



**UNDERSTANDING OF FEMA
PROVISIONS FOR OVERSEAS INVESTMENTS IN
COMPANIES & LLPs**

**RAJKOT CHAPTER OF WIRC OF THE ICSI
28TH APRIL 2018**

CA RAJESH H DHRUVA

**Overseas Indians ; Foreigners & Foreign Companies
can freely invest in India barring few restrictions & conditions.**

**Governing Laws are framed under
the Foreign Exchange Management Act 1999 (FEMA)**

**Companies Law ; Security Exchange Board of India Rules &
Income Tax Law do cover the ground**

**BUT WHEN THERE IS CONFLICTING PROVISIONS
FEMA OVERRIDES ALL OTHER LAWS**

**Foreign Exchange Management (Transfer or Issue of Security by a Person Resident
outside India) Regulations, 2017 is indeed the GOVERNING LAW**

**Non Resident Indians (NRI) being Indian citizens and Overseas Citizens of India
cardholders (OCI) residing abroad (except citizens of Pakistan & Bangladesh) can
freely invest on repatriation as also non-repatriation basis whereas Foreigners &
Foreign Companies subject to conditions can invest on repatriation basis only**

NON-RESIDENT INDIAN (NRI) - DEFINITION UNDER FEMA AND I. T. ACT:-

I. DEFINITION UNDER FEMA:-

1. Foreign Exchange Management Act, 1999 [FEMA] defines a Non-Resident Indian (NRI) Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2017 **defines** :-

.01 Regu 2(xxxv) 'Non-Resident Indian (NRI)' means as an individual resident outside India who is citizen of India;

.02 Regu. 2(xxxvi) defines 'Overseas Citizen of India (OCI)' as an individual resident outside India who is registered as an Overseas Citizen of India Cardholder under Section 7(A) of the Citizenship Act, 1955;

It may be noted that Person of Indian Origin (PIO) being Foreign Citizen of Indian Origin permanently residing outside India is replaced by **OCI**.

2. OCI Card can be availed by Foreign Citizen (other than Pakistan or Bangladesh) by
 - .01 Individual who was earlier Indian Citizen or
 - .02 Was eligible to become Indian Citizen or is a child , grandchild or great grand child of an Indian Citizen.
 - .03 Spouse of Indian Citizen or OCI Card Holder.
3. FEMA has wedded returning NRI's residential status to number of days exceeding 181 in a preceding year whereby in the year of return he continues to be an NRI which is a fallacy. Ideally an NRI is a resident when he returns to India for permanent settlement.

II. DEFINITION UNDER INCOME TAX ACT, 1961 [I.T. ACT] :-

1. The definition under Income Tax Act, 1961 [I. T. Act] is wedded to stay of an individual in the current year ; last 4 yrs, 7 yrs & 10 yrs.

2. Income Tax definitions are:-

A. Resident:-

An individual who stays in India for 181 days in F.Y. OR
More than 59 days in F. Y. AND More than 364 days in preceding 4 years.

- For a returnee NRI the rule of 59 + 364 days will apply.

B. Such a Resident is Not Ordinarily Resident (R but NOR) if :-

He is Non Resident in 9 out of 10 preceding years. OR
His stay does not exceed 729 days in preceding 7 years.

C. Resident and Ordinarily Resident (R & OR):-

A Resident not fulfilling EITHER of the conditions of R but NOR is Resident and Ordinarily Resident (R & OR).

D. Non Resident:-

i. An individual residing outside India or if an Indian citizen leaving India as a crew member of an Indian ship or to take up employment outside India, will be defined as a Non Resident if his stay in India does not exceed 181 days in a F.Y.

ii. The date of arrival and departure are included in stay in India.

OVERSEAS DIRECT INVESTMENTS IN COMPANIES:

1. NRIs , OCIs , Foreigners & Foreign Companies can freely invest in Equity Shares , Convertible Debentures and fully redeemable shares of Indian Private Limited Company and Public Limited Company.
2. NRIs can invest on repatriation basis as also non repatriation basis.
3. Foreigners and Foreign Companies can invest only on repatriation basis.

PAYMENT MODE :

1. NRIs can invest from NRE account , Forex Deposits / FCNR account or remittance from abroad for repatriation basis. Copy of Foreign Inward Remittance Certificate (FIRC) is to be provided.
 - .02 Investments on non repatriation basis can be made from above sources and also NRO account.
2. Foreigners & Foreign Companies cannot have NRE and FCNR account.
 - .02 As such their investments can be made by way of forex remittance from abroad only.
 - .03 Foreigners & Foreign Companies have to provide Know Your Customer (KYC) Certificate from Foreign Bank wherein Bank account is maintained.



PROCEDURES

I. ALLOTMENT ON REPATRIATION BASIS :

1. Under Company Law application money can be retained in separate Bank account and as such application money cannot be utilized till allotment of shares.
2. Earlier FEMA required allotment within six months .
.02 However Now as Companies Act, 2013 requires issuance of shares within 2 months the same is to be followed .
.03 If shares are not allotted within 2 months of application money being received then the same is to be refunded.
3. Company Laws allow issuance of non redeemable preference shares but FEMA does not permit the same.

II. ALLOTMENT ON NON REPATRIATION BASIS :

1. No procedural compliance is required for shares or debentures issued on non repatriation basis.
2. Shares and debentures can be issued on non repatriation basis only to NRIs or OCIs.

PROCEDURES :

1. FEMA requires filing of Advanced Remittance Form (ARF) being intimation of receipt of application money.
 - .02 ARF is to be filed on **e-Biz** portal within 30 days from receipt of application money .
 - .03 The application is required to be submitted together with :
 - .04 FIRC for Remittance of funds received from NRE account.
 - .05 Reserve Bank of India normally requires Indian Bankers Certificate regarding balance in NRE account being out of forex remittance abroad.
2. In case of forex remittance from abroad Foreign Bank's Know Your Customer (KYC) Certificate is required to be provided which requires investor's name , address , account number , period of relationship and ID number..
3. Upon allotment Form FC-GPR (Foreign Currency – Gross Provisional Return) is also to be filed on e-Biz portal within 30 days.
 - .02 CA's certificate regarding Fair Market Value of the equity shares of Indian Company and Company Secretary's Certificate regarding compliance of FEMA & Company Law Regulations is to be submitted.
4. Filing delays are subject to penalties for which compounding applications can be made.
5. Investee Company is to file annual return before 15th July.

PROCEDURES :

III. VALUATION :

1. The Fair Market Value that is present value is to be certified by Company's Auditors or any other Chartered Accountant following internationally accepted method.

IV. INVESTMENT VALUATION RULES :

1. Inbound investments can be made at Net Asset Value (NAV) or Higher Value.
2. Transfer of shares by Overseas Investors is permissible at Net Asset Value or Lower Price.
3. It seems that the intention of the Regulators is to ensure that India receives inward forex remittance more than Net Asset Value (NAV) and the Foreign Investors take away forex at NAV or lesser value..
4. However provisions of Gift being allowed amongst NRIs / OCIs or NRIs and Residents defies logic and moral support.

PROCEDURES :

V. TRANSFER OF SHARES :

1. Form FC-TRS is to be filed within 60 days after payment is made in case of shares issued on repatriation basis.
2. Existing shares of Indian Company can be purchased and sold by Overseas Investors from Residents , NRIs or any Overseas Investor.
3. Upon price being paid by Overseas Investor Form FC-TRS is to be submitted to Resident Seller's Indian Bank.
4. Resident Seller's Indian Bank is to certify that funds have been received and credited in Seller's Bank account.
5. Upon formalities being completed the company is required to transfer shares in name of Overseas Buyer.

NRI INVESTMENT - TRANSFER OF SHARES :

1. TRANSFER BY RESIDENT : Resident to NRI ; Foreigner or Foreign Company other than OCB :

.01 Gift - only to close relative -Sec. 6 of Co. Act ; max. \$ 50,000 [Anomaly - should be \$ 250,000 ; RBI's Prior Permission; Valuation certified by CA as per SEBI Guidelines.

.02 Sale - freely permissible barring certain sectors like Agriculture , Tea Sector , Mining , Financial Services etc.

Auto Route - Form FC-TRS is to be filed on eBiz Portal and pricing of shares should not be less than DFCF method.

2. TRANSFER BY NRI :

.01 NRI to NRI - by way of sale or gift - No procedures.

.02 NRI to Overseas Corporate Body - by way of sale or gift : No procedures.

.03 NRI to Resident - GIFT - No procedures.

.04 NRI to Resident - Sale of listed shares on stock Exchange - No procedures.

.05 NRI to Resident - Sale of unlisted shares is permitted under Auto Route & requires reporting in FC-TRS and Pricing of shares should be more than DFCF method.

3. TRANSFER BY FOREIGNER OR FOREIGN COMPANY :

.01 Foreigner to NRI , Foreigner and / or Overseas Corporate Body : Sale or gift permissible & no reporting requirements.

.02 Sale to Resident - Auto Route & requires reporting in FC-TRS . Pricing of shares should be more than DFCF method.

.03 Foreigner or Foreign Co. to Resident - GIFT is permissible & no reporting requirements.

.04 It may not be intentional but the Law surprisingly allows gifts by NRIs and Foreigners to Residents without any reporting while requiring report of sale at market price.



NRI INVESTMENT - LOANS AND DEPOSITS :

I. ACCEPTANCE BY COMPANIES :

1. Indian companies prohibited to accept deposits from NRIs since 24/04/2004.
 - .01 Foreigners also cannot place deposits as such.
2. Deposits from NRI's Non-Resident Ordinary (NRO) account permissible.
 - .01 However such NRO balance should not be created out of NRE ; FCNR transfer or forex remittance.
3. Deposits from NRO account acceptable on non-repatriation basis.
4. The Companies Act, 1956 has no ceiling on NRI shareholding deposits.
 - .01 FEMA restricts NRI Debentures only through Public Offer i.e. 35% of Capital Reserves.

II. DEBENTURES :

1. Company can accept Indian Rupee borrowings by issuing Non-Convertible Debentures (NCDs).
2. Such NCDs are to be issued through Public Offer.
 - .01 Thus, private limited company cannot issue NCDs to NRIs / PIOs nor to Foreigners.
3. Such NCDs may be issued on repatriation basis or otherwise.
 - .01 For repatriation benefit, investment should be made from NRE / FCNR account or forex remittance from abroad.
4. NCDs can be issued for a period of not less than 3 years.
5. NCDs can be offered only to NRIs / PIOs.
 - .01 Such NCDs cannot be subscribed by the foreigners.



NRI INVESTMENT - LOANS AND DEPOSITS :

6. PROCEDURE :

1. For acceptance of Company Deposits from NRO account no reporting is required.
2. For Convertible Debentures issued on repatriation basis the procedure will be alike issue of shares on repatriation basis.
3. Convertible Debentures issued on non repatriation basis no reporting is required.
4. And in case of NCDs Indian Company is to file a report with the Reserve Bank :
 - .01 within 30 days of receipt of remittance - full details of remittance received.
 - .02 within 30 days of issue of Non-convertible Debentures (NCDs) - full details of the investment.
7. **TAX** : Interest income subject to tax at 0% to 33% based on the level of income.
 - .01 However Tax Deduction at Source (TDS) @30% U/S 195 of IT Act.
 - .02 Tax will be applicable at a lower rate as provided in Double Tax Avoidance Agreement (DTAA) provided Tax Residency Certificate (TRC) for relevant Tax Year is submitted.
 - .03 In such case TDS will also be at lower rate specified in DTAA.
 - .04 TDS requires Permanent Account Number (PAN card).



NRI INVESTMENT - EXTERNAL COMMERCIAL BORROWING :

1. **GENERAL** : A company can accept foreign currency as well as Indian Rupees Loan from NRI or Foreigners or Overseas Entities by way of ECB.
 - .01 ECBs can be availed under Automatic Route upto US\$ 100mn by Micro Finance Co.; US\$ 200mn by Software Co. ; US\$ 750mn by Infrastructure , Manufacturing , NBFC-IFCs, NBFC-AFCs, Holding & Core Investments Cos. ; US\$ 500mn by other Cos.
2. **Eligible borrowers** : Corporate entity being Private or Public Limited Cos.
3. **INTEREST** :
 - .01 Average maturity of 3 years upto 5 years LIBOR+3% and
 - .02 Average maturity more than 5 years LIBOR+5%
4. **LENDER:-** Foreign bank; financial institutions; supplier of plant and a Shareholder of the Co. having 25% or more equity.
5. **ECB CEILING** :
 - .01 ECB upto US\$ 5mn - No conditions.
 - .02 Limits not linked to capital.
 - .03 ECB of more than US\$ 5mn - Debt to Equity ratio of maxi. 4:1.
6. **PROCEDURES** :
 - .01 Appropriately drafted Loan Agreement to be executed by the Borrower and the Lender.
 - .02 Loan Registration Number (LRN) to be availed from RBI through Co.'s Bank.



NRI INVESTMENT - EXTERNAL COMMERCIAL BORROWING :

- .03 Monthly and annual statements to be filed reporting Receipts and Payments.
- .04 Changes in terms and conditions permissible as per rules but need to be notified.

7. END-USE :

- .01 Capital Expenditure being Plant & Machinery; Equipments etc.
- .02 Purchase of Land and Construction of Building not permissible.
- .03 Working capital or other objectives now permissible but from Shareholder having 25% or more Equity.

8. TAX :

- .01 15% vide Section 115BBD of Income Tax Act, 1961 (IT Act).
- .02 TDS at 20% as per Section 115A of IT Act.
- .03 Lower rate applicable in case of DTAA if Tax Residency Certificate (TRC) for current year is provided.
- .04 TDS requires Permanent Account Number (PAN) Card which is necessary.

- 9. Non-Convertible, Optionally Convertible or Partially Convertible Preference Shares or Debentures are to be treated as ECB.

10. HEDGING REQUIREMENTS FOR ECB IN FOREIGN CURRENCY :-

- .01 Co. in infrastructure ; NBFC-IFCs, NBFC-AFCs, Holding & CICs – upto 100% at all times.
- .02 Co.'s Banks to verify compliance.
- .03 Other entities - hedging as required by the concerned sectoral or prudential regulator.



PLANNING AND SUGGESTIONS

- ❑ As Deposits are not permissible Third Party Loan against security of NRI's NRE / FCNR Deposit and Forex Deposits in Overseas Bank by Foreigners and Foreign Companies
- ❑ Authorized capital and paid up capital should be examined.
 - .02 Often share application money in excess of authorized capital.
- ❑ Time limit of 2 months should be adhered to.
 - .02 Same is applicable to issue of shares on non-repatriation basis too.
- ❑ Valuation - based on latest audited accounts.
- ❑ Annual return has replaced Part B of Form FC-GPR.
 - .02 If accounts not audited, important changes require submission of revised Annual return.
- ❑ Overseas Corporate Bodies (OCBs) prohibited since 03/10/2003. However, active investments in manufacturing / industrial companies should not be viewed as prohibited.
- ❑ Change of residential status - Residents becoming NRIs and NRIs returning back home and becoming Resident.

thanx
&
njoy

