. INR 10.63 Crores), whichever is lower</li> </ul>
<b>Appointment of Custodian</b>	<ul style="list-style-type: none"> <li>• Cat I or Cat II – Sponsor / Manager to appoint Custodian if corpus exceeds USD 70 million (approx. INR 496 Crores)</li> <li>• Mandatory for Cat III irrespective of corpus</li> </ul>
<b>Angel Funds</b>	<ul style="list-style-type: none"> <li>• Minimum corpus – USD 750,000 (approx. INR 5.32 Crores)</li> <li>• Angel Investor – a) Individual investor with net tangible assets of at least USD 300,000 (approx. INR 2.13 Crores) b) body corporate – net worth of at least USD 15 million (approx. INR 106 Crores)</li> <li>• Minimum investor investment – USD 40,000 (approx. INR 28.35 Crores)</li> <li>• Minimum Sponsor / Manager commitment – 2.5% of corpus or USD 80,000 (approx. INR 0.57 Crores)</li> </ul>



	<ul style="list-style-type: none"><li>• Investment conditions –<ul style="list-style-type: none"><li>– Shall invest in VCU with turnover less than USD 3.75 million (approx. 26.6 Crores)</li><li>– VCU not promoted or sponsored by or related to an Industrial group whose group turnover exceeds USD 45 million (approx. INR 319 Crores)</li><li>– Investment in any VCU shall not be less than USD 45,000 (approx. INR 0.28 Crores) and not exceed 1 million (approx. INR 7 Crores)</li></ul></li></ul>
<b>Applicability of SEBI AIF Regulations</b>	<ul style="list-style-type: none"><li>• All provisions of AIF regulations including guidelines, circulars shall be applicable</li><li>• Provisions relating to Overseas Investment by AIF (circular dated 31 October 2015) shall not be applicable</li><li>• AIF reporting shall be denominated in USD million</li></ul>
<b>Fees for registration</b>	<ul style="list-style-type: none"><li>• Application fee – USD 1,500 (approx. INR 1.06 Lakhs)</li><li>• Registration fee<ul style="list-style-type: none"><li>– Cat I (other than Angel Funds) – USD 7,500 (approx. INR 5.32 Lakhs)</li><li>– Cat II – USD 15,000 (approx. INR 10.63 Lakhs)</li><li>– Cat III – USD 22,500 (approx. INR 15.95 Lakhs)</li><li>– Angel Funds – USD 3,000 (approx. INR 2.12 Lakhs)</li><li>– Scheme fee other than Angel Funds – USD 1,500 (approx. INR 1.06 Lakhs)</li><li>– Re-registration fee – USD 1,500 (approx. INR 1.06 Lakhs)</li></ul></li></ul>

An AIF, its Sponsor / Manager set up in IFSC should be regarded to be unit of the IFSC and hence eligible to the tax benefits accorded to such units under the Income-tax Act, 1961, such as:

- Tax holiday on income of the unit of IFSC from its business for which it has been approved:
  - 100% for first five years;
  - 50% for next five years;
- Reduced Minimum Alternative Tax, Alternate Minimum Tax rate of 9% (applicable only to income earned in foreign currency); and
- No dividend distribution tax on profits of IFSC unit (opaque company structure, largely ignored thus far, may need to be evaluated for IFSC AIFs).

Further, Goods and Services Tax also should not apply to management fee denominated in foreign exchange and earned by the Manager established in IFSC.



## **Dhruva comments**

Operating Guidelines provide much needed clarity vis-à-vis SEBI Regulations are concerned; however, further clarity is needed for AIFs in IFSC to become a reality. For instance, amendments in the Foreign Exchange Management Act, 1999 and the Regulations made thereunder would be required to clarify the following:

- Resident participation (both individual and institutional) in IFSC AIFs;
- Applicability of (a) sectoral caps for investment by an IFSC AIF such in retail or real estate; (b) end use conditions (such as in case of non-convertible debentures); (c) sectoral restrictions for investment as a Foreign Venture Capital Investor; etc.
- Resident ownership (both individual and institutional) of AIF sponsor / managers incorporated in IFSC.



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