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Securities Exchange Board of India approves new framework for co-investment opportunities through Category I and II Alternative Investment Funds

The Securities Exchange Board of India (“SEBI”), at its board meeting on June 18, 2025, approved a new framework through which Alternative Investment Funds (“AIFs”) can offer co-investment opportunities in unlisted securities. The new framework permits Category I and II AIFs to offer Co-investment Scheme (“CIV Scheme”) under SEBI (Alternative Investment Funds) Regulations, 2012 (“AIF Regulations”), in addition to the option to make co-investment through the Securities and Exchange Board of India (Portfolio Managers) Regulations, 2020 (“PMS Regulations”) i.e., through the PMS Route (“PMS Route”). The CIV Scheme seeks to streamline the co-investment process, reduce regulatory and operational hurdles, and align investor interests more closely with those of the AIF.

Present framework of co-investment under the AIF Regulations

Under the AIF Regulations, ‘Co-investment’ refers to an investment made by: (a) the manager or sponsor of the AIF; or (b) an investor of a Category I and II AIFs in unlisted investee companies in which such Category I or Category II AIF(s) makes investment. In instances where the co-investment is made by investors of AIF, such investment will be through a Co-investment Portfolio Manager (“CPM”) as specified under the PMS Regulations. A CPM is a portfolio manager who manages Category I or Category II AIFs and provides services exclusively to the investors of such Category I or Category II AIFs and makes investment only in unlisted securities of investee companies where such Category I or Category II AIFs make investments. Further, the CPM may provide services to investors from any other Category I or Category II AIFs which are managed by them and are also sponsored by the same sponsor(s).

The AIF Regulations further stipulate that the terms of the co-investment in an investee company will not be more favourable than the terms of the investment offered to the AIF itself. Likewise, the terms of the exit from the co-investment in an investee company including the timing of exit by the co-investors, will be identical to the terms applicable to that of exit of the AIF. This framework ensures that co-investors do not receive preferential treatment compared to the AIF. However, it may be noted that the current AIF Regulations contain only limited provisions relating to co-investments, which has resulted in operational challenges and regulatory ambiguities in their implementation.

SEBI Consultation Paper

SEBI, on May 9, 2025, floated a consultation paper (“Consultation Paper”), inviting public comments on allowing co-investment opportunities through creation of a separate co-investment vehicle. SEBI had set up a working group on

ease of doing business (“**Working Group**”) to review the compliance requirements under the AIF Regulations highlighting certain operational issues with respect to co-investments through the extant PMS Route including the following:

1. investment managers requiring to register themselves under both the AIF Regulations and PMS Regulations; and
2. unlisted investee companies requiring to deal with a large number of shareholders.

The key concerns highlighted by the Working Group are: (a) seeking additional registration imposes further additional costs and complexity for investment managers and affects the competitiveness of domestic players in comparison to global private equity funds that face no such restrictions; (b) co-investment through the PMS Route leads to excessive documentation and execution delays, particularly due to the need to individually onboard and document each co-investor, which can affect time-sensitive transactions; (c) the requirement for identical exit terms between AIFs and co-investors, often conflicts with co-investors’ internal exit timelines; (d) the expansive definition of co-investment under the AIF Regulations may potentially cover situations where an investor of the AIF is directly approached by the investee company; (e) under the AIF Regulations, co-investment services can be provided only to investors of such funds where the sponsor is same and is being managed by the CPM. This impedes the ability of investment managers to connect investors with appropriate investment opportunity.

To address the aforementioned issues, the Working Group recommended providing a route for co-investment within the AIF structure.

CIV Scheme

SEBI, *vide* its board meeting approved the inclusion of the concept of CIV Scheme under the AIF Regulations. The CIV Scheme will have the following key features:

1. ‘Co-investment Scheme’ is defined to mean a scheme of Category I or Category II AIFs, which facilitates co-investment to accredited investors of a particular scheme of an AIF, in unlisted securities of an investee company where the scheme of the AIF is making investment or has invested;
2. a separate CIV Scheme will be launched for each co-investment in an investee company subject to safeguards to ensure that the scheme is used only for bona fide purposes; and
3. certain regulatory requirements applicable to other AIF schemes will be relaxed for CIV Schemes.

The Consultation Paper, had additionally proposed for the below features of the CIV Scheme, however, these aspects are not addressed in the minutes of the board meeting:

1. a shelf Private Placement Memorandum (“**PPM**”) of the CIV Scheme to be annexed to the PPM of the main AIF at the time of seeking registration of the main AIF. The shelf PPM of the CIV Scheme will set out the following details: (a) principles/parameters on which the investors of the main AIF will be offered co-investment right e.g. on basis of quantum of capital commitment to the main AIF; and (b) the co-investment policy of the investment manager will be made available for inspection by prospective investors prior to on-boarding in the main AIF. Existing AIFs can also file the shelf PPM with SEBI for this purpose;
2. the investment manager will seek registration of the CIV Scheme at the time of the first co-investment deal by filing the shelf PPM with SEBI and the same will be deemed approved if there are no queries from SEBI within 30 (thirty) days of such filing. CIV Scheme will be given a separate registration number so as to ensure a separate PAN can be obtained for tax purposes. Each CIV Scheme will have separate bank account, demat account and PAN;
3. tenure of the CIV Scheme to be co-terminus with the main AIF;
4. quarterly filing of the CIV Scheme will be made as per the extant format subject to exemptions conferred;
5. the CIV scheme will be exempted from the following requirements under the AIF Regulations:

- a) diversification norms per investee company will not be applicable to a CIV Scheme, since a CIV Scheme may end up making only a single co-investment with the main AIF. Hence, CIV Schemes will be exempted from conditions set out under Regulations 15 (*General Investment Conditions*), 16 (*Conditions for Category I AIFs*) and 17 (*Conditions for Category II AIFs*) of the AIF Regulations;
 - b) no separate sponsor commitment should be required for a CIV Scheme since the sponsor would have made its commitment to the main AIF;
 - c) minimum tenure of 3 (three) years will not be applicable to a CIV Scheme; and
6. CIV scheme will be subject to implementation standards, to ensure that the investments by CIV Scheme are made for bona fide purposes and that the flexibility extended in this regard is not misused.

Conclusion

It is envisaged that the introduction of the CIV Scheme will allow Category I and Category II AIFs to facilitate co-investment to accredited investors through CIV Scheme within AIF Regulations, in addition to the existing option for co-investment available through the PMS Route. Once formally notified, the amendments to the AIF Regulations are expected to address several operational challenges associated with the existing PMS Route, such as compliance burdens, onboarding complexities, and rigid exit requirements thereby facilitating AIFs and investors to co-invest and support capital formation in unlisted companies through AIFs.

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41 Ranked Lawyers



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21 Ranked Lawyers



14 Practices and
12 Ranked Lawyers



12 Practices and 50 Ranked
Lawyers



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22 Ranked Lawyers



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