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WINDING UP AIFS SET UP IN THE FORM OF TRUSTS

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This paper seeks to outline the grounds for, and compliances involved in winding up of an "alternative investment fund" set up as a trust and discusses a few lacunae in the law in this regard and some common practical issues faced by the fund upon winding up. It also seeks to highlight the interface between the SEBI (Alternative Investment Fund) Regulations, 2012 and the Indian Trusts Act, 1882. Lastly, this paper attempts to put forth a few plausible solutions for the issues highlighted in the paper.

I. Introduction

"Alternative Investment Fund" means a fund established or incorporated in India under the Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012 ("**AIF Regulations**") in the form of a trust, a company, a limited liability partnership, or a body corporate. The AIF Regulations define an alternative investment fund ("**AIF**") (i) as a privately pooled investment vehicle which collects funds from investors, whether Indian or foreign, for investing it in accordance with a defined investment policy for the benefit of its investors; and (ii) which is not covered under the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996, Securities and Exchange Board of India (Collective Investment Schemes) Regulations, 1999 or any other regulations of the Securities and Exchange Board of India ("**SEBI**") to regulate fund management activities. The AIF Regulations further specify certain trusts/ legal structures which are not considered as AIF for the purpose of the AIF Regulations, such as a family trust set up for the benefit of relatives or an employee welfare trust.

The AIF Regulations have very clearcut procedures for the setting up of an AIF and prescribe in detail, the eligibility criteria for the AIF's sponsor and the investment manager, the qualifications required for the key personnel of the AIF's investment management team, the procedure to apply for a certificate of registration including the form to be filed, the attachments that should accompany such application, the fees to be paid at the time of filing the application and at the time of registration, etc. However, in comparison, the procedures and guidelines contained in the AIF Regulations for winding up of an AIF are very rudimentary. The problems or rather, confusion regarding the proper procedure to be followed when winding up an AIF is accentuated by the fact that most AIFs are set up in the form of a private trust under the Indian Trusts Act, 1882 ("**Trusts Act**"), and neither such trusts nor the schemes of such trust, are legal entities.

II. Grounds for winding up an AIF under the AIF Regulations

Regulation 29 of the AIF Regulations governs the winding up of AIFs. Sub-regulation (1) of Regulation 29 addresses the winding up of an AIF set up as a trust. Sub-regulation (2) of Regulation 29 addresses the winding up of an AIF set up as a limited liability partnership ("**LLP**"). Sub-regulation (3) of Regulation 29 addresses the winding up of an AIF set up as a company. Sub-regulation (4) of Regulation 29 addresses the winding up of an AIF set up as a body corporate.

Sub-regulation (2) of Regulation 29 states that an AIF set up as an LLP shall be wound up in accordance with the provisions of The Limited Liability Partnership Act, 2008. Sub-regulation (3) of Regulation 29 states that an AIF set up as a company shall be wound up in accordance with the provisions of the Companies Act, 2013. Sub-regulation (4) of Regulation 29 states that an AIF set up as a body corporate shall be wound up in accordance with the provisions of the statute under which it is constituted. However, in contrast to sub-regulations (2), (3) and (4), sub-regulation (1) of Regulation 29 which addresses the winding up of an AIF set up in the form of a trust, does not state that an AIF set up as a trust shall be wound up in accordance with the provisions of the Trusts Act.

As per Sub-regulation (1) of Regulation 29, an AIF set up as a trust may be wound up on the following grounds:

a) when the tenure of the AIF or all schemes launched by the AIF, as mentioned in the AIF's placement memorandum ("**PPM**") is over; or
b) when the trustee(s) of the AIF are of the opinion that the AIF should be wound up in the interests of investors in the AIF; or
c) if seventy five percent of the investors of the AIF by value of their investment in the AIF pass a resolution at a meeting of unitholders that the AIF be wound up; or
d) if SEBI directs that the AIF be wound up in the interests of investors.

The grounds for winding up an AIF set up as a trust given in Sub-regulation (1) of Regulation 29 are almost identical to that given in Sub-regulation (2) of Regulation 29 for the winding up of an AIF set up as an LLP. Three out of the four grounds mentioned in sub-regulation (1) are mentioned in sub-regulation (2) as well and the only missing ground is the one given in Regulation 29(1)(b), which allows the trustee(s) of an AIF to wind up the AIF if they are of the opinion that it would be in the interests of the investors in the AIF to do so. Since an AIF set up as an LLP would not have any trustee or any equivalent body, it stands to reason that this ground should be omitted.

In the case of an AIF set up in the form of a company, sub-regulation (3) of Regulation 29 merely states that such an AIF shall be wound up in accordance with the provisions of the Companies Act, 2013, but does not prescribe the grounds for the winding up. Similarly sub-regulation (4) of Regulation 29 states that an AIF set up as a body corporate shall be wound up in accordance with the provisions of the statute under which it is constituted without specifying grounds for the winding up. The AIF Regulations do not provide that the board of directors of an AIF set up in the form of a company may wind up the AIF if they are of the opinion that it would be in the interests of the investors in the AIF to do so, even though the board of directors of a company has a fiduciary duty towards the company and its shareholders and such duty is comparable to that of the trustee of a trust.

SEBI's final order in the matter of ***Urban Infrastructure Venture Capital Fund***[1] dated October 31, 2022 is worth exploring in detail here, since it illustrates a scenario in which SEBI may direct a fund to wind up its activities.

Urban Venture Capital Fund ("**UIVCF**") was set up in the nature of a trust and was registered with SEBI as a Venture Capital Fund ("**VCF**"). The settlor of the fund was Urban Infrastructure Venture Capital Limited ("**UIVCL**") and the trustee of the fund was Urban Infrastructure Trustees Limited ("**UITL**"). SEBI conducted an inspection on UIVCF in February 2021 and noted that even though the term of the scheme floated by UIVCF ("**Scheme**") (including extensions) had expired on June 7, 2015, investments amounting to Rs. 1060.92 crore were yet to be liquidated by the Scheme and to be repaid to investors. On an examination of SCORES (SEBI's online portal for investors' complaints redressal), it was noted that three complaints had been received against the Scheme, two of which alleged that the Scheme had not been wound up and the investor's capital contribution had not been refunded. Based on this, SEBI issued a show cause notice to UIVCF as to why suitable direction should not be passed against the trustee and investment manager of UIVCF for violation of Regulation 23(1)(a) of the SEBI Venture Capital Funds Regulations, 1996 ("**VCF Regulations**").

It is to be noted that the VCF Regulations were the precursor to the AIF Regulations and Regulation 23(1) of the VCF Regulations is similar to Regulation 29(1) of the AIF Regulations. Regulation 23(1) of the VCF Regulations provides that a scheme of a VCF set up as a trust

[1] WTM/SM/AFD-1/AFD-1-SEC/20965/2022-23.

shall be wound up when the period of the scheme, if any, mentioned in the PPM is over. However, unlike in the case of the AIF Regulations, the VCF Regulations do not provide for any extension of the term of a VCF even with the consent of investors.

In response to the show-cause notice, UIVCL and UITL, in their common reply dated June 25, 2021 submitted that due to several impediments such as global financial crisis, delay and slow moving regulatory approval, short funding from developers, high interest rates and construction cost etc., by the end of the tenure of the Scheme in June 2015, the Scheme could return only Rs. 621 crore (25.5% of the fund corpus) to the investors. Further, the agency engaged by them to expedite exit was of the view that any effort to sell investments within fixed timelines would cause severe erosion in their value and that it expected the market conditions to improve later. Hence, the investment manager decided that liquidation of investments or in-specie distribution of investments would result in substantially depressed realization from the investments and were not in the interest of the investors. Thereafter, consent of more than 75% of the investors was obtained, for extension of the tenure of the Scheme till December 31, 2016. The Scheme distributed a further amount of Rs. 632 crores to its investors from June 2015 till December 2016. Since then, UIVCF had made numerous efforts to liquidate the assets of the Scheme including exploring the possibility of in-specie distribution amongst the investors. However, UIVCF faced a lot of impediments in the form of demonetization (in November 2016), implementation of Real Estate (Regulation and Development) Act, 2016 and introduction of Goods & Services Tax (in 2017), litigation, Covid-19 etc. due to which UIVCF was unable to liquidate its assets. Despite all this, the Scheme was able to distribute an additional Rs. 701 crores to investors till July 2018. It was submitted that since 2017, the Scheme had been in liquidation stage for orderly exit as per the PPM.

The SEBI held as follows:

1) On a reading of the provisions of VCF Regulations, it is clear that the Scheme was required to be wound up within three months from the date of intimation of the intention to wind up the Scheme.
2) Liquidation of the assets of the Scheme within the prescribed timeline was not impossible but was economically unfeasible. Avoidance of loss could not be a valid ground for not complying with the mandatory obligation prescribed under VCF Regulations.
3) The PPM contained disclosures of adequate and material risk factors and the investors in the Scheme were sophisticated (individual investment of minimum Rs. 1 crore or more). Thus, it was reasonable to infer that they had invested in the Scheme knowing very well the associated risks involved in a real estate scheme and were aware that there was a possibility of loss.
4) In the absence of any provision in law or any customary/market practice, it may not be an appropriate interpretation of the law to state that a scheme that had invited investors to invest in the fund promising it to have a definite lifespan, could be permitted to continue to exist in perpetuity only on the ground that any exit that may be provided to the unit holders, may not be profitable to them at the time of their exit.

On the basis of the above, SEBI held that "*By not winding up the Scheme of the Fund within the prescribed time frame, UIVCL and UITL and their respective directors have not only impaired the rights of its investors but the protracted and never ending time taken by UIVCL and UITL and their respective directors to wind up the Scheme of the Fund by taking various pleas, completely oblivious to their obligation to do so quickly and promptly in compliance with the VCF Regulations, sends a wrong signal to the other market entities/ intermediaries. As a regulator of the capital markets, SEBI has the duty to safeguard the interest of investors and protect the integrity of the securities market. Since the conduct of UIVCL and UITL and their respective directors, is not in the interest of investors in the securities market, appropriate*

directions need to be issued against them, else it may lead to loss of investors' trust in the securities market."
SEBI passed a direction that UIVCF, UIVCL and UITL shall ensure that the Scheme is wound up by providing exit to its investors within a maximum period of 3 months from the date of the order.

III. Processes involved in winding up an AIF and surrendering the certificate of registration

Intimation to SEBI and distribution of proceeds

Regulation 29(5) states that the trustees or trustee company or the Board of Directors or designated partners of the AIF, as the case maybe, shall intimate SEBI and investors of the AIF of the circumstances leading to the winding up of the AIF. Regulation 29(6) states that once such intimation under Regulation 29(5) has been sent to SEBI and the investors of the AIF, no further investments shall be made on behalf of the AIF so wound up. Regulation 29(7) fixes a time limit of one year from the date of intimation under Regulation 29(5) for liquidating the assets of the AIF and distributing the proceeds of such liquidation to the AIF's investors after satisfying all liabilities of the AIF. Instead of liquidating its assets, an AIF may choose to make an in-specie distribution of the AIF's assets, provided such distribution receives the prior approval of at least seventy five percent of the investors by value of their investment in the AIF and is also in compliance with requirements, if any, in the PPM and contribution agreement/subscription agreement for any specie distribution of assets.

Surrender of certificate of registration

Regulation 29(9) states that upon winding up of an AIF, the certificate of registration issued to such AIF by SEBI shall be surrendered to SEBI. In practice, after the assets of the AIF have been distributed to its investors, either in cash after liquidation or in-specie, the trustee of the AIF will write to SEBI and state that its registration as an AIF is being surrendered. Post such symbolic surrender, SEBI will cancel the registration of the AIF and the name of the AIF will be removed from the list of AIFs registered with SEBI, as displayed on SEBI's website.

Documents to be submitted to SEBI for surrender of certificate of registration

On March 23, 2022 SEBI issued the "FAQs for applications filed by AIFs with SEBI for their post registration activities" ("**FAQs**"). These FAQs endeavor to provide ease of doing business to AIFs by collating and specifying the relevant information/documents to be submitted to SEBI, which would ensure timely processing of applications at SEBI.

The FAQs address various post-registration activities including the surrender of the certificate of registration. Section 3.3 of the FAQs contains a list of documents that must be submitted by an AIF to SEBI, for surrendering its certificate of registration as an AIF. The list is quite comprehensive and requires various declarations/undertakings to be given by the manager/trustee of the AIF, such as a declaration that assets of the AIF have been liquidated and distributed to unit holders and that no further investments shall be collected by the AIF after its winding up.

Following are the documents that an AIF has to submit to SEBI (by uploading scanned copies on SEBI's portal) to receive SEBI's approval for the surrender of the AIF's certificate of registration:

a) duly signed application/cover letter giving the details of the surrender of registration of the AIF and rationale for the same;

b) self-attested copy of a board resolution or partner resolution or a copy of the resolution passed by trustee, depending upon the legal structure of the AIF;
c) duly signed and stamped declaration from the AIF's investment manager and a practicing chartered accountant that the AIF has liquidated all its assets and distributed proceeds to unit holders proportionately specifying the amounts realized by liquidation of the AIF's assets and its distribution to the unit holders;
d) duly signed and stamped declaration from the investment manager that the AIF is wound up and is not undertaking any AIF activity and shall not accept any further investments for the AIF;
e) duly signed and stamped declaration from the investment manager that it shall continue to be responsible for any liabilities, in relation to its investment management activities;
f) duly signed and stamped declaration from the AIF's investment manager and trustee that no enquiry or proceeding or any other action has been initiated or is currently pending against the AIF;
g) duly signed and stamped declaration from the AIF's investment manager and trustee that the AIF has complied with the AIF Regulations with regard to winding up;
h) duly signed and stamped declaration from the AIF's investment manager and trustee that all schemes of the AIF have been wound up;
i) self-attested latest bank statement of the AIF/latest audited financial accounts of the fund/schemes;
j) tenure/duration of the fund is to be specified; and
k) original certificate of registration of the fund (*which has to be submitted to SEBI in physical form*).

Maintenance of records post winding up

Under Regulation 27(1), the manager or sponsor of an AIF is required to maintain certain records in relation to the AIF, such as a description of the assets under the scheme, valuation policies and investment strategy. Regulation 27(2) of the AIF Regulations require AIFs to maintain the afore-mentioned records for a period of five years after the winding up of the AIF. In case of an AIF set up in the form of a trust, the trustee would ensure compliance with this requirement. In case of an AIF set up in the form of a company or an LLP, it is unclear how this requirement can be complied with, other than by entrusting the records of the AIF to a third-party escrow agent for a period of five years, with instructions to comply with any regulatory requests for information and to destroy such records after five years.

Compliances required until the certificate of registration is cancelled by SEBI

Even after an AIF has exited from its investments and returned the investment proceeds to its investors, the AIF would be required to continue doing the following, until SEBI accepts the surrender of its certificate of registration and removes it from the register of AIFs:

a) file quarterly returns with SEBI;
b) carry out an annual audit of their PPMs as required by SEBI circular bearing number SEBI/HO/IMD/DF6/CIR/P/2020/24 dated February 5, 2020; and
c) prepare an annual compliance test report.

Would a state of dormancy help?

The time taken for SEBI to cancel an AIF registration and remove such AIF's name from its register of AIFs, after receiving the surrender request, varies from AIF to AIF. Occasionally, SEBI makes enquiries and seeks information from the AIF's trustee and investment manager before cancelling the AIF's registration. Until SEBI accepts the surrender of the certificate of registration and removes the AIF's name from the register of AIFs, the AIF must continue to

file quarterly returns with SEBI, carry out an annual audit of its PPM and prepare an annual compliance test report.

Therefore, it would make logical sense for AIFs to be allowed to remain, after winding up, in a state of dormancy, whereby, the AIF may retain its certificate of registration but is not required to fulfill the compliances mentioned above. However, at the moment, SEBI regulations do not allow AIFs to remain in such a state of dormancy. It is hoped that SEBI may modify the AIF Regulations to permit AIFs to go "dormant" after the AIF has returned its investment proceeds to its investors (or made an in-specie distribution) and has applied to SEBI for surrender of its certificate of registration until SEBI accepts such surrender and removes the AIF from the register of AIFs.

Surrendering the PAN and TAN

As a general practice, even after SEBI accepts the surrender of an AIF's certificate of registration, the trustee does not cancel/surrender the AIF's PAN[2] or TAN[3] until all tax related matters, including disputes with the tax department and liabilities are settled, and refunds, if any expected, are received.

Executing a deed of dissolution

After an AIF's PAN and TAN are cancelled, it is common for the trustee to execute a deed of dissolution, to record the dissolution of the trust.

IV. Winding up of a Scheme versus Winding Up of the AIF

The AIF Regulations do not prescribe any procedure to be followed when a scheme of an AIF is being wound up. Schemes of an AIF have a fixed tenure and terminate when such tenure ends, unless extended by the unitholders in accordance with the AIF Regulations and the PPM. Regulation 29 provides for winding up of an AIF as a whole and one of the grounds for winding up an AIF under Regulation 29 is '*when the tenure of the Alternative Investment Fund or all schemes launched by the Alternative Investment Fund, as mentioned in the placement memorandum is over*'. Regulation 29(5) requires the trustees or trustee company or the board of directors or designated partners of the AIF, as the case maybe, to notify SEBI and the investors of the AIF of the circumstances leading to the winding up of the AIF. There is no requirement under the AIF Regulations to notify SEBI or the investors of the AIF when a scheme of an AIF is being wound up.

V. Extinguishment of Trusts Under the Trusts Act

Under the Trusts Act, the term "extinguishment" is used in a manner akin to the phrase "winding up" under the Companies Act, 2013. We have analysed below the relevant provisions of the Trusts Act relating to extinguishment of trusts.

Section 77 of the Trusts Act lists the various circumstances when a trust is extinguished:

> *"(a) when its purpose is completely fulfilled; or*
>
> *(b) when its purpose becomes unlawful; or*

[2] Permanent account Number, which is allocated by the income tax department.
[3] Tax Deduction Account Number or Tax Collection Account Number, which is allotted to all persons who are responsible for deducting tax at source (TDS) or who are required to collect tax at source (TCS).

(c) when the fulfillment of its purpose becomes impossible by destruction of the trust-property or otherwise; or

(d) when the trust, being revocable, is expressly revoked."

The AIF Regulations do not require an AIF set up as a trust to be extinguished when its term expires or if it is to be wound up for any other reason. However, if all the schemes an AIF have been wound up as per the procedure given under the AIF Regulations, including the surrender of its certificate of registration to SEBI, it may be said that its purpose is completely fulfilled for the purposes of Section 77(1) of the Trusts Act, and hence the trust stands extinguished. However, the Trusts Act does not prescribe any procedure for recording the extinguishment of a private trust. As mentioned above, it is common for the trustee to execute a deed of dissolution, to record the dissolution of the trust, though this is not required by the Trusts Act and every trust stands extinguished as soon as its purpose is fulfilled, even if a deed of dissolution is not executed.

Section 78 of the Trusts Act discusses the various ways in which a trust may be revoked. Section 78 reads as follows:

"A trust created by will may be revoked at the pleasure of the testator.

A trust otherwise created can be revoked only--

(a) where all the beneficiaries are competent to contract-by their consent;

(b) where the trust has been declared by a non-testamentary instrument or by word of mouth-in exercise of a power of revocation expressly reserved to the author of the trust; or

(c) where the trust is for the payment of the debts of the author of the trust, and has not been communicated to the creditors-at the pleasure of the author of the trust."

An AIF set up in the form of a trust is usually an irrevocable trust, for tax reasons and for the practical purpose of inspiring confidence in investors, though the AIF Regulations do not expressly require the trust to be irrevocable. Regulation 29(1)(c) of the AIF Regulations specifically state that an AIF can be wound up if seventy five percent of its investors (by value of their investment) pass a resolution at a meeting of unitholders that the AIF be wound up. The aforesaid Regulation 29(1)(c) appears to contradict Section 78(a) of the Trusts Act which requires the consent of all beneficiaries of an irrevocable trust to extinguish it. However, this apparent contradiction can be resolved if we take into account the fact that all investors in an AIF, at the time of investing in the AIF, are deemed to have knowledge of Regulation 29(1)(c) of the AIF Regulations which allows the AIF to be wound up with the consent of seventy five percent of its investors, by value of their investment in the AIF, which winding up would lead to extinguishment of the trust.

VI. Case law on extinguishment of trusts under the Trusts Act

In the case of *Amrit Lal Kohli* v. *Harbans Lal Kohli*[4], the plaintiff, a father of three children had set up a trust by way of a trust deed dated January 22, 1966. The primary objective of the trust was to provide for the three children, who were minors at the time of setting up the trust, with income from the trust property, and to place them in a position where they could support themselves. The trustees of the trust, who were two of the defendants in this case, had

[4] Amrit Lal Kohli v. Harbans Lal Kohli, AIR 2001 Del 24.

expressed their unwillingness to manage the trust, on account of their old age. The Court, taking into consideration the fact that one of the sons had passed away and the other two had attained majority, declared that the purpose of the trust had been fulfilled and the trust stood extinguished.

It is to be noted that while the Court held that the trust stood extinguished since its purpose had been fulfilled, the Court did not specifically refer to Section 77(a) of the Trusts Act.

In the case of *Princess Usha Trust* v. *CIT*[5], a trust was settled by Maharaja Yeshwantrao Holkar in 1950 ("**Trust**") for the benefit of his daughter Usha. The trust deed provided that after Usha's demise, the Trust properties would be divided, transferred and handed over to Usha's children. However, post the settlor's demise, Usha decided to transfer the remainderman's interest of her two minor children to an educational trust. Usha obtained a court order and settled an educational trust ("**Educational Trust**") by transferring her interest from the Trust. Usha also executed a deed of declaration settling in favour of the Educational Trust, the interest of the minors in the Trust.

When the Trust declared its income as nil for two assessment years, the income tax department held that the transfer of the interests of Usha and her children to the Educational Trust was void and took the matter to court. The High Court of Madhya Pradesh upheld the transfer of the beneficial interest in the Trust property to the Educational Trust, and further held that it had become impossible to fulfil the objectives of the Trust, which were to pay Usha the income from the Trust property during her lifetime and to transfer the Trust property to her children, after her demise. Relying on the term "otherwise" in Section 77(c) of the Trusts Act, the court declared the Trust as extinguished since the interest of all the beneficiaries had been validly transferred.

Applying the principles set out in the afore-mentioned cases, would it be possible for an AIF, which has been set up in the form of a trust, to stand extinguished, without any act on part of the trustee(s) or beneficiaries, in the following circumstances:

i. the AIF has exited from all its investments and has distributed the exit proceeds to its investors; or
ii. the AIF's investments have lost their value and have become worthless.

If prior to the expiry of its term, an AIF set up in the form of a trust exits from all its investments and distributes the exit proceeds to its investors but takes no formal action to wind up the trust, it may be argued that the purpose of the trust has been fulfilled and the trust stands extinguished as per Section 77(a) of the Trusts Act. However, it is very unlikely that a trustee of an AIF, especially a corporate trustee, would not take formal steps for the winding up of the AIF, if the AIF has exited from its investments and returned the investment proceeds to its investors. Such a formal step would involve a simple resolution passed by the board of directors of the trustee company to the effect that the trustee of the AIF is of the opinion that the AIF should be wound up in the interests of investors in the AIF.

If prior to the expiry of its term, an AIF's investments have lost their value and have become worthless, it may be argued that the fulfillment of the trust's purpose has become impossible due to the destruction of the trust-property and hence the trust stands extinguished as per Section 77(c) of the Trusts Act. However, as mentioned earlier, sub-regulation (1) of Regulation 29, states that an AIF set up as a trust may be wound up only on occurrence of one the four grounds mentioned in Regulation 29(1). Therefore, in the unlikely event that the

[5] Princess Usha Trust v. CIT, 1983 SCC OnLine MP 187.

trustee of such an AIF takes no formal action to wind up the AIF, such AIF may not be considered to be wound up.

In the case of *Anam Premkumar Reddy* v. *India Fruits Limited*[6] , the question before the court was whether a trust holding the shares of a company was extinguished by virtue of the value of the shares of the company being less than the amount of the loan and the interest outstanding. The counsel for the settlor-respondent strived to prove that 'destruction of the trust property or otherwise' in Section 77(c) of the Trusts Act would include a case where the value of the property was so reduced that there was nothing available for maintaining the corpus of the trust. However, the court distinguished the present case from the case of Princess Usha Trust v. CIT (*mentioned above*), because in the latter, after distributing the trust property, nothing remained in the corpus thereby making fulfilment of the object of the trust impossible whereas in the present case, the trust property was still in existence. According to the court, the term 'destruction' would imply that the property has ceased to exist and is no longer accessible for distribution. Therefore, 'otherwise' must also be read *ejusdem generis* so that, regardless of the procedure, the trust property itself is either nonexistent or essentially unavailable. In the present case, since the shares were actually in existence, though adversely affected by debt, it could not be stated that the property did not exist or that it was impossible for the trust's purpose to be fulfilled. Unless the shares are actually liquidated, it is not possible to assume that the trust has become extinguished solely on the ground that on that date, the estimated value of the shares was less than the outstanding liability of such company.

VII. Post- winding up liabilities

Potential liabilities post winding-up

One of the biggest challenges when winding up an AIF is to make provisions for liabilities that may arise after the AIF has been liquidated and the proceeds returned to its investors. Some of most common liabilities that may arise post-winding-up are tax liabilities and indemnity claims from entities that acquired assets (such as shares of portfolio companies) from the AIF before it was wound-up. It is common for AIFs to enter into share purchase agreements or other similar contracts ("**SPA**") to dispose of or to exit from their portfolio investments. Such SPAs usually require the seller (the AIF, in this instance) to provide representations and warranties to the buyer regarding the portfolio company and its assets and also offer indemnities to cover any breach of such representations and warranties. It is possible that an indemnity claim may arise under such SPAs after the winding up of the AIF.

Limitation period for income tax claims

Section 148 of the Income Tax Act, 1961 ("**Income Tax Act**") provides for the issue of a notice by the income tax department where income has escaped assessment. Section 149 of the Income Tax Act provides that a notice under section 148 can be issued for the relevant assessment year within ten years from the end of the relevant assessment year. Therefore, an AIF's trustee may receive a tax notice anytime within 10 years after its final exit or distribution of exit proceeds to its investors.

Role of trustee as a representative assessee

The trustee of an AIF set up as a determinate trust will be treated as a "representative assessee" as per Sections 160 to 162 of the Income Tax Act and such trustee shall be required to discharge the tax liability of each beneficiary of the trust.

[6] Anam Premkumar Reddy v. India Fruits Limited, 1995 SCC OnLine AP 350.

VIII. Solutions currently in vogue to manage post- winding up liabilities

Investor claw back

Because trusts are essentially pass-through vehicles, if any liability arises after the extinguishment of a trust, the beneficiaries of the trust, that is, the investors of the AIF, may be on the hook to the extent of the trust funds that they received at the time of winding up of the trust. The PPM of many AIFs contain clauses that specifically permit the AIF's investment manager or trustee to require the investors in the AIF to return distributions made to the investors, in order to satisfy the investors' pro-rata share of any obligations or liabilities of the AIF. This obligation is usually capped at the investor's relevant capital commitment. These clauses, referred to as "Clawback" or "Giveback" clauses, usually state that they shall continue to apply after the termination or dissolution of the AIF.

Provisioning for post winding-up liabilities

Usually when an AIF is being wound up, the trustee retains a portion of the corpus of the relevant scheme(s) until it is clear that no further liabilities can arise, at which point, the retained corpus is distributed to the investors of the scheme. The trustee may require an indemnity from the investment managers or sponsors of AIFs to cover any liability that they may incur after the winding up of the AIF.

IX. A crying need for better coordination between SEBI and the income tax department

If wishes were horses, AIFs would be able to, after exiting from their portfolio investments, immediately return all monies to their investors without retaining any reserve to meet potential tax claims, wind up and surrender their certificate of registration to SEBI, and not worry about income tax claims arising after exit proceeds have been returned to investors. In an ideal world, once the board of directors of the AIF's trustee company passes a resolution to wind up the AIF, the income tax department would work expeditiously to process all pending income tax claims relating to such AIF. However, such a situation calls for much greater coordination and cooperation between SEBI and the income tax department than what is currently in place. The need of the hour is for SEBI and the income tax department to work together and put in place a fair and efficient process for taxation of AIFs. It is also hoped that, in the near future, statutory amendments to the Income Tax Act would shorten the limitation period within which the income tax department can issue claims against an AIF.

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