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Sebi plans to set limits on fund life of AIFs: Regulator also mulls cap on large value funds

May propose fixing 30-year tenure for category I funds, 20 years for category II & 12 years for category III close-ended funds.

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The regulator may propose fixing a maximum tenure of 30 years for category I funds, 20 years for category II funds and 12 years for category III close-ended funds.

By Ashley Coutinho

The Securities and Exchange Board of India (Sebi) plans to define outer limits for the life of close-ended alternative investment funds (AIFs). The regulator is also in favour of putting a cap on the extensions that can be taken by large value funds (LVFs), which pool in money from accredited investors.

The regulator may propose fixing a maximum tenure of 30 years for category I funds, 20 years for category II funds and 12 years for category III close-ended funds, people in the know said. The fixed period will include fund extensions and may be applicable for LVFs too.

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“Today, it is theoretically possible to file an application for a fund with a tenure of 50 years, nothing in the regulations prevent you from doing that. Sebi wants to formally put in norms that cap the tenure for different categories of AIFs so that no one can manufacture a product that exceeds these periods,” an industry official said.

The average tenure of most AIFs at present is about 10 years with an option to extend them by up to two years, which is why market watchers believe that the proposed outer limits may not pose any challenge to most of the funds being launched in the country today.

The move may, however, impact foreign feeder funds raising money outside India and investing into captive AIFs. “Currently, these structures can enable longer tenure funds labelled as ‘evergreen’ funds. This is because at present no time period for a fund has been prescribed, and the tenure is as per the terms

agreed with the investors,” Parul Jain, head of fund formation at Nishith Desai Associates, said.

Jain added that the rules should make an exception for angel funds as their schemes are close-ended but the fund itself is not. “With the growth of the industry, the asset class dynamics are also changing considerably. In 2000s, most private equity funds were 7-8 years of tenure. It’s now moved to 12-13 years. Globally, permanent capital vehicles are becoming the norm,” Divaspati Singh, partner, Khaitan & Co, said.

Cap on LVFs

The regulator wants to prescribe a formula that caps extensions of LVFs to three years or 25% of the fund’s original tenure, whichever is lower.

Current AIF regulations permit close-ended AIFs to extend their tenure up to two years with the approval of two-third of its unit holders by value of their investment. LVFs, however, are permitted to extend their tenure beyond two years, subject to terms of the contribution agreement and other fund documents.

“This will curb the freedom that large value funds enjoy and will be tantamount to over-regulation,” an industry official said. “Theoretically, for a large value fund, unlimited extensions are possible. But even today it’s not that extensions are routinely given. The manager has to negotiate with investors on the circumstances that has led them to seek extensions. Restricting these may interfere with the flexibility that has otherwise been accorded to LVFs.”

An email sent to Sebi did not get a response.

“I can understand the regulator’s concerns for general AIFs, but LVFs by their very nature are raised from investors who are much more sophisticated and put in a minimum of `70 crore. Such restrictions may compel fund managers to set up structures overseas where there are no such limitations,” Singh said.

Fund extensions are particularly useful when market conditions are not favourable or when the underlying asset is not ready for sale.

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