AIF Vs. PMS

SEBI's circular dated 10th February 2012 modified the SEBI (Portfolio managers) Regulations 1993 ("**PM Regulations**") to disallow pooling of investor funds. This was a fundamental change brought about in the PM regulations which paved the way for SEBI (Alternative Investment Funds) Regulations 2012 ("**AIF Regulations**"). In this article we attempt to highlight a few salient differences between PM Regulations and AIF Regulations.

Given below are a few key points of differences between an AIF regime and the PMS regime:

Parameters	AIF	PMS
Categories	AIF may be categorized as Category I AIF, Category II AIF and Category III AIF based on the investment objective of fund.	Portfolio manager may provide discretionary of Non-discretionary portfolio management services to its client
Pooling of funds	Pooling of funds	No pooling of funds
Segregation of funds	No segregation required	Segregation of each client's holdings and separate demat accounts to be created for each client to demonstrate no pooling of assets.
Minimum Investment by an Investor	Rupees One Crore	Rupees 25 Lakhs
Minimum Corpus	Each scheme shall have a corpus of Rupees 20 crores	Not applicable
Managers Contribution	Managers continuing interest in the Category I & II AIF- not less than 2.5% or INR 50 million whichever is lower, Category III- 5% or INR 100 million whichever is lower.	Not applicable
Number of Investors	Each scheme of an AIF shall not have more than 1000 investors	No such threshold

In addition to the above key differences, set out below are some of the other distinguishing factors between AIF regime and PMS regime:

- Investment guidelines: The investment guidelines prescribed by SEBI in respect of Portfolio Managers are more liberal than those prescribed under the AIF Regulations. Portfolio managers are largely permitted to make investments in any instruments or in any manner as agreed between the portfolio manager and its client in terms of their agreement thereby giving the portfolio manager considerable latitude to determine the types of investments subject however to a few restrictions such as: PMS funds are not permitted to be deployed in bill discounting , badla financing or lending or in placements with corporate or non-corporate bodies and no investments can be made in speculative transactions. The AIF Regulations on the other hand, provide for general and specific investment guidelines in respect of each category of AIF. Some of the investment guidelines under the AIF Regulations inter alia include: (i) Category I and II AIF shall invest not more than 20% of its corpus in one investee company; (ii) Category III AIF shall invest not more than 10% of the corpus in one investee company. Apart from these, the AIF Regulations stipulate stringent specific investment conditions for each category of AIF.

- Co-Investment by manager: Under the AIF regime, the Manager or Sponsor (as defined under the AIF Regulations) is permitted to co-invest in Investee companies but not on terms more favorable than those offered to the AIF. However, under the PMS regime even though there is no express prohibition on the portfolio manager from investing in investee companies, the PM Regulations require the portfolio manager to segregate each client's funds and portfolio of securities and keep them separate from its own funds and securities and be responsible for safekeeping of clients' funds and securities.

- Listing: Units of close ended AIFs may be listed on stock exchange subject to a minimum tradable lot of INR 1 Cr after final close of the fund or scheme. Since no instrument of the portfolio manager is issued to the Investor, listing is not possible.

- Lock-in-period: Under the PMS regime, an investor can withdraw funds at any time during the term of the agreement, at his or her discretion in the manner provided in the agreement. In case of AIF regime, the contribution/subscription agreement may have lock-in periods specified in respect of Close ended funds.

- Administration and process cost: The Fund's administration of assets under the AIF regime may not be as cumbersome as under the PMS regime as under the PM Regulations, the Portfolio Manager is required to identify and keep separately assets of each investor.

- Tenure: Category I and II AIF fund or schemes shall have a minimum tenure of (3) years which may be extended for a maximum of two years in the manner as set forth under the AIF regulations. In contrast, there is no specified term under the PMS regime. It is governed by the terms of the portfolio management agreement executed between the client and the Portfolio manager.

- Winding up/termination: AIF shall be wound up
    - in case of Trust (i) expiry of tenure, (ii)75% of the investors in value decide to wind up the AIF (iii)directed by SEBI, (iv) in the opinion of trustee the AIF shall be wound up
    - In case of LLP, in accordance with the Limited Partnership Act 2008 on (i) expiry of tenure, (ii)75% of the investors in value decide to wind up the AIF (iii)directed by SEBI
    - In case of Company, in accordance with the Companies Act 1956

  However, the Portfolio Managerial services are governed by the agreement between the client and the portfolio manager and are liable to be terminated in terms of the agreement.

Conclusion

The primary objective of SEBI while introducing the AIF Regulations was to create a structure where regulatory framework is available for all types of private pooling of capital or investment vehicles so that such funds are channelized in the desired space in a regulated manner without posing systemic risk. The modifications to PM Regulations intend to ensure that no pooling of assets is undertaken by the portfolio managers. However, for all practical purposes portfolio management products offered to investors function as pooled vehicles. With the notification of the AIF Regulations, ideally all such pooling vehicles should migrate to the new structure.