

Virtual Refresher Course on FEMA
by
Western Regional Council of ICAI

Overseas Direct Investment

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Presented by
CA Hardik Mehta

Definition of Capital Account Transactions

Section 2(e) defines “Capital Account Transactions” to mean - a transaction which –

- *alters the assets or liabilities, including contingent liabilities, outside India of a PRI, or*
- *assets or liabilities in India of PROI,*

Overseas Direct Investment

- FEM Permissible Capital Account Transactions – FEMA 1
- FEM (Transfer or Issue of any foreign security) Regulations, 2004 - FEMA 120
- Master Direction on Overseas Direct Investments
- FAQs on Overseas Direct Investments
- Master Direction on Liberalised Remittance Scheme
- FAQs on Liberalised Remittance Scheme

Permissible Capital Account Transactions

- Schedule I- Transactions of Person Resident in India
- Schedule II- Transactions of Person Resident Outside India

Schedule I-Transactions by Person Resident in India

- a) Investment by a person resident in India in foreign securities
- b) Foreign currency loans raised in India and abroad by a person resident in India
- c) Transfer of immovable property outside India by a person resident in India
- d) Guarantees issued by a person resident in India in favor of a person resident outside India
- e) Export, import and holding of currency/currency notes
- f) Loans and overdrafts (borrowings) by a person resident in India from a person resident outside India

Schedule I-Transactions by Person resident in India (Contd.)

- g) Loans and overdrafts by a person resident in India to a person resident outside India
- h) Maintenance of foreign currency accounts in India and outside India by a person resident in India
- i) Taking out of insurance policy by a person resident in India from an insurance company outside India.
- j) Remittance outside India of capital assets of a person resident in India.
- k) Sale and purchase of foreign exchange derivatives in India and abroad and commodity derivatives abroad by a person resident in India.

Schedule II - Transactions by Person resident outside India

- a) Investment in India by a person resident outside India, that is to say,
- Issue of security by a body corporate or an entity in India and investment therein by a person resident outside India;
 - and
 - Investment by way of contribution by a person resident outside India to the capital of a firm or a proprietorship concern or an association of persons in India
- b) Acquisition and transfer of immovable property in India by a person resident outside India.
- c) Guarantee by a person resident outside India in favor of, or on behalf of, a person resident in India
- d) Import and export of currency/currency notes into/from India by a person resident outside India.

Schedule II-Transactions by Person resident outside India (Contd.)

- e) Deposits between a person resident in India and a person resident outside India.
- f) Foreign currency accounts in India of a person resident outside India.
- g) Remittance outside India of capital assets in India of a person resident outside India.

FEM (Transfer or Issue of any foreign security) Regulations, 2004 - FEMA 120

Reg. 2 – Definitions

Reg. 3 - General Prohibition clause on issue or transfer of foreign security

Reg. 4 – Purchase and sale of foreign security by a person resident in India

Part I Direct Investment Outside India

Reg. 5 – General Prohibition on Direct Investment Outside India

Reg. 6 – Permission for Direct Investment in certain cases - Automatic Route

Reg. 6A - Investments in Agricultural operations overseas directly or through Overseas Offices

Reg. 6B – Investment in Equity overseas by a listed Indian company

FEM (Transfer or Issue of any foreign security) Regulations, 2004 - FEMA 120

Reg. 6C – Investment by Mutual Funds

Reg. 6D – Acquiring equity of SWIFT

Reg. 7 – Investment by IP in Financial Services Sector

Reg. 8 – Investment by swap or exchange of shares (omitted)

Reg. 9 – Prior Approval Route in certain cases

Reg. 9A – Overseas Investments by Regd. Trust / Society

Reg. 10 – Unique Identification Number

Reg. 11 – Investment by Capitalization

Reg. 12 – Export of Goods towards Equity - Procedure

Reg. 13 – Post investment changes / additional investment in existing JV / WOS

FEM (Transfer or Issue of any foreign security) Regulations, 2004 - FEMA 120

Reg. 14 – Acquisition of a foreign company through bidding / tender

Reg. 15 – Obligations of the Indian Party

Reg. 16 – Transfer by way of sale of shares of JV / WOS outside India

Reg. 16A – Restructuring of the balance sheet of JV/WOS involving write-off of capital and receivables

Reg. 17 – Transfer by way of sale of shares involving write-off

Reg. 18 – Pledge of shares of JV / WOS and SDS

Reg. 18A – Creation of charge on domestic and foreign assets

FEM (Transfer or Issue of any foreign security) Regulations, 2004 - FEMA 120

Part II Investment Abroad by Individuals in India

Reg. 19 – Prior RBI approval for Proprietary concern in India to accept shares

Reg. 19A – ODI by Proprietorships / unregistered Partnership Firm in India being recognized Star Export House

Reg. 20 – Investments by Individuals for acquiring shares as consideration for professional services rendered

Reg. 20A - Acquisition or Setting up of a JV or WOS abroad by resident individual (w.e.f. 5th Aug. 2013)

FEM (Transfer or Issue of any foreign security) Regulations, 2004 - FEMA 120

PART III – Investments in Foreign Securities other than by way of Direct Investment

Reg. 21 – Prohibition on Issue of foreign security by person resident in India
(Omitted)

Reg. 22 – Purchase / acquisition of foreign securities by way of gift / inheritance / ESOP

Reg. 23 – Transfer of foreign security by way of pledge by person resident in India

Reg. 24 – General permission for acquiring of foreign securities as qualification / rights shares and foreign securities under ADR/GDR linked stock options schemes

FEM (Transfer or Issue of any foreign security) Regulations, 2004 - FEMA 120

Reg. 25 – Prior RBI approval for qualification shares in excess of limits specified under Reg. 24

Reg. 26 – Investments by Mutual Funds and other Funds

Reg. 27 – Opening of Demat Accounts with foreign depositories by Indian Clearing Corporations and Clearing Members

Schedule I – Automatic Route for Issue of FCCBs

Schedule III – Overseas Investments by Registered Trust/Society

Schedule IV – Foreign Currency Exchangeable Bonds (FCEBs)

Schedule V – ODI by Resident Individuals

Overseas Direct Investment

Introduction

- Meaning of Direct Investment Outside India
- Eligible entities
- General prohibitions for Direct Investment outside India
- General Permission for Direct Investment Outside India
- Routes of Investment – Automatic and Approval

Overseas Direct Investment

Investment in JV/WOS/SPV under Automatic Route

Definition of Indian Party



Posers –

- Individuals and unregistered partnership firms covered under the definition of Indian Party can make investment under ODI?
- Registered trusts and societies are allowed to operate under all the sectors? Is the RBI approval required for making ODI?

ODI by Indian Partnership Firm

- Permitted activities that partnership firms can undertake through ODI
- Holding of shares of the overseas JV / WOS for and on behalf of the firm by partners
- Investment in agriculture by partnership firms
- ODI by unregistered partnership
- Utilize the net worth of its Indian subsidiary / holding company for investing in a JV/WOS abroad?

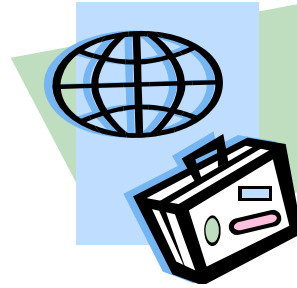
ODI by Trusts

- Registered Trusts and Societies engaged in
 - -manufacturing ;
 - - educational
 - -hospital sector
- Allowed to make investment (or financial commitment) in the same sector(s) in a JV/WOS outside India,
- With the prior approval of the Reserve Bank.

ODI by Proprietorship Concern and unregistered Partnership

➤ Eligibility

➤ Limit of investments



Overseas Direct Investment

Manner of Funding

- i) Remittance Abroad
- ii) Capitalization of Exports
- iii) Swap of Shares
- iv) Utilization of ECBs/FCCBs
- v) Exchange of ADRs/GDRs
- vi) Utilization of EEFC Account
- vii) Proceeds of ADRs/GDRs

General Permission to PRI for purchase of securities from –

- i) Out of funds in RFC
- ii) As bonus shares on existing holding of foreign currency shares
- iii) Out of the foreign currency resources if not permanently resident in India

Overseas Direct Investment

All other types of investment not included under the Automatic route would require prior RBI Approval

Factors considered by RBI before granting the approval –

- a) Prima facie viability of the JV / WOS outside India;
- b) Contribution to external trade and other benefits which will accrue to India through such investment (or financial commitment);
- c) Financial position and business track record of the Indian Party and the foreign entity; and
- d) Expertise and experience of the Indian Party in the same or related line of activity as of the JV / WOS outside India.

Overseas Direct Investment

Investment in JV/WOS/SPV under Automatic Route

➤ Investment Limit and other investment conditions -

Total financial commitment upto which an Indian party can invest is upto 400% of the net worth as per the latest audited balance sheet.

The overall limit for investment under the Automatic route is USD 1 billion.
The components of the financial commitment is as mentioned

➤ Business Activities –

JV/WOS created by the Indian entity shall engage in any **bona fide** business activity. Activities include agriculture but excludes Real Estate and Banking Business.

Funds transferred shall be utilized for the business activities and not just kept idle outside India

Components of financial commitment

The total financial commitment of the Indian Party in all the Joint Ventures / Wholly Owned Subsidiaries shall comprise of the following:

- a. 100% of the amount of equity shares and/ or Compulsorily Convertible Preference Shares (CCPS);
- b. 100% of the amount of other preference shares;
- c. 100% of the amount of loan;
- d. 100% of the amount of guarantee (other than performance guarantee) issued by the Indian Party;
- e. 100% of the amount of bank guarantee issued by a resident bank on behalf of JV or WOS of the Indian Party provided the bank guarantee is backed by a counter guarantee / collateral by the Indian Party.
- f. 50% of the amount of performance guarantee issued by the Indian Party provided that if the outflow on account of invocation of performance guarantee results in the breach of the limit of the financial commitment in force, prior permission of the Reserve Bank is to be obtained before executing remittance beyond the limit prescribed for the financial commitment.

Other Investment Conditions

1) Equity participation –

Automatic route - Loan/ guarantee can be extended to the overseas JV/ WOS only if the Indian party has equity participation in it

Approval route - Loan/ guarantee can be extended to the overseas JV/ WOS without the Indian party having equity participation in it

2) Guarantee –

Indian entities can offer corporate guarantee – Corporate or Personal that includes –

- Personal guarantee can be given by the indirect resident individual promoters of the Indian party
- Primary or collateral
- Guarantee by the promoter company / guarantee by group company, sister concern or associate company subject to certain conditions.

One of the important conditions is that the guarantee should not be open ended

Other Investment Conditions

3) The Indian Party should not be on the RBI's Exporters' caution list / list of defaulters to the banking system circulated by the RBI / CIBIL / or any other credit information company as approved by the Reserve Bank or under investigation by any investigation / enforcement agency or regulatory body.

4) **Authorised Dealer –**

All the transactions should be routed through one branch of an AD

5) **Valuation –**

In case of acquiring shares of an existing foreign company, having investment more than USD 5 million, valuation shall be made by a Category I Merchant Banker registered with SEBI or an Investment Banker / Merchant Banker outside India registered with the appropriate regulatory authority in the host country

All other cases by a Chartered Accountant or a Certified Public Accountant.

6) **Investment by partners** of the partnership firm in the overseas JV/ WOS is permitted if the host country regulations warrant such holdings

Other Investment Conditions

7) Indian party can acquire shares of the foreign company that is engaged in the bonafide business activity. Such shares can be purchased **in exchange of ADRs/ GDRs as per the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares Scheme, 1993** and the guidelines as prescribed.

8) Investment/ Financial commitment in Nepal - permissible in INR only,
Bhutan – INR and freely convertible currencies, Pakistan –Approval route

Prohibited business activity



Posers -

Can PQR LLC engage in buying and selling the properties with the sole motive of earning profit? Is leasing out the property after buying a permissible activity?

Can PQR LLC construct the commercial premises and lease out to other businesses? Is selling these premises permissible?

Can PQR LLC form another entity – XYZ LLC which will buy and sell the properties?

Guarantees by Indian Promoters

- Issue of performance Guarantee in favour of JV/WOS –FAQ20
- Permission to issue corporate guarantee on behalf of its second generation subsidiary abroad. FAQ21
- Open ended guarantee not allowed – As per A.P. (DIR Series) Circular No. 29 dated March 27, 2006 and FAQ23
- Rollover of guarantee allowed under the automatic route. –FAQ24
- Change in the end use of guarantee or overseas lender or rate of interest or amount or any other terms and conditions of the guarantee shall subject the rollover of guarantee to the extant FEMA compliance afresh.

Overseas Direct Investment

FAQ 40 - Indian party having step-down subsidiaries under the Automatic route within the overall limit

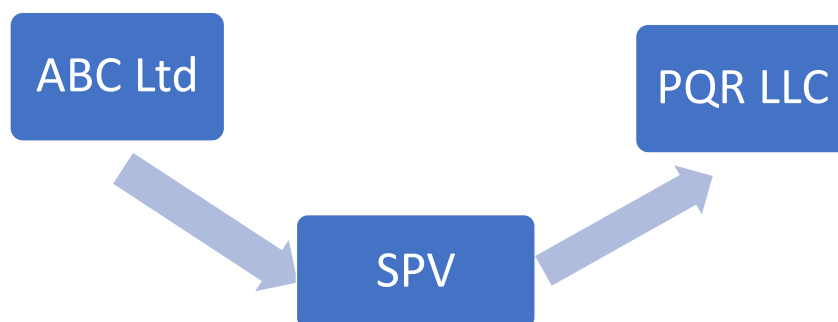


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Overseas Direct Investment

FAQ 41 – Funds can be invested by the IP through SPV under the Automatic route only for the purpose of investment in JV/ WOS



This implies that multi-layered SPVs cannot be created for investment in JV/ WOS abroad

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Disinvestment from the overseas JV/ WOS under Automatic route

Conditions for disinvestment without write-off

1. Sale effected through SE where shares of JV/ WOS are listed
2. Share prices are as certified by CA/ CPA if the shares are not listed
3. No outstanding dues like dividend, royalty, etc are pending
4. JV/ WOS operational for atleast 1 year and APR & audited accounts submitted to RBI
5. IP is not under investigation
6. Terms and conditions under Regulation 16 of the notification

Conditions for disinvestment involving write-off

1. Pre-conditions from serial no. 1 to 4 as mentioned in the disinvestment without write off
2. Shares of the JV/ WOS should be listed
3. Listed IP should have net worth of atleast 100 crores
4. Unlisted IP should not have invested more than USD 10 million in overseas JV/ WOS
5. Listed IP having net worth of less than 100 crores but investment in JV/ WOS does not exceed USD 10 million

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Restructuring balance sheet of the overseas JV/ WOS

Writing off capital & other receivables in respect of JV/ WOS even while JV/ WOS continue to function subject to the conditions -

Listed Indian companies

↓
**Write off
upto 25%**

Automatic route

Unlisted companies

↓
**Write off
upto 25%**

Approval route

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OVERSEAS DIRECT INVESTMENT

Obligations of Indian Party

- Documentary Evidences for Investments Abroad
- Repatriation of Income Earned Abroad
- Annual Performance Report
- Exit Route

OVERSEAS DIRECT INVESTMENT

Pledge of shares

IP can avail fund based/ non-fund based facility for itself or JV/ WOS/ SDS outside India

For this purpose, shares of itself/ JV/ WOS/ SDS outside India can be pledged as security in favour of an AD/ public financial institution/ overseas lender subject to terms and conditions as prescribed

Creation of charge on domestic and foreign assets

IP can create charge on its own assets as security for availing fund/ non-fund based facility from overseas lender for its JV/ WOS/ SDS outside India

IP can create charge on the assets of the overseas JV/ WOS/ SDS in favour of AD bank in India as security for availing fund based/ non-fund based facility for itself/ JV/ WOS/ SDS outside India

OVERSEAS DIRECT INVESTMENT

Rollover of guarantees

The guarantee issued will not be treated as a fresh financial commitment if the following conditions are fulfilled –

- The original guarantee was issued as per the FEMA guidelines
- There is no change in the end use of guarantee
- There is no change in the terms & conditions and the amount of guarantee except the validity period
- However, the reporting of this rollover guarantee shall be as per the fresh financial commitment in part II of form ODI
- Any investigation of the IP shall be informed to the concerned agency/body

OVERSEAS DIRECT INVESTMENT

Hedging of ODI

- Resident entities is permitted to hedge the foreign exchange rate risk associated with overseas direct investments (or financial commitment). AD Category - I banks may enter into forward / option contracts with resident entities who wish to hedge their overseas direct investments (in equity and loan), subject to verification of such exposure.
- If a hedge becomes naked in part or full owing to shrinking of the market value of the overseas direct investment (or financial commitment), the hedge may continue to the original maturity. Rollovers on the due date are permitted up to the extent of market value as on that date.

OVERSEAS DIRECT INVESTMENT

Resident Individuals – Schedule V (Regulation 20A)

- A resident individual can make ODI in the equity shares and compulsorily convertible preference shares of a JV/ WOS outside India.
- The ODI limit for the resident individuals shall be as per the provisions of Liberalised Remittance Scheme, as prescribed by the Reserve Bank from time to time.
- Resident individuals w.e.f August 5, 2013 can set-up/ acquire JV/ WOS overseas

OVERSEAS DIRECT INVESTMENT

Resident Individuals - Schedule V (Regulation 20A)

- JV/ WOS abroad should not be engaged in the real estate business or banking business or in the business of financial services activity
- JV/ WOS abroad shall be engaged in bonafide business activity
- JV/ WOS should not be located in the countries identified by the Financial Action Task Force (FATF) as "non co-operative countries and territories" as available on FATF website www.fatf-gafi.org or as notified by the Reserve Bank (Iran and North Korea)
- Should not be on the Reserve Bank's Exporters Caution List or List of defaulters to the banking system or under investigation by an enforcement agency/body
- Investment made out of the balances held in EEFC / RFC account shall also be restricted to the limit prescribed under LRS
- JV or WOS **shall be an operating entity only and no step down subsidiary is allowed** to be acquired or set up by the JV or WOS
- For the purpose of making investment under this Schedule, the valuation shall be as per Regulation 6(6)(a) of this Notification

OVERSEAS DIRECT INVESTMENT

Resident Individuals - Schedule V (Regulation 20A)

- Any change in shareholding pattern of the JV/WOS may be reported to the AD within 30 days including reporting in APR as required
- Disinvestment (partially or fully) allowed by way of transfer / sale or by way of liquidation/ merger of the JV or WOS
- Disinvestment by a resident individual shall be allowed **after one year from the date of making first remittance** for setting up or acquiring the JV or WOS abroad.
- Disinvestment proceeds shall be repatriated to India immediately and in any case not later than 60 days from the date of disinvestment and same may be reported to the designated AD
- No write off shall be allowed in case of disinvestments by the resident individuals

OVERSEAS DIRECT INVESTMENT

Resident Individuals - Schedule V (Regulation 20A)

(.....Cont'd)

- The resident individual, making overseas direct investments under the provisions of this Schedule, shall submit Part I of the Form ODI, duly completed, to the designated authorised dealer, within 30 days of making the remittance and same needs to be reported by AD bank to the RBI
- The obligations as required in terms of Regulation 15 of Notification 120 shall also apply to the resident individuals who have set up or acquired a JV or WOS under the provisions of this Schedule
- The disinvestment by the resident individual may be reported by the designated AD to the Reserve Bank in Form ODI Part IV within 30 days of receipt of disinvestment proceeds

Overseas Direct Investment

General permission has been given to an individual PRI for -

- i. Acquiring foreign securities as gift from PROI
- ii. Acquiring shares under cashless ESOP issued by a company outside India without any remittance from India
- iii. Acquiring shares by way of inheritance from PRI or PROI
- iv. Shares offered by the foreign company under the ESOP schemes to an employee/ director of Indian office/ branch of foreign company/ subsidiary in India of a foreign company/ an Indian company.

PRI can transfer the shares as acquired above by way of sale but the proceeds should be repatriated immediately/ not later than 90 days from day of sale

Overseas Direct Investment

General permission has been given to certain resident employees for acquiring foreign security by following means -

- i. Qualification shares if he is a director of a company outside India
- ii. Shares of the JV/ WOS abroad by the employees/ directors of the Indian promoter company engaged in the field of software subject to certain limits
- iii. The resident employees of the Indian company engaged in the knowledge based sector can purchase foreign securities under ADR/ GDR linked option schemes. The consideration for purchase should not exceed the ceiling as prescribed

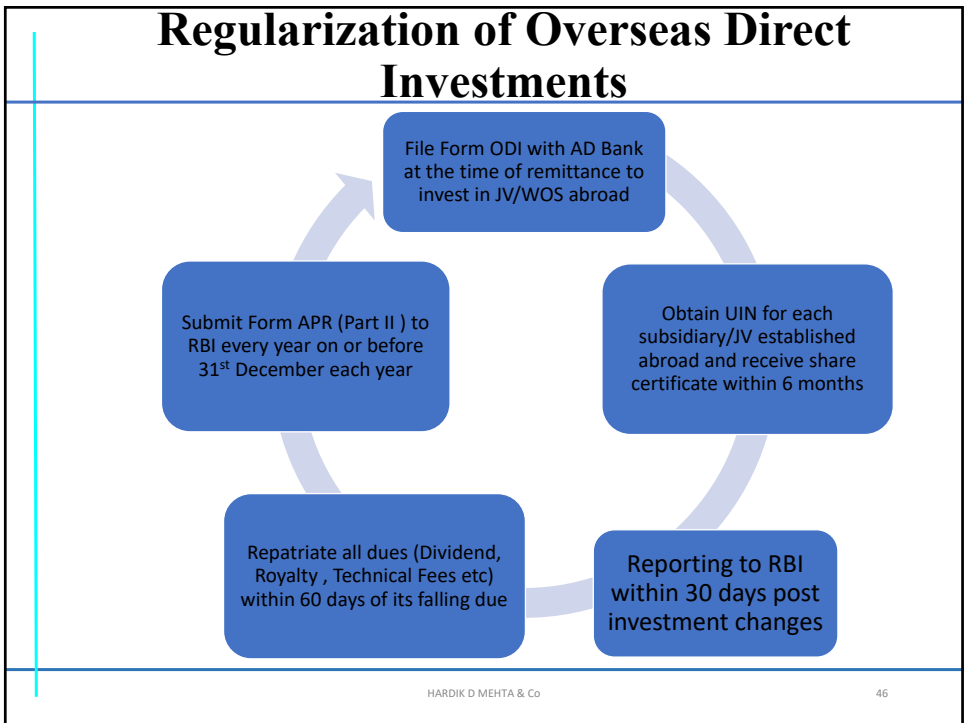
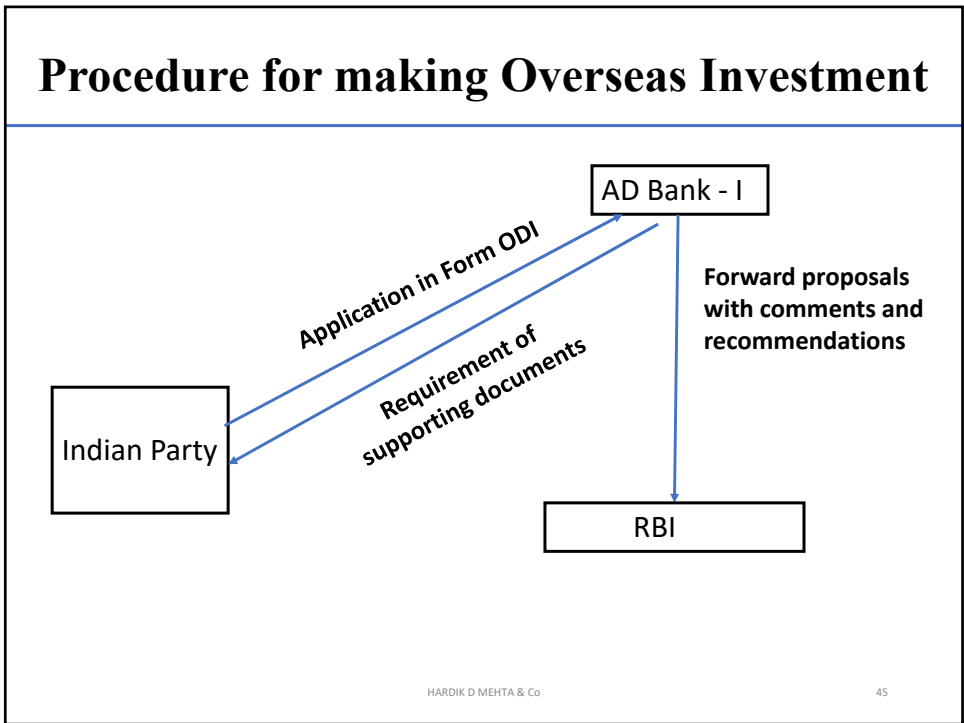
Overseas Direct Investment

Check List for Compliance

- i. Investment within limit
- ii. Investment in Eligible Entities
- iii. Investment in Eligible Activities
- iv. Remittance through Normal Banking Channel
- v. Manner of Funding
- vi. Filing of Form ODI
- vii. Obtaining Share Certificate
- viii. Yearly Reporting in Form APR
- ix. Filing of FLAIR(FLA)

ODI Forms

Form ODI (Part I)	Along with remittance for the first time (in advance for future remittances) or at the time of every remittance
Form ODI (Part II)	Reporting of remittances (or financial commitment)
Form ODI (Part III) i.e. APR (Annual Performance Report)	Every year by December 31
Form ODI (Part IV)	Within 30 days from the date of disinvestment



Reporting in Form ODI in various sections for post investment changes

- The Indian Party should report to the Reserve Bank through the AD Category - I bank,
- Within 30 days of the approval of those decisions by the competent authority of the JV / WOS concerned in terms of local laws of the host country and
- Include the same in the Annual Performance Report (APR - Part II of Form ODI) required to be forwarded to the AD Category-I bank.

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Compliances under Overseas Direct Investments

Sr. No.	Type of post investment change	Relevant Section of Form ODI
1.	Change in the details of IP/ RI viz. Change in the name, Address, contact details, status.	Section A
2.	Investigation details of the IP / RI	Section A
3.	Change in the Networth of the IP	Section A
4.	Change in capital structure of the JV/ WOS	Section B
5.	Change in status of JV/ WOS from operating entity to SPV or vice versa	Section B
6.	Change in the details of JV/ WOS such as name address etc.	Section B
7.	Reporting of setup/ incorporation/ investment / disinvestment of SDS	Section B
8.	Conversion of loan into equity and vice versa	Section C
9.	Rollover/ change in amount / validity date of the guarantee already reported to the Reserve Bank	Section C

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Issues in Overseas Direct Investments (ODI)

- ODI investments by Individuals – Change of Residential Status
- Issues in Form ODI – II i.e. Annual Performance Report (APR)
- Regularization of Overseas Direct Investments
- ODI by Indian Partnership Firms/Trusts
- Definition of Bonafide activity
- Definition of Joint Venture
- Proof of investment abroad i.e. shares, membership units, agreement, partnership share etc.
- Guarantees by Indian Promoters
- Reporting in Form ODI in various sections for post investment changes
- Differentiation between Portfolio Investment and ODI Investment

Issues in Form ODI – II i.e. Annual Performance Report (APR)

1. **Para V (iii)** : Whether income realised from JV/WOS on account of export of goods to be included under Non-Equity Exports Realised (in INR)?

2. **Para V (iii)** : Whether income realised from JV/WOS on account of export of services to be included under Non-Equity Exports Realised (in INR)? If not, then what is to be reported under Non-Equity Exports Realised (in INR)

Issues in Form ODI – II i.e. Annual Performance Report (APR) (Contd.)

3. Para V (ix) : We understand that as per Para 11.47 of BOP Manual of IMF, reinvested earnings of SDS need to be added to retained earnings of JV/WOS. However, retained earnings amount of SDS needs to be converted from reporting currency of SDS to that of reporting currency of JV/WOS? Which exchange rate is to be adopted while adding such retained earnings of SDS – year end exchange rate or average exchange rate of the year?

4. Para V : Under which head, commission service income received from JV/WOS needs to be reported - Non-Equity Exports Realised (in INR) (Para V(iii)) or Consultancy Fees(Para V(vi)) or Others(Para V(vii))?

Issues in Form ODI – II i.e. Annual Performance Report (APR) (Contd.)

5. Para V(vii) :What needs to be reported under the head 'Others'?

6. Para VI(vii) : Whether direct % stake of JV/WDS into SDS needs to be reported or indirect % stake of Indian party?

7. Para VI : Whether details of step-down portfolio investment also needs to be reported under para VI?

Issues in Form ODI – II i.e. Annual Performance Report (APR) (Contd.)

- Certificate by statutory auditors required or not for RIs.
- Loss to be mentioned in APR?
- Submission of APR to whom?
- Reporting of Redemption of Preference shares ?
- Multiple IPs / RIs invested in the same overseas JV / WOS, who shall submit APR?

Issues in Form ODI – II i.e. Annual Performance Report (APR) (Contd.)

- Where multiple IPs / RIs have invested in the same overseas JV / WOS,
 - the obligation to submit APR shall lie with the IP / RI having maximum stake in the JV / WOS.
 - or the IPs / RIs holding stake in the overseas JV / WOS may mutually agree to assign the responsibility for APR submission to a designated entity which may acknowledge its obligation to submit the APR in term of Regulation 15 (iii) of Notification, *ibid*, by furnishing an appropriate undertaking to the AD bank

Annual Return of Liabilities & Assets

- Replacement of email-based reporting system by web-based online reporting portal (FLAIR system) for submission of FLA return.
- FLA Return to be filed by all Indian Companies: which have received FDI and/or made FDI abroad (i.e. overseas investment) in the previous year(s) including the current year.
- To be submitted by July 15 of every year.
- Indian entities not complying with above, will be treated as non-compliant with Foreign Exchange Management Act, 1999 and regulations made thereunder

Opening of a Branch, Representative Office Abroad

➔ Permission under FEMA

Initial expenses up to 15% of the avg. annual sales/income or turnover during the last two F.Y. years or up to 25% of the net worth, whichever is higher.

Recurring expenses, remittances up to 10% of the avg. annual sales/income or turnover during the last F.Y. year may be sent for the purpose of normal business operations of the office (trading /non-trading) / branch or representative office outside India subject to the following terms and conditions:

- a) the overseas branch/office has been set up or representative is posted overseas for conducting normal business activities of the Indian entity;
- b) the overseas branch/office/representative shall not enter into any contract or agreement in contravention of the Act, Rules or Regulations made there under;
- c) The account so opened, held or maintained shall be closed, (a) if the overseas branch/ office is not set up within six months of opening the account, or (b) within one month of closure of the overseas branch/ office, or (c) where no representative is posted for six months, and the balance held in the account shall be repatriated to India

Opening of a Branch, Representative Office Abroad

→ Opening of Bank Accounts Abroad

- A BO may approach any AD Category-I Bank in India to open an account for its operations in India. Credits to the account should represent the funds received from Head Office through normal banking channels for meeting the expenses of the office and any legitimate receivables arising in the process of its business operations. Debits to this account shall be for the expenses incurred by the BO and towards remittance of profit/winding up proceeds.
- The details of bank accounts opened in the overseas country should be promptly reported to the AD Bank.

Opening of a Branch, Representative Office Abroad

→ Acquisition of Immovable Property

- Purchase of immovable property and other asset for the normal business operations of the overseas branch office is permitted, hence, no RBI approval required.
- Acquisition of immovable property outside India by way of lease, not exceeding a period of five years by the overseas branch or office is permitted without obtaining RBI approval.
- AD Category – I banks may also allow remittances by a company incorporated in India having overseas offices, within the above limits for initial and recurring expenses, to acquire immovable property outside India for its business and for residential purpose of its staff.

Round Tripping of Investment and recommendations of High Level Advisory Group*

➤ Foreign Direct investment (FDI) by a non-resident entity which has ODI funding from India is not a bona fide business activity in terms of the provisions of ODI Regulations.

➤ The following cases should not be considered as 'round tripping' or in violation of ODI Regulations, subject to conditions herein as stated in the respective cases:

- a) Undertaking ODI in a structure which already has an FDI in India
- b) Undertaking fresh FDI in India by entities where ODI has been made by an Indian Party

*Report of the High Level Advisory Group constituted by the Minister of Commerce and Industry, Department of Commerce, Government of India dated 12th September 2019

Undertaking ODI in a structure which already has an FDI in India

It is recommended that an Indian party should be allowed to undertake ODI in a structure which already has an existing FDI structure in India provided that:

- i. Total value of existing FDI does not exceed 25% of the consolidated net worth of the foreign entity in which ODI is being made; and
- ii. Any additional FDI should be allowed provided such funds are not directly or indirectly from India.

Undertaking fresh FDI in India by entities where ODI has been made by an Indian Party

It is recommended that in cases where such foreign JV or WOS is investing money in India through funds which are earned overseas from legitimate and bona fide business activities and such funds are invested as FDI in India through proper banking channels, such structures should be permitted under the Automatic Route, subject to fulfilment of the following conditions (which shall ensure investment is bona fide):

- i. Total value of FDI shall not be more than 25% of the consolidated net worth of the overseas entity in which ODI has already been undertaken; and
- ii. Net worth of overseas entity should be at least USD 10 million.

Case Study 1

Mr. A is an Indian resident under FEMA and wants to set up a new company in Singapore. He wants to remit USD 10,000 towards equity share capital. He also wants to provide USD 1,00,000 as loan to its Singapore company. Also, he wants to provide a personal guarantee to HSBC Singapore of USD 1,00,000 line of credit to its company in Singapore. The total remittance for the financial year would be less than USD 2,50,000.

Poser:-

Whether Mr. A can set up a company in Singapore ?

Whether it can remit funds towards equity capital and loan?

Can he provide personal guarantee to HSBC Singapore?

Case Study 2

A Ltd, an Indian company has a SPV in Singapore which has invested in the operating company B Inc situated in USA. A Ltd now wants to directly invest in B Inc and also wants to give guarantees both corporate and bank guarantees on behalf of B Inc to its bank. Bank guarantee would be for three years. No tenure for corporate guarantee is mentioned in the sanction letter issued by the bank. However, it would be renewed at the time of renewal of the line of credit.

Poser:-

Can A Ltd directly fund B Inc?

Can it provide corporate and bank guarantees on behalf of B Inc?

Whether the tenure of the guarantees are within the limit prescribed by RBI?

Case Study 3

X Ltd is an Indian unlisted Company having its WOS Y Ltd in UK. Y Ltd wants to invest in various other companies in Europe. The nature of such investments would be portfolio investments.

Poser:-

Whether Y Ltd can make such portfolio investment outside India?

Whether there is any reporting requirement for such investments under Notification FEMA 120?

Case Study 4

PQR Ltd is an Indian unlisted Company having set up its WOS XYZ Ltd in Indonesia. XYZ Ltd has shown PQR Ltd as the shareholder, however no remittance has been made by PQR Ltd towards acquisition of subscriber shares. In Indonesia, there is no time limit or compulsion to contribute towards share capital.

Poser:-

Whether PQR Ltd can acquire shares in WOS without upfront remittance or on deffered basis?

Is there any time limit by when such remittance needs to be made and how can such shares be reported without remittance?

Checklist for Audit/Due diligence of ODI Transactions

Following are the factors to be considered while undertaking due diligence on compliances under FEMA, 1999, in respect of Overseas Direct Investments (ODI):

- 1) To check whether ODI falls under the automatic route or approval route.
- 2) Check if the limit prescribed (400% of the net worth of the Indian Party) by the RBI for the overseas investments is complied with.
- 3) Check that the total amount of investments made abroad should not exceed USD 1 Billion in a financial year (even if it is within the limit of 400% for the Indian Party).
- 4) To check, while incorporating a WOS/JV abroad, the Indian Party has reported the said investment to the RBI in Form ODI Part I through the AD Category - I Bank.

Checklist for Audit/Due diligence of ODI Transactions

- 5) Whether share certificates or any other document are received as an evidence of investment within six months from the date of transactions or the date on which such amount was capitalised.
- 6) To check whether any dues receivable from the foreign entity, like dividend, royalty, technical fees etc., is received or repatriated by the Indian Party within 60 days of its falling due.
- 7) To check whether Form ODI Part II (Annual Performance Report – APR) in respect of each WOS/JV is submitted to the RBI through the AD Bank every year on or before 31st December and it has to be based on the audited annual accounts of the JV/WOS for the preceding year.
- 8) To check whether the APR is certified by the Statutory Auditor.

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Checklist for Audit/Due diligence of ODI Transactions

- 9) To check whether any changes in post investment has been intimated to the RBI in the relevant section of Form ODI Part I within 30 days of the change.
- 10) In case of closure / divestment / Voluntary Liquidation / Winding up of WOS/JV, whether Form ODI Part – III is filed with the RBI through AD Category I Bank within 30 days of the disinvestment.
- 11) Check whether sale proceeds of shares / securities has been repatriated to India immediately on receipt thereof and in any case not later than 90 days from the date of sale of the shares / securities.
- 12) To check whether Form FLA (Annual Return for Foreign Assets and Liabilities) is filed with the RBI before 15th of July of the year in which financial year ends.

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Compounding Orders

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Notification No. 120/2004 - RB

AG Technologies Pvt Ltd (CA No. 3982/2016)

Facts of the case –

The applicant is engaged in the business of designing, developing, manufacturing & marketing of micro, mini & mainframe computer based systems. It set up a WOS, AG Tech USA Inc in New York under the automatic route. After acquiring 100% stake in WOS, the remittances were made towards investment in WOS in USA.

Form ODA was submitted to the AD bank for the remittances made to WOS but it was not submitted to RBI and UIN was not obtained by the applicant.

Relevant regulation –

Regulation 15 (iii) – An IP shall submit an Annual Performance Report in form APR to RBI within 60 days from the date of expiry of the statutory period by the respective laws of host country for finalisation of accounts of JV/WOS

Regulation 6(2)(vi) – Indian party can make direct investment in a JV/WOS & has to submit form ODI part I within 30 days

Regulation 10 – RBI will allot a UIN for each JV/WOS & the Indian party shall quote such number in all its communications & report to RBI & AD

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Notification No. 120/2004 - RB

Key takeaway –

- Even though the applicant had fulfilled its requirement to report the overseas investments, the bank did not forward the same to RBI.
- In such case, the applicant continues to be held in contravention & bank would be held liable for non-compliance as the onus of compliance with FEMA lies on the applicant.
- However, one may notice that in case of Atul Limited (CA No. 4055/2016), the applicant submitted copies of the duly acknowledged forms & letters & it was considered not to be in contravention of Reg 6(2)(vi)

Notification No. 120/2004 - RB

Jasper Infotech Private Limited (CA No.4504/2017)

Facts of the case –

The applicant, JIPL was engaged in the business of digital marketing solutions through web & non –web based platforms.

Accelyst Solutions Private Limited (ASPL), an Indian company, the equity was held by Shri Kunal Shah and 50% by Tancom Electronics Pvt Ltd. Accelyst Pte Ltd (APL), incorporated in Singapore was the holding company of ASPL. APL raised funds through issuance of optionally convertible preference shares (OCPS) to NR investors. ASPL issued CCDs to APL which were converted later into equity shares.

JIPL is a widely foreign owned & controlled company & it received FDI into equity & preference shares from various non-resident companies.

JIPL acquired the shares of APL from the resident & non-resident individuals at the time when APL already had a JV in India i.e. ASPL. The acquisition of APL into ASPL resulted into ODI-FDI structure

Relevant regulation –

Regulation 6(2)(ii) – Investment in JV/WOS in bonafide activities

Regulation 5(1) r.w. regulation 6(2)(ii)– Business undertaken through structures like FDI through ODI is not treated as bonafide.

Notification No. 120/2004 - RB

Key takeaway –

- ODI-FDI structure was widely used by companies/promoters across the e-commerce industry for raising of funds overseas
- Such structures did not pass bonafide activity test applicable for overseas JV/WOS.
- One that is not directly permissible is not indirectly permissible. Therefore, raising of funds that seem to be a genuine business activity, it is not a bonafide one.

Notification No. 120/2004 - RB

Reno Mercantile Private Limited (CA No.4629/2018)

Facts of the case –

The applicant, an Indian company provides back office support service for supply chain for companies in India & abroad.

It acquired the stake in M/s Vikasa Pte, a Singapore based company from Sumanth Ramanujam and Ms. Prema Ramanujam, on 29.03.2017 when its net worth was Rs.0.93 crores

After infusion of capital from its shareholders namely Shri Aditya Srikanth Ramanujam & M/s Rohini Holdings Pvt Ltd, the investment came within 400% of net worth as on 15th June, 2017

Relevant Regulation –

Regulation 6(2)(i) - ODI in Joint Ventures/ Wholly Owned Subsidiaries shall not exceed 400%

Regulation 6(2)(vi) – Delay in submission of form ODI Part I

Notification No. 120/2004 - RB

Key takeaways -

Regularization of Reg 6(2)(i) can be under two alternative approaches –

- 1) Either make disinvestment to extent of amount in excess of 400% of net worth of Indian Party
- 2) Infuse capital in Indian Party equivalent to amount required to bring financial commitment within 400% of net worth of Indian Party

The amount of contravention is only the excess of financial commitment over 400% of net worth of Indian Party

Notification No. 120/2004 - RB

Shantanu Pande (CA No 4766 / 2018)

Facts of the case –

- The applicant, a resident individual remitted USD 3253 on Feb 2013 towards setting up a overseas, OM Exports (FZC).
- The investment was repatriated on 1st June, 2018 & not capitalized

Relevant regulation -

- Regulation 5(1) of FEMA Notification 120/2004-RB dated 7th July, 2004 – PRI shall make direct investment outside India only with prior RBI approval
- Notification no. FEMA 263/RB-2013 dated 5th March, 2013 effective from 5th August, 2013 permitted the ODI by resident individuals
- Regulation 6(2)(vi) – IP making ODI shall submit part I of the form ODI
- Regulation 15(i) - Receipt of share certificates /any other document as an evidence of investment in the foreign entity to the satisfaction of RBI within 6 months

Notification No. 120/2004 - RB

Key takeaway -

- Contravention under Reg 5(1) constitutes contravention of a substantive provision
- Reporting contravention under Regulation 20A r.w. para D(1),D(2) of Schedule V should usually be attracted for period between 5th August, 2013 till the date of filing ODI
- Regulation 6(2)(vi) is a reporting contravention.

Notification No. 120/2004 - RB

Tavisca Solutions Pvt Ltd (CA No: 4727/2018)

Facts of the case –

- A WOS namely, Tavisca LLC, in the USA was incorporated by the applicant
- The MD of the applicant invested USD 500 towards share capital of an overseas WOS by way of cash. The said amount was carried abroad by MD for a business trip & was within the permissible limit.

Relevant regulation -

- Regulation 6(2)(vi) – An IP shall submit Part I of Form ODI
- Regulation 6(3) – Permissible sources of funds – a) Balance in EEFC account b) Drawal of foreign exchange shall not exceed 100% of the net worth of the IP
- Regulation 15(i) – Receipt of share certificates /any other document as an evidence of investment in the foreign entity to the satisfaction of RBI within 6 months
- Regulation 15(iii) – An IP shall submit an Annual Performance Report in form ODI Part III in respect of each JV/WOS & other reports / documents

Notification No. 120/2004 - RB

Tavisca Solutions Pvt Ltd (CA No: 4727/2018) [cont...]

Key takeaway –

- Applicant funded the WOS through cash. However, it was purchased by the applicant for business trip of MD under Business Travel Quota (LRS)
- If any doubt arises about the source of cash used for funding such investment, the case would have been covered under para 3(a) of FEMA, 1999 and would not be eligible for compounding & refer to ED

Covid-19 Impact on ODI Transactions and Compliances

Possible Fallout on ODI Transactions and Compliances

- a) Delay in receipt of share certificates against the investment made
- b) Extension of existing guarantees by the Indian Company or Issue of New Guarantee to help the overseas Subsidiary/JV or step down subsidiaries/JVs
- c) Fresh Financial commitment might pose the problem of exceeding 400 percent net worth for leveraged companies coupled with depreciation in Indian Rupee
- d) Delay in receipt of dues receivable like dividend, royalty, technical fees, etc. beyond 60 days from the foreign entity
- e) Investment by capitalization of export dues
- f) Pledge of shares of JVs/WOS or creation of charge on domestic and foreign assets

Covid-19 Impact on ODI Transactions and Compliances

- g) Restructuring of the balance sheet of JV/WOS involving write-off of capital and receivables
- h) Delay in filing post investment changes and annual compliances like APR and FLAIR
- i) Delay in receipt of sales proceeds/securities beyond 90 days from transfer of shares
- j) Cancellation or postponement of ESOP plans by the overseas company
- k) Winding up/closure of the overseas subsidiary/JV before completion of one year of operations
- l) Confusion on ESOPs to Citizens of Neighbouring countries especially China, delay in filing Form ESOP.

Thank You