

UNDERSTANDING AIFS

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What is an Alternate Investment Fund (AIF)?

AIFs are SEBI regulated product offerings

Come under purview of regulator
SEBI introduced revised AIF regulations in 2012

Investment Goal of AIF is the same as PMS or MF

To create wealth for investors!

Private Offering

Not offered by all AMCs and by limited distributors.
Unlike MFs, cannot be bought publically

An Investment Vehicle structure similar to MFs

Stocks held in pool account
Units allocated to investors
Increase in NAV leads to wealth creation



SUMMARY – MF : PMS : AIF

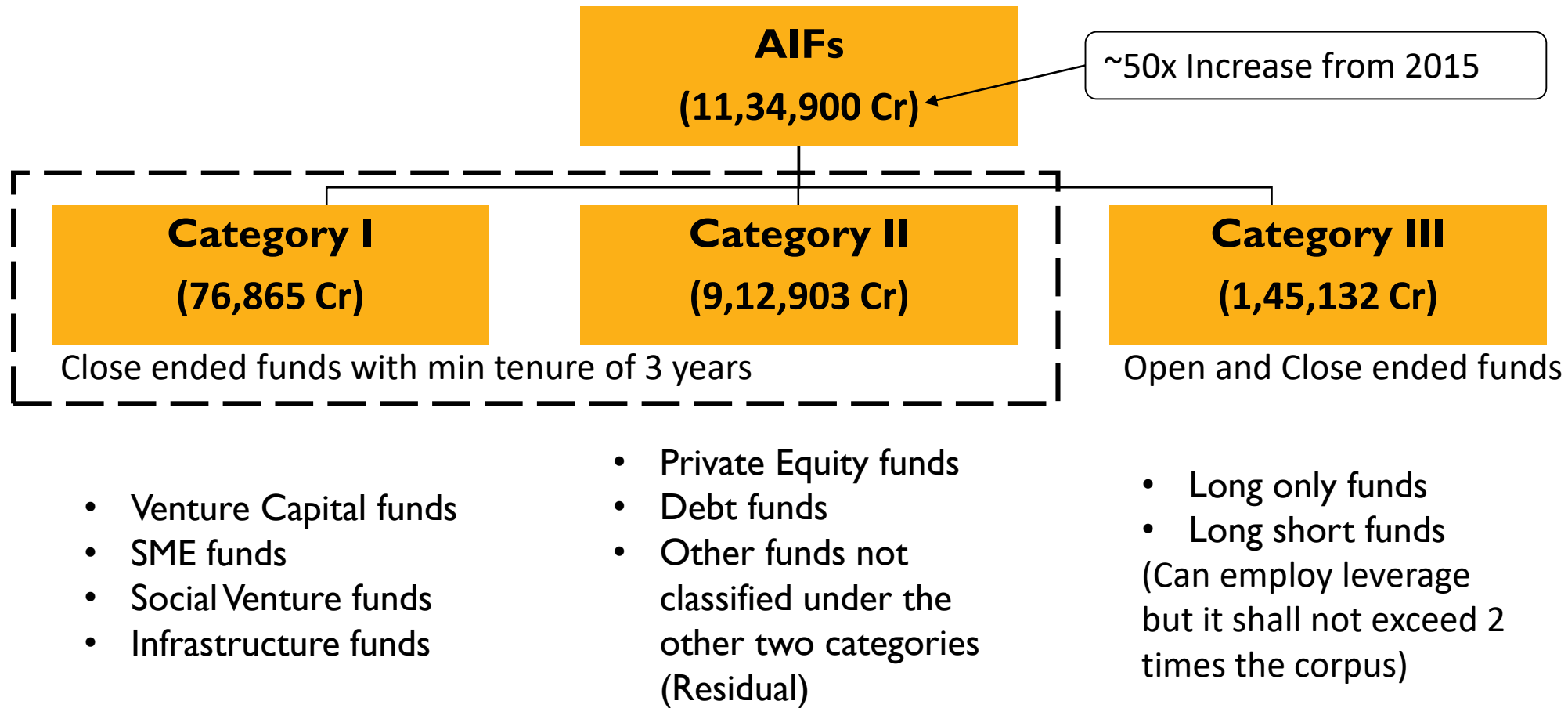
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Comparison between AIF's, PMS and Mutual Funds

Type	AIF	Mutual Fund	PMS
Regulation	Regulated by SEBI (Alternative Investment Funds) Regulations 2012	Regulated by SEBI (Mutual Fund) Regulations 1996	Regulated by SEBI (Portfolio Managers) Regulations 1993
Minimum Investment	INR 1 Crore	INR 500	INR 50 Lacs
Sponsor Commitment	Cat I & II : INR 5 Crore/ 2.5% of AUM Cat III: INR 10 Crore/ 5% of AUM; whichever is lower	For open ended: INR 50 lac /1% of AUM; whichever is lower	NIL
Exposure/ Leverage	Cat I & II:100% of the fund size Cat III: 200% of the fund size	100% of the fund size	100% of the fund size
Investment Type	Pooled	Pooled	Client
Taxation	Fund level	Individual Investor level	Individual Investor level
Demat account	NA	NA	Yes

Categories Of AIFs

AIFs can be set up as a trust or a company or a limited liability partnership or a body corporate.



Features of an AIF

A

Min investment of 1 Crore

Suitable to HNI investors looking for differentiated product and added benefits over MF/PMS

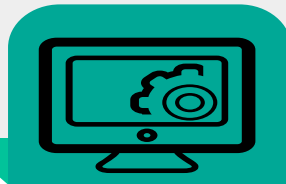


B

Lesser Restrictions on portfolio, similar to PMS

No limit of maximum 10% in single stock or 25% in a sector

No classification categories to restrict stocks by market cap



C

AIF can be closed-ended or open-ended

Open-ended AIFs run perpetually, similar to most MFs

Closed-ended AIF have a pre-decided 'maturity' date



Investment Manager's Advantage through AIFs



Decision of when to enter the market can be taken by FM

By means of calling for instalments in right situations

SIP is also a proven effective way to manage entry



Investments in IPOs can generate better returns

Higher allocations in IPOs through anchor allotment unlike PMS

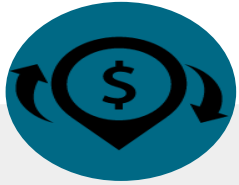


No inflow or redemption pressure after final onboarding

Portfolio does not get churned on account of entry/exit
On average 40% AuM of MF gets churned due to entry/exit

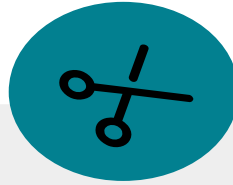
	Investor's Perspective	Fund Manager's Perspective
“Get” Money when the price is right	Drawdown structure allows for timing market opportunities to be professionally managed	Build portfolio gradually & ability to take advantage of possible corrections
Have a framework to sell	Booking profits & exiting portfolio are decided by Fund Manager	No re-investment risk at unfavorable valuations; lock-in high IRRs
Best of both PMS & MF on AIF platform	<ul style="list-style-type: none">• Flexibility in allocation (PMS)• Execution efficiency of pool account (MF)	<ul style="list-style-type: none">• Not restricted to tight regulations (Eg. 25% per sector)• Ease of building and executing portfolio in pool account

Advantages of Closed-ended AIF



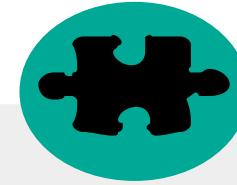
Call for Commitment amount based on market cycles

Invest capital over a market cycle even in bull phase thereby benefiting from rupee cost averaging



AIFs can pre-close or return partial capital before maturity date

Close to maturity date – fund manager does not have to re-invest booked profits in market. Partial funds can be returned, locking in high returns on investment.



AIFs can also extend the maturity date, if necessary

In adverse market scenario (for ex: Covid correction), fund period can be extended to exit at better valuations in future

Advantages of Open-ended AIF



Funds deployed immediately

Investors wary of cash flow/churn adjusted NAV could take advantage of immediate deployment of funds



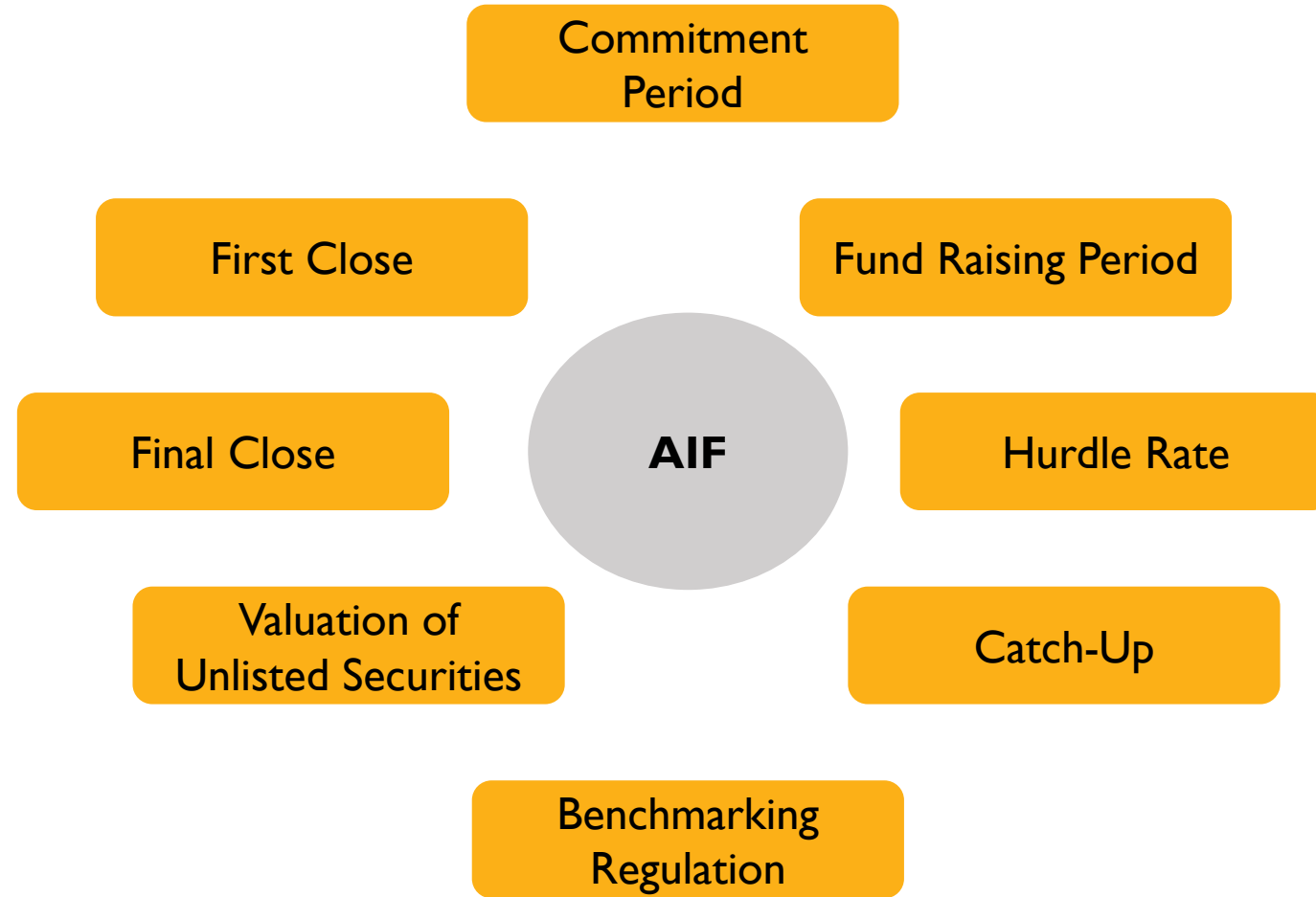
Track Record

For open ended AIFs, investors can refer to previous track record; close ended funds are time bounded



Open for subscription

Open ended AIFs are available for subscription at all times compared to close ended where funds cant be subscribed once final close is executed



Sample Working of Performance Fees

Investment Value	1,00,00,000
Mgmt Fees	1.5%
Investment Amount	98,50,000
Hurdle rate	10%
Fund Performance (Assumed)	20%

Final Holdings Value	1,18,20,000
Profit Value	19,70,000
Hurdle Value	9,85,000
Balance Distribution Proceeds in excess of Hurdle Rate of Return	9,85,000

	Without Catch-up (Performance fee on alpha generated)	With Catch-up (Performance fee on full return generated)
Performance Fees % (Eg.)	20%	15%
Performance Fees Amt	1,97,000	2,95,500
Investors' net gain	17,73,000	16,74,500
Investors final amount	1,16,23,000	1,15,24,500

Investment Window:

- *Close ended AIFs allotment occurs every Friday*
- *Open ended AIFs allotment occurs every Monday*

Exit Window:

- *Every month end post lock-in*

Liquidity Options – for any emergency needs

- *Lock-in period*
- *Prevent short-term exits due to volatility*

Portfolio Disclosures

- *Monthly portfolio holdings mailed to investors post final close*

NAV Reporting

- *Monthly NAV, portfolio valuation and IRR available to investors*

Investment Insights

- *Quarterly report with detailed rationale and updates on portfolio holdings post final close*

AIF TAXATION

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Type of instrument	Period of holding	Nature of income
Listed securities / units of equity oriented mutual fund schemes or zero-coupon bonds	More than 12 months	Long-term capital gain
	12 months or less	Short-term capital gain
Shares of a company (other than shares listed on a recognized stock exchange in India)	More than 24 months	Long-term capital gain
	24 months or less	Short-term capital gain

Set-off Rules	Long Term Gain	Short Term Gain
Long Term Loss	Yes	No
Short Term Loss	Yes	Yes

Note: Unlisted securities gain/loss can be offset against listed securities gain/loss

APPLICABLE TAX RATES

- CAT I and II AIFs have enjoy a pass through status
- Tax rates applicable as per rates applicable to the unit holder in CAT I and II AIFs
- All income earned by a CAT III AIF is taxed at the fund level itself

Capital Gains Taxes	Types of Instrument	Basic Tax	Surcharge (applied on tax)	Education Cess (applied on both tax and surcharge)	Final Rate
Long Term Capital Gains	Equity	12.5%	15%	4%	15.0%
Short Term Capital Gains	Equity*	20.0%	15%	4%	23.9%
Business Income	Futures and Options	30%	37%	4%	42.7%
Dividend Income	-	30%	15%	4%	35.9%

Rates are effective July 24, 2024 and are subject to change depending on latest government announcements etc.

Tenure for long term capital gains is above 12 months

*STCG Tax for Unlisted securities is at Slab rate

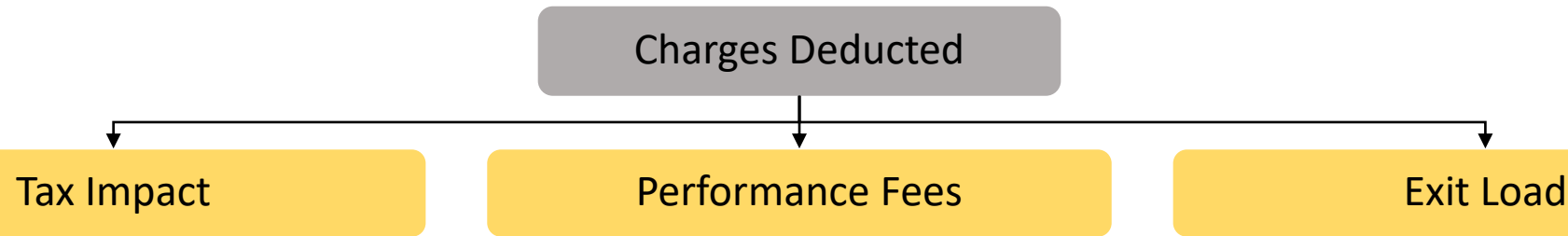
Close Ended AIFs

- The net asset value (NAV) of a fund only includes taxes on realized capital gains, due to the less inflow and outflow of funds within the maturity of the fund.
- Taxes on unrealized gains are not included in the NAV.
- These taxes are only calculated when units are redeemed.
- This ensures that the investor who exits is liable for paying taxes on their contributions.

Open Ended AIFs

- As there is a continuous inflow and outflow of funds, the Net Asset Value (NAV) includes taxes on both realized and unrealized capital gains.
- This ensures that the new investor is liable for the payment of taxes only on their contribution and not on any unrealized gains that occurred before their entry.

UNDERSTANDING FINAL AMOUNT PAID TO INVESTOR



Post-tax NAV in the SOA: This refers to the Net Asset Value of the investment fund after accounting for taxes. It includes the NAV post the realized gains/losses in the fund. Realized gains/losses are the profits or losses from the sale of securities within the fund.

Unrealized Gains/Losses: Unrealized gains/losses are the increases or decreases in the value of securities that the fund still holds but hasn't sold yet. These are not included in the post-tax NAV calculation before redemption.

Redemption Process: When an investor redeems their investment before the maturity of the fund, the unrealized tax calculation is performed. This calculation determines the tax liability on the unrealized gains of the securities held by the fund, and the amount proportionate to the investor is deducted from their redemption pay-out.

Adding Back Advance Tax: The advance tax paid by the fund until the date of redemption is added back to the redemption pay-out. This is done to avoid double taxation on the same unrealized securities. Essentially, it ensures that the investor is not taxed twice on the same unrealized gains.

In summary, the post-tax NAV in the SOA reflects the value of the investment fund after considering realized gains/losses but excluding unrealized gains/losses.

During redemption, the tax liability on unrealized gains is calculated and deducted from the payout, while advance tax paid by the fund is added back to prevent double taxation.

WORKING EXAMPLE – NET TAX, PERFORMANCE FEES AND EXIT LOAD

	Commitment Amount	1,25,00,000
A	Contribution Inward (Net of Setup Fees)	1,21,75,260
B	Closing Value Before Redemption	2,20,17,441
C	Net Tax Impact	(12,55,923)
D	AUM Post Tax (B+C)	2,07,61,519
E	Excess Amount for performance fee calculation (D-A)	85,86,259
F	Hurdle Value (10% - Compounded)	(43,62,399)
G	Excess after Hurdle (E+F)	42,23,861
H	Carried Interest (15%*G)	6,33,579
I	GST on Carried Interest (18%*H)	1,14,044
J	Total Performance Fees (H+I)	(7,47,623)
K	AUM Post Tax and Performance Fees, (B+C+J)	2,00,13,896
L	Exit Load (2%*K)	4,00,278
M	GST on exit Load (18%*L)	72,050
N	Total Exit load (L+M)	(4,72,328)
O	Total Deduction from AUM Before Redemption (C+J+N)	(24,75,874)
	Final Amount to be paid to Client (B+O)	1,95,41,568

Charges levied to the investor

For Hybrid/Variable Fee Share Class

The tax component of the investor shall be calculated on the NAV during redemption

The performance fees shall be calculated on the excess returns generated over the hurdle rate

Exit Load calculated as per the fund terms

Assumptions in this case	
Hurdle Rate	10%
Carried Interest	15%
Exit Load	2%

WORKING EXAMPLE – NET TAX AND EXIT LOAD

	Commitment Amount	1,50,00,000
A	Contribution Inward (Net of Setup Fees)	1,49,99,250
B	Closing Value Before Redemption	1,69,00,705
C	Net Tax Impact	(6,46,468)
D	AUM Post Tax (B+C)	1,62,54,237
E	Exit Load (1%*D)	1,62,542
F	GST on exit Load (18%*E)	29,258
G	Total Exit load (E+F)	(1,91,800)
H	Total Deduction from AUM Before Redemption (C+G)	(8,38,268)
	Final Amount to be paid to Client (B+H)	1,60,62,437

Charges levied to the investor

For Fixed Fee Share Class

The tax component of the investor shall be calculated on the NAV during redemption

Exit Load calculated as per the fund terms

Assumptions in this case	
Exit Load	1%

I. What is the frequency of tax charged to the investor?

Answer - Tax is charged on realized gains as & when the trades are booked. However, at the time of redemption, the unrealized gains (across the tenure of investment) in proportion to the investor's share is also taxed.

II. Does the investor receive TDS certificate against the tax paid by a Cat III fund?

Answer – Tax is paid by the trust as a representative assessee on behalf of the investor. No TDS certificate is received by the investor for Cat III fund.

III. Does the fund provide any document in respect of the tax paid to investors?

Answer – The fund shares a tax letter post the completion of audit for relevant financial year. This is considered as a substantial proof of evidence at the time of filing of returns or any scrutiny in future.

IV. Is the income of a Cat III fund tax free in the hands of investors?

Answer – Since the tax is discharged by the fund on behalf of investors, they do not have to pay additional tax separately. This holds true in case of resident individual investors. Investors with different legal entity should consult their tax advisor.

V. Can the investor utilize the fund losses against any other personal investment?

Answer – No, the fund losses cannot be passed on to the investor for offsetting any other personal gains. The same shall be carried forward by the fund for next financial year.

VI. If investor redeems during the year, will he get the benefit to offset realized gains against accumulated losses of previous years?

Answer - The Act does not specify the timing for set-off of capital losses against the capital gains, a better practice as suggested by our tax consultant is to set-off losses only at the end of the financial year based on the capital gains crystallised at the end of the financial year. This approach is based on the principle that the investors who tend to stay with the Fund for longer duration would be benefit on account of lower tax outflow due to set-off of accumulated losses.

VII. Rules of Offsetting as per Income Tax Act 1961 ('the Act')?

Answer – As per section 70 read with section 74 of the Act,

- Realized Short term capital losses (including brought forward) – Realized short term capital gains & long term capital gains.
- Realized Long term capital losses including brought forward – Realized long term capital gains

Accordingly, any realised capital loss on transfer of securities is not adjusted against notional (unrealised capital gains) as the same may tantamount to incorrect adjustment of capital losses by the Fund.

VIII. Difference between open & close ended from tax perspective?

- Open ended schemes, tax is adjusted for both realized and unrealized and thus, NAV is post tax post fees.
- Close ended schemes, tax is adjusted to the extent of realized gains only.

IX. What is the nature of the trust across our AIF schemes?

Answer – Determinate Irrevocable trust

Determinate Trust: Individual shares of the beneficiaries are expressly stated in the trust deed and are identifiable and ascertainable as on the date of the trust deed

Irrevocable Trust: The grantor transfers all ownership of assets into the trust and legally removes all of their ownership rights to the assets and the trust

X. Does the investor need to pay any additional tax on the income from gains in AIF

Since the tax is discharged by the fund on behalf of investors, they do not have to pay additional tax separately. This holds true in case of resident individual investors. Investors with different legal entity should consult their tax advisor.

Exemption to investor invested under AIF CAT III is **provided in Section 10(23FBC)**

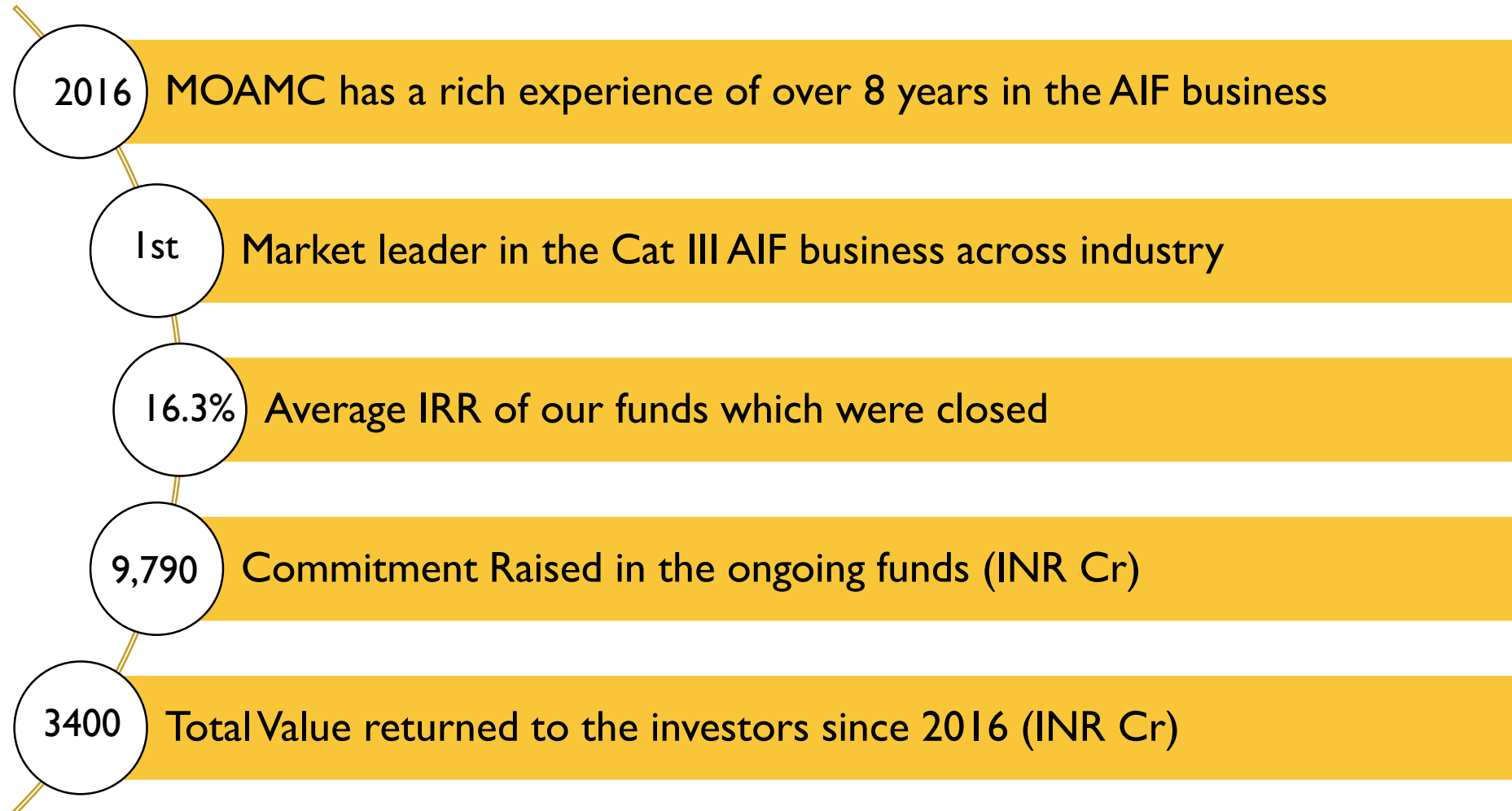
As per PPM in Tax Consideration Clause:

The NAV declared on periodic basis only covers the impact of tax on realized gains as & when booked in the scheme.

The accumulated unrealized gains over the period are taxed at the time of redemption depending on his proportionate share. It is not always necessary that the Fund Manager sells a position to execute redemption requests. Hence, certain portion is taxed as unrealized gains depending on the fund structure and its position.

MOTILAL OSWAL – LEADER IN CAT III AIFS

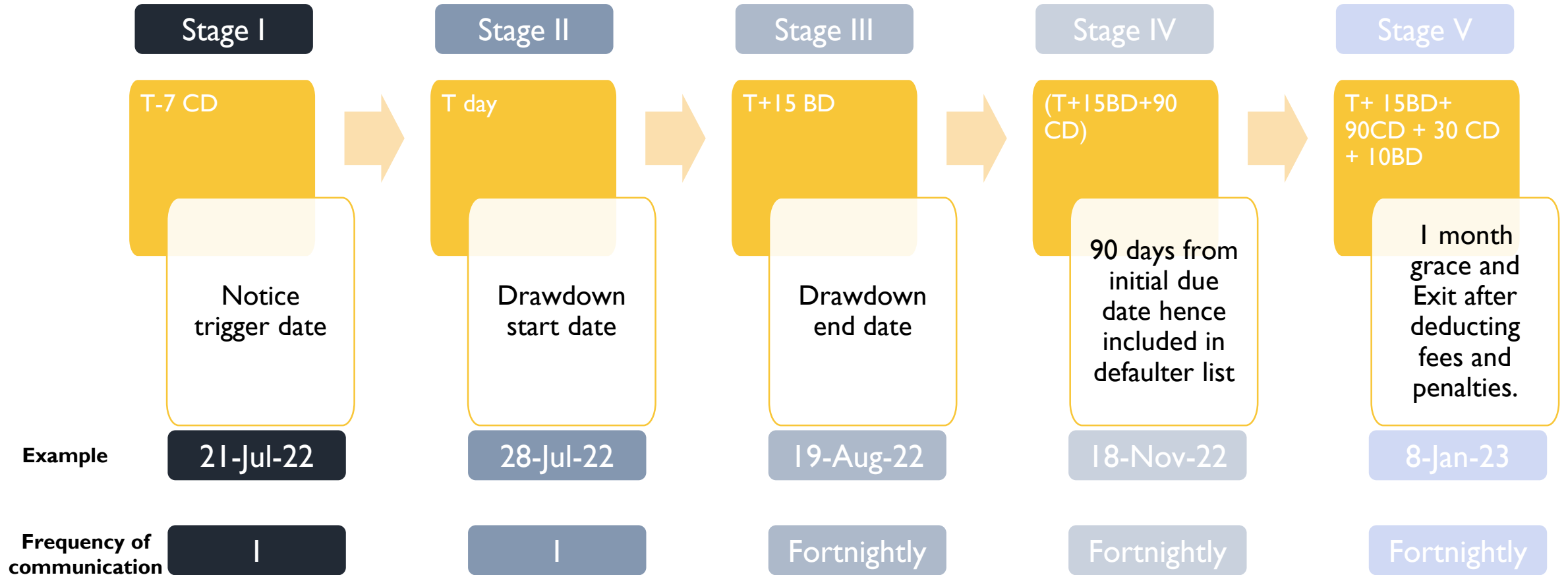
THINK EQUITY. THINK MOTILAL OSWAL.



Performance of our past AIFs (Matured)

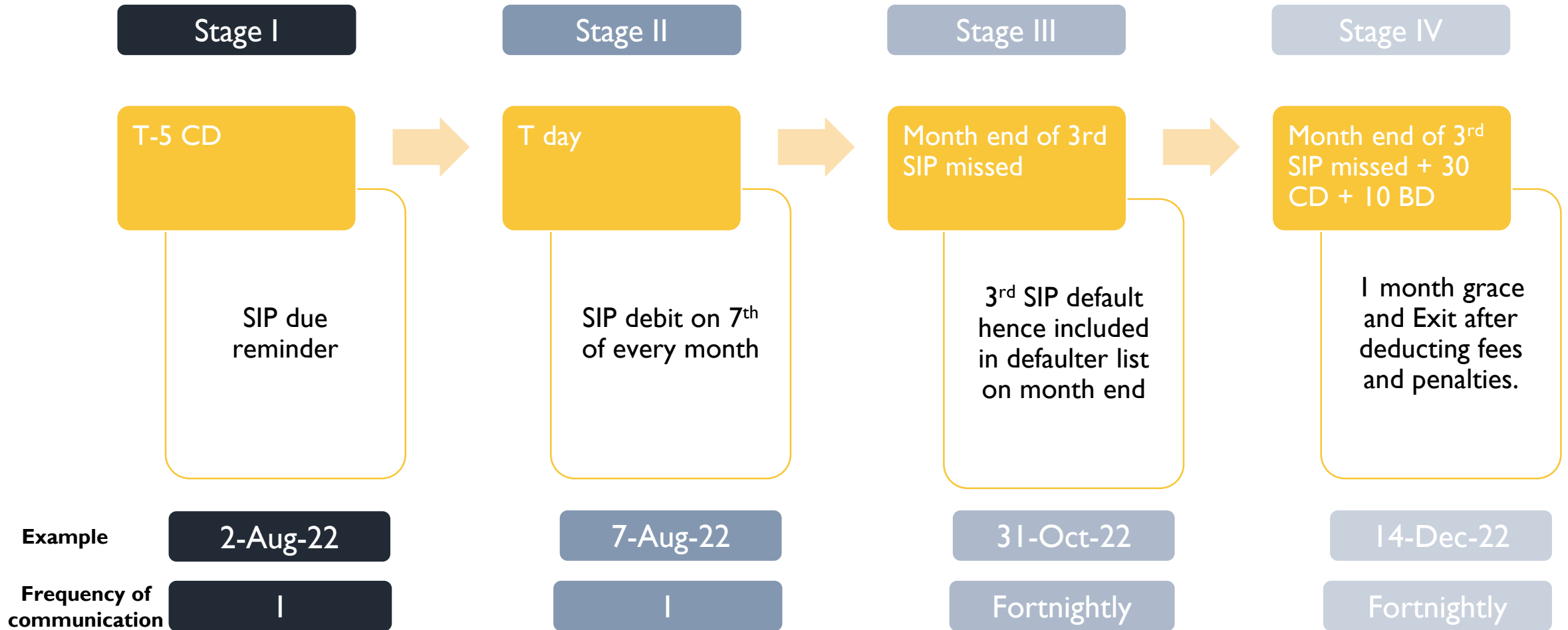
AIFs Closed	Maturity	XIRR	Start Date	Benchmark	Benchmark XIRR
Select Opportunities Fund	01-Feb-21	15.90%	02-Jan-18	BSE 200	10.64%
Focused Emergence Fund	20-Aug-21	11.90%	10-Jan-18	BSE Small Cap 100	11.10%
Rising India Fund	28-Oct-21	16.20%	05-Mar-18	BSE 200	16.43%
Business Advantage Fund	17-Apr-22	12.70%	17-Oct-17	BSE 200	12.64%

Flowchart for timelines - Drawdown



CD: Calendar days; BD: Business days

Flowchart for timelines - SIP



CD: Calendar days; BD: Business days

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