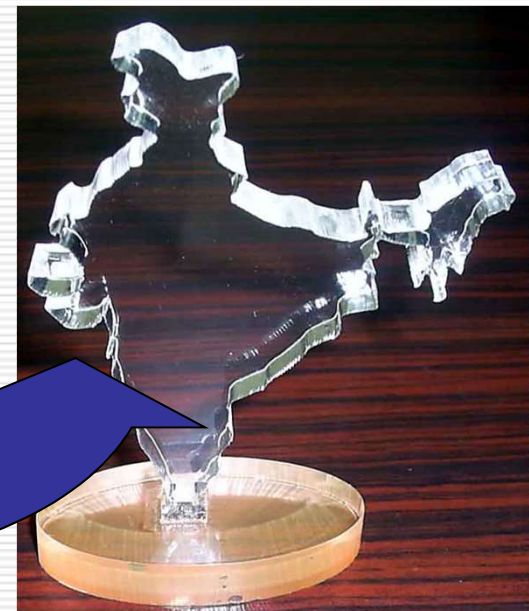


Foreign Direct Investment & Foreign Investment – Schedule I, IV and VI

J. B. Nagar CPE Study Circle of WIRC of ICAI
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Understanding Foreign Investment & Foreign Direct Investment

- Foreign Investment is a Capital Account Transaction - resulting in creation of asset for NR in India
- FI provisions are now governed by Non Debt Instrument (NDI) Rules, 2019 , these rules are in.....
- Supersession of FEM- TISPRO Regulations, 2017
- Changes due to powers relating to non debt rules now shifted from RBI to CG by virtue of Sec 6(2a)

Understanding FI & FDI in terms of NDI Rules

Definitions	Particulars
Rule 2(s) Foreign Investment	<p>Any investment made by a person resident outside India on repatriable basis in -</p> <ul style="list-style-type: none"> ➤ Equity Instruments of an Indian Company; or ➤ to the capital of an LLP. <p>(Explanation: If declaration is made by person as per provisions of Companies Act, 2013 about a beneficial interest being held by a PROI, then even though investment is made by a resident Indian citizen, the same shall be counted as Foreign Investment).</p> <p>Note: PROI may hold Foreign Investment either as FDI or FPI in any particular Indian Company.</p>
Rule 2(r) - Foreign Direct Investment (FDI)	<p>Investment through Equity Instruments by PROI -</p> <ol style="list-style-type: none"> a. In an unlisted Indian Company; or b. In 10% or more of post issue paid up capital on fully diluted basis of a listed Indian Company. <p>(Note: In case of existing investment by PROI in equity instruments of listed company, falls below 10% of post issue paid up capital, it shall continue to be treated as FDI). Non Repatriable Investment therefore is not FDI</p>



Types of FI from diff perspectives

■ From Sector Specific-

- Prohibited (chit fund, RE tdg, lottery..)
- Upper cap on sector(Print media only 26)
- Full Approval (print media, titanium mining-permissible 100% but approval), neighbouring countries
- Part Approval (Defence- 49% automatic)
- Automatic- say Software...

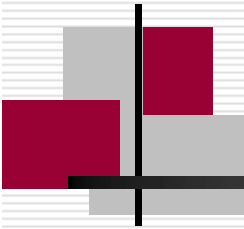
From- Repatriability

- Repatriable
- Non Repatriable (available only to NRI/OCI & entity majorly owned by them)



Types of FI

- From Characterization
- FDI (only capital instruments)
- Portfolio Investment
- Inv in LLP
- Inv in Partnership/Proprietorship (only to NRI/OCI)
- Inv by VC



OECD Benchmark definition of FDI

- *Direct investment is a category of cross-border investment associated with a resident in one economy having control or a significant degree of influence on the management of an enterprise that is resident in another economy.*
- *It also includes investment in indirectly influenced or controlled enterprise.*
- *Objective of FDI (From Foreword to OECD Benchmark Definition):*

With the right policy framework, FDI can provide financial stability, promote economic development and enhance the well being of societies.



Direct Investment *vs.* Portfolio Investment

Balance of Payment Manual issued by International Monetary Fund:

- Dir Inv is related to control or significant influence and tends to be associated with 'lasting relationship'
- Direct Investor may supply know-how, technology, management & marketing
- Enterprises in direct inv relationship are likely to trade and finance with each other
- *A direct investor is an entity or group of related entities that is able to exercise control or a significant degree of influence over another entity that is resident of a different economy.*



Portfolio Investment

- PI have lesser role in decision making of the enterprise.
- It is associated with financial markets and with their specialized service providers- exchanges, dealers, regulators.
- Definition of PI as per NDI Rules [Rule 2(t)]

Any investment made by a PROI through equity instruments where such investment is -

- *Less than 10% of post issue paid up capital on fully diluted basis of listed company; or*
- *less than 10% of paid up value of each series of equity instruments of a listed Indian Company*



Criteria to determine 'Control' & 'Influence'- as per Balance of Payment manual

- **Immediate direct investment relationships** arise when a direct investor directly owns equity that entitles it to **10 percent or more of the voting power** in the direct investment enterprise.
- **Control** is determined to exist if the direct investor owns more than 50 percent of the voting power in the direct investment enterprise.
- A **significant degree of influence** is determined to exist if the direct investor owns from 10 to 50 percent of the voting power in the direct investment enterprise.



FEMA Regulations for FDI

- FEMA 1999 amended by Finance Act of 2015 to realign powers between Central Government (CG) and RBI.
- Debt and Non Debt Instruments notified by CG vide notification dated 16th October 2019.
- The CG notification dated 17th October 2019 introduced The Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 which superseded FEMA Notification No. 20R.
- **Two new regulation notified** by RBI on 17th October 2019 – FEMA Notification 396 Non Debt Instruments Regulations 2019 and FEMA Notification No. 395 Mode of Payment and Reporting of NDI Regulations 2019.
- RBI Master Direction and FAQs.



Relevance of Press Note & Release

- FAQ of RBI
- Q.47: Whether foreign investment can be made based on the press note/ FDI policy?
- Answer: Foreign investment can be made based on a notification issued under FEMA, 1999.



Debt and Non Debt Instruments - Notification dated 16th October 2019

Debt Instruments:

- i. Government Bonds
- ii. Corporate Bonds
- iii. All tranches of securitization structure which are not equity tranche
- iv. Borrowings by Indian firms through loans
- v. Depository receipts whose underlying securities are debt instruments

Non Debt Instruments:

- i. All investments in **equity** in incorporated entities (public, private, listed and unlisted).
- ii. Capital participation in LLPs**
- iii. Instruments of investment in FDI Policy
- iv. Investment in units of AIFs, REITs and InVITs.
- v. Investment in **Mutual Funds and ETFs** which invest more than 50% in equity.
- vi. Acquisition, sale or dealing directly in immovable property.
- vii. Contribution in trusts
- viii. Depository receipts issued against equity instruments.

All other instruments which are not notified as Debt or Non Debt instruments shall be deemed as Debt Instruments.



Chapters of NDI Rules 2019

Chapter	Rules	Particulars
Chapter I	1 and 2	Preliminary and Definitions
Chapter II	3, 4 and 5	General Conditions applicable to all investors
Chapter III	6, 7, 8 and 9	Investments by Person Resident Outside India (PROI)
Chapter IV	10 and 11	Investment by Foreign Portfolio Investors (FPI)
Chapter V	12 and 13	Investment by NRI/OCI
Chapter VI	14 and 15	Investment by other NR Investors
Chapter VII	16 and 17	Investment by Foreign Venture Capital Investor (FVCI)
Chapter VIII	18 to 23	General Provisions: Issue of Convertible notes by Start-up, merger or demerger or amalgamation of Indian Companies, reporting requirements, downstream investments, pricing guidelines, remittance of sales proceeds
Chapter IX	24 to 33	Acquisition and Transfer of Immovable Property in India



Schedules of NDI Rules 2019

Schedules	Particulars
I [Rule 6(a)]	Purchase or Sale of Equity Instruments of Indian Company by a PROI
II [Rule 10(1)]	Investment by Foreign Portfolio Investors
III [Rule 12(1)]	Investment by NRI/OCI on repatriation basis
IV [Rule 12(2)]	Investment by NRI/OCI on non-repatriation basis
V [Rule 14]	Investment by other NRs
VI [Rule 6(b)]	Investment in Limited Liability Partnerships (LLPs)
VII [Rule 16]	Investment by FVCI
VIII [Rule 6(c)]	Investment by a PROI in an investment vehicle
IX [Rule 6(d)]	Investment in Depository Receipts by a PROI

NDI Rules 2019 - Important Definitions

Definitions	Particulars
Rule 2(k) - Equity Instruments	<p>Equity Instruments means Equity Shares, Convertible Debentures, Preference Shares and Share Warrants issued by an Indian Company.</p> <p>Explanation:</p> <p>(i) Equity Shares in accordance with provisions of Companies Act 2013 shall include partly paid shares also.</p> <p>“Convertible Debentures” means fully, compulsorily and mandatorily convertible debentures.</p> <p>“Preference Shares” means fully, compulsorily and mandatorily convertible preference shares.</p> <p>Share Warrants are those issued by an Indian Company in accordance with SEBI regulations.</p> <p>Optionality clause possible provided - lock in period of one year or as prescribed for specific sector, whichever is higher and no exit at ‘assured price’</p>

NDI Rules 2019 - Important Definitions

Definitions	Particulars
Rule 2(k) - Equity Instruments (contd...)	<p>(ii) Partly paid shares that have been issued to PROI shall be fully called up within 12 months of such issue or as prescribed by RBI from time to time. Equity. 25% consideration (including share premium) shall be received up front.</p> <p>(iii) In case of share warrants at least 25% consideration shall be received upfront and balance within 18 months of issuance of such share warrants.</p>

Note: Grandfathering of NC/OC/PC - Preference Shares issued up to 30 April 2007 and OC/PC - Debenture issued up to 7 June 2007 which was present in erstwhile FEMA 20 / FEMA 20R not incorporated in NDI Rules 2019.



Extension in period of CCPS

- **FAQ 3 of FDI**
- Whether extension of compulsorily convertible preference shares (CCPS) or compulsorily convertible debentures (CCDs) requires RBI approval?
- Answer: Tenor of convertible instruments will be guided by the instructions framed under the Companies Act, 2013 and the rules framed there under. However, the investee company should ensure that the price/ conversion formula of convertible capital instruments is determined upfront at the time of issue of the instruments. The price at the time of conversion should not in any case be lower than the fair value worked out, at the time of issuance of such instruments, in accordance with the extant FEMA regulations.

NDI Rules 2019 - Important Definitions

Definitions	Particulars
Rule 2(e) Convertible Notes	An instrument issued by a start up company acknowledging receipt of money initially as debt, repayable at the option of the holder, or which is convertible into such number of equity shares of such start up company, within a period not exceeding five years from the date of such issue of the convertible note, upon occurrence of specified events as per the other terms and conditions agreed to and indicated in the statement.
Rule 2(ac) - Investment	To subscribe, acquire, hold or transfer any security or unit issued by a person resident in India. Explanation: a. This will include to acquire, hold or transfer depository receipts issued outside India, the underlying of which is a security issued by a person resident in India. b. For the purpose of LLP , investment shall mean capital contribution or acquisition of profit shares ;

NDI Rules 2019 - Important Definitions

Definitions	Particulars
Rule 2(t) Foreign Portfolio Investment (FPI)	Any investment made by a PROI through equity instruments where such investment is - <ul style="list-style-type: none"> ➤ Less than 10% of post issue paid up capital on fully diluted basis of listed company; or ➤ less than 10% of paid up value of each series of equity instruments of a listed Indian Company.
Rule 2(m) FDI linked performance conditions	The sector specific conditions specified in Schedule I of NDI Rules for companies receiving foreign investment.
Rule 2(j) - Employees Stock Option (ESOP)	ESOP means “Employees Stock Option” as defined under Companies Act 2013 and issued under regulations issued by SEBI. (As per Rule 8 scheme can be either as per SEBI regulations or as per Companies Act 2013)

NDI Rules 2019 - Important Definitions

Definitions	Particulars
Rule 2(am) - Sectoral Cap	<p>The maximum investment including both foreign investment on a <i>repatriation basis</i> by PROI in equity instruments of a company or the capital of an LLP, as the case may be and indirect foreign investment, unless provided otherwise. This shall be composite limit for the Indian Investee entity.</p> <p>Explanation:</p> <p>(i) FCCBs and DRs having underlying of instruments being in nature of debt shall not be included in the sectoral cap.</p> <p>(ii) Any equity holding of a PROI resulting from conversion of any debt instrument under any arrangement shall be reckoned under the sectoral cap.</p> <p>(In Annual Return on FLA only NRI holding on repatriation basis is to be mentioned. EMF requires reporting of NRI holding on repatriation basis).</p>



FI, FDI & PI

- FAQ Q.8: Whether the foreign investment will be classified as FDI or FPI based on the schedule under which the investment is being made.

Answer: No, FDI and FPI are agnostic from the point of view of the schedule under which investment has been made. It is the **percentage which defines** whether it is direct or portfolio investment.

- Q.9: For an FPI investment, once the investment is classified as FDI (basis total holding), if the FDI holding comes back to <10%, will the holdings be classified as FPI again?

Answer: Once an FDI always an FDI.

- Issue- additional FDI in listed entity by another group entity & such investment would be less than 10%

Restrictions on Investment by PROI (Rule 3) vs. Restriction on receiving Investment (Rule 4)

Restriction on Investment by PROI - Rule 3	Restriction on receiving Investment - Rule 4
<p>Save as otherwise provided in Act, rules or regulations - - No PROI shall make any investment in India.</p> <p>RBI may on an application made to it and for sufficient reasons and in consultation with CG, permit PROI to make any investment in India subject to such conditions as may be considered necessary.</p>	<p>Save as otherwise provided in Act, rules or regulations - - Indian Entity (i.e. Company or LLP) or - Investment vehicle or - Venture capital fund or - Firm or - Association of Persons or - Proprietary Concern</p> <p>Shall not receive or record any investment in India from PROI. (RBI may on an application made to it and for sufficient reasons and in consultation with CG, permit the same on an application made to it).</p>

Note: FDI in India is entity neutral qua foreign investor.

Portfolio Inv only by registered FPI and NRI/OCI

Non Repatriable Inv only by NRI/OCI or entity majorly owned by them



Compounding Orders on Reg 3 of FEMA 20 (now Rule 3 of NDI Rules)

- C.A. No. 4246/2016 in the case of Marchmont International Finance Ltd., of Mauritius
- Inv on stock market through NRO Account
- Contraventions:
 1. undertaking investments by debit to NRO account without furnishing the necessary undertaking to the AD bank in contravention of Paragraph 1(c) of Schedule 3 of Not 5
 2. Undertaking transaction on Stk Exch through broker without specific permission of RBI- **Reg 3** of Not 20
 3. **Undertaking the secondary market transactions under the PIS although neither being an FII registered with SEBI nor being an NRI in contravention of Regulation 5(2) read with Regulation 5(3) of FEMA 20**
 4. Acquisition of the shares of the Indian companies by debit to its NRO account in contravention of Paragraph 8 of Schedule 1 of FEMA 20 (inward remittance reqd)
 5. Acquisition of the shares of an Indian entity engaged in fin. sector activity without obtaining the necessary NOC from RBI in contravention of erstwhile Regulation 10(A)(b)(v) of FEMA 20



Rule 4 of NDI Rules - Restriction on receiving Investment

- *Save as ... An Indian entity or an investment vehicle, or a VCF or a Firm or AOP or a proprietary concern shall not receive any inv from PROI or record such inv in its books*
- *Provided....(with RBI may permit on an application being made to it....in consultation with CG)*
- This Reg refers to recording of investment or receipt of consideration – otherwise than as prescribed



Investment by PROI in India- Rule 6 of NDI Rules

Rule / Schedule	Particulars
6(1) - Schedule I	<p>PROI can subscribe, purchase or sell equity instruments of Indian Company as per terms and conditions of Schedule I.</p> <p>Prior Government Approval is required for investment by an entity of country which shares land border with India or beneficial owner of an investment into Indian is situated in or is a Citizen of any such country</p> <p>Citizen of Pakistan or entity incorporated in Pakistan shall investment only under government route in sectors other than cannot defence, space, atomic energy and such other sectors or activities prohibited for foreign investment.</p> <p>In event of any transfer of ownership of an existing or future FDI in an entity in India, directly or indirectly resulting in beneficial ownership falling within restriction or purview of above provisos, such subsequent change or beneficial ownership shall also require government approval.</p>



Investment by PROI in India- Rule 6 of NDI Rules

Rule / Schedule	Particulars
6(2) - Schedule VI	PROI, other than citizen of Bangladesh or Pakistan or an entity incorporated in Bangladesh or Pakistan, may invest either by way of capital contribution or by way of acquisition or transfer of profit shares of a LLP, as per terms and conditions of Schedule VI.



Right Issue - Rule 7 of NDI Rules

PROI having investment in an Indian Company may make investment through rights issue provided -

- Offer is in compliance of Companies Act 2013
- It does not result in breach of sectoral cap
- Shareholding on basis of which rights issue made must have been acquired and held as per the provisions of these rules.
- Listed Company - Rights to PROI shall be at price determined by the Company.
- Unlisted Company - Rights to PROI shall not be at price less than the price offered to person resident in India.
- Mode of payment and attendant conditions for such transactions shall be prescribed by RBI.



Right Issue - Rule 7 of NDI Rules

- Individual PROI exercising right which was acquired when such individual was resident, shall holding instruments on non-repatriation basis.

Rule 7A - Acquisition after renunciation of rights:

PROI who has acquired right from resident person who has renounced it may acquire equity instruments (other than share warrants) as per pricing guidelines under Rule 21 of NDI Rules.



Right Issue - Rule 7 of NDI Rules

FAQs on Right Shares:

Q.21: Can a foreign investor invest in Rights shares issued by an Indian company at a discount?

Answer: There are no restrictions under FEMA for investment in Rights shares issued at a discount by an Indian company under the provisions of the Companies Act, 2013. The offer on rights basis to the persons resident outside India shall be:

- a. in case of shares of a company listed on a recognized stock exchange in India, at a price, as determined by the company; and
- b. in case of shares of a company not listed on a recognized stock exchange in India, at a price, which is not less than the price at which the offer on right basis is made to resident shareholders.



ESOPs and Sweat Equity Shares – Rule 8 of NDI Rules

- Permissible to Indian Company to issue ESOP/Sweat equity shares to its employees/directors or employees/directors of its holding company or *joint venture* or wholly owned overseas subsidiary/subsidiaries who are PROI.
- Scheme is either as per SEBI Regulations or Companies Act 2013.
- ESOP/Sweat Equity Shares shall be in compliance with sectoral caps
- **FAQ:**

Q.13: Whether the percentage of foreign investment should be calculated at the time of issuance of Employee Stock Options (ESOP) or vesting stage or exercising stage?

Answer: Foreign investment percentage has to be calculated on a fully diluted basis i.e. at the time of issuance of Employee Stock Options.

Transfer of Equity Instruments - Rule 9 of NDI Rules

Rule	Transfer Between	Mode of Transfer	Automatic/ Approval
9(1)	PROI (not NRI/OCI/OCB) to PROI	Sale or Gift (includes liquidation, merger, de-merger, amalgamation of entities or companies outside India)	Automatic Route *
9(2)	PROI to PRII	Sale or Gift (subject to pricing guidelines and reporting except when PROI holds on non-rep basis)	Automatic Route *
9(3)	PRII to PROI	Sale (adherence to entry routes, sectoral caps, pricing guidelines and other attendant conditions)	Automatic Route *

* Prior Government approval will be required for any transfer in case the company is engaged in sector which requires government approval.

Transfer of Equity Instruments - Rule 9 of NDI Rules

Rule	Transfer Between	Mode of Transfer	Automatic/ Approval
9(4)	PRII to PROI	Gift (with prior approval of RBI - 5% of paid up capital of Indian company / each series of debentures and aggregate ceiling of USD 50000 per financial year per donor)	Prior approval
9(5)	<p>PROI holding capital instruments containing optionality clause and exercising option/right, may exit without any assured return subject to pricing guidelines and lock in period of 1 year or as prescribed whichever is higher.</p> <p>Tata Teleservices and NTT Docomo matter - - "Damage" vs. "Assured return" - Over indebted countries often see run on their currency.</p>		

Transfer of Equity Instruments

- Rule 9 of NDI Rules

Rule	Transfer Between	Mode of Transfer	Automatic/A approval
9(6)	Transfer on deferred payment basis between PRII to PROI: - An amount not exceeding 25% can be paid on deferred basis within 18 months from date of transfer agreement. - can be settled through escrow account.		
9(7)	Transfer between PRII and PROI: -PROI may open an escrow account as per Deposit Regulations. -It may be funded by inward remittance through banking channels and / or by way of guarantee issued by an AD Bank.		
9(8)(i)	Pledge of Equity Instruments: -Promoter of a company which has raised ECB may pledge shares of borrowing company or that of its associate companies for purpose of securing ECB. -Period of pledge to be co-terminus with maturity of underlying ECB -In case of invocation of pledge, transfer to be made in accordance with rules and directions of RBI. -Statutory auditor to certify that company shall utilise or has utilised proceeds of ECB for permitted end use only.		

Transfer of Equity Instruments - Rule 9 of NDI Rules

Rule	Transfer Between	Mode of Transfer	Automatic/ Approval
9(8)(ii)	PROI may pledge Equity Instruments or units of an investment vehicle in favour of :		
	-Banks in India to secure credit facilities for company for bonafide purposes.		
	-Overseas banks to secure credit facilities being extended to such person or PROI who is promoter of such Indian company or overseas group company of Indian Company.		
	-NBFC registered with RBI to secure credit facilities for Indian Company for bonafide purposes.		
	-Promoter of a company which has raised ECB may pledge shares of borrowing company or that of its associate companies for purpose of securing ECB.		
	-Period of pledge to be co-terminus with maturity of underlying ECB		
	-In case of invocation of pledge, transfer to be made in accordance with rules and directions of RBI		

Transfer of Equity Instruments by NRI/OCI – Rule 13 of NDI Rules

Rule	Transfer Between	Mode of Transfer	Automatic/ Approval
13(1)	NRI or OCI to PROI	<p>Sale or Gift (if acquisition by NRI/OCI under Schedule III results in breach of limits prescribed therein, NRI/OCI shall sell the same to PRII within time stipulated by RBI in consultation with CG)</p> <p>Investment by NRI by way of subscription to shares of Listed Indian Company if less than 10% of paid up capital of company will be considered as portfolio investment.</p>	Automatic Route *
13(2)	NRI or OCI holding under Sch IV to PROI	Sale (subject to entry routes, sectoral caps, pricing guidelines and other attendant conditions. However same shall not apply if sold to another NRI or OCI under Schedule IV)	Automatic Route *

* Prior Government approval will be required for any transfer in case the company is engaged in sector which requires government approval.

Transfer of Equity Instruments by NRI/OCI - Rule 13 of NDI Rules

Rule	Transfer Between	Mode of Transfer	Automatic/ Approval
13(3)	NRI or OCI holding under Sch IV to PROI	Gift	Prior approval and subject to conditions
13(4)	NRI or OCI holding under Sch IV to another NRI or OCI under Sch IV	Gift	Automatic Route



FAQ on Deferred Payment

- Q.27: What are the instructions for transfer of shares against deferred payment?

Answer: In case of transfer of shares between a resident buyer and a non-resident seller or **vice-versa**, not more than twenty five per cent of the total consideration can be paid by the buyer on a deferred basis, within a period not exceeding eighteen months from the date of the transfer agreement. The amount deferred can also be either in the form of an indemnity or an Escrow. In all cases, the pricing guidelines should be complied with.

- Q.28. In case of transfer of capital instruments between a person resident in India and a person resident outside India on deferred payment basis, at which stage the form FC-TRS is required to be filed?

Answer: Form FC-TRS has to be filed with the AD bank on receipt of every tranche of payment. The onus of reporting shall be on the resident transferor/ transferee.



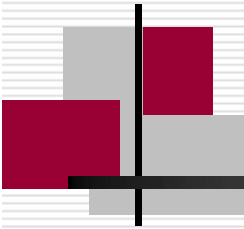
Date of transfer prior to date of receipt of consideration is considered as deferred payment

- Mr. A (Res Indian) acquired shares of B Pvt. Ltd. from Mr. C (non-resident shareholder).
- Date of Transfer was 11th June 2021 and Date of payment of consideration was 12th June 2021.
- Mr. A filed Form FCTRS.
- The delay in receipt of consideration by 1 day was considered payment of consideration on deferred basis resulting in contravention of Rule 9(6) of NDI Rules, resulting in necessity of Compounding



Merger, De-Merger and Amalgamation – Rule 19 of NDI Rules

- Shares can be issued to existing to PROI under scheme of merger, de-merger, amalgamation of two or more Indian Companies subject to approval of scheme by NCLT or competent authority.
- Transfer or issue to be in compliance with sectoral caps, entry routes and attendant conditions.
- In case of breach of percentage of sectoral caps or attendant conditions, prior approval of government required.
- Transferor or transferee company shall not engage in sectors prohibited for investment by PROI.
- In case of listed company, scheme must be in compliance of SEBI regulations.



Reporting Requirements - Rule 20 of NDI Rules and FEMA 395

- Rule 20 of NDI Rules read with Regulation 4 of FEMA Notification No. 395 and

Form	Particulars
FC-GPR	To be filed by Indian company issuing equity instruments to PROI reckoned as FDI within 30 days from date of issue. FCGPR not required to be filed in case allotment of shares under IPO or QIP (Para A.1(b)(iii) of Part IV of Master Direction on Reporting under FEMA)
Annual FLA Return	To be filed by Indian company which has received FDI or LLP which has received capital contribution every year on or before 15 th July on FLAIR Portal of RBI.
FC-TRS	For transfer of equity instruments between - a. PROI holding on repatriable basis to another PROI holding on non-repatriable basis.

Reporting Requirements - Rule 20 of NDI Rules and FEMA 395

Form	Particulars
FC-TRS contd...	<p>b. PROI holding on repatriable basis to PRII. (Onus of reporting shall be on resident transferor/transferee or PROI holding shares on non-repatriation basis).</p> <p>c. For transfer between PROI holding on non-repatriable basis to PRII, FCTRS is not required to be filed.</p> <p>d. Transfer of equity instruments on recognized stock exchange by PROI shall be reported by such person in FCTRS.</p> <p>e. Transfer of equity instrument on deferred payment basis shall be reported in FCTRS on receipt of each tranche of payment. Onus shall be on resident transferor/transferee.</p> <p>Form FCTRS is to be filed within 60 days of transfer or receipt / remittance of funds whichever is earlier.</p>

Reporting Requirements - Rule 20 of NDI Rules and FEMA 395

Form	Particulars
FC-TRS contd...	<p>Practical Issues while filing FCTRS form:</p> <ul style="list-style-type: none">a. AD Banks ask for reasons while filing FCTRS form for gift of shares of Indian company by non-resident entity to resident individual. Ideally gift of shares takes place between two individuals out of love or affection. So if FCTRS is filed for gift of shares by non resident company to individual valid reason need to be submitted for the same.b. In case of change in NR shareholder, KYC is to be filed even for new NR shareholderc. For any transaction of FCTRS reported KYC of NR transferor/transferee is to be compulsorily attached.

Reporting Requirements - Rule 20 of NDI Rules and FEMA 395

Form	Particulars
ESOP	Indian Company issuing ESOP to PROI who are its employees/directors or employees/director of its holding company/joint venture/WOS/subsidiaries shall file Form ESOP within 30 days from date of issue of ESOP.
DRR	Domestic Custodian to report in Form DRR issue/transfer of depository receipts in accordance with Depository receipt Scheme, 2014 within 30 days of close of the issue.
LLP I	LLP receiving capital contribution or acquisition of profit share shall file Form LLP I within 30 days from date of receipt of consideration.
LLP II	For reporting of disinvestment / transfer of capital contribution or profits shares between R to NR or vice versa, Form LLP II shall be filed within 60 days from date of receipt of funds.
LEC (FII)	AD Bank shall report to RBI in Form LEC (FII) purchase/transfer of equity instruments by FPIs on stock exchange.

Reporting Requirements - Rule 20 of NDI Rules and FEMA 395

Form	Particulars
LEC (NRI)	AD Bank shall report to RBI in Form LEC (NRI) purchase/transfer of equity instruments by NRIs or OCIs on stock exchange in India.
Form InVI	Investment vehicle which has issued its units to PROI shall file form InVI within 30 days from date of issue of units
DI	<p>Indian Entity or Investment vehicle making downstream investment in another Indian Entity which is considered as indirect foreign investment shall notify to Secretariat of Industrial Assistance, DPIIT within 30 days of such investment even if equity instruments are not allotted.</p> <p>Further Form DI is to be filed with RBI within 30 days from date of allotment of equity instruments.</p>
CN	<p>Indian Start up issuing Convertible Notes to PROI shall file Form CN within 30 days of issue.</p> <p>PRII who is transferor or transferee of Convertible Notes to or from PROI shall file Form CN within 30 days of such transfer.</p>

Pricing Guidelines

- Rule 21 of NDI Rules

Rule	Particulars
12(1)	Pricing Guidelines shall not apply to any transfer by way of sale done in accordance with SEBI regulations where pricing is specified by SEBI.
12(2)(a)	<p>Price of Issue of equity instruments to PROI shall not be less than -</p> <ul style="list-style-type: none"> (i) Listed Company: price as worked out in accordance with SEBI guidelines. (ii) Unlisted company: valuation done as per any internationally accepted methodology for valuation on arms length basis certified by CA or Merchant Banker registered with SEBI or Cost Accountant <p>Note: in case of CCPs or CCDs price or conversion formula to be determined upfront at time of issuance of instruments. Price at time of conversion should not be lower than fair value worked out at time of issuance of such instruments.</p>
12(2)(b)	<p>Price of transfer of equity instruments from PRII to PROI shall not be less than -</p> <ul style="list-style-type: none"> (i) Listed Company: price as worked out in accordance with SEBI guidelines. (ii) Unlisted company: valuation done as per any internationally accepted methodology for valuation on arms length basis certified by CA or Merchant Banker registered with SEBI or Cost Accountant

Pricing Guidelines

- Rule 21 of NDI Rules

Rule	Particulars
12(2)(c)	<p>Price of transfer of equity instruments from PROI to PRII shall not exceed –</p> <p>(i) Listed Company: price as worked out in accordance with SEBI guidelines.</p> <p>(ii) Unlisted company: valuation done as per any internationally accepted methodology for valuation on arms length basis certified by CA or Merchant Banker registered with SEBI or Cost Accountant</p> <p>Note: PROI is not guaranteed any assured exit price and shall exit at price prevailing at time of exit.</p>
12(2)(c)(iv)	<p>Swap of Equity Instruments –</p> <p>Valuation to be made by Merchant Banker registered with SEBI or an Investment banker outside Indian registered with regulatory authority of host country.</p>
12(2)(c)(v)	<p>Shares issued by way of subscription to MOA to PROI –</p> <p>At face value subject to sectoral caps and entry route.</p>
12(2)(c)(vi)	<p>Share Warrants –</p> <p>Price and conversion formula to be determined up front.</p>



Remittance of Sale Proceeds – Rule 22 of NDI Rules

- All transactions to be undertaken through banking channels.
- Remittance shall be subject to payment of applicable taxes and other duties or levies in India.
- AD Bank may allow remittance provided security was held on repatriation basis.
- Sale has to be in compliance with pricing guidelines or RBI's approval has been obtained as the case may be.



Downstream Investment (DI) – Rule 23 of NDI Rules

- **Downstream Investment** means investment by an Indian entity which has total foreign investment in it or an Investment Vehicle in capital instruments or capital of another Indian entity.
- **Indirect Foreign Investment** means downstream investment received by an Indian entity from:
 - Another Indian Entity (IE) which has received Foreign Investment (FI) and (i) IE is not owned and controlled by resident Indian citizens or (ii) owned or controlled by PROI.
 - An investment vehicle whose sponsor or manager or investment manager (i) is not owned or controlled by resident Indian citizens or (ii) owned and controlled by PROI.



Downstream Investment (DI) – Rule 23 of NDI Rules

■ Meaning of Ownership (threshold) :

- Indian Company – beneficial holding of more than 50% of capital instruments of the company.
- LLP – capital contribution of more than 50% and having major profit share.
- Company / LLP owned by Resident Indian Citizens – ownership is vested in resident Indian Citizens and / or Indian Companies which are owned and controlled by resident Indian Citizens.
- Company / LLP owned by PROI – ownership with PROI.



Downstream Investment (DI) – Rule 23 of NDI Rules

■ Defining ‘Control’:

- Indian Company - Right to appoint majority of directors or to control the management or policy decisions including by virtue of their shareholding or management rights or shareholders agreement or voting agreement.
- LLP - right to appoint majority of designated partners which have control over all policies of LLP.
- Company / LLP owned by **Resident Indian Citizens** - ownership is vested in resident Indian Citizens and / or Indian Companies which are owned and controlled by resident Indian Citizens.



Downstream Investment (DI) – Rule 23 of NDI Rules

- ‘Total Foreign Investment’ means the total of foreign investment and indirect foreign investment and the same will be reckoned on a fully diluted basis;
- Indian Entity (Company or LLP) receiving indirect foreign investment shall comply with entry route, sectoral caps, pricing guidelines and other relevant conditions as applicable for foreign investment.
- Downstream investment by LLP not owned or controlled by resident Indian citizens or owned or controlled by PROI is allowed in an Indian Company operating in sectors where FI up to 100% is permitted under automatic route and there are no FDI Linked conditions.



Downstream Investment (DI) – Rule 23 of NDI Rules

■ Calculation Guidelines:

- Any equity of PROI from conversion of any debt instruments shall be reckoned for total foreign investment.
- FCCBs and DRs having underlying instruments in nature of debt shall not be considered for calculation.
- Portfolio Investments as on 31st March shall be considered for computing total foreign investment.
- Methodology for calculation will apply at each stage of investment in Indian Companies.
- Indirect FI received by WOS of an Indian Company shall be limited to total FI received by company making downstream investment.



Downstream Investment (DI) – Rule 23 of NDI Rules

■ Compliance Conditions:

- BOD approval.
- Shareholders Agreement if any.
- DI must be from funds received from out of India and / or through internal accruals. Internal accruals means profits transferred to reserve account (net of taxes).
- Funds borrowed in domestic market cannot be used.
- First level Indian Company making DI shall be responsible for ensuring compliance with provisions of DI.



Downstream Investment (DI) – Rule 23 of NDI Rules

■ Compliance Conditions:


- First Level Indian Company to obtain certificate of Statutory Auditor on annual basis.
- Compliance details also to be mentioned in Directors Report in Annual Report of Indian Company.
- In case of qualified report given by Statutory Auditor, same shall be brought to notice of Regional office of RBI and acknowledgement shall also be obtained.
- To trigger DI provisions, the investment in first level company has to be Foreign Investment.



FAQ on Downstream Investment

- Q.30: Whether an Indian company (owned or controlled by persons resident outside India or not owned and not controlled by resident Indian citizens (FOCC)) investing in instruments other than capital instruments of another Indian company will be treated as downstream investment?

Answer: No



SCHEDULE I - FOREIGN DIRECT INVESTMENT

Purchase or Sale of Equity Instruments of an Indian Company by PROI



Prohibited Activities – Para 2 of Schedule I

- Lottery Business including government / private lottery, online lotteries
- Gambling and Betting including casinos
- Chit Funds
- Nidhi company
- Trading in TDRs
- Real Estate Business or Construction of Farm Houses
- Manufacturing of cigars, cheroots, cigarillos and cigarettes of tobacco or of tobacco substitutes
- Activities not open to private sector investment e.g. Atomic Energy, Railway operations (other than permitted activities).
- Foreign technology collaboration in any form including license for franchise, trademark, brand name, management contract is also prohibited in lottery business and Gambling and Betting activities.



Entry Routes – Para 3 of Schedule I

Entry Routes:

- Automatic Route – No prior approval required.
- Government Route – Prior approval is required and investment is subject to conditions stipulated therein in the approval.



Sectoral Caps – Para 3 of Schedule I

Sectoral compliance:

- Sectoral caps are indicated in the Schedule.
- Sectors/activities not listed in schedule or not prohibited are 100% under automatic route.
- Minimum capitalization shall include premium received by company.
- Investing Companies not registered as NBFC or CICs – under Approval route.
- Investing companies registered as NBFC – 100% under automatic route.



Sectoral Caps – Para 3 of Schedule I

Sectoral compliance:

- FDI is under automatic for Indian Company having no operations and no downstream investment only if its activities are under automatic route with no FDI linked conditions. If activities proposed to be commenced fall under approval route prior government approval will be required.
- If PROI specifies a particular auditor or audit firm having international network for audit of investee company, the such audit of investee company shall be carried out as joint auditors wherein one of auditor is not part of same network.



Certain Issues in FDI

- FDI inward remittance cannot be credited to EEFC account.
- Investment made with assured return by promoter or investee company is prohibited.
- NR to NR transfer of shares of company engaged in sectors/activities under approval route without obtaining prior government approval.



Manner of Investments – Issue of shares against pre-incorporation expenses

➤ Para 1(c) of Schedule 1:

- Indian WOS may issue capital instruments to its foreign parent against **pre-incorporation / pre-operative expenses** up to limit of 5% of its authorised capital or USD 5,00,000 whichever is lower, provided Indian WOS is engaged in sector where 100% Foreign investment is allowed under automatic route and there are no FDI Linked performance conditions.
- Reporting in FCGPR is to be done within 30 days from date of issue of capital instruments but not later than 1 year from date of incorporation.
- Certificate of Statutory Auditor is to be obtained certifying utilisation of funds.



Manner of Investments – Issue of shares against specific dues

➤ Para 1(d) of Schedule 1

Issue of capital instruments by Indian Company against –

- Swap of capital instruments,
- Import of capital goods/machinery/equipment (excluding second hand machinery)
- Pre-operative/Pre-incorporation expenses (including payments of rent)

shall be subject to compliance with conditions prescribed by Central Government and / or RBI and under automatic route provided Indian Company is engaged in an automatic route sector.

Government approval shall be obtained if the Indian investee company is engaged in a sector under Government route.



Additional Conditions - Issue of Shares

FDI Policy Circular of 2020 - Additional conditions for issue of shares against import of capital goods/machinery/equipment:

- Import has to be in accordance with EXIM Policy of Government of India as defined by DGFT/FEMA provisions relating to imports.
- Application must clearly indicate the beneficial ownership and identity of Importer Company as well as overseas entity.
- Application for conversion of import payables in FDI must be made within 180 days from date of shipment.



Additional Conditions - Issue of Shares

FDI Policy Circular of 2020 - Additional conditions for issue of shares against pre-operative/pre-incorporation expenses:

- FIRC for funds remitted by overseas promoters for expenditure incurred is to be submitted.
- Pre-incorporation/pre-operative expenses are to be verified and certified by Statutory Auditor.
- Payments should be made by foreign investor directly or through bank account opened by foreign investor as provided under FEMA regulations.
- Application for capitalisation complete in all respects shall be made within 180 days from date of incorporation.



Additional Conditions - Issue of Shares

FDI Policy Circular of 2020 - General Conditions:

- All request of conversion should be accompanied by special resolution of company.
- Government's approval will be subject to RBI pricing guidelines and appropriate tax clearance.
- Issue of share against import of capital goods/machinery/equipment and pre-operative/pre-incorporation expenses is to be reported to RBI in form FCGPR as per procedure prescribed.



Manner of Investment

- Issue of Shares against any funds payable

➤ Para 1(e) of Schedule I -

Issue of equity shares against any funds payable (A.P. DIR Circular No. 31 dated 17.09.2014) -

- Indian Company may issue shares against any funds payable to a person resident outside India.
- The remittance for the funds so payable must not require prior permission of Central Government or RBI.



Remittance of pre-incorporation expenses

➤ **Current Account Rules - Remittance of pre-incorporation expenses:**

Indian Entity can make remittance of:

- 5% of investment or
- USD 1,00,000

For reimbursement of pre-incorporation expenses



Modes of Payment - Reg 3 of Notification No. 395

➤ Mode of Payment:

- Inward Remittance
- Out of funds held in NRE/FCNR(B)
- Against any funds payable
- Swap of Equity Instruments

Compounding Orders for contravention of Mode of Payment:

- CA No. 4302/2017 dated 05.07.2017 in case of Mahesh Mohan Uberoi whereby payment for subscription of shares was made by an Indian company to the company issuing shares and not received through inward remittance from abroad from the non-resident investor.
- CA No. 4536/2018 dated 05.01.2018 in case of Mahesh Ramakrishnan where FDI proceeds were received through third party intermediary and not through authorised person.



Receipt of consideration from PROI other than to whom capital instruments are issued

➤ Part IV - Para A(1)(b)(iv) of Master Direction on Reporting under FEMA:

In case the Indian company issues shares to a person resident outside India other than to the person resident outside India from who the inward remittance has been received, the form FC-GPR has to be filed along with the following documents:

- KYC reports of both the remitter and beneficial owner.
- NOC from remitter for issuing capital instruments to beneficial owner mentioning their relationship.
- A letter from beneficial owner explaining reasons for the remitter making the remittance on its behalf.
- Copy of agreement/board resolution of investee company for issuing capital instruments to a person other than from whom remittance has been received.



Time Limit for allotment - Reg 3 of Notification 395

➤ Time for allotment:

- Equity Instruments to be issued within 60 days from date of receipt of consideration.
- If not issued within 60 days, the amounts to be refunded within 15 days from date of completion of 60 days.
- In case of partly paid shares period of 60 days shall be reckoned from date of receipt of each call payment.



SCHEDULE IV -

Investment by NRIs/OCIs on non-repatriation basis



Investment by NRIs/OCIs in Indian Company or LLP

1) NRI or an OCI including company, trust, partnership firm incorporated outside India owned and controlled by NRIs and OCIs may invest on non-repatriation basis -

- In equity instrument of an Indian Company without any limit either on stock exchange or outside it.
- Units of an investment vehicle
- In capital of a LLP
- In convertible notes of a start up company

2) NRI or OCI may purchase without limit or sell units of domestic mutual fund on non-repatriation basis which invest more than 50% in equity.



Prohibition on investment in certain companies

NRIs or OCIs cannot make investment in equity instruments of -

- Nidhi Company
- Company engaged in agricultural or plantation activities.
- Company engaged in Real Estate Business
- Construction of farms houses
- Dealing in TDRs



Mode of Payment and Remittance of Sale Proceeds- Reg 3 of FEMA 395

Amount of consideration shall be paid by -

- Inward remittance through banking channels
- Out of funds held in NRE/FCNR(B)/NRO account.

Sale / maturity proceeds -

- Upon disinvestment same shall be credited only to NRO account irrespective of type of account from which investment was made.
- Same shall not be allowed to be repatriated abroad.

(Note: NRI/OCI can remit the sales proceeds to NRIO account under USD 1 million scheme per financial year)



Investment in Partnership Firm / Proprietary Concern

- NRI/OCI may invest on non-repatriation basis by way of capital contribution to firm or proprietary concern.
- Such firm or proprietorship concern must not be engaged in agricultural or plantation activity or print media or real estate business.



SCHEDULE VI -

Investment in Capital of Limited Liability Partnership



Investment in Capital of LLP by PROI

- PROI other than citizen of Bangladesh or Pakistan or a foreign entity other than entity incorporated in Bangladesh or Pakistan NRI/OCI can invest in capital of LLP.
- Such entity must not be a FPI or FVCI.
- Investment is allowed only in capital of LLP operating in sectors or activities where foreign investment is 100% under automatic route and there are no FDI linked performance conditions.
- Sectors like Construction Development, Industrial Parks, Cash and Carry wholesale Trading, E-commerce etc. have FDI linked conditions and hence foreign investment in LLPs engaged in such sectors is not allowed.
- Investment by way of profit share shall fall under category of reinvestment of earnings.



Investment in Capital of LLP by PROI

- Investment shall be subject to compliance of conditions of LLP Act, 2008.
- Company having foreign investment engaged in sector where foreign investment up to 100% is allowed under automatic route and there are no FDI linked conditions can be converted to LLP and vice versa.
- Investment should not be less than fair price worked out as per any valuation norm which is internationally accepted or adopted as per market practice.
- Valuation certificate has to issued by Chartered Accountant or by practising Cost Accountant or by an approved valuer from panel of CG.



Investment in Capital of LLP by PROI

- Transfer from PRII to PROI shall not be less than fair price of capital contribution or profit share of LLP.
- Transfer from PROI to PRII shall be at consideration not more than fair price.



Round Tripping

- Round tripping as a term is nowhere defined under FEMA, nor in any circulars issued by RBI.
- It refers to a strategy wherein an Overseas Entity is established for the sole purpose of routing funds back to India.
- Round tripping arrangement leads to contravention under Outbound Investment. As ODI would not meet the criteria of *bonafide business activities* (Refer Regulation 6(2)(ii) of Notification No. FEMA.120/RB-2004)
- A.P. (DIR Series) Circular No. 41 dated November 25, 2014 was issued by RBI on Routing of funds raised abroad to India.



Round Tripping

- As a principle
- FOREIGN COMPANY WITH INDIAN SHAREHOLDER CANNOT HAVE INDIA PRESENCE



Round Tripping - Compounding Orders

- CA No. 3867/2015 dated 03.06.2016 in case of Binani Ind Ltd. – Contravention of Reg 6(2)(ii) of FEMA 120. Applicant had merged its Indian subsidiary with overseas WOS with purpose of achieving business synergy and business consolidation. Hence Post Facto was granted.
- CA No. 3946/2016 dated 29.08.2016 in case of Shubkam Ventures – Overseas WOS made investment back into an Indian entity leading to non bonafide activity. RBI asked for unwinding of transaction and carried out compounding.



THANK YOU

FIRST DESERVE

AND

THEN DESIRE!!

