

CVO Association of CAS
Intensive Study Course
On
FEMA
on 11th May 2013

Outbound Investment & Guarantees

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OVERVIEW

- History of Outbound Investment & Rationale
- Liberalization and the rationalization
- Automatic Route of Overseas Investment/LRS
- Approval Route
- Post Approval Compliance
- Hedging of Overseas Investment
- Disinvestment / Pledge etc.
- Other modes of Investment
- Factors Affecting Overseas Investment



OVERVIEW OF FEMA 120/2004/RB – PART I – DIRECT INVESTMENTS OUTSIDE INDIA

- Regn. 6 – Conditions for Automatic approval
- Regn. 6A – Investments in Agricultural operations overseas directly or through Overseas Offices
- Regn. 6B – Investment in Equity overseas by a listed Indian company
- Regn. 6C – Investment by Mutual Funds
- Regn. 7 – Investment by IP in Financial Services
- Regn. 8 – Investment by swap or exchange of shares
- Regn. 9 – Requirements for RBI Approval
- Regn. 9A – Overseas Investments by Regd. Trust / Society
- Regn. 10 – Unique Identification Number
- Regn. 11 – Investment by Capitalization
- Regn. 12 – Export of Goods towards Equity



OVERVIEW OF FEMA 120/2004/RB – PART I – DIRECT INVESTMENTS OUTSIDE INDIA

- Regn. 13 – Post investment changes / additional investment in existing JV / WOS
- Regn. 14 – Acquisition through bidding / tender
- Regn. 15 – Obligations of IP
- Regn. 16 – Transfer by way of sale of shares of JV / WOS
- Regn. 17 – Transfer involving write-off
- Regn. 18 – Pledge of shares of JV / WOS



OVERVIEW OF FEMA 120/2004/RB – PART II – INVESTMENTS ABROAD BY INDIVIDUALS IN INDIA

- Regn. 19 – Prior RBI approval for Proprietary in India to accept shares
- Regn. 19A – Overseas Investments by Proprietorships / unregistered Partnership Firm in India being recognized Star Export House
- Regn. 20 – Investments by Individuals for acquiring shares as consideration for professional services rendered



OVERVIEW OF FEMA 120/2004/RB – PART III – OTHER THAN DIRECT INVESTMENTS

- Regn. 21 – Issue of foreign security (FCCB) by person resident in India
- Regn. 22 – Purchase / acquisition by way of gift / inheritance / ESOP
- Regn. 23 – Transfer of foreign security by way of pledge by person resident in India
- Regn. 24 – General permission for acquiring qualification / rights shares and foreign securities under ADR/GDR linked stock options schemes
- Regn. 25 – Prior RBI approval for qualification shares in excess of limits specified under Regn. 24
- Regn. 26 – Investments by Mutual Funds / Venture Cap.Funds
- Regn. 27 – Opening of Demat Accounts with foreign depositories by Indian Clearing Corporations and Clearing Members



AUTOMATIC ROUTE OF INVESTMENT

- Types of Investments
- Who can Invest? What are the conditions?
- How much can be Invested?
- Financial Commitments
- What is Prohibited & Exempted?
- Methods of Investments
- Financial Sector
- Step Down Subsidiary/ies
- International Bid/Offer



Auto Route-Types of Investments

■ Direct Investment outside India Reg.2(e)

- Subscription to the M/A or contribution to the capital of the foreign entity or by purchase of shares of the foreign entity either by market purchase or through stock exchange or through private placement but does not include Portfolio Investment.

Note: Compulsorily Convertible Preference Shares are treated at par with equity shares and the IP is allowed to undertake financial commitment based on the exposure to JV by way of CCPS

■ Portfolio Investment

- Not defined under the regulation

■ Other Investment

- Not defined under the regulation



Auto Route-Who can Invest & its Conditions

- Indian Party
- Companies, Body Corporates, any other entity notified by the RBI
- Registered Partnership Firms
- Navratna PSUs and Oil Companies
- Agricultural Operations
- Portfolio Investments by Listed Indian Companies

■ Conditions

- Bonafide business activity
- IP is not in adverse list
- Remittance through designated Authorized Dealer
- Filing form ODI on-line as well with the AD
- Unique Identification Number (UIN No.)
- Have filed all the APRs for existing investments



Auto Route-How much can be Invested?

- Overall ceiling of the investment: “Financial Commitment” plus amount in EEFC A/c plus amount raised via ADR/GDR issue
- Financial commitment of the IP can not be more than 400% of the Net worth of the IP
- Net worth: Regn. 2(o)-Paid up capital and free reserves
- What is Financial Commitment? [Reg.2(f)]



Auto Route-Financial Commitment

- Financial Commitment Reg.2(f):
Amount of Direct Investment by way of contribution to the equity and loan and 100% of guarantees issued by an IP to or on behalf of its overseas JVC or WOS.
- Contribution to Equity can be by
 - Cash contributions or
 - Purchase of Shares or by Capitalization of Exports and Repatriable Entitlements
 - Swap of IP's shares or
 - ADR GDR Swap
- Loan to Overseas Entity
- Guarantees to or on behalf of overseas entity



Auto Route-Financial Commitment (con't)

- Guarantees to or on behalf of overseas entity
 - Cannot be open-ended; Period & amount to be specified
 - Corporate guarantees only
 - In case of performance guarantees by IP, 50% is considered for financial commitment; if invocation leads to breach of ceiling of 400% of net worth of IP, prior RBI approval is required before remitting funds from India [*Ref: Cir. No. 69 dt. 27/05/2011*]
 - Bank guarantee issued by a resident bank on behalf of an overseas JV / WOS of the IP, which is backed by a counter guarantee / collateral by the IP, shall be reckoned for computation of the financial commitment of the IP [*Ref: Cir. No. 96 dt. 28/03/2012*]

Auto Route-What is Prohibited & Exempted?

■ Prohibitions:

- Portfolio Investment, Real Estate & Banking Sector

■ Exemptions:

- Investment through RFC A/c
- Bonus issue
- Investment by Persons Resident in India but not permanently resident in India.



Auto Route - Methods/Source of Investments

- Purchase of Foreign Exchange
- EEFC A/c
- ADR-GDR issue
- SWAP of shares of IP
- Capitalization of Exports & Repatriable Entitlements that are not overdue
- ECB



Approval Route – Financial Commitment

- Proposals from the Indian party for undertaking financial commitment without equity contribution in JV / WOS may be considered by the Reserve Bank under the approval route keeping in view the business requirement of the Indian party, particularly the legal requirement of the host country. AD banks may forward proposals from their constituents after ensuring that the laws of the host country permit incorporation of a company without equity participation by the Indian party [*Ref. A.P. (DIR Series) Circular No. 96 dt. 28/03/2012*)]
- Wherever the laws of the host country permit incorporation of a company without equity participation by the Indian party, AD banks may obtain prior approval from the Reserve Bank before allowing the remittances towards the loan/issue of guarantee to/on behalf of the overseas JV/WOS

Approval Route – Financial Commitment

- Proposals from the IP for creation of charge in the form of pledge / mortgage / hypothecation on the immovable / movable property and other financial assets of the IP and their group companies may be considered by the Reserve Bank under the approval route within the overall limit fixed (400%) for financial commitment subject to submission of a 'No Objection' by the Indian Party and their Group companies from their Indian lenders *[Ref. A.P. (DIR Series) Circular No. 96 dt. 28/03/2012)]*



VALUATIONS

- Purchase of existing company by remittance from India:
 - > US\$ 5 mn: Valuation by SEBI regd. Category I Merchant Banker or Investment Banker / Merchant Banker registered in host country
 - < US\$ 5 mn: Valuation by CA / CPA
- Purchase partly or fully through issue of IP's shares:
 - Valuation by SEBI regd. Category I Merchant Banker or Investment Banker / Merchant Banker registered in host country
- ADR/GDR Swap: Valuation by Investment Banker
- Disinvestments - no distinction as to the amount; valuation by CA / CPA in case of sale of unlisted overseas companies by private arrangement; No reference to DCF method



Auto Route-Financial Sector (FS)

- Conditions for investment in Overseas Financial Services (OFS)
 - a) Net profit for past 3 years from FS activity
 - b) Registered with Indian Regulatory Authority for conducting FS activity
 - c) Obtained approval from Concerned Regulatory Authority both in India & O/I
 - d) Fulfilled prudential norms
- Unregulated & Regulated Financial Service in India by IP
- Only when unregulated IP is engaged in overseas non financial service sector, conditions of Reg.7 is not required to be observed



Auto Route-Step Down Subsidiary/ies

- It has to be SPV? meaning of SPV
- It is permitted only for the purpose of investment
- Other Cases-Regulation 13-
Diversification of activity, step down subsidiary and alteration of shareholding pattern due to local laws



Auto Route – Oil Sector

- Branch of an Indian Party
- Investments in unincorporated entities overseas in oil sector by Navratna PSUs without any limit
- Investments in unincorporated entities overseas in oil sector by other Indian Companies up to 400% of its net worth



Auto Route - Telecom Sector

- Indian Companies can participate in a consortium with international operators to construct & maintain submarine cable systems on co-ownership basis
- Above is subject to necessary license from DOT to install, operate & maintain International Long Distance Services.



Auto Route-International Bid/Offer

- Applicable in case of bidding or tender
- Remittance towards earnest money/bid bond guarantee
- Successful bid/tender may result into Auto/Approval route.
- Form ODI to be filed to AD within 30 days of remittance or Application to RBI is required.



APPROVAL ROUTE

- Where IPs' not able to comply with Reg.6(2)
- Individuals & Proprietary Business
- Unregistered Partnership Firms
- Star Export House - Proprietary business and Unregistered Firms
- Societies & Trust in mfg/education/hospitals
- Oil & Energy Sector (Other than Navratna PSU) by Indian Companies in excess of 400%
- Investment in Pakistan [*Ref: Cir. No. 25 dt.07/09/2012*]



Approval Route-Proprietary Concern

- Individual as a proprietary concern
- Capitalisation only up to 50% of the fees to be realized but not exceeding 10% of the capital of the Foreign Company



Approval Route-Individual

- Professional fees are receivable
- Factors considered by RBI, Credentials, Net worth, Nature of the profession, Forex earnings, Financial & Business track record, likely benefits to the country in forex
- However, general permission is granted to resident individuals to acquire shares of a foreign entity in part / full consideration of professional services rendered to the foreign company or in lieu of Director's remuneration within the overall ceiling prescribed for the resident individuals under the Liberalized Remittance Scheme (LRS) in force at the time of acquisition [*Ref: Cir No. 97 dt. 28/03/2012*]



Approval Route-Star Exporters

- Recognized Star Exporters
- Proven track record & Export performance
- Proprietors & Unregistered Firms
- DGFT recognized Star Export House
- KYC & not in the Adverse notice of the Regulatory Authority in India
- Lower of 10% of Average export realisation for 3 years or 200% of Net Owned Funds



Approval Route-Societies & Trust

- Registration & Operational for at least 3years
- Approval by Trustees & object as per Trust deed.
- KYC by Bank & no Adverse notice of Regulatory Authorities
- AD should ensure that Special License if any required from MoH GoI or Local Authority, is obtained



Approval Route-Oil & Natural Resource Sector

- Oil, Gas, Coal & Mineral Ores
- Over 400% of the Net worth
- Unincorporated Sector Overseas or otherwise Overseas Company



Reporting requirements – Filing by Indian Party

- Physical filing of Form ODI with AD
- Under Approval route, physical application to be submitted to RBI through AD in addition to on-line reporting of Part I by AD

Reporting requirements – Filing by Authorized Dealer

- On-line reporting of ODI forms by Centralized Unit / Nodal Office of AD Category – I banks mandatory w.e.f. 2nd March, 2010 of Parts I, II & III
- Enables on-line generation of UIN, acknowledgement of remittance/s and filing of Annual Performance Reports
- Physical filing by IP with AD also continues
- Under Approval route, physical application to be submitted to RBI by AD in addition to on-line reporting of Part I by AD



Reporting requirements – Disinvestments

- Disinvestment Report to be filed physically in cases by AD with RBI

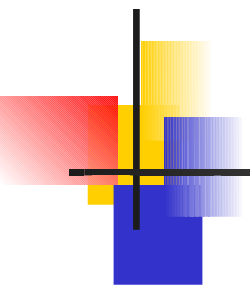


POST APPROVAL COMPLIANCE

- Obtaining Share Certificate
- Submission of Documents to AD
- Audit of the Accounts
- Furnishing the Report of Performance
- Furnishing the Report of Disinvestment & Liquidation if any

Reporting requirements – Annual Performance Report

- Annual Performance Report (APR) in Form ODI Part III in respect of each JV or WOS outside India to be submitted to RBI on or before the 30th of June each year and has to be based on the latest audited annual accounts of the JV / WOS, unless specifically exempted by the RBI
- If the law of the host country does not mandatorily require auditing of the books of accounts of JV / WOS, the APR may be submitted based on the un-audited annual accounts of the JV / WOS provided:
 - a. The Statutory Auditors of the Indian party certifies that 'The un-audited annual accounts of the JV / WOS reflect the true and fair picture of the affairs of the JV / WOS' and
 - b. That the un-audited annual accounts of the JV / WOS has been adopted and ratified by the Board of the Indian party



Reporting requirements – Annual Performance Report

- Annual return on Foreign Liabilities and Assets (FLA) is required to be submitted directly by all the Indian companies which have received FDI and/or made FDI abroad (i.e. overseas investment) in the previous year(s) to RBI by July 15 of every year [*Ref: Cir. No. 133 dt. 20/06/2012*]



HEDGING / PLEDGE OF OVERSEAS INVESTMENT

- IP is permitted to Hedge the risk arising out of Foreign Exchange
- Cancellation of the contract is also permitted
- Hedge & shrinkage in the value of overseas investment – Rollover up to original maturity is permitted
- Pledge either to Bank or FI in India or with an Overseas Bank



DISINVESTMENT

- Disinvestment when transferee is another Resident
 - Compliance of Regn.6(2) by transferee
- Disinvestment to PROI - Auto Route applicable if
 - Overseas company is a listed company
 - Listed Indian Party with 100 Cr. Net worth
 - Unlisted Indian Party with total investment not over US\$ 10mn
 - Listed Indian Party with less than 100 Cr. Net worth but also investment is less than US\$ 10mn



Disinvestment-Conditions

- Sale is effected through stock exchange
- Valued by CA/CPA if sold through a private arrangement
- Overseas concern in operation for at least full year
- All APR & Accounts are filed with the ADs
- IP is not in adverse notice of Regulatory Authorities in India
- Amount is repatriated not later than 90 days from date of sale



Disinvestment - Write-off

- Indian Promoter holding at least 51% capital of the Overseas Venture
 - Listed Indian company can write-off Capital & repatriable entitlements upto 25% of Equity investment in the JV/WOS
 - Unlisted company can do so with prior approval
 - Report write-off within 30 days of write-off with copy of Balance Sheet of the overseas JV / WOS and projections for next 5 yrs indicating benefit of write-off

Form ODI-Extract of Part IV

Whether APRs submitted regularly? (Y/N)

Date of submission and period to which last APR relates: _____

Details of Investment

Equity	Loan	Guarantees Issued

Details of Remittances

Equity	Loan	Guarantees Invoked

Changes in the capital Structure since the last APR

Equity	Loan	Guarantees Issued

Amount Repatriated on disinvestments

Equity	Loan



OTHER MODE OF INVESTMENTS

- Not a direct Investment
- FCCB up to US\$ 750mn
- Gift
- Cash less option
- Inheritance
- Foreign Co's share to the Employee of the Indian Branch or the Subsidiary Co.
- Qualification Shares for Director within LRS limits
- Right Shares
- Indian Co's ADR/GDR linked stock option to employee's and working directors
- Purchase of shares & securities by Mutual fund and VCF in India



KYC & Bank Accounts

- Brief CV of shareholder who are individuals with identity proof of Residence
- Bank Reference
- Practice issues



OVERVIEW OF FEMA 8/2000/RB – GUARANTEES / SURETIES

- Applicable to guarantee / surety by person resident in India covering debt / obligation / liability owed to or incurred by a person resident outside India
- Rationale: Contingent Liabilities outside India is a Capital Account transaction under FEMA
- Authorized Dealer can give guarantee on behalf of:
 - Exporter from India
 - Importer under RBI approved deferred payment terms
 - For import of goods under Foreign Trade Policy
 - Person resident outside India for debt owed to person resident in India if counter-guaranteed by bank of international repute
 - Foreign airlines/ IATA approved agents
 - Customer /Branch outside India for defective / missing documents



OVERVIEW OF FEMA 8/2000/RB – GUARANTEES / SURETIES

- Persons other than Authorized Dealers can give guarantees as under:
 - Exporter company for performance of project outside India / availing credit from bank outside India for such project
 - Exporter company in lieu of Bid Bond guarantee upto 5% of contract value
 - On behalf of overseas JV / WOS in connection with its business
 - Indian agent of foreign shipping or airline company on behalf of its parent company for obligations owed to statutory or Govt. authority in India



FACTOR AFFECTING OVERSEAS INVESTMENT

- General Factors
- Corporate Factors
- Tax Factors
- KYC & Bank Accounts



General Factors

The selection of the most suitable jurisdiction for either international trade or investment can often be difficult and requires very careful consideration. It is important to select a jurisdiction that is well suited to specific corporate and personal needs and it should meet the following criteria :-

- 1) Political and Economic Stability
- 2) Legislation
- 3) Basic Desirable Corporate Characteristics
- 4) Professional Infrastructure
- 5) Comparison of Company Law
- 6) Time Zone
- 7) Market globalization and deregulation
- 8) The Internationalization of business
- 9) The lifting of trade barriers
- 10) A trend towards steady global economic growth
- 11) Global relaxation of foreign exchange controls



Corporate Factors

1. Limited Liability
2. Directors liability [local]- directors are generally responsible for the acts of a company and its beneficial owners
3. Minimal or optional statutory filing obligation
4. Nominee shareholders allowed
5. The availability of bearer shares
6. Disclosure of beneficial ownership
7. Low capital requirements
8. Directors and/or shareholders meetings anywhere in the world
9. Audit requirements – optional or mandatory
10. On shore/Off shore business – facility
11. Redomiciliation



Tax Factors

1. To be relatively simple to set up and operate
2. To rely only upon a provision or an interpretation accepted by the revenues
3. Credible commercial basis
4. To make possible a full reporting of all income and expenses and audited accounts
5. To avoid the use of a objectionable/ blacklisted device or location
6. Usually, to result in the payment of some tax, though significantly less tax under the structure than would be payable if it was not used
7. Double Taxation Agreements

BRANCH VS SUBSIDIARY

KEY FACTORS

Key Factor	Branch	Subsidiary
Liability	Of parent company as branch is not a distinct legal entity	Of subsidiary; limited to the extent of its paid-up capital
Territory of operation	Normally restricted by local jurisdictions	Generally, wider area of operation
Registration	Comprehensive details of parent company required	Subsidiary is regulated
Set-off of losses	Can be set-off by parent company in its tax return	In most cases, set-off by parent company may not be possible
Taxation	Parent company can take tax credit for taxes paid by branch	Subsidiary itself taxed as corporation being a distinct entity
Remittances	Branch may not pay taxes on remittances	Subsidiary would have to pay withholding tax on dividends
Tax Credit	No	Yes



INVESTMENT IN USA

Types of Business Entities:

- Limited Partnership
- General Partnership
- Limited Liability Company (LLC)
- C Corporation
- S Corporation
- Sole Proprietor



INVESTMENT IN USA

Regulatory environment:

- No stipulation as to local participation
- No exchange controls; i.e. currency is free from any restrictions
- Businesses are governed by State Govt.s; hence no permissions / restrictions from Federal Govt. except in case of few important sectors
- Far states offer incentives in the form of either no tax or lower taxes if place of business is established in that state
- Commerce and agricultural department of Federal Government requires substantial reporting requirements for foreign Investment in U.S. Reporting is also required under International Investment Survey Act, 1976



INVESTMENT IN USA

Taxation:

- Income Tax: Levied by Federal Govt., State Govt. and Local Authorities
- in case of corporates, taxes on income is levied at two levels one on corporation and two while it is distributed to shareholders by way of withholding tax on shareholders
- Indirect Taxation :
 - (i) Social Security Tax (ii) State and Federal unemployment insurances (iii) Self employment Tax on independent service providers (iv) Workers Compensation Insurance (v) Sales and / or Use Tax (vi) Property Taxes (vii) Gift & Estate Taxes (viii) Customs duties and Excise
- Anti trust laws are enforced by the Antitrust division of US Department of Justice and by the Federal Trade Commission. Civil and criminal action can be taken on violations. Even mergers and acquisitions can be prohibited



INVESTMENT IN USA

Double Taxation Avoidance Agreements:

- It has signed over 70 tax treaties including with India
- Follows OECD model and advocates resident based taxation for most of the income under Treaty
- Offers hardly any use of offshore jurisdictions on account of stringent anti avoidance provisions under domestic laws
- US Treaties have a different approach towards definition of PE
- US does not ask for tax sparing provisions during negotiations
- US model provides for treaty based anti avoidance provisions by way of article on “limitations of treaty benefits”



INVESTMENT IN SINGAPORE

Types of Business Entities:

- Private Limited Company
- Exempt Private Limited Company
- Foreign Company Registrations:
 - Options of Subsidiary, Branch or Representative Office
- Non-profit Entity
- Limited Liability Partnership
- Sole Proprietorship



INVESTMENT IN SINGAPORE

Types of Business Licences in Singapore:

- Business activity Licenses and Permits required to conduct specific types of businesses
- Occupational licenses for professionals such as lawyers, doctors, financial planners, accountants, commodity traders
- Compulsory licences – Certain types of businesses require a special licence before they can operate such as Private schools, travel agencies, money remittance agencies



INVESTMENT IN SINGAPORE

COST STRUCTURE & COMPONENTS

Incorporation of the company/Entity
Registered office cost
Nominee Director/s
Secretary of the co.
Accounts and Audit
Tax filings cost
Transaction Cost(Variable)



INVESTMENT IN SINGAPORE

Taxation:

- Income Tax:
 - Territorial basis of taxation where Singapore sourced income is taxed
 - Singapore's tax regime known for attractive tax rates, zero capital gains tax and extensive double tax treaties
 - Interest, royalties, management/technical fees, directors' fees paid to non-residents are subject to withholding tax
 - Corporate Tax rate is capped at 17%
 - Personal Tax rates start at 0% and capped at 20%
- Other types of Taxes:
 - (i) Property Tax (ii) Estate Duty (iii) Customs & Excise Duties (iv) Goods & Services Tax (v) Stamp Duty (vi) Betting Taxes (vii) Foreign Worker levy
- Singapore has more than 50 bilateral tax treaties including with India



Thank You
