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SEBI Protection measures for AIF Investors

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I. Introduction:

This article aims to delve into the regulatory framework established by the Securities and Exchange Board of India (SEBI) for safeguarding the interests of Alternative Investment Fund (AIF) investors. By scrutinizing SEBI's protection measures, we seek to understand their purpose, effectiveness, and limitations in the present context. In the realm of Alternative Investment Funds (AIFs), the Securities and Exchange Board of India (SEBI) plays a pivotal role in safeguarding investor interests. As the regulatory authority, SEBI implements measures to ensure transparency, fairness, and accountability within the AIF space.

To foster venture capital and private equity as a source of risk capital for entrepreneurs and innovation, the Government of India enacted the Securities and Exchange Board of India (Venture Capital Funds) Regulations, 1996 (VCF Regulations). Later, SEBI introduced a comprehensive legal framework in the form of SEBI (Alternative Investment Funds) Regulations, 2012 (AIF regulations), repealing and replacing the erstwhile SEBI (Venture Capital Funds) Regulations, 1996.

Alternative investment funds (AIFs) are defined in Regulation 2(1)(b) of SEBI (Alternative Investment Funds) Regulations, 2012. AIFs refer to privately pooled investment funds, which are not covered by any regulation of SEBI governing fund management, nor come under the direct regulation of other sectoral regulators in India. AIFs have been divided into three categories in the SEBI (Alternative Investment Funds) Regulations, 2012. AIFs include venture capital funds, private equity funds, debt funds, infrastructure funds, social venture funds amongst others. AIFs include funds which employ diverse or complex trading strategies in the secondary markets in the securities of listed companies. These latter funds account for less that 10% of the AIF investments made.

What are the Current Prohibitions on Category I and Category II AIFs?

SEBI's AIFs, under Regulation 16(1)(c) and Regulation 17(c) of the AIF regulation, impose an explicit bar on Category I and II AIFs against any form of direct or indirect borrowing. Category I AIFs invest majorly in

Startups, SMEs and projects which are socially and economically viable while Category II AIFs majorly invest in Equity and Debt securities of companies. As clarified through the consultation paper, the usage of the terminology “directly or indirectly” indicates a wide ambit, proscribing AIFs from involvement in any kind of leverage- not solely borrowings by the fund itself but also extending to asset encumbrance in the form of securities pledged to secure debt for portfolio companies. By deterring even indirect exposure to leverage, the intent is to insulate investor capital from potential erosion resulting from enforced transfers or disposal of equity assets held by the AIFs consequent to defaults on loans backed by securities belonging to the fund’s investee firms.

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India: Alternative Investment Funds by Category (As of September 2015)

Category	**Commitments Raised (Rs Crores)**	**Funds Raised (Rs Crores)**	**Investments Made (Rs Crores)**	**No. of AIF's**
Category 1				
Infrastructure Fund	6875.69	1970.25	1350.08	8
Social Venture Fund	600.52	259.52	216.52	3
Venture Capital Fund	1382.39	798.48	487.85	36
SME Fund	135.00	123.79	20.03	8
Category I Total	8993.60	3152.04	2074.61	55
Category II	14375.71	8079.29	6792.38	87
Category III	2162.79	1568.88	896.43	26
Grand Total	25532.10	12800.21	9763.42	167

What are the primary objectives of SEBI's protection measures for AIF investors, and why are they essential in the current landscape of alternative investments?

SEBI's protection measures are designed to mitigate risks, enhance transparency, and promote investor confidence within the AIF space. But what specific risks do these measures target, and how do they align with investor expectations and regulatory objectives?

Disclosure Requirements:

SEBI mandates extensive disclosure norms for AIFs, covering various aspects such as investment strategies, risk factors, and fee structures. How do these disclosures empower investors to make informed decisions, and what role do they play in reducing asymmetric information between fund managers and investors?

Eligibility Criteria for Fund Managers:

SEBI imposes stringent eligibility criteria for AIF fund managers, including minimum net worth requirements and track record criteria. What is the rationale behind these criteria, and how do they ensure the competency and integrity of fund managers entrusted with investor funds?

II. Conclusion:

The reason for the growth is majorly because AIF helps reduce instability usually related to traditional investments as their performances are not reliant on the ups and downs of a stock market. It also helps in diversification in terms of markets strategies and investment styles and strong potential in improving performance. Although, nonetheless, to say, Alternative investments funds are complex, and due diligence is needed before investing in them. There is a high investment amount required, which is impossible for small-scale investors. The SEBI has proactively reestablished its advisory committee on alternative investment policy to provide guidance on obstacles to the growth of the start-up ecosystem and the alternative investment industry. The AIF business is anticipated to expand rapidly and establish itself as a popular alternative investment choice provided the necessary steps are taken.