

# **FDI in India – Statute, Recent Changes, etc. (Schedule 1 of NDI Rules 2019)**

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**CTC - Intensive study course on FEMA  
Mumbai**

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# Overview of FEMA

- **FEMA 1999**
  - Replaced the draconian Foreign Exchange Regulation Act 1973
  - Appointed date 1 June 2000
- **Aims of FEMA**
  - Facilitate external trade and payments
  - Promotion of foreign exchange markets
- **FEMA Rules / Regulations**
  - Rules notified by the Central Government and
  - Regulations notified by the RBI
  - **Consultation betn. Government and RBI**
- **RBI website ([www.rbi.org.in](http://www.rbi.org.in))**
  - A P (Dir Series) - issued from time to time
  - Master Directions – updated now periodically
  - FAQs
- Every Transaction either Current (generally permissible unless prohibited) or Capital Account – (only if and as permitted)

- **Other Statutes:** Many other statutes impact / enshrined in FEMA, e.g.
  - FDI Policy
  - Foreign Trade Policy
  - Sectoral Regulation
    - NBFC, Insurance, SEBI, etc.
  - Companies Act
- Several powers /responsibilities delegated to the **AD / Banker by RBI – their role / concurrence critical but primary responsibility is of constituents and their role is compliance & monitoring**
- Representation by CAs / Lawyers – not a warm welcome

***In view of complexities and voluminous content – Always refer, research, debate and than conclude...every time***

# Inbound investments – Key recent developments

- **Abolishing of the FIPB in June 2017**

- The work of granting government approval for foreign investment entrusted to the concerned Administrative Ministries/Departments

- **Revised DIPP role**

- DIPP has the responsibility of overseeing the applications filed on the FIFP portal and to forward to the concern Administrative Ministries
- SOPs developed for the same
- FIFP Portal and its FAQ for online filing

- **Online reporting of Forms to RBI**

- Foreign Investment Reporting and Management System (FIRMS)
- Foreign Liabilities and Assets Information Reporting (FLAIR) System

- **Late Submission Fees v. Compounding**

- **FEMA Inbound**

- The Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Reg. 2000 (FEMA 20) dt. 3 May 2000 substituted by FEMA 20(R) dt. 7 Nov. 2017
- The FEMA 1999 amended by the **Finance Act 2015** inter alia to realign powers between Central Government (CG) and RBI.
- Debt and Non-Debt Instruments notified by CG under S. 6(7) of FEMA 1999 - Dt. 16 Oct 2019
- The CG Notification dt. 17 Oct 2019 supercedes FEMA 20(R) - The Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 ('NDI Rules')
- Two new RBI Reg. notified dt. 17 Oct 2019 – (i) Debt-Instruments Reg. 2019 (FEMA 396) and (ii) Mode of payment and Reporting of NDI Reg. 2019 (FEMA 395)
- NDI (Amendment) Rules 2019 dt. 5 Dec 2019 - incorporates PN 4 of 2019 & anomaly removals and few from date of original NDI Rules

# Notification dt. 16 Oct 19 under Section 6(7) of FEMA 1999

## 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 securities

## Non-Debt Instruments

- i. All investments in equity in incorporated entities (public, private, listed, unlisted)
- ii. Capital participation in LLPs
- iii. Instruments of investment as 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. Juniormost layer (e.g. equity tranche) of securitization structure
- vii. Acquisition, sale or dealing directly in immovable property
- viii. Contribution to trusts
- ix. 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**

# The NDI Rules 2019 -- Chapters

Chapter	Rule & Particulars
Chapter I	<b>Rule 1</b> - Preliminary – <b>Rule 2</b> -Definitions
Chapter II	<b>Rule 3, 4 and 5</b> - General conditions applicable to all Investors
Chapter III	<b>Rule 6, 7, 8 and 9</b> – Investment by Person Resident Outside India (PROI)
Chapter IV	<b>Rules 10 – 11</b> - Investment by FPI
Chapter V	<b>Rules 12 – 13</b> - Investment by NRI / OCI
Chapter VI	<b>Rules 14 – 15</b> - Investment by other NR investors
Chapter VII	<b>Rules 16 – 17</b> - Investment by FVCI
Chapter VIII	<b>Rules 18 to 23</b> - General Provisions: Issue of convertible notes by Start-up, merger or demerger or amalgamation of Indian Companies, Reporting requirements, downstream investments, pricing guidelines, remittances of sale proceeds
Chapter IX	<b>Rules 24 to 33</b> - Acquisition and transfer of immovable property in India

**NDI Rules 2019 stipulate at several places consultation of RBI with the Central Government**

# The NDI Rules 2019 – Schedules

Schedules	Investments by PROI
<b>I</b>	Purchase or sale of equity instruments of an Indian Company by a PROI
<b>II</b>	Purchase or sale of equity instruments by Foreign Portfolio Investors (FPI)
<b>III</b>	Investment by NRI / OCI on repatriation basis
<b>IV</b>	Investment by NRI / OCI on non-repatriation basis
<b>V</b>	Investment by other non- resident investors
<b>VI</b>	Investment in an Indian LLP
<b>VII</b>	Investment by SEBI Registered Foreign Venture Capital Investors
<b>VIII</b>	Investment in an Investment Vehicle viz. AIF, REIT, InvIts
<b>IX</b>	Investment in Depository Receipts by PROI
<b>X</b>	Issue of Indian Depository Receipts

# NDI Rules 2019 - Key definitions (1 of 5)

**Equity Instruments** - means equity shares, convertible debentures, preference shares and share warrants issued by an Indian company;

Explanation

(i) Equity shares issued in accordance with the provisions of the Companies Act, 2013 shall include equity shares that have been partly paid.

“Convertible debentures” means fully, compulsorily and mandatorily convertible debentures.

“Preference shares” means fully, compulsorily and mandatorily convertible preference shares.

Share Warrants are those issued by an Indian company in accordance with SEBI regulations.

Equity instruments can contain an optionality clause subject to a minimum lock-in period of one year or as prescribed for the specific sector, whichever is higher, but without any option or right to exit at an assured price.

(ii) Partly paid shares that have been issued to a PROI shall be fully called-up within twelve months of such issue or as may be specified by the RBI from time to time. Twenty- five per cent of the total consideration amount (including share premium, if any) shall be received upfront.

(iii) In case of share warrants, at least twenty-five per cent of the consideration shall be received upfront and the balance amount within eighteen months of the issuance of share warrants.

**The grandfathering for NC/ OC / PC - Preference shares issued up to 30 April 2007 and OC/ PC - Debenture issued up to 7 June 2007 in FEMA 20 / FEMA 20R not incorporated in NDI Rules 2019**



## NDI Rules 2019 - Key definitions (2 of 5)

Definitions	Particulars
<b>FDI linked performance conditions</b>	means the sector specific conditions specified in Schedule I of these rules for companies receiving foreign investment;
<b>FDI</b>	<p>means investment through equity instruments by a PROI in an unlisted Indian company; or in ten per cent or more of the post issue paid-up equity capital on a fully diluted basis of a listed Indian company;</p> <p>Note:- In case an existing investment by a PROI in equity instruments of a listed Indian company falls to a level below ten percent, of the post issue paid-up equity capital on a fully diluted basis, the investment shall continue to be treated as FDI;</p> <p>Explanation: - Fully diluted basis means the total number of shares that would be outstanding if all possible sources of conversion are exercised;</p>
<b>Foreign investment</b>	<p>means any investment made by a PROI on a repatriable basis in equity instruments of an Indian company or to the capital of a LLP;</p> <p>Explanation: - If a declaration is made by a person as per the provisions of the Companies Act, 2013 about a beneficial interest being held by a person resident outside India, then even though the investment may be made by a resident Indian citizen, the same shall be counted as foreign investment;</p> <p>Note:- PROI India may hold foreign investment either as FDI or as FPI in any particular Indian company;</p>

## NDI Rules 2019 – Key definitions (3 of 5)

Definitions	Particulars
<b>Government approval</b>	means the approval from the erstwhile Secretariat for Industrial Assistance (SIA), Department of Industrial Policy and Promotion, Government of India and/ or the erstwhile Foreign Investment Promotion Board (FIPB) and/ or any of the ministry/ department of the Government of India, as the case may be;
<b>Group Company</b>	means two or more enterprises which, directly or indirectly, are in a position to (i) exercise twenty-six per cent, or more of voting rights in other enterprise; or (ii) appoint more than fifty per cent of members of Board of Directors in the other enterprise;
<b>Hybrid Instrument</b>	<p>Means instruments such as optionally / partially convertible preference shares / debenture / any other instruments as specified by the CG issued by Indian Company or trust to PROI</p> <p>This definition is currently not used elsewhere in the Rules.</p> <p>The Finance Minister while presenting the Union Budget 2018 had announced that a separate policy for hybrid instruments shall be introduced.</p> <p>In line with the said policy announcement, a new definition of “hybrid securities” has been introduced.</p>

## NDI Rules 2019 – Dey definitions (4 of 5)

Definitions	Particulars
<b>Investment Vehicle</b>	Means REITs, Invts, AIFs  <i>Note: NDI Rules, 2019 included MF which invest more than 50% in equity but NDI Amendment Rules dt. 5 Dec 2019 deleted this entry retrospectively</i>
<b>Indian Company</b>	means a company incorporated in India;
<b>Indian Entity</b>	shall mean an Indian company or a LLP ;
<b>Investing Company</b>	means an Indian company holding only investments in other Indian company/ies directly or indirectly, other than for trading of such holdings or securities;
<b>Listed Indian company</b>	means an Indian company which has any of its equity instruments listed on a recognised stock exchange in India and the expression “unlisted Indian company” shall be construed accordingly  <i>Note: NDI Rules 2019 included the condition of listed debt instrument but NDI Amendment Rules deleted this with retrospective effect.</i>

# NDI Rules 2019 - Key definitions (5 of 5)

Definitions	Particulars
<b>Sectoral Cap</b>	<p>Sectoral Cap means the maximum investment including both foreign investment on a repatriation basis by PROI in equity <del>and debt</del> <i>(words omitted by NDI Amendment Rules retrospectively)</i> instruments of a company or the capital of a LLP, as the case may be, and indirect foreign investment, unless provided otherwise.</p> <p>This shall be the composite limit for the Indian investee entity.</p> <p>Explanation:</p> <ul style="list-style-type: none"><li>(i) FCCBs and DRs having underlying of instruments being in the nature of debt shall not be included in the sectoral cap</li><li>(ii) any equity holding by a PROI resulting from conversion of any debt instrument under any arrangement shall be reckoned under the sectoral cap</li></ul>

# NDI Rules 2019 – Rules 6 & 7

Rule	Particulars
<b>Rule 6 – Investments by PROI in an Indian Company</b>	<ul style="list-style-type: none"> <li>• PROI can subscribe, purchase or sale of equity instruments of an Indian company subject to the terms and conditions of Schedule 1</li> <li>• PROI to be other than citizens of / entities incorporated in Pakistan and Bangladesh and even under Approval Route, their investments can be for sectors other than defence, space, atomic energy and sectors or activities prohibited for foreign investments</li> <li>• Issue or transfer of participating interest or rights in oil field by Indian Company is FDI and to comply with Schedule 1</li> </ul>
<b>Rule 7 – Rights / Bonus Issue of an Indian Company</b>	<ul style="list-style-type: none"> <li>• Permissible subject to same terms of original issues (NR basis if by PROI for shares acquired when Resident)</li> <li>• Rights issue by listed Indian Company – price as determined by the Indian company</li> <li>• Rights issue unlisted Indian Company – shall not be at a price which is less than the price offered to PRI</li> <li>• Additional rights and renunciation of rights by PRII in favor PROI permitted</li> </ul> <p><b>Note: FEMA 396 -Rule Issue of Bonus NCRPS / NCDs: Permitted from General Reserves under scheme of arrangement approved by NCLT subject to sectoral conditions and other compliance (earlier this provision was part of FEMA 20(R))</b></p>

# NDI Rules 2019 - Rule 8

Rule	Particulars
<b>Rule 8 - ESOP &amp; Sweat Equity Shares to PROI (other than citizens of Pakistan / Bangladesh)</b>	<ul style="list-style-type: none"><li>• Issue of share under ESOP and Sweat Equity scheme permitted to be issued by an Indian Company to PROI who are<ul style="list-style-type: none"><li>- Its employees/ directors</li><li>- Employees/ directors of its holding company / joint venture/ wholly owned overseas subsidiary or subsidiaries</li></ul></li><li>• The Scheme to be drawn up as per SEBI Guidelines / Companies Act [Share and Debenture Rules 2014)</li><li>• If sector is under Approval Route then prior approval of Gol</li><li>• To be held on Non-Repatriation basis by PROI exercising option which was issued when he or she was PRII</li></ul>

# NDI Rules 2019 - Rule 9 for Transfer of equity instruments (1 of 3)

Rule	Seller	Buyer	Permissible Mode	Pricing & Reporting Guidelines	Government Approval
9(1)	PROI (not NRI, OCI & OCBs)	PROI	Sale / Gift - It covers transfer pursuant to liquidation, merger, de-merger and amalgamation of entities or companies outside India	No (yes if seller holds on NR basis and buyer acquires on Rep basis with attendant conditions)	Yes for sectors under Approval Route
9(2)	PROI	PRII	Sale / Gift – sale is subject to pricing guidelines & reporting	Yes for sale (except when PROI holds on Non-Rep basis)	No
9(3)	PRII	PROI	Sale – adherence to entry routes, sectoral caps or investment limits, pricing guidelines and other attendant conditions	Yes	Yes for sectors under Approval Route
9(4)	PRII / NRIs & OCIs on Non-Rep basis	PROI	Gift – with prior RBI approval - 5% of the paid –up capital of Indian Company / each series of debentures and aggregate ceiling of USD 50K per financial year qua donor	Yes	Yes though not expressly mentioned
9(5)	PROI holding equity instruments of an Indian Company with optionality clause can exit without any assured return subject to minimum lock-in period of one year				

# NDI Rules 2019 - Rule 9 for Transfer of equity instruments (2 of 3)

Rule	Seller	Buyer	Mode
9(6) – sale on deferred consideration	Between PRII and PROI		<p>Sale on deferred consideration subject to following</p> <ul style="list-style-type: none"> <li>• Deferred consideration not to exceed 25% of the total consideration</li> <li>• Deferment period not to exceed 18 months from date of transfer agreement</li> <li>• Can be settled through Escrow arrangement</li> <li>• Can be indemnified by the seller for a period not exceeding 18 months from the date of the payment of the total consideration if total consideration has been paid by the buyer to the seller</li> <li>• Total consideration to be compliant with applicable pricing guidelines</li> </ul> <p>Issues – 1) Variable consideration whether falls within the ambit of deferred consideration mechanics as above? 2) Price to be Rs v. Fx?</p>



## NDI Rules 2019 - Rule 9 for Transfer of equity instruments (3 of 3)

Rule	Seller	Buyer	Mode
9(7) – Escrow	PRII and PROI		<ul style="list-style-type: none"><li>• Escrow account to be in accordance with FEMA Deposit regulations and it can be funded by inward remittance of AD-Bank Guarantee</li></ul>
9(8)	Pledge of Equity Instruments		<ul style="list-style-type: none"><li>• Pledge for ECB subject to conditions</li><li>• Pledge of equity instruments for borrowing in India (Banks / NBFC) by such Indian company and in favor of overseas bank for PROI promoter / overseas group company</li></ul>

# NDI Rules 2019 -Rule 18 Start-up Indian Company

<b>Meaning</b>	<ul style="list-style-type: none"><li>• A 'startup company' means a private company incorporated under the Companies Act, 2013 and identified under G.S.R. 180(E) dated February 17, 2016 issued by the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry</li></ul>
<b>Investment by FVCI</b>	<ul style="list-style-type: none"><li>• <b>FVCIs can invest in equity / equity instruments / debt instruments issued by startup irrespective of the sectors in which the startup is engaged</b></li></ul>
<b>FDI through Convertible note</b>	<ul style="list-style-type: none"><li>• 'Convertible Note' is an instrument issued by a startup company evidencing receipt of money initially as debt, which is repayable at the option of the holder, or which is convertible into such number of equity shares of such startup company, within a period not exceeding five years from the date of issue of the convertible note, upon occurrence of specified events as per the other terms and conditions agreed to and indicated in the instrument.</li><li>• PROI (other than citizens/ entities of Pakistan or Bangladesh) permitted to invest in convertible notes issued by startup of twenty five lakh rupees or more in a single tranche.</li><li>• Prior Government approval required if sectors is under Approval Route</li></ul>
<b>Form CN</b>	<ul style="list-style-type: none"><li>• For Indian Start-ups issuing CNs to PROIs to report to RBI within 30 days from the issue</li><li>• For transfer of CN between PROI and PRI and to be reported by PRI within 30 days from date of transfer</li></ul>

# Other issues to PROs by Indian Company

- **Rule 19 – issue of shares on merger / demerger /amalgamation of Indian Companies**

- Issue of shares to PROI permitted under merger / demerger / other scheme subject to approval by NCLT / Competent Authority
- The transfer / issue to be in compliance with the entry route, sectoral cap and attendant conditions to be complied including Government approval for sectoral cap
- Scheme to be compliant with SEBI Guidelines if any of the companies is listed on the stock exchange in India
- Issue – is fair valuation an attendant condition?

# Rule 20 & FEMA 395 Key FDI Reporting Requirements

Form	When to file?	Due date?
FC-GPR	Indian company issuing capital instruments to a PROI Also in case of conversion of ECB into equity along with Form ECB-2 (Part V: Annex III)	30 days from the date of issue of capital instruments.
FLA Return	Indian company which has received FDI or an LLP which has received investment by way of capital contribution	By 15 July of the corresponding year
FC-TRS	For transfer of capital instruments	60 days of transfer or receipt / remittance of funds (which is earlier)
ESOP	Indian company issuing employees' stock option to PROI	30 days from the date of issue of ESOPs.
DRR	For issue/ transfer of depository receipts issued in accordance with the Depository Receipt Scheme, 2014	30 days of close of the issue
LLP (I)	LLP receiving amount of consideration for capital contribution and acquisition of profit shares	30 days from the date of consideration
LLP (II)	Disinvestment/ transfer of capital contribution or profit share of LLP between a resident and a non-resident	60 days from the date of receipt of funds
LEC(FII)	Purchase/ transfer of capital instruments by FPIs on the stock exchanges in India	NA
LEC(NRI)	Purchase/ transfer of capital instruments by Non-Resident Indians or Overseas Citizens of India stock exchanges in India	NA
DI	Indian entity or an investment Vehicle making downstream investment in another Indian entity	30 days from the date of allotment of capital instruments
CN	Indian startup company issuing Convertible Notes to a person resident outside India	30 days of such issue
InVi	Investment vehicle which has issued its units to a person resident outside India	30 days from the date of issue of units

# Rule 21 - Pricing for Issue & Transfer

- **Pricing guidelines do not apply if transfer by way of sale is governed by SEBI guidelines or price is specified by SEBI**
- **Issue price of equity instruments to PROI – price should not be lower than:**
  - For Listed Company – SEBI Guidelines including for Delisting
  - For Unlisted Company – Internationally accepted pricing methodology (IAPM) for valuation on arm's-length basis
- & Valuation by Merchant Banker / CAs / Cost Accountants

Note: CCPS and CCD - price conversion formula to be determined upfront. Also, price should not less than FV on issuance date. This was restated in NDI Rules 2019 vide NDI (amendment) Rules 2019 dated 5 Dec 2019 with retrospective effect

- **Transfer of equity instruments – price for transfer between PRII to PROI**
  - PRII to PROI – price not to be less than SEBI guidelines (issue or preferential allotment or delisting ) for Listed Company and IAPM for unlisted company as above
  - PROI to PRII – price not to exceed SEBI guidelines for listed company and IAPM for unlisted company as above
  - Valuation by Merchant Banker / CAs / Cost Accountants

Note: PROI cannot be guaranteed assured exit price and the exit to be at prevalent price

Note: Pricing is not applicable for investment by PROI on non-repatriation basis

# Rule 21 & 22 - Pricing for Issue & Transfer

- **Others cases**
  - Swap of shares – valuation only by SEBI Registered Merchant Banker / Investment Banker registered with Host Country
  - Subscription to MoA / AoA – face value (shall used instead of May)
  - Share warrants – pricing / conversion formula to be determined upfront
- **Rule 22 - Remittances of sales proceeds**
  - All transaction through banking channel
  - Payment of applicable taxes /duties / levies in India
  - AD Bank to verify that the security was held on repatriation basis (RBI registration letter for equity instruments issued to PROI or AD-Bank approval of FC-TRS for equity instruments acquired by PROI)
  - Sales is as per pricing guidelines or with prior RBI approval in other cases

# Rule 23 – Downstream Investments (1 of 3)

- **Concept of ownership**

- Ownership of Indian Company – beneficial holding of more than 50% of the equity instruments
- Ownership of Indian LLP - more than 50% in capital and having majority profit share
- Indian Company / LLP owned by Resident Indian Citizens – ownership is vested in Resident Indian Citizens or Indian companies / Indian Entities which are ultimate owned and controlled by them
- Indian Company / LLP owned by PROI – Ownership is with PROI)

- **Concept of control**

- Control for Indian company: Control shall mean the right to appoint a majority of the directors or to control the management or policy decisions including by virtue of their shareholding or management rights or shareholders agreement or voting agreements.
- Control of Indian LLPs is right to appoint majority of the designated partners who have control over all policies of LLP (in specific exclusion of others)
- Indian Company / LLP controlled by Resident Indian Citizens – control is vested in Resident Indian Citizens or Indian companies / Indian Entities which are ultimate owned and controlled by them
- Company / LLP owned by PROI – control is with PROI

**IOCC – Indian Owned and Controlled Company & IOCL = similar situation for LLPs**  
**FOCC – Foreign Owned or Controlled Company & FOCL – similar situation for LLPs**

## Rule 23 – Downstream Investments (2 of 3)

- Downstream Investment' means an investment made by an Indian entity which has received foreign investment or by an Investment Vehicle in the capital instruments or the capital, as the case may be, 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 and **which is not owned and not controlled** by resident Indian citizens or is owned or controlled by persons resident outside India; or
  - an investment vehicle whose sponsor or manager or investment manager is not owned and not controlled by resident Indian citizens or is owned or controlled by persons resident outside India.
- Total Foreign Investment' is the sum of foreign investment and indirect foreign investment which will be reckoned on a fully diluted basis
- Indian entity which has received Indirect foreign investment to comply with entry route, sectoral caps, pricing guidelines and other attendant conditions. No PRII other than Indian entity can receive Indirect Foreign Investment
- Downstream investment by LLP which is FOCL is allowed only in an Indian company where foreign investment up to 100% is permitted under Automatic Route and where there are no FDI linked performance related conditions
- Exceptions (from 31 July 2012) – Downstream investments by Banking company as part of CDR/ loan restructuring / trading books / loan defaults and which are not strategic investments (as defined)



# Rule 23 – Downstream Investments (3 of 3)

## • Computation Methodology

- Apply at every stage of investments
- All types of foreign investment included except by NRIs / OCIs on NR basis under schedule 4
- Portfolio investment – 31 March of previous year
- FOCC – Downstream FDI – (a) if foreign ownership is less than 100% then downstream investment is full investment made by the FOCC / FOCL (b) if downstream investment is in a WOS, then it is the foreign investment in the FOCC/ FOCL
- Indirect foreign investment permitted in and by LLP permitted in sectors where foreign investment is allowed 100% under Automatic Route and there are no FDI linked performance conditions

## • Conditions for downstream investments

- Approval of Board / Shareholders
- Investment from funds received outside India and / or internal accruals
- Leveraging funds from domestic market is not permitted
- Reporting to RBI and DIPP / FIFP portal
- Reporting by Statutory Auditor of the Indian Investor Company at the first level

## • Transfer of equity instruments by FOCC of downstream Investee Indian Entity

- Sale to PROI - reporting in Form FC-TRS **but no pricing guidelines**
  - Sale to PRII –**subject to pricing guidelines**
  - Sale to another FOCC – **no reporting and no pricing guidelines**
- Similar provisions apply to LLPs

# Schedule 1 - Sectoral aspects

- **Prohibited Sectors**

- Lottery – Online / Government or Private (foreign technology / trademark / brand / management agreement also prohibited)
- Gambling & Betting including Casinos
- Chit Funds
- Nidhi Companies
- Trading in TDRs
- Real Estate Business or construction of Farm Houses
- Manufacturing Cigars, etc.
- Activities not open to private sector (reserved for PSUs) – Atomic Energy and Railways (other than those permitted under Schedule I)

- **Entry Routes**

- Automatic Route – no prior RBI or Government approval for investments by PROI
- Government Route – prior approval from the Government warranted and subject to additional conditions imposed therein

**Note: Sectoral caps part of Schedule I as compared to Regulation 16 of FEMA 20R**

# Schedule 1 - Sectoral aspects

- **Sectoral Policy**

- An Indian company to issue equity instrument to PROI subject to entry-routes, sectoral caps and attendant conditions
- Sectoral caps and government approval indicated against each sector in the schedule
- All other sectors / activities under Automatic Route
- SOPs issued by DIPP specifies process and Ministries for Government Approval Route
- Minimum capitalization to include premium received by the company (credit for same also in transfer / sales price)
- Approval route for investing companies not registered with RBI as NBFC and CIC
- Indian company with no operations and no downstream investment – automatic route only if activities undertaken are under automatic route and with no FDI linked performance conditions and government approval to be obtained if activities proposed to be commenced fall under approval route
- If PROI specifies a particular auditor or audit firm having international network for the audit of the Indian investee company, then audit to be carried out as joint audit wherein one of the auditors is not part of the same network.

# Sectoral caps (illustrative purpose only)

## Automatic Route with / without conditions

1. Agriculture (Floriculture / Horticulture/ other items) & Animal Husbandry - 100%
2. Plantation - 100%
3. Mining / Coal & Lignite / Titanium – 100%
4. Petroleum & Natural Gas (100% for exploration and 49% for refining by PSUs)
5. Manufacturing - 100% #
10. Construction Development: Townships, Housing, Built-up infrastructure
11. Industrial Park
12. Satellites – Establishment and Operations
15. Trading – Four parts - C&C + WT / E-commerce / SBRT / Duty Free Shops #
17. Railway infrastructure

## Partly Automatic Route & Partly under Government Route with / without conditions

6. Defence - 49% Auto Route and beyond that up to 100% under Approval route
7. Broadcasting - 100% under Auto Route or 49% under Government Route as per activity
8. Print Media - 100% under Automatic Route or 26%/ 49% under Approval Route as per activity
9. Civil Aviation - 100% under Auto Route except Air Transport Services @ beyond 49% under Approval Route for PROI other than NRIs / OCIs)
14. Telecom - 49% Auto Route and beyond that up to 100% under Approval route
16. Pharma – Auto Route is Greenfield upto 100% and Brownfield upto 74% Auto and beyond under Approval Route
17. Financial Services – 20%/ 49% / 74% / 100% Auto as well as Approval route

**Prior Approval Route:** (13.) Private Security Agencies – 49% & # (15) Trading (i) MBRT – 51% & (ii) Under Manufacturing - 100% Retail Trading of Food products manufactured and / or produced in India including through E-commerce

# Schedule I (1 of 2)

- **Schedule I**

- PROI to purchase shares in listed company on stock of exchange of India if
  - PROI has acquired control as SEBI SAST regulations and continues to hold control
  - Consideration can be paid out of dividends by Indian Investee Company (as per mechanism stipulated)
- Issue of equity instrument against pre-incorporation / pre-operative expenses (including rent)
  - 5% of authorized capital or USD 500,000 whichever is lower.
  - Indian company is a **WOS of NR Entity** and is engaged in a sector where 100% FDI permitted under Automatic Route with no FDI linked performance conditions
  - Statutory Auditor Certificate
  - Reporting within thirty days of issue of equity instruments but not later than one year from the date of incorporation or such time permitted by RBI
  - Issues – (i) Route not available to Indian JVs or where NR is not an entity or deposits for Rent? And (ii) how to interpret timeline condition ?
  - *Missing Explanation from FEMA 20(R) to NDI Rules 2019 - Pre-incorporation/ pre-operative expenses shall include amounts remitted to Investee Company's account, to the investor's account in India if it exists, to any consultant, attorney or to any other material/ service provider for expenditure relating to incorporation or necessary for commencement of operations*

# Schedule I (2 of 2)

- **Schedule I**

- Issue of equity instruments against inward remittance through banking channels / as specified under FEMA 395
- Issue of equity instruments also permitted against
  - Swap of equity instruments
  - import of capital goods / machinery /equipment (excluding second hand machinery)
  - NRE / FCNR (B) – NRIs / OCIs
  - any funds payable by Indian company to a PROI, the remittance of which is permitted under FEMA by RBI / GoI or post obtaining all approvals for payments and completion of actions for delay such as compounding

- Time limits for issue of equity instruments
  - Within 60 days from receipt of consideration else refund within 15 days from completion of such 60 days
- Foreign Currency Account
  - The consideration for equity instrument can be deposited in a foreign currency account with AD Bank :
  - There must be impending foreign currency expenditure
  - The account needs to be closed immediately after the requirements are completed or within six months of opening whichever is earlier

# Sector - Manufacturing

**Manufacture** with its grammatical variations, means a change in a non-living physical object or article or thing (i) resulting in transformation of the object or article or thing into a new and distinct object or article or thing having a different name, character and use; or (ii) bringing into existence of a new and distinct object or article or thing with a different chemical composition or integral structure;

**A manufacturer is permitted to sell its products manufactured in India through wholesale and/or retail, including through e-commerce without Government approval.**

*PN 4 of 2019 and NDI Amendment Rules 2019: Manufacturing activities may be carried out either as self manufacturing by the investee entity or contract manufacturing in India through a legally tenable contract, whether on Principal to Principal or Principal to Agent basis.*

- Whether processing is manufacturing?
  - Disputes surrounding what is manufacture or processing are not uncommon?
  - Definition of cash and carry wholesale trading / wholesale trading (including sourcing from MSEs) – it also includes processing and thereafter sale?
  - Better view - Processing is not manufacturing
- Meaning of P2P and P2A? Whether P2P manufacturer can do retail trading?
- Whether definition is FDI linked performance related conditions for LLP?

# Sector - E-Commerce (1 of 2)

## E-commerce

- B2B – subject to guidelines for cash & carry wholesale trading
- Marketplace model of E-commerce
  - E-commerce means buying / selling of goods / services including digital products over digital or electronic networks
  - Inventory based e-commerce model is not permitted
  - Facilitation model between buyer and seller by providing information technology platform over digital / electronic network –vast ambit such as computers, TVs, internet applications, webpages, mobile applications, extranet, etc.)
  - Marketplace entity can enter into transactions with sellers registered on platform on B2B basis
  - Marketplace entity cannot exercise ownership / control over inventory of vendors i.e. goods proposed to be sold. Deemed control if more than 25 percent of purchases of a vendor are from marketplace or its group company in which case the model = Inventory based and prohibited [Earlier the condition was sales by vendor on platform to be restricted to 25%]
  - Entities having equity participation from marketplace entity or its group companies or having control on its inventory or its group companies not permitted to sell on the market platform
  - The sellers name, address and other details to be displayed on the platform. Post sales, delivery of goods, customer satisfaction & Warranty of goods / services to be responsibility of Seller



# Sector - E-Commerce (2 of 2)

Marketplace model of e-commerce ....

- Marketplace entity can facilitate payment for sale as per RBI Guidelines
- Marketplace entity shall not directly or indirectly influence the sale price of goods / services and maintain level playing field.
- Marketplace entity can provide vendors with logistic, warehousing, advertising or marketing payments, financing, etc. Cash back by group companies or marketplace entities should be fair and non-discriminatory
- Services provided by marketplace entity or other entities to all vendors to be at arm's-length and in a fair and non-discriminatory manner i.e. same terms in similar circumstances to all vendors
- No ecommerce entity to mandate any seller to sell any of their products exclusively on its platform
- Marketplace entity to obtain compliance report from the statutory auditor by 30th of September for preceding financial year (introduced by NDI Amendment Rules 2019)

*Note: NDI Rules - E-commerce entity definition now excludes a foreign company u/s 2(42) of the Companies Act 1961 or its branch, office or agency in India as per FEMA 1999 which existing in earlier Regulations*

# Sector - SBRT (1 of 2)

**Single Brand Retail Trading** - Several liberalizations since last decade to make this sector popular

- 100% under Automatic Route (NDI Rules 2019 carried old sectoral cap which got rectified retrospectively by NDI Amendment Rules)
- Products to be sold should be of a 'Single Brand' only
- Products should be sold internationally in one or more countries other than India
- Products to be are branded during manufacturing.
- PROI who is owner of the brand or otherwise can undertake SBRT through a legally tenable agreement executed between the Indian entity undertaking SBRT
- Indian Brands eligible to receive FDI as SBRT and brand owner / overseas country sale condition not applicable
- Allowing Wholesale Trading Entity to also engage in SBRT
- Retail online trade may be undertaken prior to opening of brick and mortar stores, subject to the condition that the entity opens brick and mortar stores within 2 years from the date of commencement of online retail
- Sourcing norms for foreign investments beyond 51% - see next slide.

# Sector - SBRT (2 of 2)

- **Sourcing norms from India for foreign investment in SBRT beyond 51%**
  - Sourcing of 30 percent of the value of goods purchased preferably from MSMEs, village and cottage industries, artisans and craftsmen, in all sectors.
  - To be met as an average of five years total value of goods purchase beginning from year of commencement. Thereafter, on annual basis.
  - Self certification / Statutory Auditor certificate
  - All procurements made from India by the SBRT entity for its single brand, at any time, will now be considered towards the local sourcing requirement, irrespective of whether the goods procured are sold in India **or exported**.
  - The **entire sourcing** from India for global operations of the SBRT Entity, and not just the 'incremental sourcing' (value of such sourcing over and above previous year) for global operations, will now be considered towards fulfilling the Local Sourcing Requirement. Further, the current cap of considering exports for 5 years only has been removed.
  - Procurement of goods from India for global operations may now be done by a SBRT Entity or its Group Company (resident or non-resident) or **indirectly by them through a third-party**, under a legally tenable agreement.
  - No sourcing norms for up to three from commencement of business for state of art / cutting edge technology products where local sourcing is not possible. Committee under DPIIT and Niti Aayog examine such claims.

# Sector - Real Estate (1 of 3)

## Construction Development: Townships, Housing, Built-up infrastructure – 100% Automatic

- Each phase of construction development project considered as a separate project
- Exit of NR simplified – (i) lock in of three years qua each tranche of foreign investment (ii) NR to NR not subject to any lock-in nor any government approval

### Project requirements

- a. Project to confirm to norms and standards including land use and community facility as per relevant regulations (Building Control, State, Municipal Or Local Board)
- b. Indian Investee company permitted to sell only developed parts
- c. Indian Investee company permitted to obtain all necessary approval including for building / layouts as per applicable laws
- d. State Government / Municipal / local Board to monitor the compliance of above conditions for the developer.

### Other conditions

1. Foreign investment is not permitted in an entity which is engaged or proposes to engage in **real estate business**, construction of farm houses and trading in transferable development rights (TDRs).
2. Condition of lock-in period shall not apply to Hotels and Tourist Resorts, Hospitals, Special Economic Zones (SEZs), Educational Institutions, Old Age Homes and investment by NRIs or OCIs.
3. Completion of the project shall be determined as per the local bye-laws/ rules and other regulations of State Governments.

# Sector- Real Estate (2 of 3)

## Real Estate Business

- Investment in SEBI registered / regulated REITs or earning of rent income on lease of the property, not amounting to **transfer** will not amount to real estate business.
- Transfer in relation to real estate includes,
  - (i) the sale, exchange or relinquishment of the asset; or
  - (ii) the extinguishment of any rights therein; or
  - (iii) the compulsory acquisition thereof under any law; or
  - (iv) any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882 (4 of 1882); or
  - (v) any transaction, by acquiring capital instruments in a company or by way of any agreement or any arrangement or in any other manner whatsoever, which has the effect of transferring, or enabling the enjoyment of, any immovable property.

## Issues

- Is leasing of property a permissible activity?
- DIPP clarification of 2015 for facility sharing between group companies (Annual lease rent not to exceed 5% of total revenue of Lessor Company) a better proposition?

# Sector - Real Estate (3 of 3)

## Other Conditions

### 4. Completed projects

- Foreign investment up to 100 percent under automatic route is permitted in completed projects for operating and managing townships, malls/ shopping complexes and business centres.
- Consequent to such foreign investment, transfer of ownership and/ or control of the investee company from persons resident in India to persons resident outside India is also permitted.
- Lock-in-period of three years, calculated with reference to each tranche of foreign investment and transfer of immovable property or part thereof is not permitted during this period.

### 5. Real estate broking services

- Real estate broking services is excluded from the definition of "real estate business"
- 100% foreign investment is allowed in real estate broking services under automatic route

# Sector - Pharma (7 of 10)

## Pharma

- Greenfield – 100% Automatic Route and Brownfield 100% (74% under Automatic Route and beyond that under Government Route)
  - Non-compete clause not permitted
  - Production level of NLEM drugs / consumables being maintained over next 5 years at an absolute quantitative levels (benchmark with highest level in three financial year immediately preceding the foreign investment)
  - R&D expenses being maintained over next 5 years at an absolute quantitative levels at the time of induction of foreign investment (benchmark with highest level in three financial year immediately preceding the foreign investment)
  - Complete information to be provided for transfer of technology, if any, to be provided to the administrative ministry.
- Medical devices manufacturing excluded from aforementioned conditions – products include diagnostics, investigation, disinfection, supporting / sustaining life, control of conception, etc.
- Currently, all the Pharma Application filed over the last one year or more are pending with DIPP / Department of Pharmaceuticals for clearances / approvals

# Sector - Financial Services

## Other Financial Services (OFS)

- OFS mean financial services activities regulated by financial sector regulators, viz., Reserve Bank, Securities and Exchange Board of India, Insurance Regulatory and Development Authority, Pension Fund Regulatory and Development Authority, National Housing Bank or any other financial sector regulator as may be notified by the Government of India.
- Foreign investment in OFS shall be subject to conditionalities, including minimum capitalization norms, as specified by the concerned Regulator/Government Agency
- OFS activities need to be regulated by one of the Financial Sector Regulators.
- If OFS not regulated or partly regulated or doubt - Government approval route.
- Any activity which is specifically regulated by an Act, the foreign investment limits shall be restricted to those levels/ limit that may be specified in that Act, if so mentioned.
- Downstream investments by any of these entities engaged in "Other Financial Services" that is treated as indirect foreign investment for the investee entity shall be subject to these rules.
- **Issues – First of a kind of back-step taken by the Government as most other sectors have been gradually liberalizing for foreign investments**



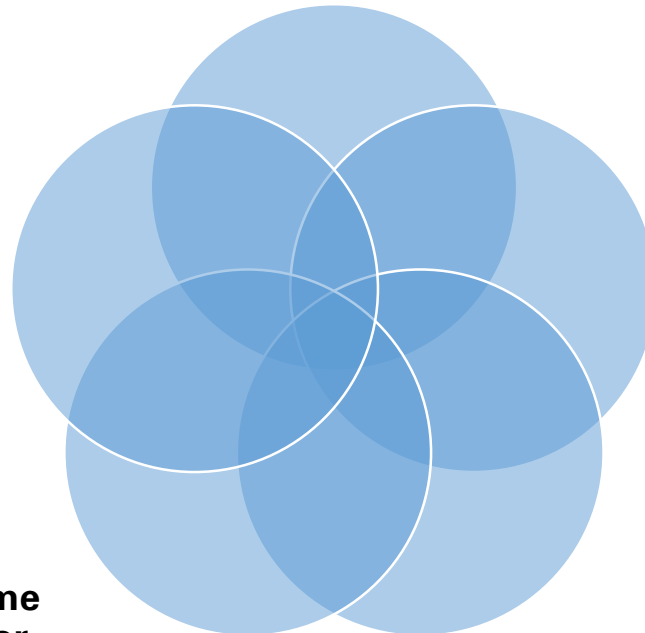
# Things to watch out for

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## Key Sectoral liberalization

- Other FS Sector
  - Pharma
- E-commerce platform
- Downstream investments for sectors under Automatic Route

**Government policy  
on Hybrid  
Instruments**



**Expediting  
Government  
approval process and  
transparency in  
proceedings**

**Liberalization of  
pricing norms – some  
leeway for higher or  
lower deals**

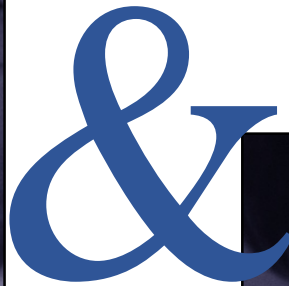
**Public participation  
in evaluation of the  
FDI policy**

# Q&A

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**Questions**



**Answers**

**THANK YOU ALL FOR YOUR ATTENTION !**

**CA Shabbir Motorwala**

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