

Annexure II: Test Objectives
NISM-Series-XIX-D: Category I and II Alternative Investment Fund Managers Certification
Examination

Section A: Basics of Investments

Chapter 1: Investments Landscape

- 1.1 Define Investment
- 1.2 Distinction between Investment and Speculation
- 1.3 Know the objectives of Investments
- 1.4 Estimating the required rate of return
 - 1.4.1 Concept of Nominal rate of return, Real Risk-free rate and Expected Inflation
 - 1.4.2 Concept of Risk Premium
 - 1.4.3 Understand the various types of risks:
 - Business Risk
 - Financial Risk
 - Liquidity Risk
 - Exchange rate Risk
 - Political Risk
 - Geopolitical Risk
 - Regulatory Risk
 - Market Risk
 - Interest Rate Risk
 - 1.4.4 Understand the relationship between risk and return
- 1.5 Overview of Indian Securities Markets

Chapter 2: Types of Investments

- 2.1 Distinguish between Traditional investments and Alternate investments.
- 2.2 Know the types of Traditional Investments and their role and characteristics
 - 2.2.1 Equity
 - 2.2.2 Fixed Income Securities
 - 2.2.3 Derivatives
 - 2.2.4 Money Market Instruments
- 2.3 Outline the different types of alternate investments:
 - 2.3.1 Venture Capital (including venture debt)
 - 2.3.2 Private Equity
 - 2.3.3 Private Debt
 - 2.3.4 Hedge Funds (including CDS)
 - 2.3.5 Real Estate and Infrastructure
 - 2.3.6 Distressed Securities
 - 2.3.7 Other (sunrise sector funds, special situation funds, fund of funds etc)

- 2.4 Know the channels for making investments
 - 2.4.1 Direct investments
 - Understanding the role of Registered Investment Advisers (RIAs)
 - 2.4.2 Investments through managed portfolios
 - Mutual Funds
 - Collective Investment Schemes
 - Portfolio Management Services
 - Alternative Investment Funds
 - Specialised Investment Funds
- 2.5 Explain the role of Alternate Investments in overall portfolio with regard to the benefits and limitations of Alternate Investments.
- 2.6 Trace the global evolution and growth of Alternate investments and its transformation over time to its present context.
 - 2.6.1 Compare the investments made by PE/VC funds globally vis-à-vis in India

Section B: Understanding the AIF Ecosystem

Chapter 3: Alternative Investment Funds in India and its Suitability

- 3.1 Trace the evolution and growth of AIFs in India.
- 3.2 Identify the factors that enable India to be one of the top AIF markets in the world.
- 3.3 List and compare the fund categories as per SEBI (Alternative Investment Funds) Regulations 2012.
 - 3.3.1 Category I AIF
 - Venture Capital Fund
 - Angel Fund
 - Infrastructure Fund
 - SME Fund
 - Social Impact Fund
 - Special Situations Fund
 - Corporate Debt Market Development Fund
 - 3.3.2 Category II AIF
 - Private Equity Fund
 - Debt Fund
 - 3.3.3 Category III AIF
- 3.4 Analyse the suitability of AIF products to particular classes of investors (based on Investors' risk-return profile)
 - 3.4.1 Ascertain the suitability of a Category I and II AIFs
 - 3.4.2 Describe asset allocation for HNI and Institutional investors looking to invest in AIFs.
- 3.5 Discuss the size and segments of AIF market in India, no. of AIFs registered with SEBI.
- 3.6 Assess the role of AIF in Portfolio Diversification
- 3.7 Interpret the use of AIF as a Risk Management tool:

3.7.1 Alpha Management

3.7.2 Beta Management

Chapter 4: Alternative Investment Fund Ecosystem

4.1 Explain the concepts prevalent in the AIF industry:

4.1.1 AIF Ecosystem:

- Investors
- Sponsors
- Trustees
- Investment Managers

4.1.2 Crowdfunding and Corporate Venture Funding

4.1.3 Co-investments

4.1.4 Service Providers

- Fund Administrators
- Fund Infrastructure
- Distributors and Placement Agents
- Tax Advisors
- Registrar and Transfer Agents
- Legal Advisors
- Custodian
- Auditors
- Investment Advisers
- Merchant Bankers
- Independent Valuers

4.1.5 Capital Committed and Sponsor Commitment

4.1.6 Drawdown and Capital Invested

4.1.7 Due Diligence

4.1.8 Environment, Social and Governance (ESG)

4.1.9 First Close and Final Close

4.1.10 Green shoe option

4.1.11 Fees and Expenses:

- Lock-in Period and Exit Load
- Management Fees
- Set-up Costs and Operational Expenses
- Hurdle rate and High Watermark

4.1.12 Additional returns (carry) and Performance Fees

4.1.13 Distributions and Distribution Waterfall

- Clawback

4.1.14 Term Sheet/ Summary of Principal Terms (SOPT)

4.1.15 Private Placement Memorandum (PPM)

Chapter 5: Alternative Investment Fund Structuring

5.1 Explain the concept of 'pooling' and how it is different from individual portfolio management.

5.2 Identify the main considerations in deciding the geographical jurisdiction for 'pooling' from an offshore Investor perspective for an India focussed fund.

5.3 Summarise the overall regulatory perspective and tax in the context of setting up of an India focussed AIF.

5.4 Identify and explain the main pooling structures possible in India for a domestic AIF.

- 5.5 Discuss with reference to the Trust Structure / LLP Structure/ Company structure, the composition of a domestic AIF in India.
- 5.6 Discuss the regulatory implications of fund structure on domestic AIF investors.
- 5.7 Explain the common fund structures of AIF:
 - 5.7.1 On-shore and Off-shore Funds
 - 5.7.2 Unified and Co-Investment Structures
 - 5.7.3 Parallel Structures and Master Feeder Structures

Chapter 6: Fee Structure of AIFs

Fee Structure:

- 6.1 Describe and calculate Management Fees and Incentive Fees charged by AIF. Discuss the concept of Total Fee.
- 6.2 Discuss the importance of Hurdle Rate, when computing Fees and forming the Fee Structure of AIF.
- 6.3 Explain the principle of High watermark and catch-up and discuss its importance.
 - 6.3.1 Calculate and analyse Pre and Post fees returns of an AIF.
 - 6.3.2 Analyse the impact of GST on Fees

Worked-out Case:

- 6.4 Outline the concepts of additional return, clawback and waterfall as applied in commercial arrangements between investors and investment managers
- Case Study: Fee structure and commercial arrangements involving expense calculations and operating costs

Chapter 7: Fund Performance and Benchmarking of AIFs

Fund Performance Evaluation:

Risk Metrics:

- 7.1 Summarise the risk of adverse selection by the Investors (contributory) based on various criteria that would impact their interests
- 7.2 Interpret the key risk areas based on the disclosure in the Private Placement Memorandum (PPM):
 - 7.2.1 Investor Level Risks (for both equity and debt funds under AIF)
 - 7.2.2 Governance/Fund Level Risks (for both equity and debt funds under AIF)
- 7.3 Explain the types of risks involved in AIF (such as Market risk, Liquidity risk etc.)

Return Metrics:

- 7.4 Discuss the main approaches to evaluate Fund Performance
 - 7.4.1 The Internal Rate of Return (IRR) method – Gross and Net IRR computation with scenario analysis and illustrations
 - Explain with scenario analysis reasons for differential IRRs in Fund Performance
 - 7.4.2 The J Curve approach and how to view the J Curve in conjunction with the IRR.

- 7.4.3 Discuss the concepts of Total Value to Paid-in-Capital (TVPI), Distributions to Paid-in-Capital (DPI) and Residual Value to Paid-in-Capital (RVPI) and their application to benchmarking with industry performance.
- 7.5 Discuss the other return measurement metrics used in Alternative Investments
 - 7.5.1 Kaplan-Schoar Public Market Equivalent (KS-PME)
 - 7.5.2 Direct Alpha
- 7.6 Explain the concept of Multiple on Invested Capital (MOIC)
- 7.7 Analyse the impact of direct and indirect taxes on performance of AIFs
 - 7.7.1 Calculate Pre and Post Tax Returns of AIFs

Benchmarking:

- 7.8 Discuss about Performance Benchmarking i.e. relevant benchmark for the AIFs, which has the similar characteristics and risk-return profile, as the fund under consideration. Discuss suitability of appropriate benchmarks for AIF, based on its investment strategy and support with example.
 - 7.8.1 Benchmarking Agencies
 - 7.8.2 Role of a benchmark in evaluating alpha generated by AIF.

Chapter 8: Legal Documents and Negotiations

Understand the broad description and purpose of the type of documentations used in AIF investment activity.

8.1 Fund Documentation

- 8.1.1 The Private Placement Memorandum (PPM)
 - Additional Disclosures under PPM
 - Investor Charter
 - Disclosure of Complaints
 - PPM Audit
 - Material changes in PPM
- 8.1.2 The Trust Indenture (Trust Document/ Limited Liability Partnership Deed/ Memorandum and Articles of Associations)
- 8.1.3 The Subscription (Investor Contribution) Agreement
 - Side Letters with Investors
- 8.1.4 Preferential Rights to Investors
- 8.1.5 Investment Management Agreement
- 8.1.6 Support Service Agreements
 - Distribution Agreement (between the Investment Management Company and a Distributor)
 - Agreement with Merchant Banker
 - Agreement with Custodian
 - Agreement with Depository Participants

Section C: Managing AIF Investments – Category I and II

Chapter 9: Investment Strategies

Equity Strategies

- 9.1 Discuss equity investment strategies used by Cat I and II AIF
 - 9.1.1 Venture/ PE/ Growth perspective/ Angel Fund/ Syndication deals and their components
- 9.2 Difference between idea and opportunity and the process of deal sourcing
- 9.3 Discuss the process of deal generation and building deal pipeline by Investment Managers

Chapter 10: Investment Process and Governance of Funds

Investment Process:

- 10.1 Discuss the stages in an AIF investment deal
 - 10.1.1 Initial assessment
 - 10.1.2 Business Due Diligence
 - 10.1.3 Negotiations by the Investment Managers
 - 10.1.4 Summarise the purpose, principal terms and process of finalising a term sheet
 - 10.1.5 Thesis-based/ thematic investing, portfolio management and asset diversification

Governance of Funds:

- 10.2 Explain Investor Due Diligence (IDD) and who performs it. Discuss the principal areas of IDD.
- 10.3 Outline the scope, coverage and brief overview of Investor Due Diligence (IDD).
- 10.4 Identify the Definitive Agreements entered into as part of the deal documentation by the fund and the investee company.
- 10.5 Distinguish the important specific rights (Cat I and II) negotiated by the fund with the investee company with suitable illustrations.
 - 10.5.1 Milestone Valuation
 - 10.5.2 Dividend Rights
 - 10.5.3 Anti-Dilution Rights (full ratchet and broad based weighted average ratchet)
 - 10.5.4 Affirmative and Veto Rights and Voting Rights
 - 10.5.5 Liquidation Preference (participating and non-participating)
 - 10.5.6 Exit Rights, Drag Along Rights and Tag Along Rights
 - 10.5.7 Extent of option pool
 - 10.5.8 Auto convert clause
 - 10.5.9 Protective provisions (majority of Series A etc.)
 - 10.5.10 Board composition (common/ preferred shares mix)
- 10.6 Evaluate the role of the Investment Committee, transparency and governance standards in a Fund.

- 10.6.1 Role of Fund Governance
- 10.6.2 Fund Governance Structure
- 10.6.3 Investment Committee (IC) Approvals
- 10.6.4 Investor Advisory Committee
- 10.6.5 Role of Board of Directors of AMC
- 10.6.6 Conflict of Interest Issues
- 10.6.7 Investor Grievances and Dispute Resolution
- 10.6.8 Managing the stakeholders in PE deals
- 10.7 Summarise the process of decision making in a fund and internal measures to be taken to avoid conflict of interest. Discuss the role of human capital and fund manager and its team.
- 10.8 Explain the concept of Co-investments in AIFs
- 10.9 Discuss the Code of Conduct of Investment Managers of AIF
- 10.10 Discuss industry best practices

Chapter 11: Valuation

- 11.1 Describe briefly the general approaches to valuation of AIF investments in investee companies
 - 11.1.1 The Income Approach using DCF methodology
 - 11.1.2 The Market Approach using Relative Valuation
 - EBITDA Multiple
 - Price to Book Value Multiple
 - Price to Earnings Multiple
- 11.2 Distinguish between Enterprise Value and Equity value of a company.
- 11.3 Discuss the general approaches to valuing early-stage companies.
- 11.4 Outline the general approaches to valuation of Debt fund investments.
- 11.5 Summarise the general approach to Fund Valuation and the valuation of Investor interest in a fund.
 - 11.5.1 Explain using the J-Curve concept, the difficulty in fund valuation for early-stage funds as compared to those in vintage years.
 - 11.5.2 Valuation of AIF Portfolio Investments (Investee Companies) based on the IPEV Valuation Guidelines
- 11.6 Discuss the concept of Net Asset Value (NAV).
- 11.7 Discuss the role of third-party registered valuers and the frequency of such valuation. Also specify the timeline for generation of valuation reports and limitation of valuation reports.

Chapter 12: Fund Monitoring, Reporting and Exit

- 12.1 Monitoring Alternative Investment Fund Progress and Performance
 - 12.1.1 Context and Scope of Effective Fund Monitoring
- 12.2 List the periodic reporting process of the Fund / Investment Managers to the Investors under their:
 - 12.2.1 Regulatory obligations

- Specific Transparency and Periodic Disclosure Requirements
 - Maintenance of Records
 - Submission of reports to SEBI
- 12.2.2 Contractual obligations
- 12.2.3 Additional information
- 12.3 Describe a reporting template.
- 12.3.1 Conflicts and Concerns in Fund Reporting
- 12.4 Outline the available exit options for an AIF
- 12.4.1 Exit from its investee/ portfolio companies
- 12.4.2 Exit due to Material Changes in PPM
- 12.4.3 Change in Manager/ Change in control
- 12.4.4 Other exit scenarios
- 12.5 Compare IPO, Strategic Sale (M&A), Secondary sale, Buyback and Liquidation as exit options.
- 12.6 Identify the role and significance of 'secondaries' and their current status in India.
- 12.7 Discuss about winding up of an AIF

Section D: Taxation and Regulatory Framework

Chapter 13: Taxation

AIF Category I and II

- 13.1 Income streams for the AIF from its investments
- 13.2 Characterisation of income
- 13.3 Taxation of the AIF
- 13.3.1 Explain the concept of 'tax pass through' and its relevance from an AIF perspective
- 13.3.2 Evaluate in comparative terms, the taxation framework for a domestic AIF in India constituted as a trust or LLP.
- 13.3.3 Discuss the tax treatment for Category I and II AIFs for business income and losses.
- 13.3.4 Discuss provisions relating to deemed income and deemed distribution
- 13.4 Withholding tax obligations and compliances
- 13.5 Investor reporting requirements
- 13.6 Identify the tax implications on transfer of units of AIF by the investors
- 13.7 Structuring options for offshore investors
- 13.8 Concept of Double Tax Avoidance Agreement (DTAA) and General Anti-Avoidance Rules (GAAR).
- 13.9 Discuss about the Indirect Taxes as applicable to AIFs
- 13.9.1 GST Regime
- Stamp Duty and Local Taxes

Chapter 14: Regulatory Framework

Discuss the general framework of regulations and their purpose.

A. SEBI (Alternative Investment Funds) Regulations, 2012

- 14.1 Outline the registration process of AIFs and the eligibility criteria to seek registration
 - 14.1.1 Registration requirements
 - 14.1.2 Registration criteria and Documentations
 - 14.1.3 Conditions for Registration
- 14.2 List the principal and general obligations of Sponsors and Investment Managers of AIFs
 - 14.2.1 Sponsor and Manager Commitment
- 14.3 Concept of open ended and closed ended funds
 - 14.3.1 Analyse why Category I and II AIFs are allowed only to be closed ended funds
- 14.4 Tenure of Fund and Schemes
- 14.5 Requirements with regard to subscriptions to the fund by investors
- 14.6 Discuss the concepts of Accredited Investor, Accreditation Agencies and the Accredited Investor Framework:
 - 14.6.1 Accredited Investors
 - 14.6.2 Accreditation Agency
 - 14.6.3 Large value fund for Accredited Investors
- 14.7 Raising of Corpus Capital and Role of PPM and fund documents
- 14.8 Regulatory framework applicable to investments
 - 14.8.1 General Investment Conditions for all AIFs
 - 14.8.2 Specific Investment Conditions for Category I AIFs
 - 14.8.3 Specific Investment Conditions for Category II AIFs
 - 14.8.4 Special Dispensation for Angel Funds
 - 14.8.5 Special Dispensation for Special Situation Funds
- 14.9 List General Obligations and Responsibilities of a Category I/II AIFs
 - 14.9.1 General Obligations
 - 14.9.2 Code of Conduct
 - 14.9.3 Exemption from enforcement of the regulations in special cases
- 14.10 List the periodic and exceptional disclosures and reporting to be made by AIFs

B. Foreign Exchange Management Act, 1999

- 14.11 Explain briefly the concept of foreign direct investment (FDI) and its economic significance for India.
- 14.12 Analyse why there are restrictions on FDI in Indian companies and on full convertibility of the rupee.
- 14.13 Identify when the FDI policy under FEMA gets attracted to AIF investments by foreign investors.
- 14.14 Outline the principal investment requirements under FEMA as are applicable to AIF investments

E. Prevention of Anti-Money Laundering Act

- 14.15 Demonstrate the importance of disclosures made by a AIFs under the Prevention of Anti-Money Laundering Act

F. SEBI (ICDR) Regulations

- 14.16 Pricing of securities issued in IPO
- 14.17 Lock-in restriction in case of securities issued in IPO
- 14.18 Preferential Allotment of Shares in a QIP
- 14.19 Lock-in Restriction in case of Preferential Allotment
- 14.20 Sale of Shares by a Category II AIF, in an Offer for Sale (OFS)

H. Other Regulations

- 14.21 Discuss the regulatory and reporting requirements under FATCA and CRS

Glossary of Terms