

Business Standard

AIF trustees seek more powers to fulfil their obligations amid Sebi probe

They complain about delayed or no disclosure from investment managers

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The Securities and Exchange Board of India's (Sebi's) investigation into alleged circumvention of regulations in alternative investment funds (AIFs) has put trustees in a spot of bother. Many are now seeking more rights to fulfil their obligations, which include overseeing the conduct of AIFs and safeguarding the interests of unitholders.

Trustees are also tasked with compliance-related work for AIFs, besides conducting KYC checks on investors, obtaining beneficial ownership details from offshore investors, and disseminating information to investors. However, many trustees report that they do not receive timely disclosures or at times, no disclosure from investment managers.

“We don't have any defined rights as trustees,” said a trustee who manages dozens of AIFs. “We're seeking more rights from the market regulator so we can obtain the necessary information from AIFs to ensure proper compliance by funds.”

In case of any red flag or suspected violation, trustees can report issues to the Financial Intelligence Unit (FIU) on its portal. However, trustees said they first need to obtain information from the managers — a process that often leads to a dead end.

“Many managers withhold information due to confidentiality agreements,” said another trustee. “They only share information after an investment is made, which is often too late. It then becomes difficult for us to dig up information even when we want to.”

Some trustees have expressed concern that without a clear demarcation of rights, they lack protection when it comes to circumvention or malpractices found within the AIF space and are unable to conduct due diligence based on the disclosed information.

According to a Sebi official, several entities have been found circumventing norms to invest in entities and assets through AIFs where they would otherwise be prohibited due to shareholding caps or legal issues.

Trustees have pointed out challenges in conducting detailed due diligence where complex family offices or trust structures are involved. Some AIFs even consist of only two or three participating entities and are formed with a specific objective.

“There should be demarcation on who would be held responsible for what part — the trustee or the manager. Only a manager should be held accountable for due diligence related to investments, while trustees should be held responsible for compliance related issues. There is no demarcation right now, and if something goes wrong, trustees would definitely be made a party to the show-cause,” a trustee said.

According to legal experts, while the rules may be well laid down in theory, they don't always play out smoothly in practice.

“Trustees are the legal owners of the AIF and cannot be excluded from any legal notice or show cause. A trustee typically retains the right to seek information and copy documents. However, investment managers may withhold information due to confidentiality. There have been specific clarifications from Sebi periodically on the fiduciary duties of trustees,” said Nandini Pathak, Partner, Nishith Desai Associates.

If an investment manager fails to perform their duties adequately, the trustee has the power to seek information, write to the contributors or investors, or even resign.

Earlier this year, Sebi directed trustees of Vistaar Capital Advisors to wind up the fund within six months due to alleged violations. The matter is now before the Securities Appellate Tribunal (SAT).

“Managers have the obligation to stick to the private placement memorandum and fund documents for decisions of the AIF as per the regulations. In case of any issue, trustees should be able to demonstrate that they made adequate efforts to seek information from the manager and ensure compliance,” added Pathak.

In a spot

Sebi has found several instances of circumvention of regulations by entities through AIFs

Trustees are legal owners of an AIF, responsible for regulatory compliance

Trustees want right to seek more information from investment managers

They flag delayed disclosures or no information after investment decisions

Trustees point out challenges in doing due diligence

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