

FAQs for AIFs in IFSC

1. What is International Financial Service Centre (IFSC)?

An IFSC is a special jurisdiction from where global financial service providers offer financial services / products to global customers in foreign currencies.

In India, the role of an IFSC is to undertake financial services transactions that are currently carried on outside India by overseas financial institutions and overseas branches / subsidiaries of Indian financial institutions.

Gujarat International Finance Tec-City (GIFT City) is India's only approved IFSC located in the city of Gandhinagar, Gujarat.

2. How is an IFSC regulated?

In India, an IFSC has to be approved by the Central Government under the Special Economic Zones (SEZ) Act, 2005 and is also governed by several Financial Services regulators such as Reserve Bank of India (RBI), Securities and Exchange Board of India (SEBI) and Insurance Regulatory and Development Authority (IRDAI)¹.

The IFSC Authority Act, 2019 was enacted in 2019, to provide for an establishment of IFSC Authority to develop and regulate the financial services market in IFSC in India, which will replace the Financial Services regulators - SEBI, RBI and IRDAI. Recently, on 1 October 2020, the IFSC Authority assumed the powers over SEBI, RBI and IRDAI to develop and regulate the IFSC jurisdiction.

3. Who are the participants in an IFSC?

The participants in an IFSC are as follows:

Capital Markets	Offshore Banking	Offshore Insurance	Offshore Asset Management	Ancillary Services
<ul style="list-style-type: none"> • Stock Exchanges • Brokerage services • Permissible Securities 	<ul style="list-style-type: none"> • Corporate Banking • Servicing JV/WOS of Indian companies registered abroad • Factoring / Forfeiting of export receivables 	<ul style="list-style-type: none"> • General / Life Insurance • Co-Insurance • Reinsurance • Captive Insurance etc. 	<ul style="list-style-type: none"> • Fund Accounting • Investment services • Custodial services • Trust services etc. 	<ul style="list-style-type: none"> • Legal, Accounting & Audit • Research & Analytics etc. • Compliance, Recruitment • Risk Management etc.

4. What is the key difference between an IFSC unit and a domestic unit?

A unit set up in IFSC is treated as a “person resident outside India” (i.e. non-resident) for exchange control purposes whereas a domestic unit is treated as a “person resident in India”. Hence, an IFSC unit enjoys the privileges of a non-resident under exchange control provisions.

¹ IFSC Authority Act, 2019 empowers Central Government to establish IFSC Authority which shall replace all the FS regulators

5. What does the IFSC mean to the global fund managers?

Global fund managers managing offshore funds, traditionally operate from offshore financial centres such as Singapore, Hong Kong, London, Ireland, etc., for making investments into Indian assets.

They have now started recognizing IFSC regime to make investments in India. IFSC has contributed to the growth of the entire Fund Management eco-system (Make in India for Fund Managers) including custodians, fund accountants, etc. in India.

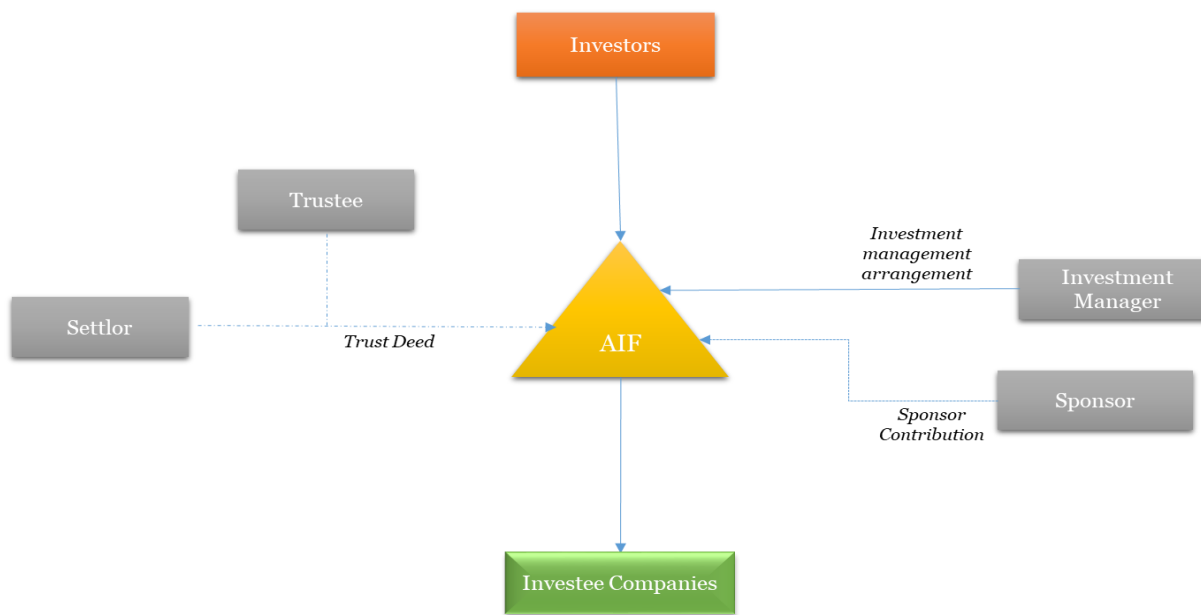
6. How are the funds regulated in IFSC?

In 2015, the SEBI issued guidelines to facilitate and regulate the securities market in IFSC at GIFT City including the fund framework in IFSC. On 26 November 2018, the SEBI issued Operating guidelines for Alternative Investment Funds (AIF) in IFSC (Operating guidelines) which provide a framework for setting up AIFs in IFSC and a major boost to Indian fund industry.

7. How does an AIF operate?

An AIF is an investment vehicle, set up in India, which privately pools funds / monies from domestic as well foreign investors and invests such funds / monies in securities as per a defined investment policy. In India, an AIF, along with its constituents, is regulated by the SEBI under the SEBI (AIF) Regulations, 2012 (SEBI AIF Regulations).

8. Operational structure of an AIF:



9. How can an AIF be set up in IFSC?

An AIF can be set up in the form of a trust, company, LLP or body corporate in the IFSC.

10. What are the different categories of AIFs permitted to be set up in IFSC?

SEBI IFSC guidelines read along with the SEBI AIF regulations recognises the following types of AIFs:

- (a) Category I AIF: Funds which invest in start-ups, early stage ventures, social ventures, small and medium enterprises, infrastructure sector or areas which Govt consider as desirable.
- (b) Category II AIF: Residual category i.e. other than Category I and III AIF and do not undertake leverage other than to meet day-to-day operational requirements as per SEBI AIF Regulations.
- (c) Category III AIF: Funds which employ diverse or complex trading strategies and leverage including through investment in listed or unlisted securities / derivatives.

11. Who is a Sponsor of an AIF?

A Sponsor is a person who sets up an AIF (i.e. moots the idea of an AIF).

12. Who is a Manager of an AIF?

A Manager is a person who manages investments of the AIF in return for a management service fees. In many cases, the Manager entity also acts as the Sponsor entity for an AIF.

13. How can a Sponsor and/or Manager be set up in IFSC?

A first time Sponsor and/or Manager can be setup only as a company or limited liability partnership (LLP) in IFSC. However, if the person is already an existing Sponsor and/ or Manager to an AIF, such Sponsor and/or Manager is also permitted to set up a branch in IFSC.

14. What are the obligations of a Sponsor and / or Manager with respect to the AIF in IFSC?

The Manager or Sponsor is required to maintain a continuing investment interest in the AIF as follows:

- For Category I and II AIF: Lower of:
 - 2.5% of corpus
 - USD 750,000
- For Category III AIF: Lower of:
 - 5% of corpus
 - USD 1,500,000

However, any waiver of management fees will not be considered for the above purposes.

15. Who is permitted to invest in an AIF set up in IFSC?

Permissible investors in an AIF are as follows:

- (a) a person resident outside India;
- (b) a non-resident Indian;
- (c) institutional investor resident in India eligible under exchange regulations to invest funds offshore - to the extent of outward investment permitted;
- (d) person resident in India (having minimum net worth of USD 1 million during preceding financial year) eligible under FEMA to invest funds offshore - to the extent allowed in Liberalized Remittance Scheme (LRS).

16. Can AIF in IFSC raise money in any foreign currency?

Yes, an AIF in IFSC can raise money in any foreign currency.

17. What is the minimum investment size for an investor in an AIF?

The minimum investment by an investor in an AIF is as follows:

- (a) For employees or directors of the AIF or its manager - USD 40,000;
- (b) For other investors - USD 150,000

18. Where can the AIF deploy/invest its funds?

An AIF is permitted to invest in:

- (a) Securities listed in IFSC;
- (b) Securities issued by companies incorporated in IFSC;
- (c) Securities issued by companies incorporated in India or foreign jurisdiction
- (d) Units of an AIF
- (e) Securities which a domestic AIF is permitted to invest in.

19. Can an AIF in IFSC invest in listed securities in India?

Yes. An AIF in IFSC can invest in listed securities in India under the Foreign Portfolio Investor (FPI) route. For this purpose, the AIF should also obtain an FPI license from SEBI under the SEBI (FPI) regulations, - 2019.

20. What are the investment routes available to an AIF investing in India?

AIFs in IFSC are permitted to invest in India under the following routes:

- (a) Foreign portfolio investment (FPI) – AIF has to obtain FPI license under SEBI (FPI) regulations, 2019; or

- (b) Foreign venture capital investment (FVCI) - AIF has to obtain FVCI license under SEBI (FVCI) regulations, 2000; or
- (c) Foreign direct investment (FDI).

21. Are there any limits for investment into India or outside India by an AIF in IFSC?

An AIF in IFSC can invest subject to the following limits:

- (a) For investment in India – FPI/ FVCI/ FDI limits to apply; and
- (b) For investment outside India – No limits for investment made outside India.

Overall limits specified under SEBI AIF Regulations and Operating guidelines need to be factored in.

22. What are the key benefits for an AIF in IFSC?

The key benefits for an AIF in IFSC are as follows:

- (a) Various tax and regulatory incentives and exemptions granted
- (b) Lower operating costs due to subsidies granted by the Gujarat Government
- (c) Availability of skilled labour
- (d) Proximity to the onshore market
- (e) World class infrastructure, unparalleled connectivity and transportation access.

23. What is the tax framework for AIFs in IFSC?

The tax framework for an AIF in IFSC is as follows:

- Category I & II AIF:
 - Category I and II AIFs are considered to be tax pass through entity for Indian income-tax purposes, except for business income which is taxed at the AIF level.
 - Income accruing or arising or received by non-resident investors from offshore investments through a Category I and II AIF is not taxable in India
 - Exemption has been provided to non-resident investors from obtaining a PAN card and filing return of income in India, provided they earn income only from investments made in a Category I or Category II AIFs in IFSC and tax has been deducted on the distribution made by such AIFs to non-resident investors. The AIF is required to electronically file, on a quarterly basis, details collected from its non-resident investors to the relevant tax authorities in the prescribed form.
- Category III AIF²:
 - Category III AIFs are subject to fund level taxation.

² subject to the condition that all units of Category III AIF are held by non-residents other than units held by its Sponsor / Manager.

- The following income earned by the Category III AIF, which is attributable to non-resident investors in the AIF, is exempt from tax:
 - Income on transfer of any securities (other than shares in a company resident in India), including derivatives, debt securities and offshore securities.
 - Income from securities issued by a non-resident (not being a Permanent Establishment) and where such income otherwise does not accrue or arise in India
 - Income from a securitisation trust chargeable under the head “profits and gains of business or profession
 - Income on transfer of specified securities³ listed on a recognised stock exchange located in IFSC where consideration for such transaction is in convertible foreign exchange
- Income on transfer of shares in an Indian company is taxable as follows to the Category III AIF:
 - Short-term Capital Gains - 15% if Securities Transaction Tax paid, else 30%;
 - Long-term Capital Gains - 10%
- Income in respect of securities (such as interest, dividend) is taxable to the Category III AIF at the rate of 10% (5% in case of interest income on certain rupee denominated bonds, Government securities or municipal debt securities referred to in section 194LD)
- Any income accruing or arising to or received from the Category III AIF or on transfer of its units is exempt from tax in the hands of investors.
- Surcharge on certain Long-term Capital Gains, Short-term Capital Gains and dividends earned by the Category III AIF is capped at 15%. Further, the provisions of Alternate Minimum Tax are not applicable to the Category III AIF.

24. What are the approvals required for setting up an AIF in IFSC?

Approvals required to be obtained for setting up an AIF in IFSC are as follows:

- (a) Approval from SEZ authorities
- (b) Approval from SEBI / IFSC Authority

25. To whom the application for setting up an AIF in IFSC be made?

Application for setting up an AIF in IFSC should be made in:

- (a) Form F to Development Commissioner, Kandla SEZ for SEZ approval.
- (b) Form A to the Deputy General Manager, Division of Funds-1, Investment Management Department, SEBI / IFSC Authority for SEBI/ IFSC Authority approval.

26. What are the steps for setting up an AIF in IFSC?

The key steps for setting up an AIF in IFSC are as follows:

- (a) Identification of office space in GIFT City and obtaining NOC from GIFT SEZ.

³ bonds, GDRs, rupee denominated bonds of Indian company, derivatives, foreign currency denominated bond, unit of mutual fund, unit of business trust, foreign currency denominated equity share of a company, units of AIF and other securities (to be notified by central government)

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- (b) Apply for incorporation of the entities.
 - (c) Application to SEZ authorities and obtain letter of approval.
 - (d) Obtain SEBI/ IFSC Authority approval.
 - (e) On obtaining approvals from SEZ authorities and SEBI/ IFSC Authority, GIFT SEZ to issue Final Letter of Allotment for allocation of space.
 - (f) Execute lease deed / leave and license with the Developer for the allotted space.

For any further queries relating to AIF in IFSC:

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