

FEMA OVERVIEW & FDI POLICY

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FEMA OVERVIEW



Framework of FEMA

Overview of Foreign Exchange Management Act

▪ **Statement of Objects of FEMA:**

- An Act to consolidate and amend the law relating to foreign exchange with the objective of **facilitating external trade and payments** and for **promoting the orderly development and maintenance of foreign exchange market** in India.

▪ **Jurisdiction of FEMA:**

- Whole of India (including J&K)
- Extra-territorial jurisdiction (since it applies even to branches, offices and agencies o/s India owned & controlled by a PRI)

▪ **Policy Instruments under FEMA:**

- Notifications by RBI + CG for making / revising Regulations and Rules
- A.P.(Dir Series) Circular by RBI
- Press Notes by DIPP
- Master Directions by RBI
- FDI Policy by DIPP

▪ **Overall Scheme of FEMA:**

- All current account transactions are freely permitted. However, CG can impose reasonable instructions.
- Capital account transactions are permitted to the extent allowed by RBI/CG
- RBI authorizes 'Authorized Persons' to deal in foreign exchange.

Framework of FEMA

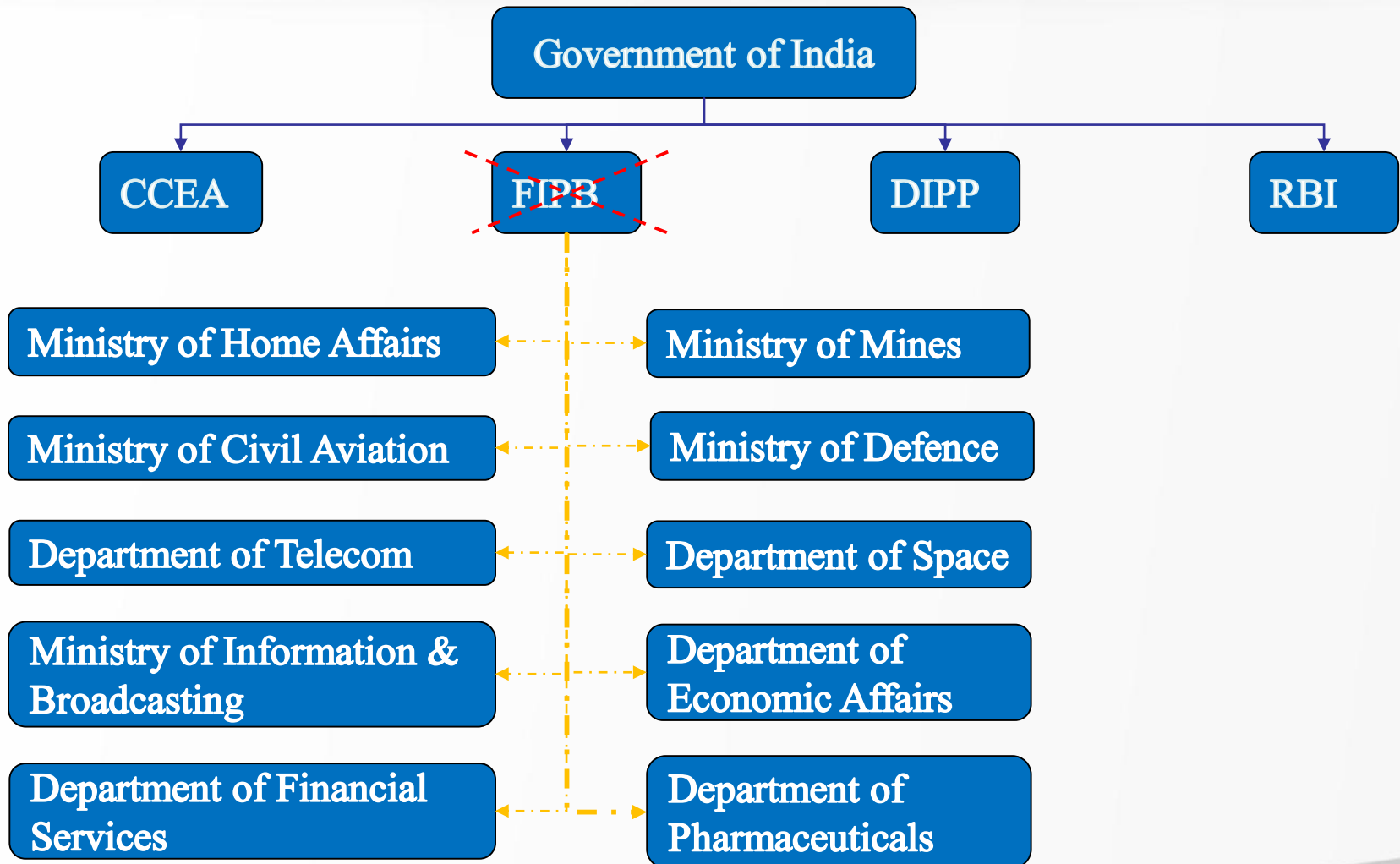
Overview of Foreign Exchange Management Act

Structure of FEMA:

Chapter	Chapter title	Subject	Sections
I	Preliminary	Jurisdiction, Definitions	1-2
II	Regulation & Management of Forex	<ul style="list-style-type: none"> • Restriction on dealing with PROI • Holding of forex • Current a/c transactions • Capital a/c transactions • Export of goods & services • Realization and repatriation of forex with exemptions 	3-9
III	Authorised Persons	Provisions relating to Authorised Persons	10-12
IV	Contravention and Penalties	Provisions relating to Contravention, its consequences and Compounding	13-15
V	Adjudication and Appeal	<ul style="list-style-type: none"> • Provisions relating to terms of service, composition, appointment of Adjudicating Authority, Members to Appellate Tribunal • Provisions relating to Appeal to Special Director (Appeals), Appellate Tribunal and High Court 	16-35
VI	ED	Provisions relating to Appointment & Powers (*37A*)	36-38
VII	Miscellaneous	Power to make Rules and Regulations, etc	39-49

Framework of FEMA

Administration of FEMA



Framework of FEMA

Regulation of Foreign Exchange

- **Sec 3 (Restrictions on dealing in foreign exchange)**

Save as otherwise provided in this Act, rules or regulations made thereunder, or with the general or special permission of the Reserve Bank, no person shall—

- a) deal in or transfer any foreign exchange or foreign security to any person not being an authorised person; (Refer to Sec. 5 & 6)
- b) make any **payment** to or for the credit of any **PROI** in any manner;
- c) **receive** otherwise (than) through an authorised person, any payment by order or on behalf of any **PROI** in any manner;

Explanation.—For the purpose of this clause, where any person in, or resident in, India receives any payment by order or on behalf of any PROI through any other person (including an authorised person) **without a corresponding inward remittance** from any place outside India, then, such person shall be deemed to have received such payment otherwise than through an authorised person;

- d) enter into any **financial transaction** in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person.

Explanation.—For the purpose of this clause, **financial transaction** means making any payment to, or for the credit of any person, or receiving any payment for, by order or on behalf of any person, or drawing, issuing or negotiating any bill of exchange or promissory note, or transferring any security or acknowledging any debt.



Framework of FEMA

Important definitions - Residence

- **Sec 2(u) - Person:**

- Individual
- Hindu undivided family,
- Company,
- Firm
- AOP/BOI
- Artificial juridical person
- any agency, office or branch owned or controlled by such person

- **Sec 2(v) – Person Resident in India:**

- **Individuals**

- **Basic Rule:** > 182 days in preceding FY
- **Exception 1 to Basic Rule:** Gone out of India for:
 - ✓ For employment o/s India
 - ✓ For carrying on business / vocation o/s India
 - ✓ For any other purpose indicating intention to stay o/s India for uncertain period
- **Exception 2 to Basic Rule:** Come to India for:
 - ✓ For employment in India
 - ✓ For carrying on business / vocation in India
 - ✓ For any other purpose indicating intention to stay in India for uncertain period

Framework of FEMA

Important definitions – Residence & Others

- **Sec 2(v) – Person Resident in India:**
 - **Other than Individuals**
 - any person or body corporate registered or incorporated in India
 - an office, branch or agency in India owned or controlled by PROI
 - an office, branch or agency outside India owned or controlled by PRI
- **Sec 2(l) – Export:**
 - the taking out of India to a place outside India any goods,
 - provision of services from India to any person outside India
- **Sec 2(p) – Import:**
 - means bringing into India any goods or services
- **Sec 2(ze) – Transfer:**
 - includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien



Framework of FEMA

Capital A/c Transactions vs. Current A/c Transactions

- **Sec. 2(e) – Capital A/c Transaction:**

- transaction which **alters the assets or liabilities, including contingent liabilities**, outside India of persons resident in India or assets or liabilities in India of persons resident outside India, and includes transactions referred to in sub-section (3) of section 6

Vs.

- **Sec 2(j) – Current A/c Transaction:**

- transaction other than a capital account transaction **and without prejudice to the generality of the foregoing such transaction includes**,
 - payments due in connection with foreign trade, other current business, services, and short-term banking and credit facilities in the ordinary course of business,
 - payments due as interest on loans and as net income from investments,
 - remittances for living expenses of parents, spouse and children residing abroad, and
 - expenses in connection with foreign travel, education and medical care of parents, spouse and children;



Capital A/c Transactions vs. Current A/c Transactions

FEMA Notf. 1 – Permissible Capital A/c Transactions

▪ Schedule I – For PRI:

- 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 favour 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
- g) Maintenance of **foreign currency accounts in India** and outside India by a person resident in India
- h) Taking out of **insurance policy** by a person resident in India from an insurance company outside India
- i) **Loans and overdrafts** by a person resident in India to a person resident 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

Capital A/c Transactions vs. Current A/c Transactions

FEMA Notf. 1 – Permissible Capital A/c Transactions

- **Schedule II – For PROI:**
 - a) **Investment in India** by a person resident outside India, that is to say,
 - i. Issue of **security** by a body corporate or an entity in India and investment therein by a person resident outside India;
 - ii. 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 favour 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.
 - 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.

Capital A/c Transactions vs. Current A/c Transactions

Permissible Capital A/c Transactions

- **Sec. 6(4) – PRI:** Assets abroad
- **Sec. 6(5) – PROI:** Assets in India
- **LRS and Capital account transactions:**
 - Opening of foreign currency a/c abroad with a bank;
 - Purchase of property abroad;
 - Making investments abroad – acquisition & holding shares of both listed and unlisted overseas company or debt instruments;
 - Acquisition of qualification shares of an overseas company for holding the post of Director;
 - Acquisition of shares of a foreign company towards professional services rendered or in lieu of Director's remuneration;
 - Investment in units of Mutual Funds, Venture Capital Funds, unrated debt securities, promissory notes;
 - Outbound investment;
 - Extending loans including loans in Indian Rupees to Non-resident Indians (NRIs) who are relatives as defined in Companies Act, 1956

Capital A/c Transactions vs. Current A/c Transactions

GSR 381(E) – Current A/c Transactions

- **Schedule I – Transactions which are prohibited**
- **Schedule II – Transactions which require prior approval of Central Government**
- **Schedule III – Transactions requiring RBI approval above certain limits**
 - **LRS transactions for Individuals**
 - Private visits
 - Gift/donation
 - Going abroad on employment
 - Emigration
 - Maintenance of close relatives abroad
 - Business trip
 - Medical treatment abroad
 - Facilities available to students for pursuing their studies abroad (Also see Circular 45 of 2003)



Capital A/c Transactions vs. Current A/c Transactions

GSR 381(E) – Current A/c Transactions

- **Schedule III – Transactions requiring RBI approval above certain limits**
 - **Other facilities for persons other than individuals**
 - Donations
 - » Creation of chair
 - » Contribution to funds promoted by educational institution
 - » Contribution to technical institution
 - Commission to foreign agents for sale of residential/commercial plots in India
 - Remittances for consultancy services procured from outside India
 - Remittance for re-imbursement of pre-incorporation expenses



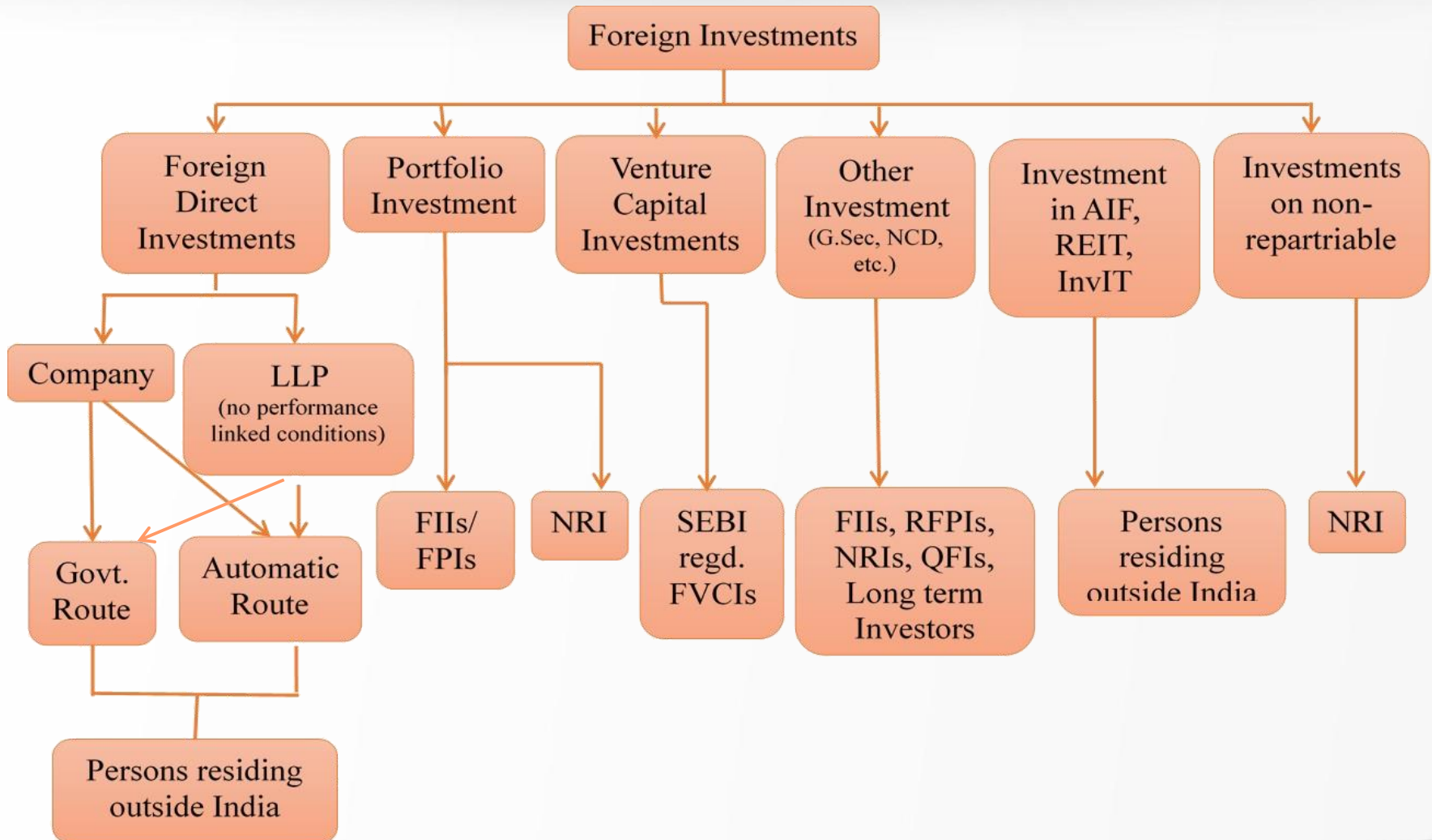
Foreign Direct Investment

FDI in India



Inbound Investments

Notification No. FEMA 20(R)/2017-RB dated November 7, 2017



Foreign Investment - Important Definitions

■ Foreign Investment

‘Foreign Investment’ means any investment made by a person resident outside India on a **repatriable basis** in capital instruments of an Indian company or to the capital of an LLP;

- **Note:** A PROI may hold foreign investment either as Foreign Direct Investment or as Foreign Portfolio Investment in any particular Indian company.

■ Foreign Direct Investment (FDI)

FDI means investment through capital instruments by a person resident outside India in an **unlisted Indian company**;

or

in **10 percent or more** of the post issue paid-up equity capital on a fully diluted basis of a **listed Indian company**;

- **Note:** In case, an existing investment by a PROI in capital instruments of a listed Indian company falls to a level below 10% of the post issue paid-up equity capital on a fully diluted basis, the investment shall continue to be treated as FDI.

Foreign Investment - Important Definitions (Cont.)

■ Capital Instruments

Capital Instruments means:

- **Equity shares:** Equity shares issued in accordance with the provisions of the Companies Act, 2013 shall include equity shares that have been **partly paid**. Partly paid shares that have been issued to a person resident outside India shall be fully called-up within twelve months of such issue. Twenty five percent of the total consideration amount (including share premium, if any), shall be received upfront.
- **Debentures:** ‘**Debentures**’ means fully, compulsorily and mandatorily convertible debentures.
- **Preference shares:** ‘**Preference shares**’ means fully, compulsorily and mandatorily convertible preference shares.
- **Share warrants:** **Share Warrants** are those issued by an Indian Company in accordance with the Regulations issued by the SEBI. In case of share warrants at least twenty five percent of the consideration shall be received upfront and the balance amount within eighteen months of issuance of share warrants.

Foreign Investment - Important Definitions (Cont.)

■ Capital Instruments

- Capital 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.
- Capital instruments shall include:
 - non-convertible/ optionally convertible/ partially convertible preference shares issued as on and up to April 30, 2007 and optionally convertible/ partially convertible debentures issued up to June 7, 2007 till their original maturity.
 - Non-convertible/ optionally convertible/ partially convertible preference shares issued after April 30, 2007 shall be treated as debt and shall conform to External Commercial Borrowings guidelines regulated under Foreign Exchange Management (Borrowing and Lending in Foreign Exchange) Regulations, 2000

Foreign Investment - Important Definitions (Cont.)

■ Foreign Portfolio Investment

‘Foreign Portfolio Investment’ means any investment made by a person resident outside India through capital instruments where such investment is **less than 10 percent** of the post issue paid-up share capital on a fully diluted basis of a **listed Indian company** or less than 10 percent of the paid up value of each series of capital instruments of a listed Indian company;

■ Foreign Portfolio Investor (FPI)

FPI means a person registered in accordance with the provisions of Securities Exchange Board of India (Foreign Portfolio Investors) Regulations, 2014.

■ Sectoral Cap

Sectoral cap’ means the maximum investment including both foreign investment on a repatriation basis by persons resident outside India in capital instruments of a company or the capital of an LLP, as the case may be, and indirect foreign investment, unless provided otherwise. This shall be the composite limit for the Indian investee entity;

Entry Routes for Inbound Investments

(Regulation 5 of FEMA 20(R))

Sch. No.	Reg.	Particulars
1	5(1)	Purchase / Sale of Capital Instruments of an Indian company by a person resident outside India
2	5(2)	Purchase / Sale of Capital Instruments of a listed Indian company on a recognized stock exchange in India by FPI
3	5(3)	Purchase/ Sale of Capital Instruments of a listed Indian company on a recognised stock exchange in India by NRI or OCI on repatriation basis
4	5(4)	Investment on non-repatriation basis by NRI or OCI
5	5(5)	Purchase and sale of securities other than capital instruments by a person resident outside India
6	5(6)	Investment in a LLP
7	5(7)	Investment by FVCI
8	5(8)	Investment by a person resident outside India in an Investment Vehicle
9	5(9)	Investment in Depository Receipts by PROI
10	5(10)	Issue of Indian Depository Receipts

Exit Routes for Inbound Investments

(Regulation 10 of FEMA 20(R))

Reg.	Seller	Buyer	Mode of Transfer
10(1)	PROI (Other than NRI / OCI / OCB)	Any PROI (including NRI / OCI) (on Repatriation or Non Repatriation basis)	Sale / Gift
10(2)	NRI / OCI (on Repatriation basis)	Any PROI (including NRI / OCI) (on Repatriation or Non Repatriation basis)	Sale / Gift
10(3)	PROI (including NRI / OCI) (on Repatriation or Non Repatriation basis)	PRI	Sale / Gift
10(4)	PRI / NRI / OCI on Non Repatriation basis	Any PROI (including NRI / OCI) (on Repatriation or Non Repatriation basis)	Sale
10(5)	PRI / NRI / OCI on Non Repatriation basis	Any PROI (including NRI / OCI) (only Repatriation basis)	Gift with limits (RBI Approval)
10(6)	NRI / OCI on Non-Repatriation basis	Any NRI / OCI on Non Repatriation basis	Gift
10(8)	OCB	<ul style="list-style-type: none"> ▪ NRI ▪ PRI 	<ul style="list-style-type: none"> ▪ Sale / Gift ▪ Sale
10(9)	PRI / PROI	PROI / PRI	Sale (deferred consideration)



Acquisition through Rights Issue or Bonus Issue

- PROI having investment in Indian company may acquire capital instruments (other than share warrants) issued by such company as a **rights issue or a bonus issue** provided that:
 - The offer is in compliance with the provisions of the Companies Act, 2013;
 - Such issue shall not result in a breach of the sectoral cap applicable to Indian company;
 - **Original shareholding must have been acquired and held as per the provisions of FEMA 20/20(R);**
 - For listed Indian company: Rights issue to persons resident outside India shall be at a price determined by the company;
 - For unlisted Indian company: Rights issue to persons resident outside India shall not be at a price less than the price offered to persons resident in India.
 - The amount of consideration shall be paid as inward remittance from abroad through banking channels or out of funds held in NRE/ FCNR(B) account maintained in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016.
 - If the **original investment has been made on a non-repatriation basis**, the amount of consideration may also be paid by debit to the NRO account maintained in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016.
- An individual who is a person resident outside India exercising a right which was issued when he/ she was a person resident in India can hold the capital instruments so acquired on exercising the right on a non-repatriation basis.

Renunciation of entitlement + Issue of ESOP

Renunciation of rights

- PRI & PROI can **subscribe for additional shares over and above the shares offered on rights basis** by the company and **also renounce the shares** offered either in full or part thereof in favour of a person named by them.
- Pricing guidelines to be followed
- Rights shares shall be subject to the same conditions including restrictions in regard to repatriability as applicable to the original shareholding.

Issue of Employees' Stock Options Scheme (ESOP) and Sweat Equity Shares

An Indian company is permitted to issue “employees’ stock option” and/ or “sweat equity shares” to **its employees/ directors or employees/ directors of its holding company or joint venture or wholly owned overseas subsidiary/ subsidiaries who are resident outside India**, subject to the following conditions:

- Compliance with SEBI Regulations or the Companies (Share Capital and Debentures) Rules, 2014;
- Compliance with the sectoral cap applicable to the said company;
- Issue of “employee’s stock option”/ “sweat equity shares” in a company where investment by a person resident outside India is under the approval route requires prior Government approval.

Merger / Demerger / Amalgamation of Indian companies

Issue of Capital Instruments upon Merger / Amalgamation / Demerger:

Upon approval by National Company Law Tribunal (NCLT)/ Competent Authority, the transferee company or the new company, as the case may be, can **issue capital instruments to the existing holders of the transferor company who are resident outside India**, subject to the following conditions:

- The transfer or issue should comply with entry routes, sectoral caps or investment limits, as the case may be, and the attendant conditionalities of foreign investment;
- In case the foreign investment is likely to breach the Sectoral caps or the attendant conditionalities, the transferor company or the transferee or the new company should obtain necessary Government approval;
- The transferor company or the transferee company or the new company should not be in a sector prohibited for foreign investment.

Issue of Redeemable NCPS / Redeemable NCD as bonus in Scheme of Arrangement:

Upon approval by National Company Law Tribunal (NCLT)/ Competent Authority, the Indian company can **issue such instruments to shareholders who are resident outside India, out of its general reserves by way of distribution as bonus**, subject to the following conditions:

- The original investment made in the Indian company by a person resident outside India is in accordance with FEMA 20(R) and the conditions specified therein;
- The said issue is in accordance with the provisions of the Companies Act, 2013 and the terms and conditions, if any, stipulated in the scheme approved by National Company Law Tribunal (NCLT)/ Competent Authority;
- The Indian company is not engaged in any activity/ sector in which foreign investment is prohibited.

Cross Border Merger – Inbound Merger

Company Law:

- **Position under Companies Act, 1956** [Section 394(4)(b)]: “a “*transferee company*” does not include any company other than a company within the meaning of this Act, but “*transferor company*” includes any body corporate, whether a company within the meaning of this Act or not.” Accordingly, “transferee company” could only be an Indian company while a “transferor company” could include foreign companies as well. Therefore, only inbound cross-border mergers were possible and not outbound mergers.
- **Companies Act, 2013:** MCA notified Sec. 234 w.e.f. 13.04.2017 enabling inbound as well as outbound mergers.

Foreign Exchange Management (Cross Border Merger) Regulations, 2018

[Notification No. FEMA.389/2018-RB Dated: March 20, 2018]

- **‘Inbound merger’** means a cross border merger where the resultant company is an Indian company;
- The resultant company may **issue or transfer any security and/or a foreign security, as the case may be, to a person resident outside India** in accordance with the pricing guidelines, entry routes, sectoral caps, attendant conditions and reporting requirements for foreign investment as laid down in Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2017.
- Any transaction on account of a cross border merger undertaken in accordance with these Regulations shall be deemed to have prior approval of the Reserve Bank as required under Rule 25A of the Companies (Compromises, Arrangement and Amalgamations) Rules, 2016.

Downstream Investment

Downstream Investment:

- **Total Foreign investment in a company** = Direct + Indirect Foreign Investment
- **‘Downstream investment’** means indirect foreign investment, by an eligible Indian entity, into another Indian company /LLP, by way of subscription or acquisition.
- **‘Ownership’** shall mean:
 - A **Company** shall be considered as owned by resident Indian citizens if more than 50% of the capital in it is beneficially owned by resident Indian citizens and/or Indian companies, which are ultimately owned and controlled by resident Indian citizens.
 - A **Limited Liability Partnership** will be considered as owned by resident Indian citizens if more than 50% of the investment in such an LLP is contributed by resident Indian citizens and/ or entities which are ultimately ‘owned and controlled by resident Indian citizens’ and such resident Indian citizens and entities have majority of the profit share.
- **‘Control’** shall include:
 - **Company** – 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 agreements or voting agreements.

Downstream Investment (Cont.)

Downstream Investment:

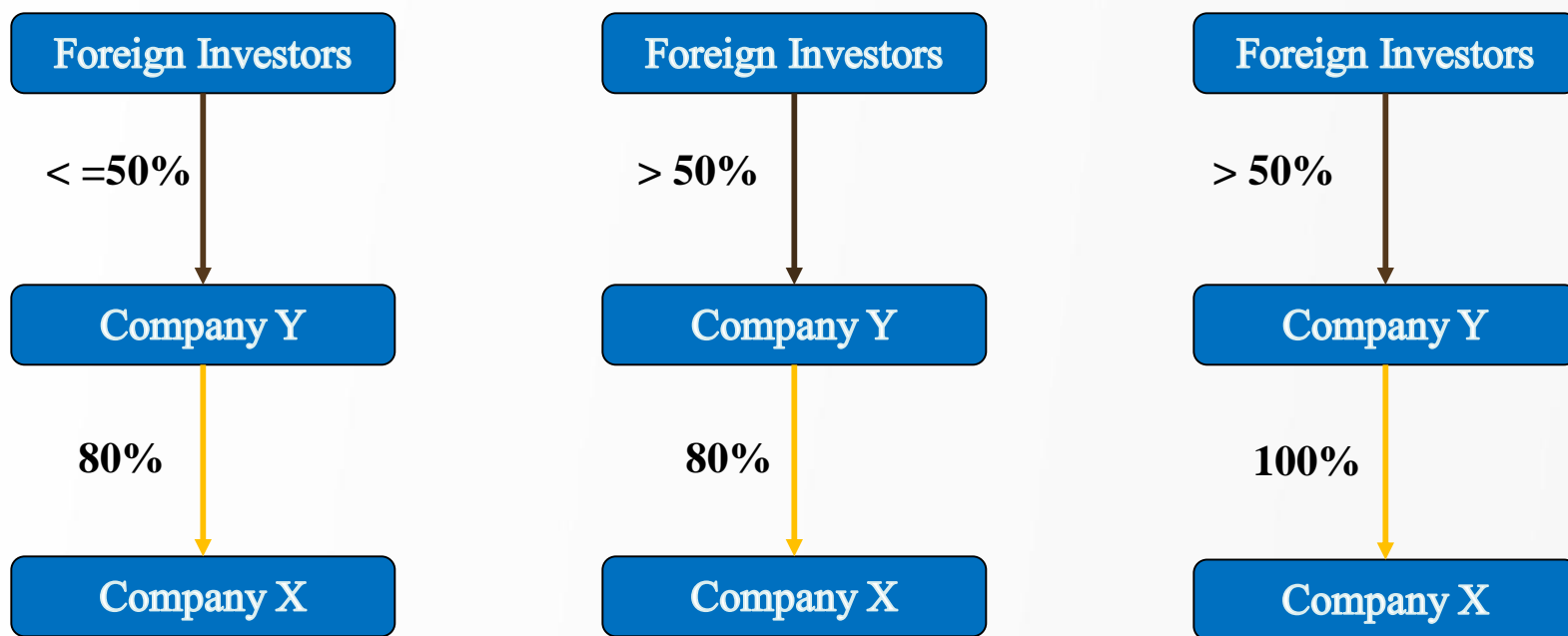
- ‘Control’ shall include:
 - **Limited Liability Partnership** – Right to appoint majority of the designated partners, where such designated partners, with specific exclusions to others, have control over all the policies of Limited Liability Partnership.
- If the investing company / LLP is owned *or* controlled by ‘non-resident entities’, the entire investment by the investing company /LLP into the subject Indian Company / LLP would be considered as indirect foreign investment. Otherwise, indirect foreign investment would be taken as the percentage of downstream investment.
- Downstream investments which is treated as Indirect Foreign Investment for the investee Indian entity can be made through by bringing in requisite funds from abroad or through internal accruals. For this purpose, internal accruals will mean profits transferred to reserve account after payment of taxes.
- Foreign investment in investing companies registered as Non-Banking Financial Companies (NBFCs) with the Reserve Bank, will be under 100% automatic route.
- When Indian investing company does not have any operations at the time of downstream, investment and subsequently commences business(s), it will have to comply with the relevant sectoral conditions on entry route, conditionalities and caps.

Downstream Investment (Cont.)

Downstream Investment:

- Examples:

Indian Company Y has received foreign investment from non-resident investors. Company Y makes further investment into Indian Company X.



Verdict for Total Indirect Investment in Company X:

0% since Co. Y owned by Resident Indian citizens

80% since Co. Y is not owned by Resident Indian citizens

100% since mirror image

Downstream Investment (Cont.)

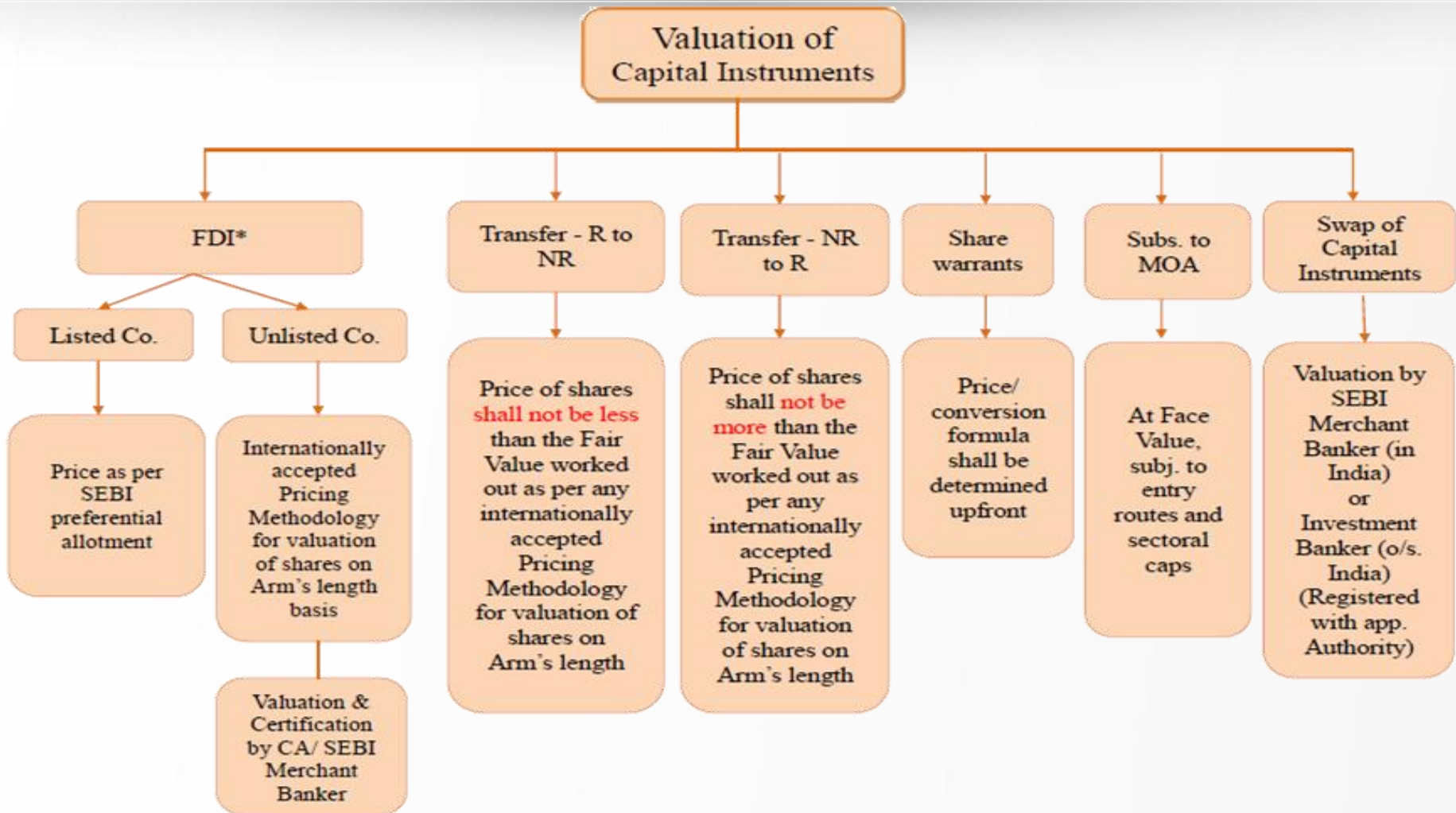
Transfer of Downstream Investment:

Transferor	Transferee
First level IndCo / LLP	PROI
First level IndCo / LLP	PRI
First level IndCo / LLP	Comparable first level IndCo / LLP

Compliance Obligation:

- First level Indian company making downstream investment to be responsible for ensuring compliance with provisions of these regulations for the downstream investment made by it at second level and so on and so forth.
- Such first level company to obtain a certificate to this effect from its statutory auditor on an annual basis.
- Such compliance of these regulations to be mentioned in the Director's report in the Annual Report of the Indian company.
- In case statutory auditor has given a qualified report, the same needs to be immediately brought to the notice of the Regional Office of the Reserve Bank in whose jurisdiction the Registered Office of the company is located and shall also obtain acknowledgement from the RO.

Pricing Guidelines

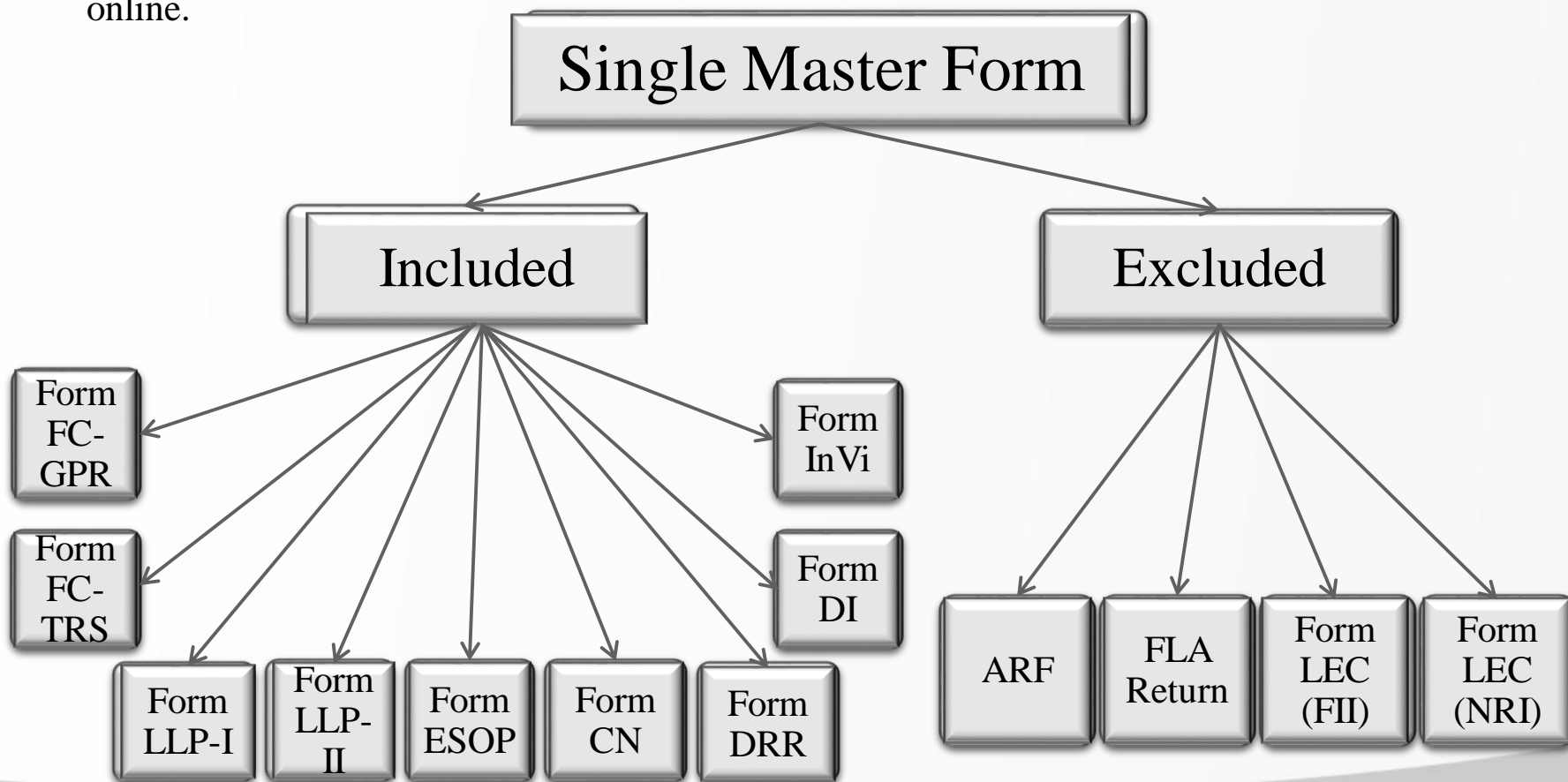


*For Convertible capital instruments, price / conversion formula to be determined upfront. Further, price at the time of conversion cannot be < fair value determined at the time of issuance.



Comprehensive Reporting Requirement

- With the objective of integrating the extant reporting structures of various types of foreign investment in India, a Single Master Form (SMF) for reporting of foreign investments by companies/LLPs/Start-ups in India has been prescribed. It is a single stop form for all reporting relating to foreign investment subsuming all previously notified forms. The SMF is to be filed online.



Optionality Clauses

❖ Provisions under FEMA for optionality clauses:

- Reg. 2(v) Expl (a): Capital 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.

[In other words, the optionality clause obliges the buy-back of securities from the investor at the price prevailing/value determined at the time of exercise of the optionality so as to enable the investor to exit without any assured return.]

- Reg. 11(3) Expl.: The guiding principle would be that the person resident outside India is not guaranteed any assured exit price at the time of making such investment/ agreement and shall exit at the price prevailing at the time of exit.

❖ Legal validity of optionality clauses:

Case 1: *NTT Docomo Inc. vs. Tata Sons Ltd.* [O.M.P.(EFA)(COMM.) 7/2016 & IAs 14897/2016, 2585/2017] [Delhi HC] [dated 28.04.2017]

Optionality Clause: Put option @ 50% of investment amount upon failure to satisfy certain KPI.

Optionality Clauses (Cont.)

Judgement:

Para 59. The SHA, therefore, could not be said to be void or opposed to any Indian law including the FEMA, much less the ICA. FEMA contains no absolute prohibition on contractual obligations. It envisages grant of special permission by RBI. As rightly held by the AT, Clause 5.7.2 of the SHA always was legally capable of performance without the special permission of RBI, using the general permission under sub-regulation 9(2) of FEMA 20.

Case 2: *Cruz City 1 Mauritius Holdings v/s Unitech Limited [EX.P.132/2014 & EA(OS) Nos. 316/2015, 1058/2015 & 151/2016 & 670/2016] [Delhi HC] [dated 11.04.2017]*

Optionality Clause: Put option @ price which yielded post tax IRR of 15% on capital contribution if commencement of construction of real estate project is delayed beyond specified period.

Judgement:

Para 104. A Division Bench of this court in the case of SRM Exploration Pvt. Ltd v. N & S & N Consultants S.R.O.: 2012 (129) DRJ 113, after referring to various provisions of FEMA and FERA, held that although provisions of FERA prohibited entering into transactions/contracts which are in violation of the said Act, FEMA did not contain any provision which voided the transaction entered in contravention thereof.

Optionality Clauses (Cont.)

Para 119. The Put Option provided to Cruz City under the Keepwell Agreement could be exercised only within a specified time and was contingent on the Santacruz project not being commenced within the prescribed period. This was not an open ended assured exit option as is sought to be contended by Unitech. Cruz City had made its investment on a representation that the construction of the Santacruz Project would commence within a specified period. Plainly, if the construction of the Santacruz project had commenced within the specified period - that is, by 17.07.2010 - Cruz City would not be entitled to exercise the Put Option for exiting the investment. Further, the Put Option could only be exercised within a fixed time period of 180 days and the said option would be lost thereafter.

Para 122.Secondly, the contention is premised on an erroneous assumption that the Keepwell Agreement provides for an assured return in violation of FEMA. As stated above, the Put Option was relevant only if the construction of the Santacruz Project was not commenced within the specified period of two years. Cruz City had no assurance of exit at a pre-determined return under the Keepwell Agreement in the event the execution of the project was commenced on schedule.

Prohibited Activities

(Reg. 15 to FEMA 20(R))

- Lottery Business including Government/ private lottery, online lotteries**
- Gambling and betting including casinos**
- Chit funds**
- Nidhi company**
- Trading in Transferable Development Rights (TDRs)**
- Real Estate Business or Construction of Farm Houses**
- Explanation: For the purpose of this regulation, “real estate business” shall not include development of townships, construction of residential /commercial premises, roads or bridges and Real Estate Investment Trusts (REITs) registered and regulated under the SEBI (REITs) Regulations 2014.**
- Manufacturing of Cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes**
- Activities/ sectors not open to private sector investment e.g. (I) Atomic energy and (II) Railway operations**
- Foreign technology collaboration in any form including licensing for franchise, trademark, brand name, management contract is also prohibited for Lottery Business and Gambling and Betting activities**



Schedule 1 to FEMA 20(R)

Schedule 1 – Purchase/ Sale of capital instruments of an Indian company by a person resident outside India

❖ An Indian company may **issue** capital instruments to PROI subject to Reg. 16 viz.:

- Entry Routes → Automatic or Government Approval
- Sectoral Caps and Attendant Conditionality(s) → Sector wise- caps on foreign investment permitted under automatic / approval route; In sectors/ activities not listed in Reg. 15 or 16, foreign investment is permitted up to 100 percent on the automatic route

❖ PROI may **purchase** capital instruments of a **listed Indian company** on a **stock exchange** in India provided that:

- PROI making the investment has already acquired control of such company in accordance with SEBI (SAST) Regulations, 2011 and continues to hold such control;
- Amount of consideration may be paid as per the mode of payment prescribed in this Schedule or out of the dividend payable by Indian investee company

❖ WOS can issue capital instruments against **pre-incorporation / preoperative expenses** incurred by **NR entity** for lower of (a) limit of 5% of authorized capital & (b) USD 500,000:

- WOS operates in sector with 100% FDI under Automatic Route and no FDI linked performance conditions;
- Compliance of reporting requirement;
- Statutory Auditor utilization certification for pre-incorporation / preoperative expenses.

Schedule 1 to FEMA 20(R) (Cont.)

Schedule 1 – Purchase/ Sale of capital instruments of an Indian company by a person resident outside India (cont...)

- ❖ An Indian company may **issue** capital instruments to a PROI **under automatic route**, if the Indian investee company is engaged in sector under automatic route against:
 - Swap of capital instruments,
 - Import of capital goods/ machinery/ equipment (excluding second-hand machinery),
 - Pre-operative/ pre-incorporation expenses (including payments of rent etc.)
- ❖ An Indian company may **issue** equity shares **against any funds payable by it** to PROI, the remittance of which is permitted under FEMA
- ❖ Mode of Payment → Inward remittance from abroad through banking channels or out of funds held in NRE/ FCNR(B)/ Escrow account
- ❖ Remittance of sale proceeds → Sale proceeds (net of taxes) of the capital instruments may be remitted outside India or may be credited to the NRE/ FCNR(B) [i.e. Repatriable]

Schedule 4 to FEMA 20(R)

Schedule 4 – Investment on Non-Repatriable Basis

❖ Non-Repatriable means -

- Only Dividend / Interest can be sent back abroad
- Principal + Gains cannot be repatriated

A. Purchase/ sale of capital instruments or convertible notes or units or contribution to the capital of an LLP

❖ Eligible Investor:

- NRI
- OCI
- a company, a trust and a partnership firm incorporated outside India and owned and controlled by NRIs or OCIs [*Owned & Controlled not defined in Sch.4, therefore as per Reg.14 Ownership shall mean beneficial holding of 50% + of Share Capital / LLP and major profit share Control shall mean right to appoint majority of Directors / Partners / DPs with NRIs*]

❖ Investment in:

- Capital instruments i.e. shares / CCDs / warrants etc. without any limit either on the stock exchange or outside it
- Units issued by an investment vehicle without any limit, either on / off stock exchange
- The capital of a Limited Liability Partnership without any limit.
- Convertible notes issued by a startup company in accordance with these Regulations.

Schedule 4 to FEMA 20(R) (Cont.)

Schedule 4 – Investment on Non-Repatriable Basis (Cont...)

- ❖ **Investment deemed to be domestic investment at par with the investment made by residents**
- ❖ Shall not invest in capital instruments or units of a Nidhi or company engaged in agricultural/ plantation activities or Real Estate Business or Construction of Farm Houses or dealing in TDRs.
 - Real Estate Business means Dealing in land to earn profits but excludes Leasing of property / Investment in REIT units / earning of rent income
- ❖ **Mode of Payment** → inward remittance from abroad through banking channels or out of funds held in NRE/ FCNR(B)/ NRO account
- ❖ **Sale/ maturity proceeds** →
 - Credited **only to the NRO account** of the investor, irrespective of the type of account from which the consideration was paid
 - Amount invested + capital appreciation shall not be allowed to be repatriated abroad [**NRI may avail USD \$ 1 Million scheme**]

Schedule 4 to FEMA 20(R) (Cont.)

Schedule 4 – Investment on Non-Repatriable Basis (Cont...)

B. Investment in a Firm or Proprietary Concern

❖ **Eligible Investor:**

- NRI
- OCI

❖ **Investment in:**

- Capital of firm / proprietary concern

❖ **Restricted Sectors for NRIs/ OCI:**

- Agricultural / Plantation / Real Estate Business / Print Media

❖ **Mode of Payment** → inward remittance from abroad through banking channels or out of funds held in NRE/ FCNR(B)/ NRO account

❖ **Sale/ maturity proceeds** →

- Credited **only to the NRO account** of the investor, irrespective of the type of account from which the consideration was paid
- Amount invested + capital appreciation shall not be allowed to be repatriated abroad [**NRI may avail USD \$ 1 Million scheme**]

Schedule 6 to FEMA 20(R)

Sch. 6 – Investment in LLP

❖ **Contribute to the capital of an LLP operating in sectors/ activities where**

- Foreign investment up to 100% is permitted under automatic route
- There are no FDI linked performance conditions
- Investment in compliance of LLP Act, 2008

❖ **No FDI in LLP in following cases:**

- Sectors with performance linked conditions. [E.g. FS, Real Estate, Single Brand Retail]
- Sectors eligible to receive less than 100% FDI under Automatic Route
- Sectors where FDI possible only with Govt. permission
- Agriculture / Plantation / Print Media / Private Security
- Sectors not opened up for FDI – Tobacco / Railways

❖ **Foreign Investors not allowed to Invest in LLP:**

- Pakistani / Bangladeshi entity / citizen
- FVCI
- FPI

❖ **Meaning of FDI Linked Performance Conditions:**

- FDI linked performance conditions are the sector specific conditions stipulated in regulation 16 of FEMA 20(R) for companies receiving foreign investment



Schedule 6 to FEMA 20(R) (Cont.)

Sch. 6 – Investment in LLP

❖ Pricing

- Capital Contribution \geq FMV worked out as per any Int'l Accepted Valuation Methodology by CA / CMA / Regd. Valuer
- Transfer of Capital Contribution or profit Share from R to NR \geq FMV & vice versa

❖ Payment

- Only Cash Consideration (no CoC as allowed for FDI)
- Inward remittance / NRE / FCNR (B) Account

❖ **Automatic Route Conversion of Co. with FDI into LLP and Conversion of LLP with FDI into Co. only if :**

- Sector where FDI up to 100% in Automatic Route
- No FDI linked Performance Conditions

❖ Other Conditions

- Designated Partner – must be an Indian Company / Indian Resident
- Resident DP u/s. 7 of LLP Act must be a Resident u/s. 2 of FEMA, 1999
- DP responsible for all compliances and penalties on LLP
- LLPs cannot avail ECBs

SECTOR SPECIFIC POLICY FOR TOTAL FOREIGN INVESTMENT



Manufacturing Sector

(Regulation 16.B of FEMA 20(R))

Activity	Sectoral Cap	Entry Route
Manufacturing Sector	100%	Automatic

- Manufacturer is permitted to sell its products manufactured in India through Wholesale and/or Retail including by way of E-commerce without the Government approval.
- Notwithstanding the Provision of these Regulations on Trading Sector, 100% Foreign Investment under Government approval route is allowed for Trading, including through E-commerce, in respect of food products manufactured and/or produced in India (locally produced and packaged foods products). Applications for foreign investment in food products retail trading would be processed in the Department of Industrial Policy & Promotion before being considered by the Government for approval.



Construction Development Sector

(Regulation 16.B of FEMA 20(R))

Activity	Sectoral Cap	Entry Route
Construction-Development Projects (which would include development of townships, construction of residential/commercial premises, roads or bridges, hotels, resorts, hospitals, educational institution, recreational facility, city and regional level infrastructure, townships.)	100%	Automatic

▪ **Conditions:**

1. Each phase of the construction development project would be considered as a separate project.
2. The investor will be permitted to exit on completion of the project *or* after development of trunk infrastructure i.e. roads, water supply, street lighting, drainage and sewerage.
3. Notwithstanding anything contained at (b) above, a person resident outside India will be permitted to exit and repatriate foreign investment before the completion of project under automatic route, provided that a lock-in period of three years, calculated with reference to each tranche of foreign investment has been completed. Further, transfer of stake from a person resident outside India to another person resident outside India, without repatriation of foreign investment will neither be subject to any lock-in period nor to any government approval.
4. The Indian investee company to sell only developed plots. For the purposes of this policy "developed plots" will mean plots where trunk infrastructure i.e. roads, water supply, street lighting, drainage and sewerage, have been made available.

Construction Development Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

Note:-

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 will not apply to Hotels and Tourist Resorts, Hospitals, Special Economic Zones (SEZs), Educational Institutions, Old Age Homes and investment by NRIs/ OCIs.
3. Completion of the project will be determined as per the local bye-laws/ rules and other regulations of State Governments.
4. 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.** However, there would be a 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** shall be excluded from the definition of “real estate business” and 100% foreign investment is allowed in real estate broking services under automatic route.

Construction Development Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

‘**Real estate business**’ means dealing in land and immovable property with a view to earning profit therefrom and does not include development of townships, construction of residential/commercial premises, roads or bridges, educational institutions, recreational facilities, city and regional level infrastructure, townships;

- 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..

Construction Development Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

Issues:

- How does one interpret the term “phase”? – Area allocation vs. sanctioned plan
- What if trunk infrastructure is pre-existing? Would that make exit simpler for investor? – City projects vs. suburban projects
- When is the project considered to have been completed? – BCC vs. OC
- Should “developed plots” also include completed premises built thereupon?
- Activity of Leasing of property is not considered as ‘real estate business’. Can an investor invest into a pure leasing company?
- Leasing of Property should not amount to transfer. However transfer includes any agreement or arrangement enabling enjoyment of property?

E-Commerce Sector (Regulation 16.B of FEMA 20(R))



TUESDAY, 31 JULY 2018

RESTRICTIONS ON RETAIL STRATEGIES OF ECOMM COS WITH SUBSIDIARIES

Draft Ecommerce Policy Champions India First

Suggests curbs that may hit foreign-owned cos and give more control to Indian founders with minority stakes

Kirtika.Suneja@timesgroup.com

New Delhi: The government's draft ecommerce policy makes a strong case for championing 'Indian' online enterprise and may have major implications for foreign-owned ecommerce majors operating in India.

Key recommendations include barring group companies of ecommerce players from "directly or indirectly influencing" sale prices. This may mean restrictions on retail strategies of ecommerce majors with subsidiaries.

The draft mentions that bulk purchases of branded goods like mobile phones, white goods, fashion items "by related party sellers

On The Table
Ecommerce group companies are barred from influencing sale prices. The draft also suggests Indian-owned and Indian-controlled online marketplaces be allowed to hold inventory as long as products are 100% domestically produced. This relaxation on marketplace ecommerce firms is not available for entities controlled by

ET was the first to report on July 6 about the draft ecommerce policy

which lead to price distortions in a marketplace" will be prohibited. This, if accepted in the final policy, may seriously affect sale strategies of big ecommerce players.

The policy also suggests Indian-owned and Indian-controlled online marketplaces be allowed to hold inventory as long as products are 100% domestically produced. This relaxation on marketplace ecommerce firms is not available for entities controlled by

Checks & Balances

Draft plan for ecommerce

Pricing Strategies
Group cos of ecomm marketplace barred from influencing prices
No bulk buys of white goods, fashion by related party sellers
Sunset clause defining maximum duration of deep discounts

Promoter Control

Inventory Model
Restricted inventory based model for even FDI-funded online cos
Majority India-owned and Indian managed portals can sell to retail using this model
Relaxation limited to India made goods

Differential voting rights giving founders more control

Tighter Regulation

Separate ED wing to look into alleged violations
CCI to examine potentially competition-distorting M&A
Single regulator, single law to address digital economy

Data Localisation

India generated data subject to controls and restrictions
Govt can access data stored in India for national security, public policy subject to privacy, consent

Data Localisation to Hit Foreign Tech Cos



India's new ecommerce policy, which recommends stronger form of data localisation, has added to the woes of foreign Internet and social media companies, reports Surabhi Agarwal. >>> 6

Greater Scrutiny of M&As >>> 14

E-Commerce Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

Activity	Sectoral Cap	Entry Route
B2B E-commerce	100%	Automatic
Market Place Model	100%	Automatic

▪ Conditions:

1. 'E-commerce' means buying and selling of goods & services over digital and electronic network.
2. 'E-commerce entity' means a company incorporated under CA 2013 or a foreign company covered under section 2 (42) of CA 2013.
3. 'Inventory based model of e-commerce' means an e-commerce activity where inventory of goods and services is owned by e-commerce entity and is sold to the consumers directly;
4. 'Market place model of e-commerce' means providing of an information technology platform by an ecommerce entity on a digital & electronic network to act as a facilitator between buyer and seller.
5. 'Digital & electronic network' will include network of computers, television channels and any other internet application.
6. Marketplace e-commerce entity will be permitted to enter into transactions with sellers registered on its platform on B2B basis.

E-Commerce Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

▪ Conditions(Cont.):

7. E-commerce marketplace may provide support services to sellers in respect of warehousing, logistics, order fulfillment, call centre, payment collection and other services.
8. An e-commerce entity will not permit more than 25 percent of the sales value on financial year basis affected through its marketplace from one vendor or their group companies.
9. Goods/ services made available for sale electronically on website should clearly provide name, address and other contact details of the seller.
10. Payments for sale may be facilitated by the e-commerce entity in conformity with the guidelines issued by the Reserve Bank in this regard.
11. Any warranty/ guarantee of goods and services sold will be the responsibility of the seller.
12. E-commerce entities providing marketplace will not directly or indirectly influence the sale price of goods or services and shall maintain level playing field.

▪ Issues

- Since 'e-commerce' means buying and selling of services too, how does one determine if it owns inventory of services?
- How does one ensure before end of year that 25% limit is not breached?
- What is meant by directly / indirectly influencing sale price?

Cash and Carry Wholesale Trading Sector

(Regulation 16.B of FEMA 20(R))

Activity	Sectoral cap	Entry Route
Cash and Carry Wholesale Trading / Wholesale Trading (including sourcing from MSEs)	100%	Automatic

▪ **Definition:**

1. Cash and Carry Wholesale trading (WT)/ Wholesale trading, shall mean sale of goods/ merchandise to retailers, industrial, commercial, institutional or other professional business users or to other wholesalers and related subordinated service providers.
2. Wholesale trading shall, accordingly, imply sales for the purpose of trade, business and profession, as opposed to sales for the purpose of personal consumption. **The yardstick to determine whether the sale is wholesale or not shall be the type of customers to whom the sale is made and not the size and volume of sales.** Wholesale trading shall include resale, processing and thereafter sale, bulk imports with export/ ex-bonded warehouse business sales and B2B e-Commerce.

▪ **Conditions:**

1. Except in cases of sales to Government, sales made by the wholesaler shall be considered as 'cash and carry wholesale trading/ wholesale trading' **with valid business customers**, only when WT is made to the following entities:
 - i. Entities holding sales tax/ VAT registration/ service tax/ excise duty/Goods and Services Tax (GST) registration; or

Cash and Carry Wholesale Trading Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

- ii. Entities holding trade licenses i.e. a license/ registration certificate/ membership certificate/ registration under Shops and Establishment Act, issued by a Government Authority/ Government Body/ Local Self Government Authority, reflecting that it is itself/ himself/ herself engaged in a business involving commercial activity; or
 - iii. Entities holding permits/ license etc. for undertaking retail trade (like tehbazari and similar license for hawkers) from Government Authorities/ Local Self Government Bodies; or
 - iv. Institutions having certificate of incorporation or registration as a society or registration as public trust for their self-consumption.
3. Full records indicating all the details of such sales like name of entity, kind of entity, registration/ license/ permit etc. number, amount of sale etc. should be maintained on a day to day basis.
 4. WT of goods shall be permitted among companies of the same group. However, such WT to group companies taken together shall not exceed 25 percent of the total turnover of the wholesale venture.
 5. WT can be undertaken as per normal business practice, including extending credit facilities subject to applicable regulations.
 6. A wholesale/ cash and carry trader can undertake single brand retail trading. An entity undertaking wholesale/ cash and carry as well as retail business will be mandated to maintain separate books of accounts for these two arms of the business and duly audited by the statutory auditors. Conditions under these Regulations for wholesale/ cash and carry business and for retail business have to be separately complied with by the respective business arms.

Single Brand Product Retail Trading Sector

(Regulation 16.B of FEMA 20(R))

Activity	Sectoral Cap	Entry Route
Single Brand Product Retail Trading (SBRT)	100%	Automatic

▪ **Conditions:**

1. Products to be sold - 'Single Brand' only. **Covers only products - branded during manufacturing.**
2. Products should be **sold under the same brand internationally.** [Not applicable to Indian brands.]
3. A PROI, whether owner of the brand or otherwise - permitted to undertake 'single brand' product retail trading in the country for the specific brand - **directly by the brand owner or through a legally tenable agreement executed between the Indian entity undertaking single brand retail trading and the brand owner.** [Not applicable to Indian brands.]
4. **A SBRT operating through brick and mortar stores - permitted to undertake retail trading through e-commerce.**
5. Indian brands are those which are owned and controlled by resident Indian citizens and/or companies which are owned and controlled by resident Indian citizens.

Single Brand Product Retail Trading Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

▪ Conditions (Contd.):

6. Sourcing norms:

- If foreign investment > 51%, then **minimum sourcing** to be done from India = **30% of the value of goods purchased**, preferably from MSMEs, village and cottage industries, artisans and craftsmen, in all sectors. || Self certification for domestic sourcing + Verification by Statutory auditors from a/cs. || **Sourcing norm to be met as an average of first 5 FY years. Thereafter, it is to be met on an annual basis.** || Sourcing should be done by FDI recipient Indian company only.
- Only during first 5 FY years from opening of 1st store, y-o-y incremental sourcing from India by group entities can be offset by FDI recipient Indian company against 30% India sourcing norm.
- Exemption from sourcing norms **for first three years from opening of 1st store** for products having state-of-the-art and cutting-edge technology and where local sourcing not possible. || A Committee under the Chairmanship of Secretary, DIPP, with representatives from NITI Aayog, concerned Administrative Ministry and independent technical expert(s) on the subject will examine the claim of applicants on the issue of the products being in the nature of ‘state-of-art’ and ‘cutting-edge’ technology where local sourcing is not possible and give recommendations for such relaxation.

Multi Brand Retail Trading Sector

(Regulation 16.B of FEMA 20(R))

Activity	Sectoral Cap	Entry Route
Multi Brand Retail Trading (MBRT)	51%	Govt. Approval

▪ Conditions:

1. Fresh agricultural produce, including fruits, vegetables, flowers, grains, pulses, fresh poultry, fishery and meat products can be unbranded. Government will have the first right to procure agricultural products.
2. Minimum amount as foreign investment - USD 100 million.
3. Of USD 100 million – 50% of the total foreign investment brought in the first tranche - invested in 'back-end infrastructure' within 3 yrs
 1. 'back-end infrastructure' will include capital expenditure on all activities, excluding that on front-end units; for instance, back-end infrastructure will include investment made towards processing, manufacturing, distribution, design improvement, quality control, packaging, logistics, storage, warehouse, agriculture market produce infrastructure etc.
 2. Expenditure on land cost and rentals, if any, will not be counted for purposes of back-end infrastructure. Subsequent investment in the back-end infrastructure would be made by the MBRT retailer as needed, depending upon its business requirements.
4. Retail trading, **in any form**, by means of e-commerce, - not permissible for companies with foreign investment in MBRT..

Multi Brand Retail Trading Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

▪ Conditions (Contd.):

5. **Sourcing norms:** \geq 30% of the procurement value of manufactured/ processed products to be sourced from Indian micro, small and medium industries, which have a total investment in plant & machinery not exceeding USD 2 million. || MSME valuation would refer to the value at the time of installation, without providing for depreciation. Their status would be reckoned only at the time of first engagement with the retailer and such industry shall continue to qualify as a MSME for this purpose, even if it outgrows the said investment of USD 2 million during the course of its relationship with the said retailer. || Sourcing from agricultural co-operatives and farmers co-operatives would also be considered in this category. || **Sourcing norm to be met as an average of first 5 FY years. Thereafter, it is to be met on an annual basis.**
6. Self-certification by company and verification by Statutory audites required for compliance with Sourcing norms, minimum capitalisation norms and capital utilisation norms for back-end infrastructure building
7. Retail sales outlets may be set up opened only in cities which cross threshold population. Provision to be made for requisite facilities such as transport connectivity and parking. || State / Union Territories can have their own state policy for implementation.

Other Financial Services Sector

(Regulation 16.B of FEMA 20(R))

Activity	Sectoral Cap	Entry Route
Other Financial services	100%	Automatic

▪ Conditions:

1. Other Financial Services will mean financial services activities **regulated by financial sector regulators**, viz., RBI, SEBI, IRDA, PFRD, NHB or any other financial sector regulator as may be notified by the Government of India.
2. 'Other Financial Services' activities need to be regulated by one of the Financial Sector Regulators. In all such financial services activity which are **not regulated by any Financial Sector Regulator** or where **only part of the financial services activity is regulated** or where there is doubt regarding the regulatory oversight, foreign investment up to **100 percent will be allowed under Government approval route** subject to following minimum capitalization requirement:

Type	Entity	Activity	Minimum FDI Capital
Fund Based activities	Unregistered / Exempted	Unregulated	US\$ 20mn
Non-Fund based activities	Unregistered / Exempted	Unregulated	US\$ 2mn

Other Financial Services Sector (Cont.)

(Regulation 16.B of FEMA 20(R))

- **Conditions (Contd.):**
- 3. **Fund based activities:** Merchant Banking, Under Writing, Portfolio Management Services, Stock Broking, Asset Management, Venture Capital, Custodian Services, Factoring, Leasing & Finance, Housing Finance, Credit Card Business, Micro Credit, Rural Credit
- 4. **Non-fund based activities:** Investment advisory services, Financial Consultancy, Forex Broking, Money Changing Business, Credit Rating Agencies'
- 5. Any activity which is specifically regulated by an Act, the foreign investment limits will be restricted to those levels/ limit that may be specified in that Act, if so mentioned.
- 6. Downstream investments by any of these entities engaged in "Other Financial Services" will be subject to these Regulations.

Case Studies - I

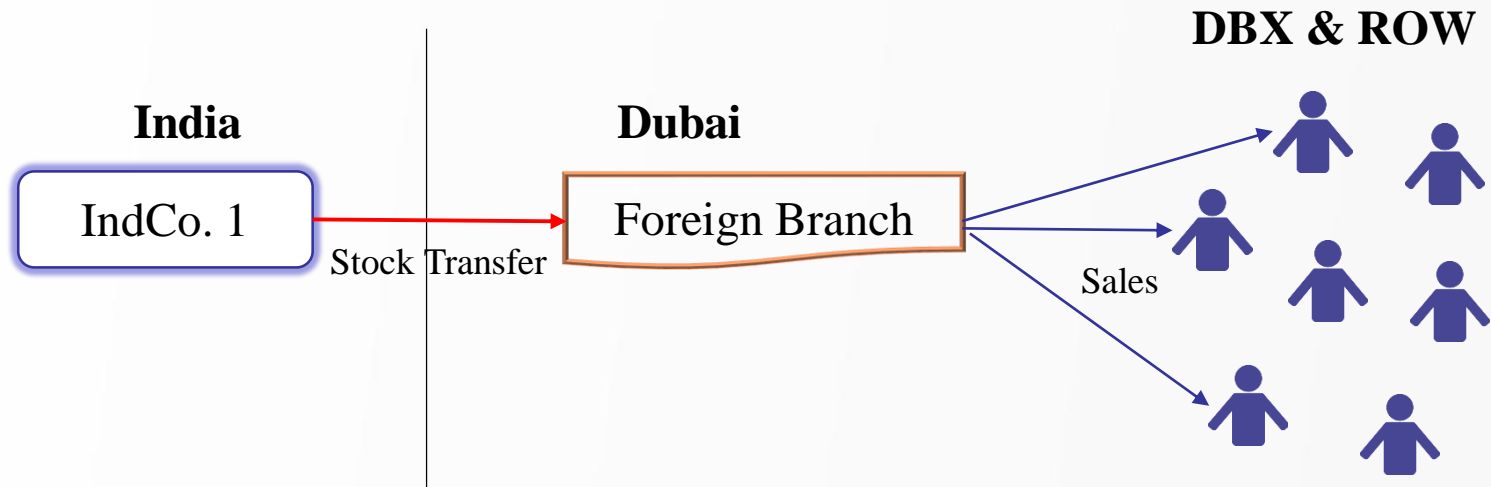
Facts: US Co. sells chemical products to various Indian customers in returnable cylinders. Since Indian customers are sluggish in returning the cylinders to US Co., US Co. intends to begin with charging a refundable deposit per cylinder for such returnable cylinders.



Question: Can US Co. charge refundable deposit from Indian Customers? 

Case Studies - II

Facts: Indian Company intends to open its first branch in Dubai for carrying on indenting activity outside India.



Question: Would 'export' of goods be considered when Indian Company transfers stock to branch *or* when branch actually effects a sale as an indenting agent?



Case Studies - III

Facts: An Indian resident incorporated a Private limited company in India somewhere in 1980s. It has now become an Indian conglomerate. The promoter has become NRI recently and as a measure of succession planning, wants to gift his shareholding to his children. His son is PRI whereas his daughter is PROI.



Question: Can he gift his promoter shareholding in Indian company to his children?



Case Studies - IV

Facts: A foreign company successfully runs a fantasy gaming app outside India. It wants to incorporate an Indian company to replicate its overseas success in popular Indian sports such as kabaddi and cricket.

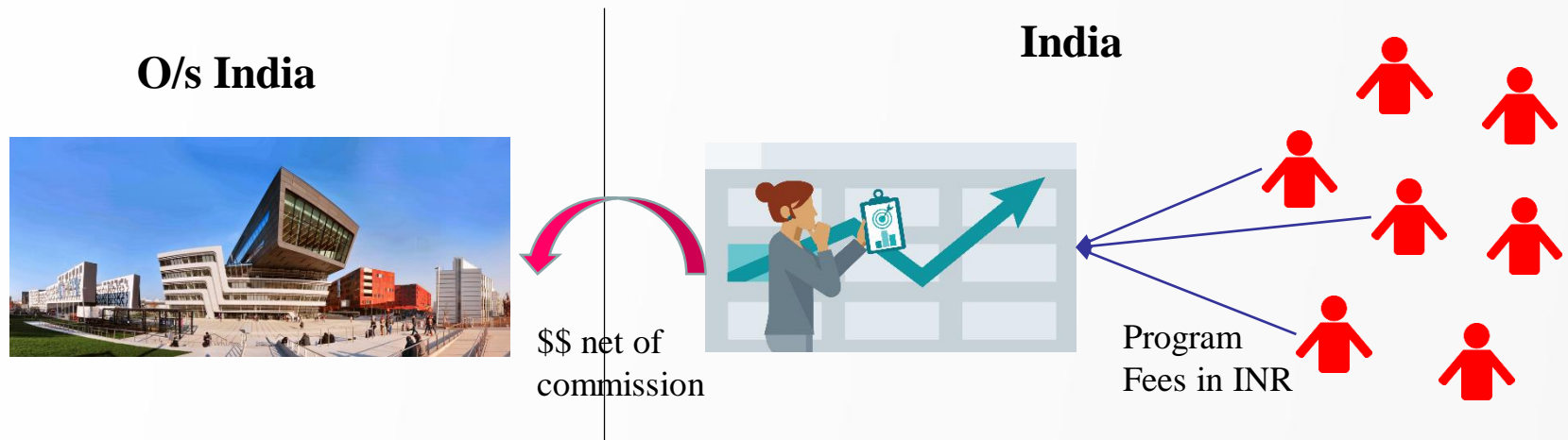


Question : Can the foreign company make investment under FDI into Indian company which proposes to operate fantasy gaming app in India on a paid / subscription basis?



Case Studies - V

Facts: A renowned foreign university wants to offer executive management programs in India. It has already engaged an exclusive marketing partner in India. However, the foreign university does not want the hassle of collecting payments from each participant and wants the Indian marketing partner to collect participant fees in India on its behalf. Subsequently, the Indian partner could remit the net participant fees after deduction of its commission fees.



Question: Can the Indian marketing partner collect fees in India on behalf of the foreign university and subsequently remit them net of its commission fees?

Case Studies - VI

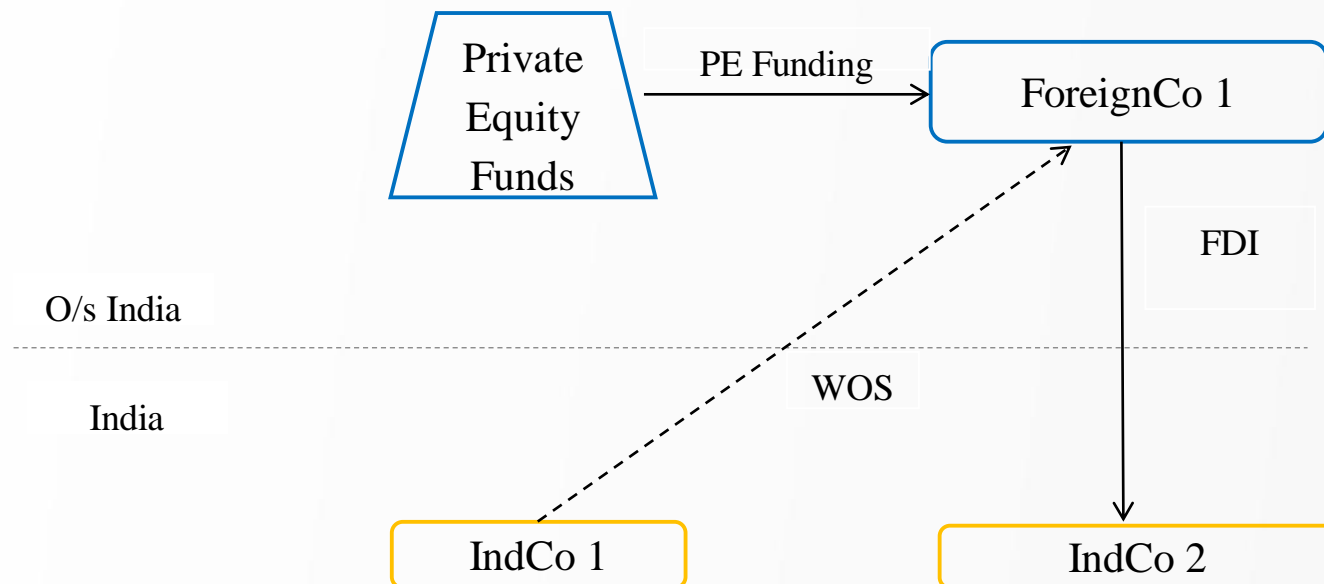
Facts: An Indian start-up company issues CCDs to investors in seed funding round. Valuation guidelines for convertible instruments stipulate that the price/ conversion formula of the instrument should be determined upfront at the time of issue of the instrument. Further, the price at the time of conversion should not in any case be lower than the fair value worked out, at the time of issuance of such instruments.

Question: If conversion ration is not fixed upfront, then which of the following clauses could possibly be considered as appropriate conversion formula?

1. CCD holders shall be entitled to receive the Conversion Equity Shares which shall entitle the CCD holders to collectively hold 15% of the Paid up Share Capital of the Company on a fully diluted basis as on the date of conversion.
2. In case of conversion of the CCDs, such conversion shall be (i) at 15% discount to the pre-money valuation of the Series-A funding round, or (ii) at valuation of USD 1 Million, whichever is higher.
3. Conversion of CCDs into equity shall be based on the firm value derived by management provided forward multiple of EV/Sales at the time of conversion.

Case Studies - VII

Facts: IndCo 2 intends to sell a majority stake in its company to pare down its high debt levels. IndCo 1 has tied up with foreign PE funds to purchase majority stake in IndCo2. However, foreign PE funds advice IndCo 1 to incorporate a new company ForeignCo 1 in tax friendly jurisdiction which will act as a pooling vehicle for acquisition of IndCo 2.



Question: Can IndCo 1 acquire IndCo 2 through ForeignCo 1 by partnering with foreign PE funds?

Thank you



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