

# ALTERNATIVE INVESTMENT FUND



## REGULATORY UPDATE

### SEBI NOTIFIES SPECIFIC DUE DILIGENCE REQUIREMENTS OF INVESTORS AND INVESTMENTS OF AIFs

Securities and Exchange Board of India (“SEBI”), *vide* SEBI (Alternative Investment Funds) (Second Amendment) Regulations, 2024 had inserted Regulation 20(20) in the SEBI (Alternative Investment Funds) Regulations, 2012, which requires every alternative investment fund (“AIF”), manager of the AIF and Key Management Personnel (“KMP”) of the manager and AIF to exercise specific due diligence, with respect to their investors and investments, to prevent facilitation of circumvention of various laws.

SEBI, *vide* its circular dated October 8, 2024 (“SEBI Circular”), has now specified specific due diligence to be carried out by AIFs, managers of AIFs and their KMP, to prevent facilitation of circumvention of regulatory frameworks as elaborated below:

- (a) [Investors availing benefits designated for qualified institutional buyers \(“QIBs”\) through AIFs](#): AIFs have been designated as QIBs under the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018 (“ICDR Regulations”). Further, certain benefits are provided to QIBs under the ICDR Regulations and other regulations. To prevent AIFs from facilitating investors who are ineligible for QIB status, from availing benefits designated for QIBs, necessary due diligence as per the implementation standards of Standard Setting Forum for AIFs (“SFA”), shall be carried out prior to availing benefits available to QIBs, for every scheme of AIFs having an investor or investors belonging to the same group who contribute(s) 50% or more to the corpus of the scheme.

The term ‘same group’ shall mean ‘related parties’ and ‘relatives’ as defined in SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

- (b) [Investors availing benefits designated for qualified buyers \(“QB”\) through AIFs](#): AIFs have been notified as QBs under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (“SARFAESI Act”), and are eligible to subscribe to security receipts (“SRs”) issued by asset

reconstruction companies (“ARCs”). To prevent AIFs from facilitating investors who are ineligible for QB status, from availing benefits available for QBs, necessary due diligence as per the implementation standards of SFA, shall be carried out prior to making any investments in SRs issued by ARCs or availing benefits designated for QBs under the SARFAESI Act, for every scheme of AIFs having an investor or investors belonging to the same group who contribute(s) 50% or more to the corpus of the scheme.

- (c) [Reserve Bank of India \(“RBI”\) regulated lenders/entities ever-greening their stressed loans/assets through AIFs:](#) To address the issue of ever-greening of stressed loans/assets by RBI regulated lenders/entities through AIFs and to prevent circumvention of norms specified by RBI relating to income recognition, asset classification, provisioning and restructuring of stressed loans/assets, necessary due diligence as per the implementation standards of SFA, shall be carried out for every scheme of AIFs:
- (i) whose manager or sponsor is an entity regulated by RBI; or
  - (ii) that has investor(s) regulated by RBI who: A. individually or along with investors of the same group contribute(s) 25% or more to the corpus of the scheme; or B. is an associate of the manager or sponsor of the AIF; or C. by itself, or through its representative(s)/nominee(s), has majority or veto power in voting over decisions of the investment committee set up by the manager.

Further, if an investor is an AIF or a fund set up outside India or in International Financial Services Centres (IFSC), then, the criteria check for investor(s) shall be carried out on a look through basis.

Furthermore, the manager shall ensure that the scheme does not make any investment that would lead to the RBI regulated lender/entity acquiring or holding interest/exposure in the investee company indirectly, which they are not allowed to acquire or hold directly.

If the proposed investments pertaining to schemes of AIFs falling under para (a), (b) and (c) do not satisfy the due diligence checks specified by SFA, then: either such investor or investors of same group shall be excluded from the investment, subject to necessary disclosures in the private placement memorandum for exclusion of investors or the investment shall not be made.

- (d) [Investment from countries sharing land border with India through AIFs:](#) In accordance with the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 read with Press Note 3 of the FDI Policy 2020, an investor of a country which shares land border with India or the beneficial owner of an investment into India who is situated in or is a citizen of any such country, shall invest in India only with the prior approval of the Government. To ascertain whether investors from countries sharing land borders with India are investing in Indian companies through AIF, necessary due diligence as per the implementation standards of SFA, shall be carried out prior to making any investment, for every scheme of AIFs where 50% or more of the corpus of the scheme is contributed by investors:

- (i) who are citizens of or are situated in a country which shares land border with India; or
- (ii) whose beneficial owner(s) as determined under the Prevention of Money Laundering (Maintenance of Records) Rules, 2005, are citizens of or are situated in a country which shares land border with India.

Post the due diligence, such scheme shall report details of its investment, which would lead to the scheme holding 10% or more equity or equity-linked securities, on a fully diluted basis, issued by an investee company, to its custodian within 30 days of the investment, in the format specified by SFA. Further, the custodians must compile the data on a monthly basis and report to SEBI within 10 working days from the end of the month.

## Due-diligence for existing investments

- (a) For schemes falling under the ambit of para (a), (b) and (c) above: Due diligence checks prescribed as per the implementation standards formulated by SFA must also be carried out for existing investments held by the scheme as on date of the SEBI Circular. Post the due diligence checks, if any existing investments of such schemes does not satisfy the due diligence checks, details of such investment shall be reported to the custodian in the format specified in the SEBI Circular. If all the existing investments satisfy the due diligence checks, manager of the AIF shall submit an undertaking to this effect to the custodian. The above-mentioned requirements shall be fulfilled on or before April 7, 2025.
- (b) For schemes falling under the ambit of para (d) above: Details of the existing investments where the scheme holds 10% or more equity or equity-linked securities, on a fully diluted basis, issued by an investee company, shall also be reported to the custodians, in the format as specified by SFA, on or before April 7, 2025.

## Other compliances:

The implementation standards formulated by SFA shall be adopted by AIFs, managers of AIFs and their KMP.

To read the SEBI Circular [click here](#)

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