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Investments in Alternative Investment Funds (AIFs)

Dated:27th March 2024

Source-RBI/2023-24/140 DOR.STR.REC.85/21.04.048/2023-24.

Background of the Circular

Referring to RBI Circular **DOR.STR.REC.58/21.04.048/2023-24 dated December 19, 2023**, provides instructions aimed at resolving regulatory concerns regarding investment in **Alternative Investment Funds (AIFs) by regulated entities (REs).**

Brief of the Circular

With a view to ensuring uniformity in implementation among the REs, and to address the concerns flagged in various representations received from stakeholders, it is advised as under:

i. Downstream investments referred to in **paragraph 2 (i)** of the Circular shall exclude investments in equity shares of the debtor company **of the RE**, but shall include all other investments, including investment in hybrid instruments.

ii. Provisioning in terms of **paragraph 2(iii)** of the Circular shall be required only to the extent of investment by the RE in the AIF scheme which is further invested by the AIF in the debtor company, and not on the entire investment of the **RE in the AIF scheme.**

iii. **Paragraph 3 of the Circular** shall only be applicable in cases where the AIF does not have any downstream investment in a debtor company of the RE. If the RE has investment in subordinated units of an AIF scheme, which also has downstream exposure to the debtor company, then the RE shall be required to comply with **paragraph 2 of the Circular.**

iv. Further with regard to **paragraph 3 of the Circular:**
   - The proposed deduction from capital shall take place equally from **both Tier-1 and Tier-2 capital.**
   - Reference to investment in subordinated units of AIF Scheme includes all forms of subordinated exposures, including investment in the nature of sponsor units.

v. Investments by REs in AIFs through intermediaries such as **fund of funds or mutual funds are not included in the scope of the Circular.**

Impact

1. **Clarity in Investment Scope:** The circular provides clear guidelines on downstream investments, excluding equity shares of debtor companies, ensuring consistency in investment practices among regulated entities (REs).
2. **Reduced Financial Burden:** Targeting provisioning requirements only to the portion of REs' investments in AIF schemes further invested in debtor companies reduces financial burdens, aligning provisioning with actual risk exposure.
3. **Streamlined Regulatory Compliance:** The differentiation in applying provisions based on downstream investments ensures tailored regulatory measures, promoting effective risk management practices and regulatory compliance within the AIF sector.

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