



**Consultation paper on dematerialisation of units of AIFs**

**1. Objective:**

To seek comments and inputs from stakeholders and members of public on mandating dematerialisation of units of Alternative Investment Funds (AIFs).

**2. Background:**

- 2.1. As per SEBI (Alternative Investment Funds) Regulations, 2012 ('AIF Regulations'), AIFs/schemes of AIFs may raise funds from any investor by way of issuance of units which represents beneficial interest of the investors in the scheme. The units may be fully or partly paid up.
- 2.2. Units issued by AIFs are 'securities' as defined under Securities Contracts (Regulation) Act, 1956. Accordingly, depositories Central Depository Services (India) Limited (CDSL) and National Securities Depository Limited (NSDL), have laid down procedures for dematerialisation of units of AIFs.
- 2.3. However, it is observed that units of most of the AIFs are not dematerialised and are held in physical form. As on December 31, 2022, there are 1022 AIFs registered with SEBI. As per the information collected from depositories, it is observed that only 12 ISINs have been created with CDSL for 5 schemes of AIFs as on October 03, 2022 and 87 ISINs have been created with NSDL for 29 schemes of AIFs as on December 20, 2022. It is understood from the discussion with depositories that the aforesaid schemes of AIFs have dematerialised their units upon demand/request from their investors.

**3. Issues for Consideration:**

- 3.1. Presently, AIFs appear to prefer issuing their units in physical form, considering the following:
  - (i) Limited number of investors in their schemes;
  - (ii) AIFs raise funds through private placement by issue of placement memorandum;
  - (iii) AIF units are hardly traded and even if they are traded, these are private transactions;
  - (iv) Issuance of classes/sub-classes of units with differential rights (commercial or otherwise) to different investors;
  - (v) Managers of AIFs prefer to retain control/discretion with respect to transfer of units of AIFs by investors;
  - (vi) Cost and procedural compliances associated with dematerialisation; and
  - (vii) Lack of demand for dematerialised units from investors of AIFs etc.



3.2. Irrespective of the reasons highlighted above, it is evident that issuing and holding units of AIFs in dematerialised form brings numerous benefits to all stakeholders, including managers, investors and regulators, such as:

- (i) Ease of monitoring for investors (enables depositories to issue Consolidated Account Statement which would include details of investment in AIFs);
- (ii) Ease of administration and monitoring for managers, for regulatory compliances;
- (iii) Ease of transfer and transmission of AIF units; and
- (iv) Safer option to hold securities - reduces risk of loss/damage of certificate, forgery etc.

Dematerialization of units of AIFs is a step towards digitalization of all types of financial securities and is envisaged to facilitate transparency and adequate monitoring.

3.3. While there is a cost associated with dematerialisation of units (to AIF) and holding the units in demat form (to investors), the same may not act as a barrier for investors, as AIF investors are sophisticated investors with adequate infrastructure.

3.4. It is pertinent to mention that AIF Regulations enables listing of units of close ended schemes of AIFs and therefore, dematerialisation of units of AIFs lays down the basic infrastructure for framework for listing of units, going forward.

3.5. The aforesaid issue was deliberated in meeting of Alternative Investment Policy Advisory Committee (AIPAC) held on October 11, 2022. While the Committee in principle agreed with proposal to mandate AIFs to issue units in dematerialised form, it also recommended to take into consideration the following concerns with respect to the proposal:

- (i) Administrative hassle/ burden for foreign investors to open demat account,
- (ii) Transferability of AIF units without the knowledge/control of the managers of AIFs and
- (iii) Demat requirement affecting ease of doing business for small fund managers and Angel Funds.

3.6. Subsequently, in meeting held on January 20, 2023, AIPAC after deliberating on the concerns highlighted above, recommended the following proposals:

- (i) Dematerialisation of units to be mandated for AIFs with corpus above INR 500 Crore.
- (ii) Foreign investors to also open demat account.
- (iii) A time period of 1 year may be provided for dematerialisation of existing AIF units from the date of mandate.

Both depositories (CDSL and NSDL) were represented at this AIPAC meeting.



#### 4. Proposal:

Taking into account the recommendations of AIPAC and based on internal deliberations, the following is proposed:

- 4.1. Dematerialisation of units of AIFs shall be made mandatory.
- 4.2. As part of first phase of this mandate, by April 01, 2024, all schemes of AIFs with corpus more than INR 500 crores shall compulsorily dematerialise their units.
- 4.3. The terms of transfer of units of AIFs held by an investor shall continue to be governed by the terms of private placement memorandum (PPM), agreements made with investor and other fund documents.

#### 5. Public Comments:

- 5.1. Public comments are invited for the proposal given above. The comments / suggestions may be provided as MS Excel file as per the format given below:

Name of the person/ entity proposing comments:	
Name of the organization (if applicable):	
Contact details:	
Category: whether market intermediary/ participant (mention type/ category) or public (investor, investee company, academician etc.)	

Sr. No.	Para. no. of the consultation paper	Extract from the consultation paper	Comments / Suggestions	Rationale

- 5.2. Kindly mention the subject of the communication as, *"Comments on consultation paper on dematerialisation of units of AIFs"*.

- 5.3. Comments as per aforesaid format may be sent to the following, latest by February 18, 2023, in any of the following manner:

- (i) Preferably by email, to Shri Sanjay Singh Bhati, Deputy General Manager ([ssbhati@sebi.gov.in](mailto:ssbhati@sebi.gov.in)) and/or to Ms. Padma Bharathi S, Assistant Manager ([padmab@sebi.gov.in](mailto:padmab@sebi.gov.in)); or



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**Securities and Exchange Board of India**

- (ii) By post to:  
Shri Sanjay Singh Bhati,  
Deputy General Manager,  
Alternative Investment Fund and Foreign Portfolio Investors Department,  
Securities and Exchange Board of India, SEBI Bhavan, C4-A, G-Block,  
Bandra Kurla Complex, Bandra (East), Mumbai -400051

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