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Limit close to being exhausted: Sebi asks RBI to raise overseas investment cap for AIFs

The overseas investment conundrum was discussed at a meeting of the AIPAC, headed by NR Narayana Murthy, a few days ago.

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By Ashley Coutinho

The Securities and Exchange Board of India (Sebi) has asked the Reserve Bank of India to increase limits for overseas investments that apply to alternative investment funds (AIFs), said two people in the know.

the past year to Rs 6.94 trillion, while the amount invested has increased 43% to Rs 3.11 trillion.

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The overseas investment conundrum was discussed at a meeting of the Alternative Investment Policy Advisory Committee (AIPAC), headed by NR Narayana Murthy, a few days ago. Sebi has subsequently written to the apex bank in this regard, asking for doubling of the current limits. An email sent to Sebi and the RBI did not receive an immediate reply.

“The issue regarding investment overseas by Indian AIFs has once again hit the wall with the outbound limits nearing exhaustion. The need for approaching Sebi each time for approval adds to the deal timelines, and is not always efficient. The overall limit of 25% of corpus of an AIF towards overseas investments also adds to restrictions,” said Parul Jain, co-head – international tax practice at Nishith Desai Associates.

The AIF industry, represented by bodies such as IVCA, has been batting for the limit to be linked to the amount raised by AIFs. Alternatively, it wants the limits to be automatically replenished or enhanced every time it is going to run out.

“With the rupee depreciating by more than 7% this year and forex reserves down by more than \$70 billion since September, nobody expects the RBI to do a reset right away. But, the hope is that something will be done in the next

Holding companies of several Indian tech firms, especially SaaS ones, are being set up outside India. This is because of the ease in capital availability and the ease of getting listed. But business operations of most of these companies are in India. AIFs that invest in these companies have to do so at the level of the holding company which is outside India.

“If the foreign limits are exhausted, then this entire segment gets impacted, giving an undue advantage to overseas funds. Besides, AIFs that have already invested in the first round can’t do a follow-up investment if limits are exhausted,” said Divaspati Singh, partner, Khaitan & Co.

Sebi takes around three months to review applications for these ODI investments. This puts Indian funds at a disadvantage as most of the investments are in startups, which do not have the luxury of waiting that long for an investment and can access ready capital from foreign funds, said Singh.

One of the other suggestions that was mooted during the AIPAC meeting was increasing the limits, specifically for foreign investors. “Even if the regulator cannot increase the limit for resident Indians, it could at least look at giving some leeway to funds that have foreign investors,” said a person familiar with the matter.

However, experts believe that giving separate limits for foreign investors does not make sense as it will be difficult to monitor and create disjointed assets.

“While investments from foreign investors into an AIF can be pooled into an overseas vehicle and invested outside India without any limits, nonetheless, the inability for Indian investors into an AIF to participate on a proportionate basis in such investments would result in different returns for these separate category of investors, which may not work commercially from a fund formation perspective,” said Jain.