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AIFs Nearing End of Lifecycle may get a 2-yr Breather

Synopsis
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The Securities and Exchange Board of India (Sebi) is considering a plan to allow Alternative Investment Funds (AIFs) to extend by two more years the lifecycle of investment products that are set to be wound up, said people with direct knowledge of the matter. The development assumes significance as several PE and venture capital funds that are in the last few months of their lifecycle are finding it challenging to offload unlisted investments with liquidity conditions tightening.

Under the current rules, a close-ended AIF can have a fund life of minimum three and maximum 10 years. However, this 10-year period can be further extended by two more years if the AIF obtains the consent of investors. Sebi is mulling an extension of another two years beyond this.

This implies a total fund life of 14 years. However, the Sebi move may come with caveats.

One of the key proposals being considered by Sebi is the introduction of higher investor consent thresholds for extending fund life—two-thirds support for the first two years of extension, three-fourths for the third and 90% for the fourth. "Keeping the liquidity conditions of unlisted markets in mind, Sebi plans to issue operating procedures for such extension," said one of the persons cited above. "Until now, Sebi has been giving extensions on a case-to-case basis but these new rules will allow all AIFs to benefit from the changes."

Sebi didn't respond to queries.

ET reported on August 11 that AIFs scheduled to wind up in the next few months have been struggling to sell their holdings in unlisted ventures and startups, as investors stay clear of risky investments.

The impact is largely on Category I and Category II AIFs, which typically invest in unlisted securities, apart from the debt market. Most of these AIFs are either not keen to sell their holdings or have been unable to find buyers at desired valuations because of liquidity-related challenges. Central banks across the world have trimmed balance sheets, adversely impacting fund flows into unlisted companies, especially tech-driven startups.

"If AIFs get two additional years to extend their tenure, giving them flexibility to extend the tenure in total up to four years, it will give some relief to many AIFs who are looking at winding up in 2022-23, but are unable to find appropriate exit opportunities due to unfavourable market conditions," said Nandini Pathak, head of fund practice, Nishith Desai Associates. "Hopefully, Sebi will also provide some relief around the liquidation period and creation of reserves."

AIFs have also sought Sebi's intervention on extending the liquidation period. Currently, once a fund completes its lifecycle, it is required to liquidate its holdings and distribute them among investors within one year. The industry has made representations to Sebi seeking extension of this period too by one more year, i.e. two years for liquidation in total.