Study Notes for
NISM-Series-XIX-A: Alternative Investment Funds (Category I and II) Distributors

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Examination Details

Multiple Choice Questions [80 questions of 1 mark each]	80*1 = 80
Case-based Questions [5 cases (each case with 4 questions of 1 mark each)]	5*4*1 = 20

Total marks	**100**
Duration	**2 hours**
Pass mark	**50**
Negative marking	10 percent of the marks assigned to a question.

WEIGHTAGE

Chapter No.	Chapter Name	Weightage (%)
Chapter 1	Overview of Alternative Investments	5
Chapter 2	Alternative Investment Funds in India	5
Chapter 3	Concepts in Alternative Investment Funds Industry	5
Chapter 4	Regulatory Framework – Indian Context	10
Chapter 5	Alternative Investment Fund Structuring	10
Chapter 6	Risk and Return – Investor and Fund Perspective	10
Chapter 7	Investment Process and Governance of Funds	10
Chapter 8	Fund Due Diligence – Investor Perspective	15
Chapter 9	Legal Documents and Negotiations – Investor Perspective	10
Chapter 10	Fund Monitoring, Reporting and Exit	5
Chapter 11	Valuation	5
Chapter 12	Taxation – India specific	5
Chapter 13	Good Practices	5

NISM-Series-XIX-A: Alternative Investment Funds (Category I and II) Distributors

CHAPTER 1: OVERVIEW OF ALTERNATIVE INVESTMENTS

Alternative Investments: Alternative investments are defined as assets not falling under conventional categories like stocks, bonds, and cash.

Risk Diversification: Alternative investments help diversify risk by moving beyond traditional asset classes.

Investment Strategies: AIFs employ diverse strategies like venture capital, private equity, and real estate investments.

Higher Risk: Alternative investments often involve higher risk compared to traditional investments due to their complexity.

Illiquidity: AIFs are typically less liquid, requiring longer holding periods.

Regulatory Framework: In India, AIFs operate under SEBI (Alternative Investment Funds) Regulations, 2012.

Venture Capital: Investments in startups with high growth potential but high risk of failure.

Private Equity: Investments in mature companies, often for control acquisitions or buyouts.

Real Estate: Investments in real estate involve direct property ownership or real estate-backed securities.

Infrastructure Funds: Focus on unlisted securities of infrastructure companies for long-term growth.

Hedge Funds: Use complex trading strategies and leverage, unlike Category I and II AIFs.

Returns Objective: Investors seek higher returns or early-mover advantages in new asset classes.

Portfolio Diversification: Alternative investments reduce portfolio correlation with traditional markets.

Global Trends: Increasing interest in alternative investments due to low yields in traditional markets.

Technological Disruption: Rapid technological changes increase uncertainty in alternative investments.

Market Volatility: Economic uncertainties impact investor sentiment in alternative investments.

ESG Considerations: Environmental, Social, and Governance factors influence alternative investment decisions.

Fund Structures: AIFs can be structured as trusts, LLPs, or companies in India.

Investor Base: High-net-worth individuals and institutional investors dominate AIF investments.

Performance Metrics: Returns are measured using metrics like IRR, DPI, RVPI, and TVPI.

Risk-Return Tradeoff: Higher potential returns come with increased risk in alternative investments.

Fund Tenure: AIFs, especially Category I and II, are typically close-ended with fixed tenures.

Regulatory Oversight: SEBI ensures investor protection through stringent AIF regulations.

Global PE Market: Private equity is a significant segment globally, with buyouts being prominent.

Early-Stage Investments: Venture capital focuses on early-stage startups with high growth potential.

Debt Investments: AIFs may invest in distressed debt or structured debt instruments.

Fund Managers: Play a critical role in identifying and managing alternative investment opportunities.

Investor Expectations: Investors expect superior returns adjusted for risk in AIFs.

Market Benchmarking: Performance is compared to benchmarks adjusted for risk differences.

Fund Governance: Strong governance ensures alignment with investor interests.

Tax Implications: Tax structures impact the attractiveness of alternative investments.

Liquidity Constraints: Limited exit options due to the illiquid nature of AIFs.

Investment Horizon: Long-term commitment is required, often 5-10 years.

Due Diligence: Rigorous due diligence is essential before investing in AIFs.

Portfolio Monitoring: Continuous monitoring is needed to manage risks effectively.

Exit Strategies: Exits via IPOs, buybacks, or secondary sales are common in AIFs.

Valuation Challenges: Valuing illiquid assets is complex and requires specialized methods.

Fund Performance: Performance varies based on fund strategy and market conditions.

Sector-Specific Risks: Investments in specific sectors carry unique risks.

Investor Education: Understanding AIF complexities is crucial for informed investing.

Regulatory Compliance: Adherence to SEBI guidelines ensures transparency.

Fund Documentation: PPM and trust deeds outline fund terms and conditions.

Risk Management: Strategies to mitigate risks like market and operational risks.

Global Economic Impact: Recessions and economic cycles affect AIF performance.

Investor Sentiment: Uncertainty in markets influences AIF investment decisions.

CHAPTER 2: ALTERNATIVE INVESTMENT FUNDS IN INDIA

AIF Definition: AIFs are privately pooled investment vehicles registered with SEBI under 2012 regulations.

Category I AIFs: Invest in startups, SMEs, and socially beneficial sectors like infrastructure.

Category II AIFs: Invest in debt or equity without leverage, not fitting Category I or III.

Category III AIFs: Use complex trading strategies and leverage, including hedge funds.

Venture Capital Funds: Category I AIFs focusing on early-stage startups.

Angel Funds: Sub-category of Category I AIFs for angel investments in startups.

Infrastructure Funds: Category I AIFs investing in unlisted infrastructure securities.

Social Venture Funds: Category I AIFs focusing on social impact investments.

SME Funds: Category I AIFs supporting small and medium enterprises.

Corporate Debt Market Fund: Close-ended AIF for corporate debt market development.

SEBI Regulations: Govern AIF operations, ensuring investor protection and transparency.

Fund Growth: AIF market in India grew to INR 10.66 lakh crore by March 31, 2025.

Investment Restrictions: Category I AIFs have specific investment conditions for startups and SMEs.

Tenure Extension: Existing VCF schemes can extend tenure up to 2 years with conditions.

Accredited Investors: Eligible investors with relaxed regulatory requirements.

Fund Corpus: Minimum corpus for an AIF scheme is INR 20 crore.

Investor Limits: Maximum 1,000 investors per scheme, except for angel funds.

Foreign Investment: Regulated under FEMA for cross-border investments.

Tax Pass-Through: Category I and II AIFs enjoy tax pass-through status for certain incomes.

Private Equity Growth: Indian PE industry has evolved into a robust AIF sector.

Fund Structuring: AIFs can be trusts, LLPs, or companies for operational flexibility.

Regulatory Updates: SEBI circulars refine AIF regulations periodically.

Investment Strategies: Vary based on fund category and objectives.

Market Evolution: Indian AIFs have grown since SEBI regulations in 2012.

Investor Profile: HNIs, family offices, and institutional investors dominate.

Fund Management: Requires skilled managers for effective investment decisions.

Risk Profile: Category I and II AIFs have lower risk than Category III.

Economic Impact: AIFs support economic growth through capital allocation.

Startup Financing: Government initiatives boost AIF investments in startups.

SEBI Oversight: Ensures compliance with investment and reporting norms.

Fund Registration: Mandatory with SEBI for legal operations.

Placement Memorandum: PPM outlines fund strategy and terms.

Custodian Requirement: Mandatory for Category I and II AIFs holding securities.

Transparency: SEBI mandates periodic disclosures to investors.

Market Status: AIFs have significant capital commitments across sectors.

Regulatory Flexibility: SEBI allows innovation in securities markets.

Fund Closure: Close-ended AIFs have fixed tenures with defined exits.

Investor Consent: Required for changes in fund terms or tenure.

Due Diligence: Mandatory for investments in unlisted securities.

Fund Performance: Measured against benchmarks for investor evaluation.

Tax Benefits: Pass-through status reduces tax liability for investors.

Sector Focus: Real estate and infrastructure are key AIF investment areas.

Global Integration: Indian AIFs align with global investment trends.

Compliance Test Reports: Ensure adherence to SEBI regulations.

Investor Protection: SEBI enforces measures to safeguard investor interests.

CHAPTER 3: CONCEPTS IN THE AIF INDUSTRY

Sponsor Commitment: Sponsors must invest a minimum amount to align interests.

Investment Manager: Responsible for managing AIF investments and operations.

Trustees: Required for trust-based AIFs to oversee fund governance.

Custodian Role: Ensures safekeeping and accurate reflection of fund securities.

Fund Structures: AIFs can be trusts, LLPs, or companies under SEBI regulations.

Drawdowns: Capital calls made as per investment needs of the fund.

Management Fees: Charged by investment managers for fund operations.

Carried Interest: Profit share paid to managers after hurdle rate is met.

Distribution Waterfall: Defines order of return distribution to investors and managers.

First Close: Initial capital commitment phase for launching an AIF.

Final Close: Last phase of capital commitment before fund closure.

Hurdle Rate: Minimum return threshold before carried interest is paid.

American Waterfall: Distributes carried interest earlier than European model.

European Waterfall: Returns capital and hurdle rate before carried interest.

Key Man Clause: Ensures critical personnel remain with the fund.

ESG Integration: Environmental, Social, and Governance factors in investment decisions.

Fund Governance: Ensures alignment of interests and regulatory compliance.

Investment Committee: Approves investment decisions for the AIF.

Valuation Policies: Define methods for valuing fund assets periodically.

Net Asset Value (NAV): Represents unit value disclosed periodically.

Co-Investment: Investors may co-invest alongside the AIF in opportunities.

Fund Expenses: Include operational costs chargeable to the fund.

Due Diligence: Critical for evaluating investee companies.

Portfolio Monitoring: Continuous oversight of investments for performance.

Risk Management: Strategies to mitigate investment and operational risks.

Fund Documentation: Includes PPM, trust deeds, and contribution agreements.

Investor Reporting: Periodic updates on fund performance and investments.

Regulatory Compliance: Adherence to SEBI and FEMA regulations.

Fund Lifecycle: Involves setup, investment, and exit phases.

Performance Metrics: DPI, RVPI, and TVPI measure fund performance.

Manager Expertise: Critical for identifying and executing investment opportunities.

Conflict of Interest: Policies to manage conflicts in fund operations.

Fund Strategy: Defines investment focus and risk appetite.

Investor Alignment: Ensures manager actions align with investor goals.

Capital Commitment: Investors commit capital to be drawn down as needed.

Fund Tenure: Close-ended funds have fixed investment periods.

Exit Strategies: Include IPOs, buybacks, or secondary sales.

Portfolio Diversification: Reduces risk through varied investments.

Regulatory Oversight: SEBI ensures transparency and compliance.

Fund Reporting: Includes financial and operational disclosures.

Valuation Challenges: Illiquid assets require specialized valuation methods.

Investment Process: Involves deal sourcing, due diligence, and execution.

Manager Compensation: Includes management fees and carried interest.

Fund Closure: Final close marks the end of capital raising.

Investor Rights: Include voting and information rights in fund agreements.

CHAPTER 4: AIF REGULATORY FRAMEWORK

SEBI Regulations: SEBI (AIF) Regulations, 2012 govern AIF operations in India.

Category I AIFs: Invest in startups, SMEs, and socially beneficial sectors.

Category II AIFs: Do not use leverage and invest in debt or equity.

Category III AIFs: Use leverage and complex trading strategies.

Minimum Corpus: INR 20 crore required for each AIF scheme.

Investor Limits: Maximum 1,000 investors per scheme, except angel funds.

Accredited Investors: Eligible for relaxed regulatory requirements with INR 70 crore investment.

Placement Memorandum: PPM is mandatory for outlining fund terms.

Custodian Requirement: Mandatory for Category I and II AIFs holding securities.

Investment Restrictions: Specific conditions apply to Category I AIFs.

Tenure Extension: VCF schemes can extend tenure up to 2 years.

Foreign Investment: Regulated under FEMA for cross-border transactions.

Co-Investment: Allowed for Category I and II AIF investors with conditions.

Compliance Test Reports: Ensure adherence to SEBI regulations.

Fund Governance: Involves trustees, investment committees, and managers.

Valuation Norms: SEBI mandates independent valuation for AIFs.

Investor Consent: Required for changes in fund terms or tenure.

Regulatory Updates: SEBI issues circulars to refine AIF regulations.

Fund Registration: Mandatory with SEBI for legal operations.

Transparency: SEBI mandates periodic disclosures to investors.

Tax Pass-Through: Category I and II AIFs enjoy pass-through status for certain incomes.

Conflict of Interest: Policies to manage and mitigate conflicts.

Due Diligence: Mandatory for investments in unlisted securities.

Fund Monitoring: Continuous oversight of investments and compliance.

Exit Strategies: Include IPOs, buybacks, or secondary sales.

FEMA Compliance: Governs foreign investments in AIFs.

Accreditation Agencies: Facilitate investor accreditation under SEBI guidelines.

KYC Requirements: Mandatory for investor onboarding and compliance.

Fund Reporting: Includes financial and operational disclosures.

Investment Committee: Approves all investment decisions.

Manager Responsibilities: Ensure compliance with SEBI regulations.

Sponsor Commitment: Minimum investment to align interests.

Fund Closure: Close-ended funds have fixed tenures with defined exits.

Regulatory Flexibility: SEBI allows innovation in securities markets.

Investor Protection: SEBI enforces measures to safeguard investor interests.

Portfolio Diversification: Reduces risk through varied investments.

Valuation Challenges: Illiquid assets require specialized valuation methods.

Fund Documentation: Includes PPM, trust deeds, and contribution agreements.

Risk Management: Strategies to mitigate investment and operational risks.

Fund Performance: Measured against benchmarks for investor evaluation.

Tax Implications: Impact the attractiveness of AIF investments.

Sector Focus: Real estate and infrastructure are key investment areas.

Global Integration: Indian AIFs align with global investment trends.

Fund Lifecycle: Involves setup, investment, and exit phases.

Investor Rights: Include voting and information rights in fund agreements.

CHAPTER 5: ALTERNATIVE INVESTMENT FUND STRUCTURING

Pooling Principle: AIFs pool investor capital for collective investment.

Trust Structure: Most common for domestic AIFs, registered under Indian Trusts Act.

LLP Structure: Offers flexibility and tax neutrality for AIFs.

Company Structure: Less common due to governance and compliance requirements.

Domestic AIF Structure: Involves Indian sponsors and investors in domestic companies.

Offshore AIF Structure: For foreign investors investing in Indian companies.

Parallel AIF Structure: Combines domestic and offshore structures for flexibility.

Unified AIF Structure: Integrates domestic and offshore investors in one fund.

Tax Neutrality: Structuring aims to minimize tax liability for investors.

Jurisdictional Selection: Based on anti-money laundering and tax treaty benefits.

FDI Compliance: Direct investments must adhere to FDI policy.

Fund Governance: Ensures alignment with investor interests.

Investor Rights: Defined in trust deeds or LLP agreements.

Contribution Agreements: Outline investor commitments and drawdowns.

SEBI Regulations: Govern AIF structuring and operations.

Sponsor Role: Provides initial capital and aligns interests.

Investment Manager: Manages fund operations and investments.

Custodian Role: Ensures safekeeping of fund securities.

Regulatory Compliance: Adherence to SEBI and FEMA regulations.

Fund Documentation: Includes PPM, trust deeds, and contribution agreements.

Risk Management: Strategies to mitigate structural and operational risks.

Valuation Policies: Define methods for valuing fund assets.

Investor Protection: SEBI enforces measures to safeguard interests.

Fund Tenure: Close-ended funds have fixed investment periods.

Exit Strategies: Include IPOs, buybacks, or secondary sales.

Due Diligence: Critical for evaluating investee companies.

Portfolio Monitoring: Continuous oversight of investments.

Fund Performance: Measured using DPI, RVPI, and TVPI metrics.

Tax Implications: Impact fund structuring decisions.

Co-Investment: Investors may co-invest alongside the AIF.

Fund Closure: Final close marks the end of capital raising.

Investor Consent: Required for changes in fund terms.

Transparency: SEBI mandates periodic disclosures to investors.

Conflict of Interest: Policies to manage and mitigate conflicts.

Fund Lifecycle: Involves setup, investment, and exit phases.

Valuation Challenges: Illiquid assets require specialized methods.

Regulatory Updates: SEBI issues circulars to refine structuring norms.

Investor Alignment: Ensures manager actions align with investor goals.

Portfolio Diversification: Reduces risk through varied investments.

Manager Compensation: Includes management fees and carried interest.

Fund Reporting: Includes financial and operational disclosures.

Investment Committee: Approves investment decisions.

ESG Integration: Influences fund structuring decisions.

Fund Expenses: Include operational costs chargeable to the fund.

Investor Education: Understanding fund structure is crucial for investors.

CHAPTER 6: RISK AND RETURN - FUND AND INVESTOR PERSPECTIVE

Risk Types: Include market, liquidity, operational, and sector-specific risks.

Return Metrics: DPI, RVPI, and TVPI measure fund performance.

Internal Rate of Return (IRR): Measures annualized return on investment.

Distribution Waterfall: Defines order of return distribution to investors and managers.

Hurdle Rate: Minimum return before carried interest is paid.

Management Fees: Charged for fund operations and management.

Carried Interest: Profit share paid to managers after hurdle rate.

J Curve: Represents initial negative returns followed by growth.

Liquidity Risk: AIFs are illiquid, impacting investor exits.

Market Risk: Economic cycles affect fund valuations.

Operational Risk: Arises from fund management and processes.

Sector Risk: Specific to the industry of investment.

Debt Financing Risks: Impact fund valuations and returns.

Valuation Challenges: Illiquid assets require specialized methods.

Fund Performance: Measured against benchmarks for evaluation.

Investor Expectations: Seek high returns adjusted for risk.

Due Diligence: Critical for assessing risk before investment.

Portfolio Monitoring: Continuous oversight to manage risks.

Exit Strategies: Include IPOs, buybacks, or secondary sales.

Fund Tenure: Close-ended funds have fixed investment periods.

Regulatory Compliance: Adherence to SEBI regulations mitigates risks.

Fund Governance: Ensures alignment with investor interests.

Risk Diversification: Achieved through varied investments.

Fund Documentation: Outlines risk factors and terms.

Investor Rights: Include information and voting rights.

Tax Implications: Impact net returns to investors.

Performance Metrics: DPI reflects distributed returns, RVPI reflects unrealized value.

Fund Lifecycle: Involves setup, investment, and exit phases.

Manager Expertise: Critical for managing risks and returns.

Conflict of Interest: Policies to mitigate manager-investor conflicts.

Fund Reporting: Includes financial and risk disclosures.

Valuation Policies: Define methods for valuing fund assets.

Investment Committee: Approves investment decisions to manage risks.

ESG Risks: Environmental, Social, and Governance factors impact returns.

Market Volatility: Affects fund performance and investor sentiment.

Capital Calls: Drawdowns impact investor liquidity.

Residual Value: Estimated value of unrealized assets.

Fund Closure: Final close marks the end of capital raising.

Investor Alignment: Ensures manager actions align with investor goals.

Transparency: SEBI mandates periodic risk disclosures.

Regulatory Oversight: SEBI ensures risk management compliance.

Fund Expenses: Impact net returns to investors.

Investment Process: Involves deal sourcing and risk assessment.

Co-Investment Risks: Additional risks for co-investing investors.

Economic Cycles: Influence risk and return profiles.

CHAPTER 7: INVESTMENT PROCESS AND GOVERNANCE OF FUNDS

Investment Process: Involves deal sourcing, due diligence, and execution.

Due Diligence: Includes business, financial, and legal reviews.

Investment Committee: Approves all investment decisions.

Fund Governance: Centered on trustees, managers, and investment committees.

Deal Flow: Managers develop pipelines for investment opportunities.

Term Sheet: Outlines preliminary investment terms and conditions.

Shareholders Agreement: Defines rights and obligations of investors.

Affirmative Rights: Include veto rights on key company decisions.

Ratchet Mechanism: Protects investors in down-round valuations.

Anti-Dilution: Protects investor equity from dilution in future rounds.

Tag-Along Rights: Allow investors to sell shares with promoters.

Drag-Along Rights: Enable majority shareholders to force a sale.

Pre-emption Rights: Give existing shareholders first right to new shares.

Information Rights: Provide investors with company financial data.

Board Representation: Investors may appoint board members.

Exit Strategies: Include IPOs, buybacks, or secondary sales.

Fund Monitoring: Continuous oversight of portfolio companies.

Valuation Policies: Define methods for valuing fund assets.

Regulatory Compliance: Adherence to SEBI regulations.

Conflict of Interest: Policies to manage and mitigate conflicts.

Fund Documentation: Includes PPM, trust deeds, and agreements.

Investor Protection: SEBI enforces measures to safeguard interests.

Portfolio Diversification: Reduces risk through varied investments.

Manager Expertise: Critical for effective investment decisions.

Fund Reporting: Includes financial and operational disclosures.

Compliance Test Reports: Ensure adherence to SEBI regulations.

Investment Strategy: Defines fund focus and risk appetite.

Due Diligence Review (DDR): Conducted by investment team or external experts.

Business DDR: Assesses industry and company potential.

Financial DDR: Evaluates financial health and projections.

Legal DDR: Reviews compliance and litigation risks.

Fund Tenure: Close-ended funds have fixed investment periods.

Investor Consent: Required for changes in fund terms.

Transparency: SEBI mandates periodic disclosures to investors.

Fund Closure: Final close marks the end of capital raising.

ESG Integration: Influences investment decisions and governance.

Fund Expenses: Include operational costs chargeable to the fund.

Investor Alignment: Ensures manager actions align with investor goals.

Performance Metrics: DPI, RVPI, and TVPI measure fund performance.

Risk Management: Strategies to mitigate investment risks.

Co-Investment: Investors may co-invest alongside the AIF.

Valuation Challenges: Illiquid assets require specialized methods.

Fund Lifecycle: Involves setup, investment, and exit phases.

Manager Compensation: Includes management fees and carried interest.

Regulatory Oversight: SEBI ensures transparency and compliance.

CHAPTER 8: FUND DUE DILIGENCE - INVESTOR PERSPECTIVE

Fund Due Diligence: Critical for assessing AIF suitability for investors.

Manager Evaluation: Assesses track record and expertise of fund managers.

Alignment of Interests: Ensures manager and investor goals are aligned.

Investment Strategy: Must match investor risk appetite and objectives.

Track Record: Evaluates past performance and consistency.

PPM Analysis: Reviews disclosures in Private Placement Memorandum.

Risk Assessment: Identifies fund-specific and market risks.

Fund Structure: Impacts risk, returns, and tax implications.

Manager Commitment: Sponsors and managers must invest in the fund.

Management Fees: Impact net returns to investors.

Carried Interest: Profit share paid to managers after hurdle rate.

Key Man Clause: Ensures critical personnel remain with the fund.

Fund Reporting: Includes financial and operational disclosures.

Regulatory Compliance: Adherence to SEBI regulations.

Investor Protection: SEBI enforces measures to safeguard interests.

Valuation Policies: Define methods for valuing fund assets.

Exit Strategies: Include IPOs, buybacks, or secondary sales.

Fund Tenure: Close-ended funds have fixed investment periods.

Due Diligence Questionnaire: Used to assess fund operations and risks.

ESG Integration: Influences fund selection and investment decisions.

Portfolio Diversification: Reduces risk through varied investments.

Conflict of Interest: Policies to manage and mitigate conflicts.

Fund Documentation: Includes PPM, trust deeds, and agreements.

Investor Consent: Required for changes in fund terms.

Transparency: SEBI mandates periodic disclosures to investors.

Fund Closure: Final close marks the end of capital raising.

Investment Committee: Approves investment decisions.

Manager Expertise: Critical for identifying investment opportunities.

Fund Performance: Measured using DPI, RVPI, and TVPI metrics.

Risk Management: Strategies to mitigate investment risks.

Co-Investment: Investors may co-invest alongside the AIF.

Fund Lifecycle: Involves setup, investment, and exit phases.

Investor Rights: Include information and voting rights.

Tax Implications: Impact net returns to investors.

Benchmarking: Performance compared to industry benchmarks.

Sales Strategy: Distributors tailor offerings to investor needs.

Fund Governance: Ensures alignment with investor interests.

Valuation Challenges: Illiquid assets require specialized methods.

Regulatory Oversight: SEBI ensures transparency and compliance.

Fund Expenses: Include operational costs chargeable to the fund.

Investor Education: Understanding fund complexities is crucial.

Performance Reporting: Must include INR and USD terms.

Due Diligence Process: Involves assessing fund strategy and risks.

Investor Suitability: AIFs are suitable for high-net-worth investors.

Reputation of Managers: Critical for investor confidence.

CHAPTER 9: LEGAL DOCUMENTATION AND NEGOTIATION - INVESTOR PERSPECTIVE

Private Placement Memorandum (PPM): Outlines fund terms, strategy, and risks.

Trust Deed: Defines legal structure for trust-based AIFs.

LLP Agreement: Governs LLP-based AIF operations and investor rights.

Subscription Agreement: Outlines investor commitments and terms.

Side Letters: Provide specific arrangements for individual investors.

Fund Governance: Ensures alignment with investor interests.

Regulatory Compliance: Adherence to SEBI regulations for documentation.

Investor Rights: Include information, voting, and exit rights.

Risk Disclosures: PPM must detail fund-specific and market risks.

PPM Audit: Mandatory to ensure compliance with terms.

Custodian Agreement: Governs safekeeping of fund securities.

Manager Agreement: Defines roles and compensation of fund managers.

Conflict of Interest: Policies to manage and mitigate conflicts.

Fund Tenure: Close-ended funds have fixed investment periods.

Exit Strategies: Include IPOs, buybacks, or secondary sales.

Investor Consent: Required for changes in PPM terms.

Transparency: SEBI mandates periodic disclosures to investors.

Fund Closure: Final close marks the end of capital raising.

Valuation Policies: Define methods for valuing fund assets.

Investment Committee: Approves investment decisions.

Manager Expertise: Critical for effective fund management.

Fund Performance: Measured using DPI, RVPI, and TVPI metrics.

Risk Management: Strategies to mitigate investment risks.

Co-Investment: Investors may co-invest alongside the AIF.

Fund Lifecycle: Involves setup, investment, and exit phases.

Tax Implications: Impact net returns to investors.

Due Diligence: Critical for assessing fund documentation.

Investor Protection: SEBI enforces measures to safeguard interests.

Fund Documentation: Must comply with SEBI regulations.

ESG Integration: Influences documentation and investment decisions.

Portfolio Diversification: Reduces risk through varied investments.

Fund Reporting: Includes financial and operational disclosures.

Valuation Challenges: Illiquid assets require specialized methods.

Regulatory Oversight: SEBI ensures transparency and compliance.

Fund Expenses: Include operational costs chargeable to the fund.

Investor Education: Understanding documentation is crucial.

Performance Reporting: Must include INR and USD terms.

Manager Compensation: Includes management fees and carried interest.

Fund Structure: Impacts legal and tax implications.

Investor Alignment: Ensures manager actions align with investor goals.

Due Diligence Process: Involves reviewing legal documents.

Benchmarking: Performance compared to industry benchmarks.

Reputation of Managers: Critical for investor confidence.

Sales Strategy: Distributors tailor offerings based on PPM.

Investor Charter: Outlines investor rights and grievance mechanisms.

CHAPTER 10: FUND MONITORING, REPORTING AND EXIT

Fund Monitoring: Continuous oversight of portfolio companies.

Periodic Reporting: Includes financial and operational disclosures.

Regulatory Compliance: Adherence to SEBI reporting requirements.

Investor Rights: Include access to performance and financial data.

Exit Strategies: Include IPOs, buybacks, or secondary sales.

Fund Tenure: Close-ended funds have fixed investment periods.

Valuation Policies: Define methods for valuing fund assets.

Conflict of Interest: Policies to manage and mitigate conflicts.

Fund Governance: Ensures alignment with investor interests.

Investment Committee: Approves investment decisions.

Manager Expertise: Critical for effective monitoring.

Fund Performance: Measured using DPI, RVPI, and TVPI metrics.

Risk Management: Strategies to mitigate investment risks.

Co-Investment: Investors may co-invest alongside the AIF.

Fund Lifecycle: Involves setup, investment, and exit phases.

Tax Implications: Impact net returns to investors.

Due Diligence: Critical for monitoring investments.

Investor Protection: SEBI enforces measures to safeguard interests.

Fund Documentation: Includes PPM and contribution agreements.

ESG Integration: Influences monitoring and reporting.

Portfolio Diversification: Reduces risk through varied investments.

Fund Reporting: Must comply with SEBI regulations.

Valuation Challenges: Illiquid assets require specialized methods.

Regulatory Oversight: SEBI ensures transparency and compliance.

Fund Expenses: Include operational costs chargeable to the fund.

Investor Education: Understanding reporting is crucial.

Performance Reporting: Must include INR and USD terms.

Manager Compensation: Includes management fees and carried interest.

Fund Structure: Impacts monitoring and exit strategies.

Investor Alignment: Ensures manager actions align with investor goals.

Due Diligence Process: Involves ongoing portfolio assessment.

Benchmarking: Performance compared to industry benchmarks.

Reputation of Managers: Critical for investor confidence.

Winding Up: AIFs must surrender registration upon closure.

Liquidation Scheme: For unliquidated investments post-tenure.

Secondary Sales: Transfer of investor units to new investors.

Put Options: Allow investors to sell back securities to promoters.

Portfolio Allocation: Snapshot of fund investments by company and sector.

Performance Metrics: DPI reflects distributed returns, RVPI reflects unrealized value.

Fund Closure: Final close marks the end of capital raising.

Investor Consent: Required for changes in fund terms.

Transparency: SEBI mandates periodic disclosures to investors.

Risk Disclosures: Must detail fund-specific and market risks.

Compliance Test Reports: Ensure adherence to SEBI regulations.

Investor Charter: Outlines reporting and grievance mechanisms.

CHAPTER 11: VALUATION

Valuation Basics: Critical for assessing AIF portfolio value.

Fair Value: Best measure for private equity as per IPEV Guidelines.

DCF Analysis: Discounts future cash flows to present value.

Relative Valuation: Uses earnings multiples for comparison.

Asset-Based Valuation: Based on net asset value or replacement cost.

NAV Computation: Represents fund's unit value periodically.

Independent Valuers: Required for unbiased valuation of AIF assets.

SEBI Regulations: Mandate valuation norms for transparency.

Valuation Challenges: Illiquid assets require specialized methods.

Fixed Income Valuation: Uses present value of coupon payments and maturity value.

Equity Valuation: Combines DCF, relative, and asset-based approaches.

Enterprise Value (EV): Market value of assets less liabilities.

Equity Value: Derived from EV after adjusting for debt.

Book Value: Net asset value from balance sheet data.

Replacement Cost: Cost to replace assets at current prices.

Break-Up Value: Liquidation value of company assets.

Weighted Average Cost of Capital (WACC): Used as discount rate in DCF.

Equity Beta: Measures stock volatility relative to market.

Terminal Value: Estimated value at end of forecast period.

Valuation Guidelines: IPEV provides global standards for AIF valuation.

Start-Up Valuation: Considers unique risks and growth potential.

Illiquidity Discount: Applied to reflect limited marketability.

Multiples Approach: Uses EBITDA or P/E multiples for valuation.

Regulatory Compliance: Adherence to SEBI valuation norms.

Fund Reporting: Includes valuation data for transparency.

Investor Protection: SEBI enforces valuation accuracy.

Fund Governance: Ensures proper valuation processes.

Risk Management: Valuation mitigates investment risks.

Investor Rights: Access to valuation data for decision-making.

Fund Tenure: Impacts valuation due to fixed investment periods.

Exit Strategies: Valuation influences IPOs or secondary sales.

Performance Metrics: NAV reflects fund's unrealized value.

Manager Expertise: Critical for accurate valuation.

Fund Documentation: Includes valuation policies and methods.

ESG Integration: Influences valuation considerations.

Portfolio Diversification: Affects valuation risk profile.

Fund Closure: Valuation critical at winding up.

Investor Consent: Required for changes in valuation policies.

Transparency: SEBI mandates periodic valuation disclosures.

Conflict of Interest: Policies to ensure unbiased valuation.

Fund Expenses: Include valuation-related costs.

Investor Education: Understanding valuation is crucial.

Benchmarking: Valuation compared to industry standards.

Regulatory Oversight: SEBI ensures valuation compliance.

Due Diligence: Involves assessing valuation methodologies.

CHAPTER 12: TAXATION - INDIA SPECIFIC

Tax Pass-Through: Category I and II AIFs have pass-through status for certain incomes.

Business Income: Taxed at fund level for AIFs.

Investment Income: Passed through to investors for taxation.

Withholding Tax: AIFs deduct tax under Section 194LBB of ITA.

Capital Gains: Taxed based on holding period and asset type.

DTAA Benefits: Double Taxation Avoidance Agreements reduce tax liability.

GST Applicability: Applies to management fees and fund expenses.

FATCA Compliance: Requires reporting of foreign investor accounts.

CRS Reporting: Common Reporting Standard for tax transparency.

Tax Neutrality: Structuring aims to minimize tax liability.

Non-Resident Taxation: Governed by ITA and DTAA provisions.

GAAR Provisions: General Anti-Avoidance Rules prevent tax evasion.

Securities Taxation: Treated as capital assets for AIFs.

Loss Carry Forward: Available to investors, not the fund.

Tax Certificates: Allow lower or nil withholding tax for non-residents.

Regulatory Compliance: Adherence to ITA and SEBI regulations.

Fund Documentation: Includes tax-related disclosures.

Investor Protection: SEBI ensures tax transparency.

Fund Governance: Ensures proper tax compliance.

Valuation Impact: Tax implications affect net asset value.

Fund Tenure: Impacts tax treatment of returns.

Exit Strategies: Tax considerations influence exit planning.

Investor Rights: Access to tax-related information.

Fund Reporting: Includes tax disclosures for transparency.

Manager Expertise: Critical for tax-efficient fund management.

Risk Management: Mitigates tax-related risks.

Fund Structure: Impacts tax liability and compliance.

Investor Consent: Required for changes in tax policies.

Transparency: SEBI mandates tax-related disclosures.

Conflict of Interest: Policies to manage tax-related conflicts.

Fund Expenses: Include tax compliance costs.

Investor Education: Understanding tax implications is crucial.

Benchmarking: Tax efficiency compared to industry standards.

Regulatory Oversight: SEBI and ITA ensure tax compliance.

Due Diligence: Involves assessing tax implications.

Portfolio Diversification: Affects tax risk profile.

Fund Closure: Tax considerations at winding up.

Co-Investment: Tax implications for co-investing investors.

Valuation Challenges: Tax impacts valuation of assets.

Performance Metrics: Tax affects net returns to investors.

Fund Lifecycle: Tax considerations throughout fund phases.

Investor Alignment: Ensures tax-efficient management.

ESG Integration: May influence tax considerations.

Cross-Border Investments: Governed by FEMA and DTAA.

Tax Audits: Ensure compliance with tax regulations.

Reputation of Managers: Critical for tax-efficient strategies.

CHAPTER 13: GOOD PRACTICES

Distributor Role: Facilitates investor onboarding and fund marketing.

Distributor Agreement: Outlines roles, fees, and responsibilities.

Investor Suitability: Distributors match AIFs to investor profiles.

Transparency: Distributors must provide clear fund information.

Regulatory Compliance: Adherence to SEBI regulations.

Conflict of Interest: Policies to manage and mitigate conflicts.

Investor Protection: SEBI enforces measures to safeguard interests.

Fund Documentation: Distributors explain PPM and agreements.

Risk Disclosures: Must highlight fund-specific and market risks.

ESG Integration: Influences distributor recommendations.

Fund Reporting: Distributors ensure investor access to reports.

Valuation Policies: Distributors explain valuation methods.

Fund Tenure: Distributors clarify fixed investment periods.

Exit Strategies: Distributors inform about IPOs and secondary sales.

Investor Education: Critical for informed investment decisions.

Manager Expertise: Distributors highlight manager track record.

Fund Performance: Explained using DPI, RVPI, and TVPI metrics.

Risk Management: Distributors emphasize risk mitigation.

Co-Investment: Distributors clarify co-investment opportunities.

Fund Lifecycle: Distributors explain setup, investment, and exit.

Tax Implications: Distributors inform about tax impacts.

Investor Consent: Required for changes in fund terms.

Fund Governance: Distributors highlight governance structures.

Due Diligence: Distributors conduct due diligence on funds.

Investor Rights: Include access to information and voting.

Fund Closure: Distributors explain winding-up process.

Performance Reporting: Must include INR and USD terms.

Manager Compensation: Distributors clarify fees and carried interest.

Fund Structure: Impacts risk, returns, and tax implications.

Investor Alignment: Distributors ensure manager-investor alignment.

Benchmarking: Distributors compare fund performance to benchmarks.

Regulatory Oversight: SEBI ensures distributor compliance.

Fund Expenses: Distributors explain costs chargeable to the fund.

Sales Strategy: Tailored to investor needs and risk appetite.

Reputation of Managers: Critical for distributor recommendations.

Confidentiality: Distributors must protect investor data.

Insider Trading: Prohibited under SEBI regulations.

Soft Dollar Arrangements: Distributors must avoid such practices.

Mis-Selling: Distributors prohibited from recommending unsuitable funds.

Investor Charter: Outlines rights and grievance mechanisms.

Data Privacy: Distributors must comply with data protection laws.

Client Engagement: Distributors maintain ongoing investor relationships.

Compliance Test Reports: Ensure adherence to SEBI regulations.

Ethical Practices: Distributors prioritize investor interests.

Grievance Redressal: Distributors address investor complaints promptly.

IMPORTANT NOTE :

1. Attend **ALL** Questions.
2. For the questions you don't know the right answer – Try to eliminate the wrong answers and take a guess on the remaining answers.
3. DO NOT MEMORISE the questions & answers. It's not the right to way to prepare for any NISM exam. Good understanding of Concepts is essential.

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All the Best ☺

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