RBI clamps down on evergreening via AIFs

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In the middle of concerns about the circumvention of regulations by alternative investment funds (AIFs), the Reserve Bank of India (RBI) issued an advisory on Tuesday to banks and financial companies to curb the evergreening of loans and misuse of the AIF route.

According to the RBI advisory, banks, non-banking financial companies (NBFCs), and other financial institutions like the National Bank for Agriculture and Rural Development and the Small Industries Development Bank of India (Sidbi) will not be able to make investments in any scheme of AIFs that has downstream investments directly or indirectly in a debtor company of the bank/NBFC.

This implies that if the bank or NBFC currently has exposure or had previously lent at any time during the preceding 12 months to a company, they cannot invest in an AIF scheme investing in the same company.

The RBI's advisory comes against the backdrop of the findings of the Securities and Exchange Board of India (Sebi), which said that the cases of circumvention amount to "tens and thousands of crores". Last month, a Sebi official stated that the market regulator had shared the data with RBI on AIFs being structured to enable the evergreening of financial sector assets to avoid non-performing asset (NPA) recognition.

"We have shared this data with RBI, and RBI agrees with our assessment. We have seen cases where AIFs have been used to circumvent Foreign Exchange Management Act regulations — where a particular entity not allowed to invest in another does so via an AIF," the Sebi official had said.

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DIRECTIVES & INDUSTRY CONCERNS

- **Banks, NBFCs will have to liquidate investments in the scheme within 30 days** if an AIF has any downstream investment
- **RBI directs institutions to make a 100% provision** on such investments if not liquidated within 30 days

- **RBI's advisory follows concerns raised by Sebi** regarding circumvention through AIFs
- **The AIF industry is concerned about exits** by financial institutions and growth prospects

global supply disruptions could cause recurrent commodity price volatility, increasing fiscal pressures for India. Domestically, weather shocks could reignite inflationary pressures and prompt further food export restrictions. On the upside, stronger than expected consumer demand and private investment would raise growth," the Fund said.

RBI...

"If an AIF scheme, in which regulated entity (bank or NBFC) is already an investor, makes a downstream investment in any such debtor firm, then the regulated entity shall liquidate its investment in the scheme within 30 days from the date of such downstream investment by the AIF," said RBI. If the RBI-regulated entity is not able to liquidate its investments within the 30-day timeline, then it will have to make a 100 per cent provision on such investments, advised RBI. "The regulators are closing the loophole and making it watertight. We need to watch out for the impact on large wholesale NBFCs with fund structures," said a debt AIF manager. The AIF industry has raised concerns about the impact and challenges in tracking such investments. Industry officials have said that they have commenced work on their submissions to both regulators.

"This is akin to throwing the baby out with the bathwater. Several banks have signed agreements for AIF investments. This will also restrict investments by Sidbi, the government's initiative to provide credit. Many AIFs invest in listed entities too, and there could be some credit provided by these financial institutions already. Even if a credit card or banking facility is availed of by the entity where the AIF plans to invest, then the bank/NBFC cannot invest in the said AIF," said an AIF official.

IPL...

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