

ICSI WIRC - New Framework for Overseas Investments under FEMA + Compounding Orders on ODI

Harshal Bhuta

M.Com., F.C.A., A.D.I.T., LL.M. in Intl. Tax Law
(Wirtschaftsuniversität Wien)

ODI Rules & Regulations

Overseas Investment
Rules dated 22nd
August 2022 issued by
Ministry of Finance

Overseas Investment
Regulations dated 22nd
August 2022 issued by
RBI

Overseas Investment
Direction dated 22nd
August 2022 issued by
RBI

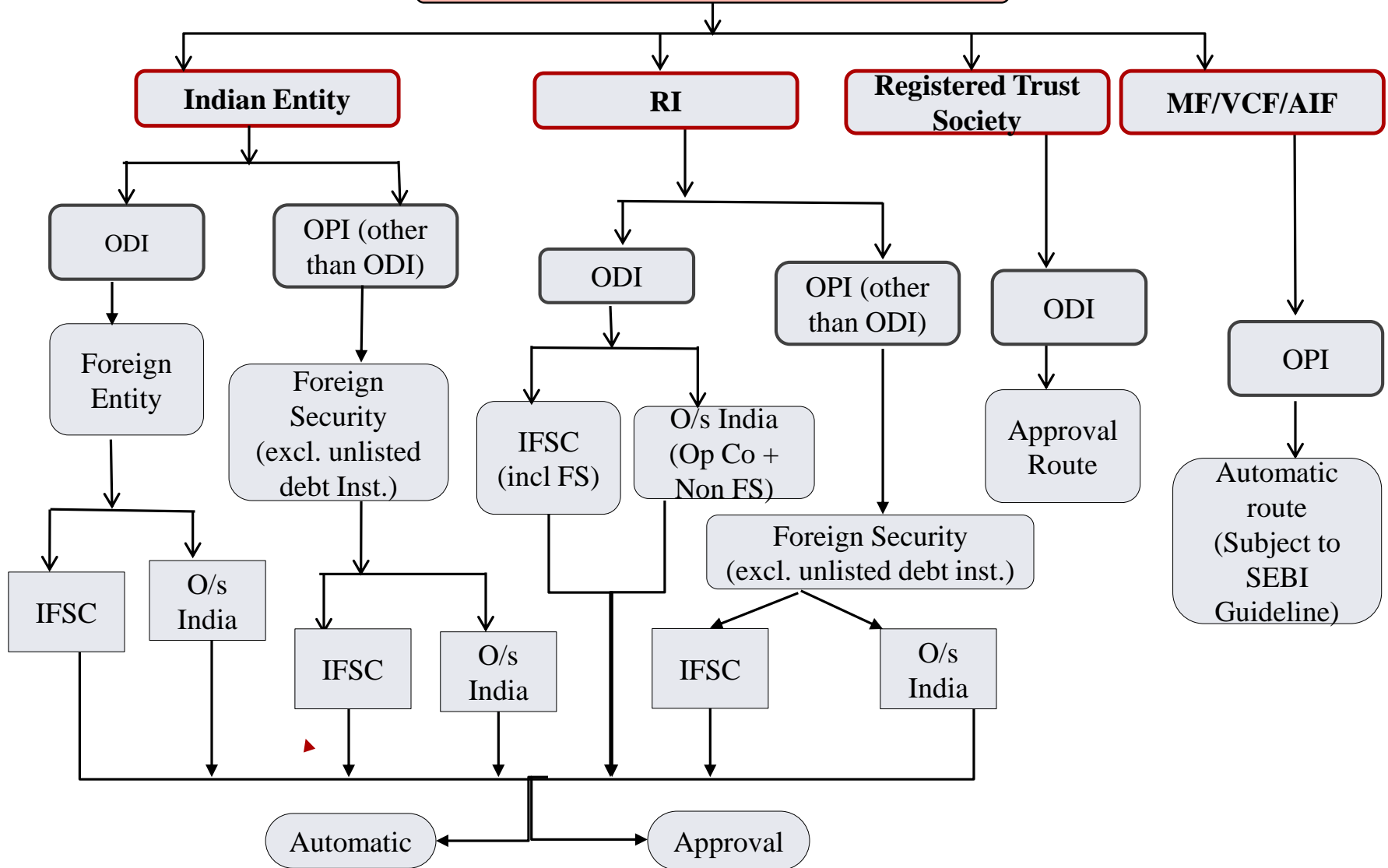
Master Direction on
Reporting (updated as
on 30th September
2022)

Master Direction on
LRS (updated as on
24th August 2022)

Master Direction on
Immovable Property
(updated as on 01st
September 2022)

Routes for Overseas Investments

Routes for Overseas Investments



Definition of ODI & Control

Erstwhile Notification No. FEMA 120	New FEMA Rules
<p>Direct investment outside India means investment by way of contribution to the capital or subscription to the Memorandum of Association of a foreign entity or by way of purchase of existing shares of a foreign entity either by market purchase or private placement or through stock exchange, but does not include portfolio investment. Also include Sponsor contribution to AIF.</p>	<p>ODI means investment by way of acquisition of unlisted equity capital of a foreign entity, or subscription as a part of the memorandum of association of a foreign entity, or investment in ten per cent, or more of the paid-up equity capital of a listed foreign entity or investment with control where investment is less than ten per cent. of the paid-up equity capital of a listed foreign entity.</p>

Definition of Control

- “control” means the right to appoint majority of the directors or to control management or policy decisions exercisable by a person or persons acting individually or in concert, **directly or indirectly**, including *by virtue of their shareholding or management rights or shareholders’ agreements or voting agreements that entitle them to ten per cent. or more of voting rights or in any other manner in the entity;*

Definition of OPI

Erstwhile Notification No. FEMA 120

- Portfolio investment not defined.
- PI by listed company permitted.
- For individuals, based on informal guidance, certain criteria to be tested:
 - ✓ Does not subscribe to MoA;
 - ✓ Not a WOS of RI;
 - ✓ RI should be a passive investor;
 - ✓ No other financial commitment;
 - ✓ Generally into listed company.

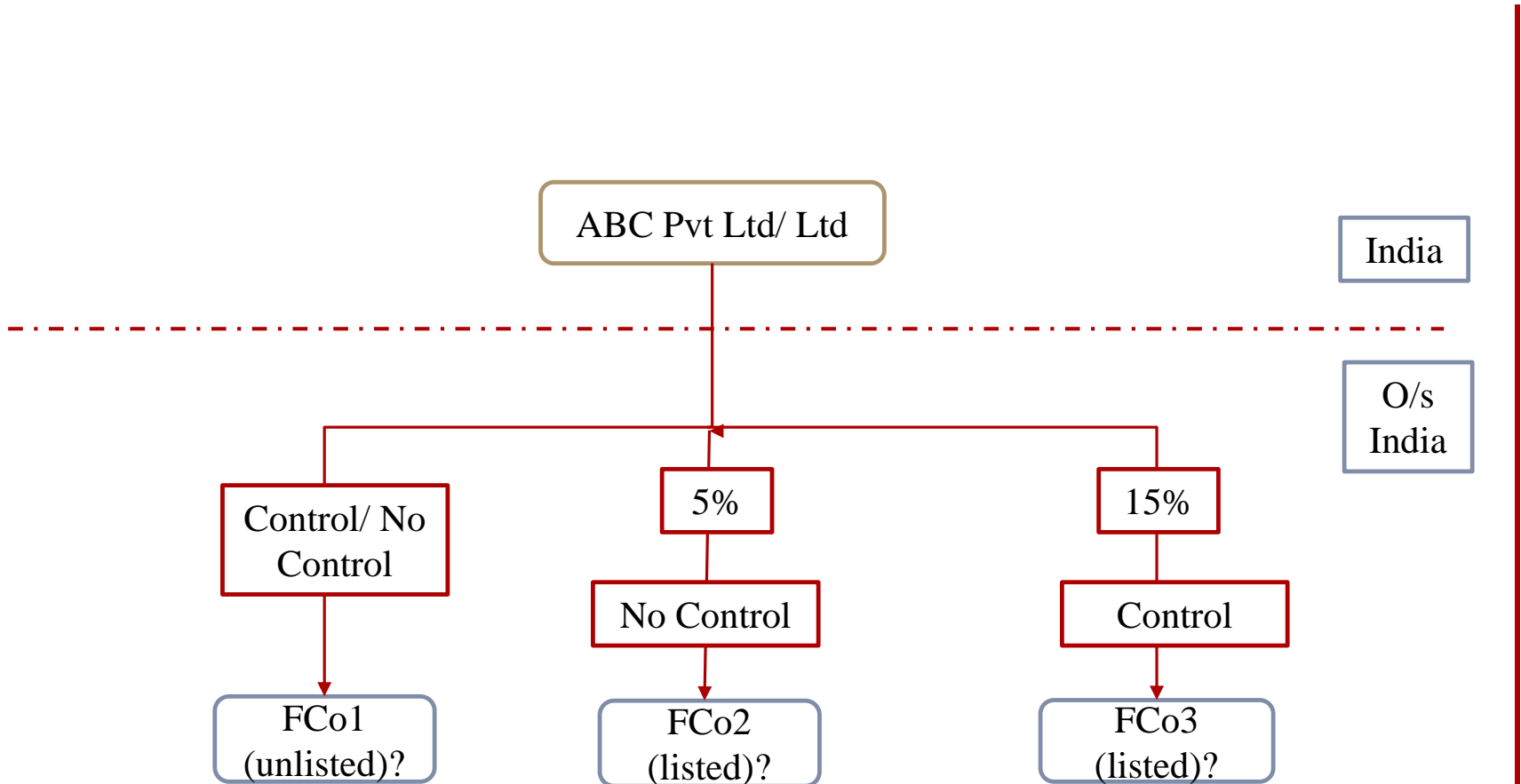
New FEMA Rules

- OPI means investment, *other than ODI*, in foreign securities, but not in any unlisted debt instruments or any security issued by a person resident in India who is not in an IFSC.
- OPI by PRI in the equity capital of a listed entity, even after its delisting shall continue to be treated as OPI until any further investment is made in the entity.

Observation/ Poser:

- ❖ Whether portfolio investment permitted anymore in an unlisted company?
- ❖ Whether resident individuals is permitted to make portfolio investments under LRS?
- ❖ What is the meaning of the term ‘foreign securities’?
- ❖ Whether ODI / OPI in derivative products is permitted?

ODI or OPI?



Net-worth Definition

Erstwhile Notification No. FEMA 120

- Net-worth means paid-up share capital & **free reserves**.
- Free reserves not defined.
- As per CA 2013, free reserves are those which are available for distribution as dividend.

New FEMA Rules

- Net-worth shall have the same meaning as assigned to it in Section 2(57) of the Companies Act, 2013.
- **Definition as per CA 2013**
 - *Net worth means the aggregate value of the paid-up share capital and all reserves created out of the profits, **securities premium account** and debit or credit balance of profit and loss account, after deducting the aggregate value of the accumulated losses, deferred expenditure and miscellaneous expenditure not written off, as per the audited balance sheet, but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation.*

Debt v/s Non-debt Instruments

Power to legislate on Capital Account Transactions w.e.f. 15.10.2019

Debt Instruments [RBI]	Non-Debt Instruments [CG]
Government Bonds	All investments in equity in incorporated entities (public, private, listed and unlisted)
Corporate Bonds	Capital participation in Limited Liability Partnerships (LLPs)
All tranches of securitisation structure which are not equity tranche	All instruments of investment as recognised in the FDI policy as notified from time to time
Borrowings by Indian firms through loans	Investment in units of Alternative Investment Funds (AIFs) and Real Estate Investment Trust (REITs) and Infrastructure Investment Trusts (InVITs)
Depository receipts whose underlying securities are debt securities	Investment in units of mutual funds and Exchange-Traded Fund (ETFs) which invest > 50% in equity
	The junior-most layer (i.e. equity tranche) of securitisation structure
	Acquisition, sale or dealing directly in immovable property
	Contribution to trusts
	Depository receipts issued against equity instruments

Other Important Definitions

- ❖ **Equity capital** means equity shares or perpetual capital or instruments that are irredeemable or contribution to non-debt capital of a foreign entity in the nature of fully and compulsorily convertible instruments;
- ❖ **Foreign entity** means an **entity formed or registered or incorporated outside India**, including International Financial Services Centre that has limited liability: Provided that the restriction of limited liability shall not apply to an entity with core activity in a strategic sector.
- ❖ **Overseas Investment or OI** means financial commitment and Overseas Portfolio Investment by a person resident in India.
- ❖ **Indian entity means**—
 - a **company** defined under the Companies Act, 2013 (18 of 2013);
 - a **body corporate** incorporated by any law for the time being in force;
 - a **Limited Liability Partnership** duly formed and incorporated under the Limited Liability Partnership Act, 2008 (6 of 2009); and
 - a **partnership firm** registered under the Indian Partnership Act, 1932 (9 of 1932).
- ❖ **Subsidiary or step down subsidiary** of a foreign entity means an entity in which the foreign entity has control.

Round Tripping

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none">The direct investment is made in an overseas JV engaged in bonafide business activity.	<ul style="list-style-type: none">No person resident in India shall make financial commitment in a foreign entity that has invested or invests into India, at the time of making such financial commitment or at any time thereafter, either directly or indirectly, resulting in a structure with more than two layers of subsidiaries.Restriction shall not apply to the companies mentioned in sub-rule (2) of rule 2 of the Companies (Restriction on Number of Layers) Rules, 2017

Observation/ Poser:

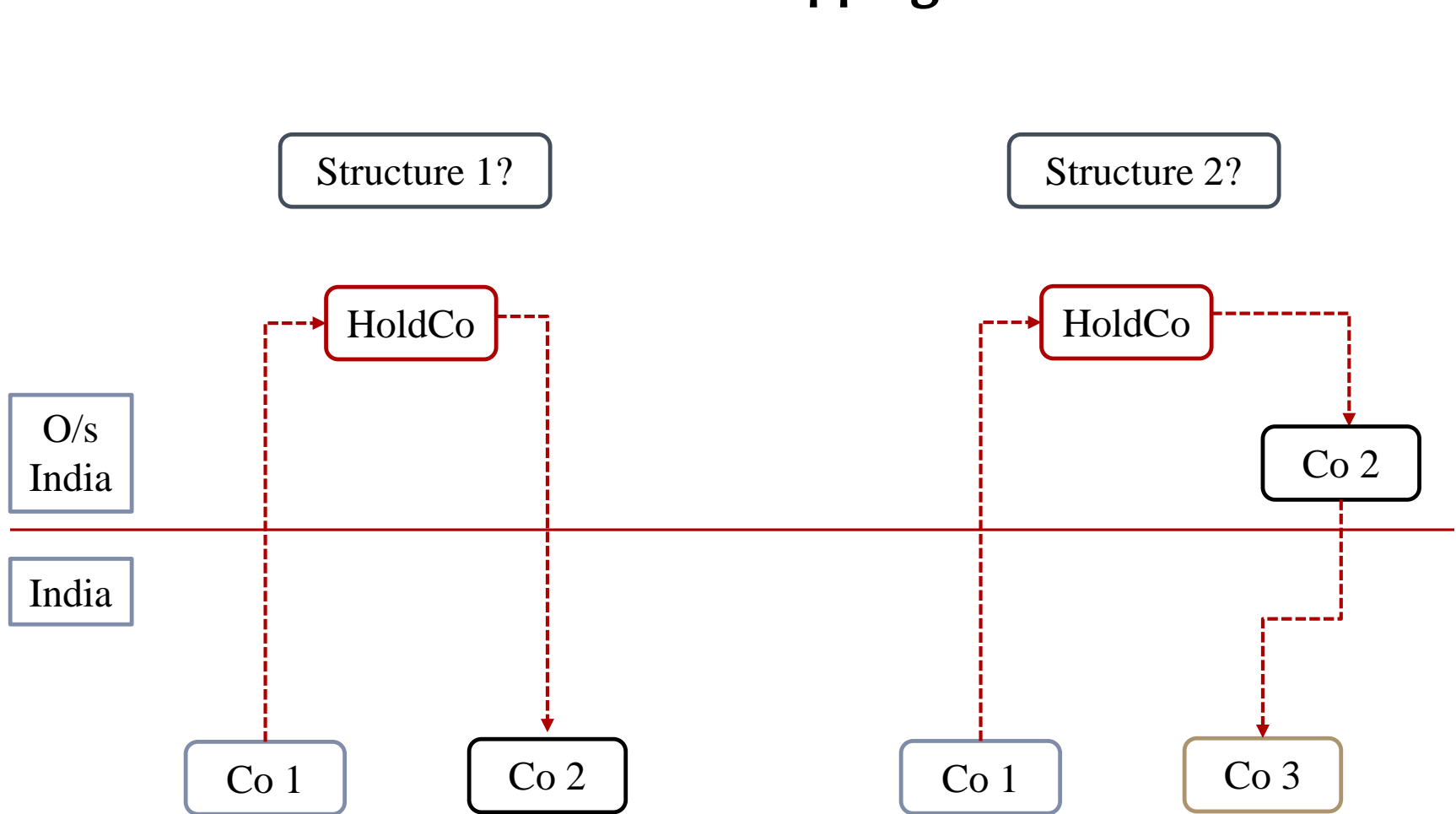
- ❖ Meaning of subsidiary?
- ❖ Starting point for counting 2 layers of subsidiaries?
- ❖ Whether ODI permitted if already a presence of > 2 layers of subsidiaries?

Round Tripping – Poll

❖ Which of the following structures may not be permitted?

- IndCo has four different Subco in UK, USA, Germany, Australia respectively
- IndCo has Subco in USA which has SDS1 in India
- IndCo has Subco in USA which has SDS1 in NL which has SDS 2 in SG which has SDS3 in India
- IndCo has Subco in USA which has SDS1 in NL which has SDS 2 in India

Round Tripping ?



Bonafide Business Activity

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none">The direct investment is made in an overseas JV/WOS engaged in bonafide business activity.	<ul style="list-style-type: none">Any investment by PRI o/s India shall be made in foreign entity engaged in bonafide business activity, directly or indirectly through SDS or the SPV.Bonafide business activity shall mean any business activity permissible under any law in force in India and the host country or host jurisdiction, as the case may be.

Observation/ Poser:

- ❖ Whether investment in the foreign company trading in crypto-currencies permitted?

Pricing Guidelines

Erstwhile Notification No. FEMA 120	New FEMA Rules
<p>(a) For the purposes of investment in an existing company o/s India, the valuation of shares of the company outside India shall be made, -</p> <p>(i) where the investment > USD 5 million - Cat I Merchant Banker or an Investment Banker/Merchant Banker outside India; In all other cases – CA/ CPA.</p> <p>(b) In case where consideration is to be paid fully or partly by issue of the Indian party's shares - valuation of shares of the company outside India needs to be carried out by a Cat I Merchant Banker or an Investment Banker/Merchant Banker outside India.</p> <ul style="list-style-type: none">• In case of disinvestment – CA/ CPA	<ul style="list-style-type: none">• Issue or transfer of equity capital of a foreign entity from PROI or PRI to PRI who is eligible to make such investment or from PRI to PROI shall be subject to a <i>price arrived on an arm's length basis</i>.• AD bank before facilitating a transaction to ensure compliance with ALP taking into consideration the valuation as per <i>any internationally accepted pricing methodology for valuation</i>.

Poser:

- ❖ Whether CA/ CPA can do valuation in all cases now? Validity Period of report?
- ❖ Concept of price v/s pricing - What if there is any deviation from ALP price? Eg: ALP 100 & shares are issued at 80

Disinvestment/ Transfer

Erstwhile Notification No. FEMA 120

- For transfer other than write-off certain conditions were required to be satisfied such as:
 - ✓ Pricing guidelines;
 - ✓ No o/s dues by way of dividend, *technical know-how fees, royalty, consultancy, commission or other entitlements and/or export proceeds*;
 - ✓ *1 year of operation* & APR submission;
 - ✓ IP not under investigation.
- In case of a write-off, apart from the above condition, certain limits were provided for eligibility. In other cases, RBI approval was required.

New FEMA Rules

- Where the disinvestment by a person resident in India pertains to ODI–
 - ✓ the transferor, in case of full disinvestment other than by way of liquidation, shall not have any dues outstanding for receipt, which *such transferor is entitled to receive from the foreign entity as an investor in equity capital and debt*;
 - ✓ the transferor, in case of any disinvestment, must have stayed invested for at least **one year from the date of making ODI:...**

Observation/ Poser:

- ❖ Disinvestment permitted in case o/s dues is in the nature of trade transaction?
- ❖ Whether write-off allowed now without any limit or without eligibility criteria?

Restructuring of FE Balance Sheet

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none">• Listed Indian party who had set up WOS or holding > 51% stake in overseas JV was permitted to write-off capital & other receivables up to 25% of equity investment under automatic route.• Docs such as certified copy of BS evidencing loss + projection for next 5 years indicating benefit to Indian party pursuant to restructuring was required to be furnished.• Unlisted Indian party who had set up WOS or holding > 51% stake in overseas JV was permitted to write-off capital & other receivables up to 25% of equity investment under approval route.	<ul style="list-style-type: none">• Permitted if FE incurs losses for the 2 PYs as evidenced by audited BS.• Compliance with reporting, documentation, and diminution in the total value of o/s dues after restructuring not exceed the proportionate amount of accumulated loss• Certification of diminution value at arms' length required if – OF investment amount > USD 10 million or amount of diminution > 20% of total o/s dues.• Certificate should be dated < 6 months before the date of transaction.

Deferred Payment

Erstwhile Notification No. FEMA 120	New FEMA Regulations
<ul style="list-style-type: none">• RBI Approval Route.	<ul style="list-style-type: none">• Where PRI acquires equity capital by way of subscription to an issue or by way of purchase from a person resident outside India or where a PROI acquires equity capital by way of purchase from PRI, and where such equity capital is reckoned as ODI, the payment may be deferred for such definite period from the date of the agreement subject:–<ul style="list-style-type: none">✓ Foreign securities shall be transferred or issued upfront;✓ Compliant with the applicable pricing guidelines upfront.• Deferred part of the consideration in case of PRI shall be treated as non-fund based commitment.

Observation/ Poser:

- ❖ Period of deferment needs to be decided upfront. Period within which remittance will be made needs to be defined in the relevant agreement
- ❖ What about delayed payment in case of subscription to MOA?

Restrictions/ Prohibitions for ODI

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none">• Direct investment in a foreign entity engaged in real estate business or banking business not permitted.	<ul style="list-style-type: none">• No person resident in India shall make ODI in a foreign entity engaged in:<ul style="list-style-type: none">✓ real estate activity;✓ gambling in any form; and✓ dealing with financial products linked to the Indian rupee without specific approval of the Reserve Bank. <p><i>Explanation</i>– For the purposes of this sub-rule, the expression "real estate activity" means buying and selling of real estate or trading in Transferable Development Rights but does not include the development of townships, construction of residential or commercial premises, roads or bridges for selling or leasing.</p>

Observation/ Poser:

- ❖ Whether ODI in Fco engaged in buying & leasing of property permitted?

ODI in Start-ups

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none">No restrictive condition.	<ul style="list-style-type: none">Any ODI in start-ups recognised under the laws of the host country or host jurisdiction as the case may be, shall be made by an Indian entity only from the internal accruals whether from the Indian entity or group or associate companies in India and in case of resident individuals, from own funds of such an individual.

Observation/ Poser:

- What if there are no regulations for recognition of start-ups in the host country?

No Objection Certificate

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none">• Prior approval of RBI.• Jindal Steel Power Ltd vs. RBI [LSI-352-HC-2021(DEL)]	<ul style="list-style-type: none">• PRI having an account appearing as a Non-Performing Asset (NPA) or is classified as wilful defaulter or is under investigation by a financial service regulator/ investigative agency shall obtain a NOC from the lender bank/regulatory body/investigative agency.• For obtaining NOC, an application in writing is required to be made to the concerned authority.• In case such concerned authority fails to furnish NOC within 60 days from receipt of such application – presume that there was no objection to the proposed transaction.

Pre-incorporation Expenses

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none">• Capitalisation of pre-incorporation expenses was permitted.• Expenses?• Receivables?	<ul style="list-style-type: none">• AD may allow remittance up to USD 1,00,000 per foreign entity.• For RI – LRS limit applicable.• PRI may capitalise such expenses or recognise as receivables or account them as expenses in their books of account.• However, unless recognised as financial commitment, such expense will not attract provisions of OI Rules/Regulations.

Overview of Schedules

Schedule I

- ODI by Indian Entity (IE)

Schedule II

- OPI by Indian Entity (IE)

Schedule III

- Overseas Investment by Resident Individual (RI)

Schedule IV

- Overseas Investment by PRI other than IE & RI

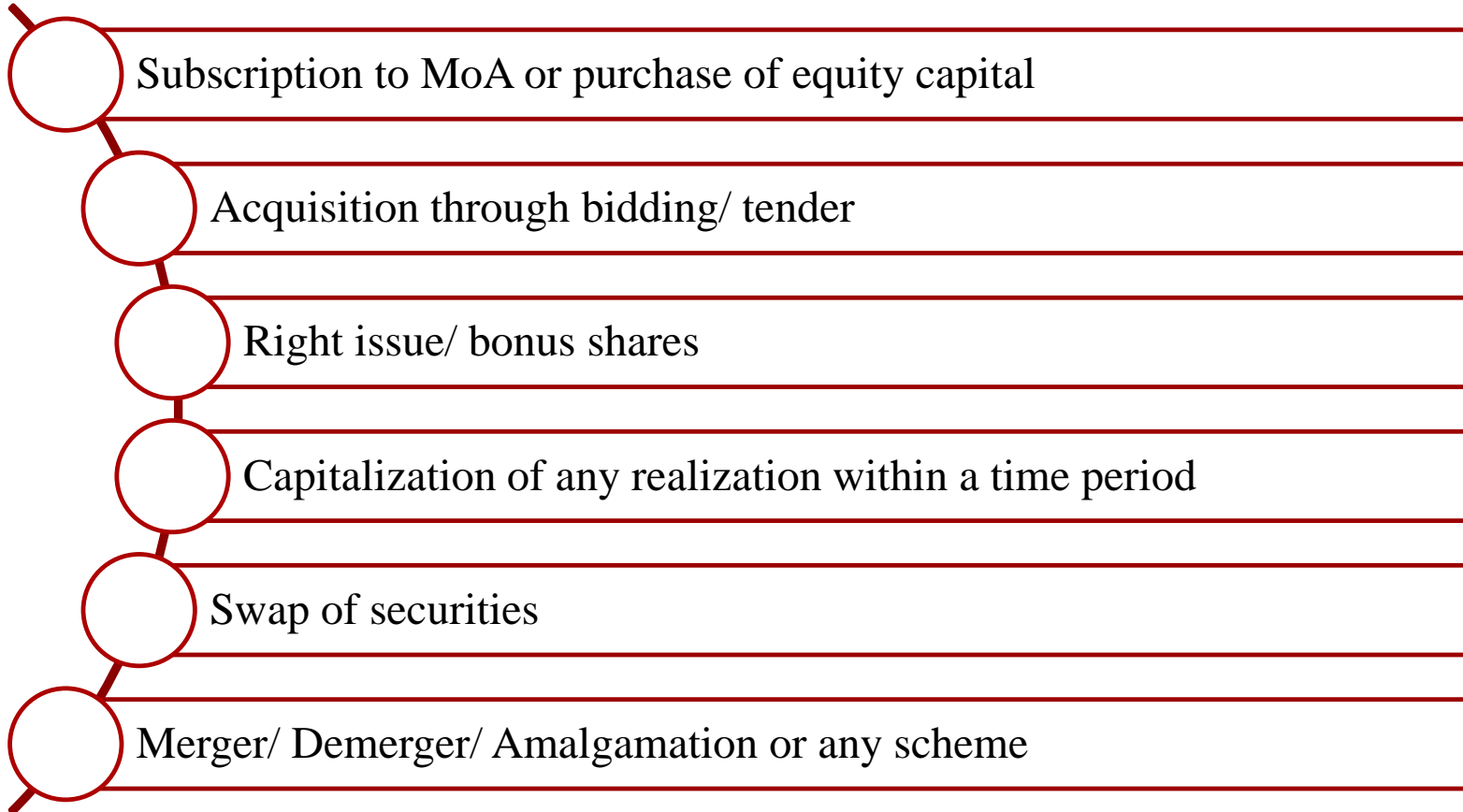
Schedule V

- Overseas Investment in IFSC by PRI

Sch I – ODI by Indian Entity (IE)

❖ Manner of Making ODI

- IE permitted to make ODI by way of:



Sch I – ODI by Indian Entity (IE)

❖ ODI in Financial Service Activity

Erstwhile Notification No. FEMA 120

- Indian party engaged in FS activity permitted subject to - 3 PYs NP criteria from FS activity; Registered/ regulated in India; Obtained approval in & o/s India; Fulfilled prudential norms. IP not engaged in FS activity – Not permitted.

New FEMA Rules

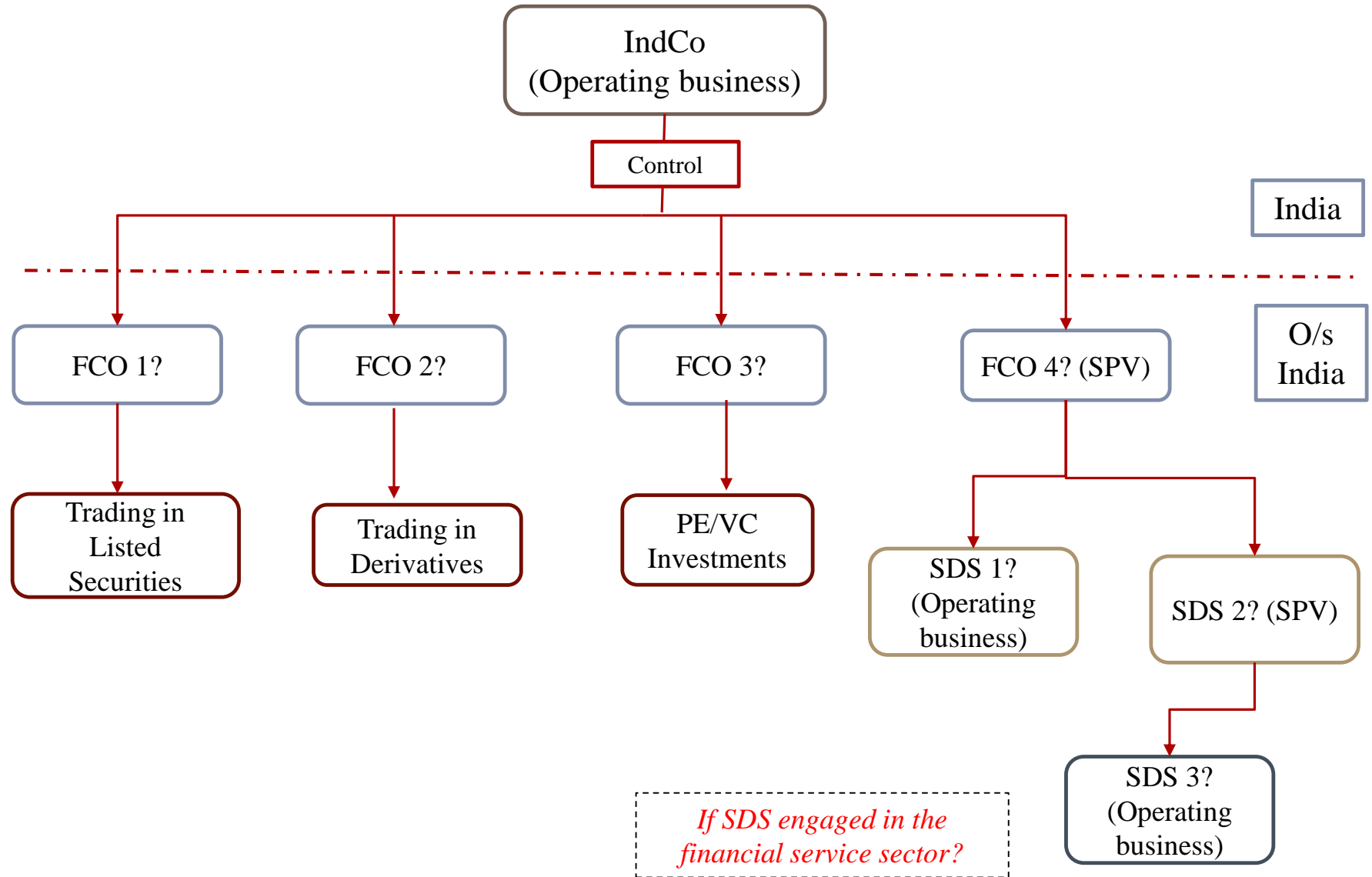
Indian Entity	ODI in Foreign Entity	Subject to FC/ Reporting/ other provisions
Engaged in FS Activity	Engaged in FS Activity	3 Year NP + Regulated/ registered + Approval criteria
	Not engaged in FS Activity	Subject to the guidelines issued by the respective regulator
Not Engaged in FS Activity	Engaged in FS Activity (Exc. Banking/ Ins.)	3 Year NP criteria
	Gen. & Health Ins.	3 Year NP criteria + supporting core activity

Sch I – ODI by Indian Entity (IE) - Poll

❖ Can IndCo incorporate FCo for the purpose of trading in trading in foreign securities?

- Yes, but only if they are listed equity stocks
- No, if they are unlisted bonds
- Yes, without any restrictions
- Not a permitted activity

Sch I – ODI by Indian Entity (IE)



Sch I – ODI by Indian Entity (IE)

❖ Limit for financial commitment

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none">• Total financial commitment of Indian Party shall not exceed 400% of its net worth as on the last audited balance sheet.• Net worth of HoldCo/ SubCo permitted to be used for computing net worth.• Net worth definition: paid-up capital + free reserves.	<ul style="list-style-type: none">• Total financial commitment of IE in all foreign entities shall not exceed 400% of its net worth as on the last audited balance sheet.• Capitalization of retained earnings should not be included in reckoning such limit.• Net worth of HoldCo/ SubCo now not permitted to be used for computing net worth.• Net worth definition aligned to CA Act definition.

Sch II – OPI by Indian Entity (IE)

- ❖ An Indian entity may make **OPI which shall not exceed fifty percent of its net worth** as on the date of its last audited balance sheet, in the manner and subject to the conditions laid down in this Schedule.
- ❖ A **listed Indian company may make OPI including by way of reinvestment.**
- ❖ An **unlisted Indian entity may make OPI** only under the following modes:
 - **Right issue/ bonus shares;**
 - **Capitalization** of any realization within a time period;
 - **Swap** of securities;
 - **Merger/ Demerger/ Amalgamation or any scheme.**

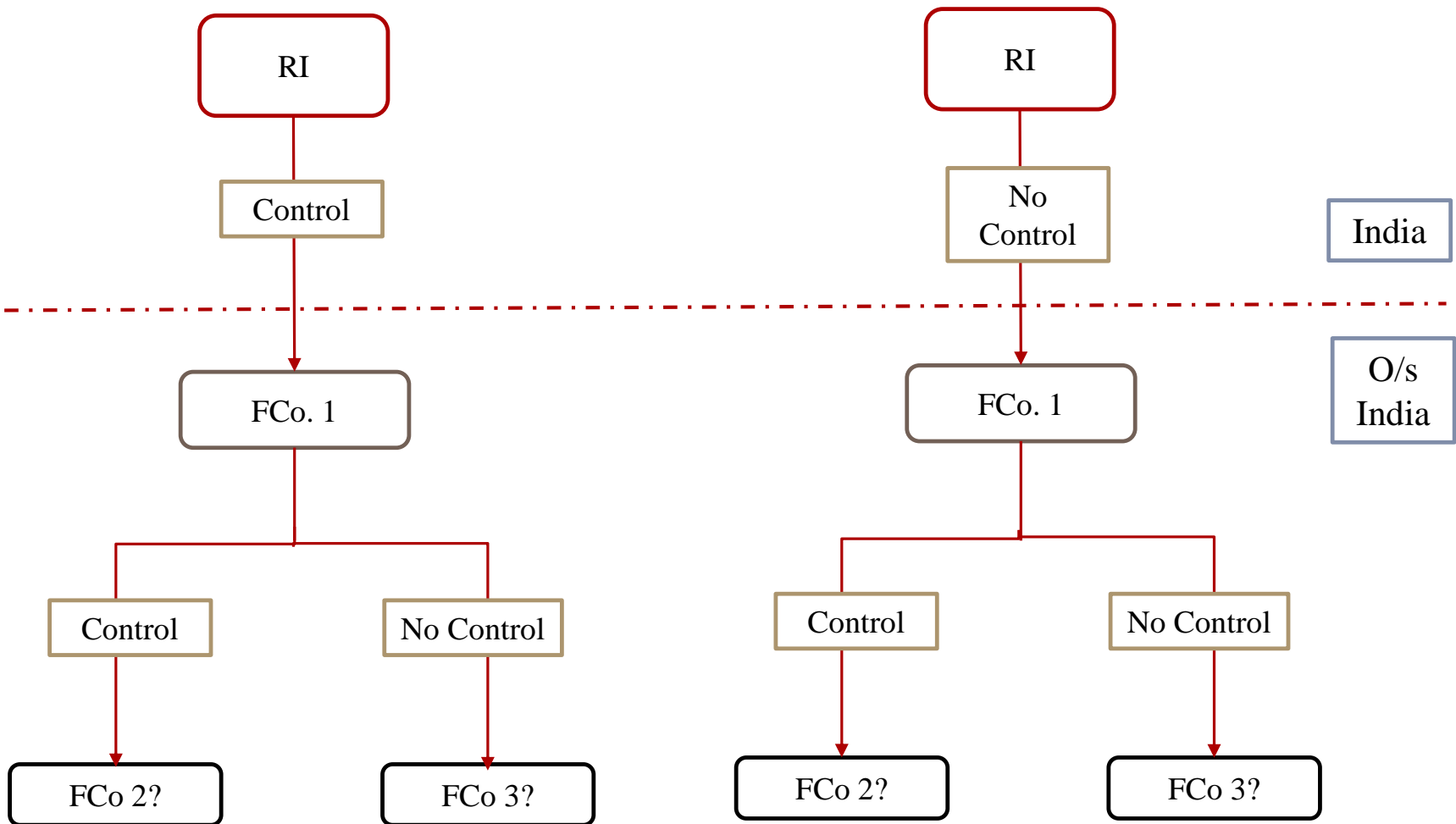
Sch III – Overseas Investment by RI

- ❖ **RI is permitted to make ODI or OPI subject to LRS limit** in the following manner:
 - ODI in an **operating foreign entity not engaged in FS activity** and which **does not have a subsidiary or step down subsidiary** where RI has **control in foreign entity**.
‘Subsidiary’ or ‘step down subsidiary’ of a foreign entity means an entity in which the foreign entity has control;
 - **OPI including reinvestment;**
 - **ODI or OPI by way of:**

Capitalization of any amount due within time period	Bonus shares or rights issue	Swap on account of merger/ demerger/ amalgamation/ liquidation	Gift
Inheritance	Sweat Equity Shares	Minimum Qualification Shares	ESOP Scheme

- ❖ ODI allowed if FE carries FS activity or has SDS in case of in **red** + **blue** mark.
- ❖ Holding < 10% shall be considered as OPI in case **blue** mark items.

Sch III – Overseas Investment by RI



Sch III – Overseas Investment by RI

❖ Acquisition by way of gift or inheritance:

Modes	Transferor	Transferee	Limits
Inheritance	PROI	PRI	Without any limits
Inheritance	PRI	PRI	Without any limits
Gift	PRI Relative	PRI	Without any limits
Gift	PROI	PRI	Without any limits

❖ Acquisition under ESOP Plan/ Scheme

Who can Receive	Limits
RI who is an employee/ director of the office in India or BO of an overseas company or Subco in India of an overseas entity or an Indian entity in which overseas entity has direct/ indirect equity	<ul style="list-style-type: none"> • Acquisition without any limits • Remittance under LRS limit

Sch IV – Overseas Investment by other than IE & RI

❖ ODI by Registered Trust or Society

- Any person being a registered trust or registered society engaged in the educational sector or which has set up hospitals are permitted to make ODI in a foreign entity with prior RBI approval and subject to satisfaction of certain terms & conditions.

❖ OI by MF or VCF or AIF

- MF/ VCF/ AIF permitted to acquire/ transfer foreign securities in accordance with the provision of these rules and subject to other terms and conditions as laid down by RBI/ SEBI.
- Aggregate Limits: shall be decided by RBI.
- Individual Limits: SEBI instructions.
- Investment under these rules by MF/ VCF/ AIF shall be treated as OPI.
- Every transaction concerning purchase/ sale needs to be routed through the designated AD Bank in India.

Sch V – Overseas Investment in IFSC

❖ Overseas Investment in IFSC by PRI

- PRI permitted to make an investment in IFSC in accordance with Schedule I/ II/ III & IV provided:

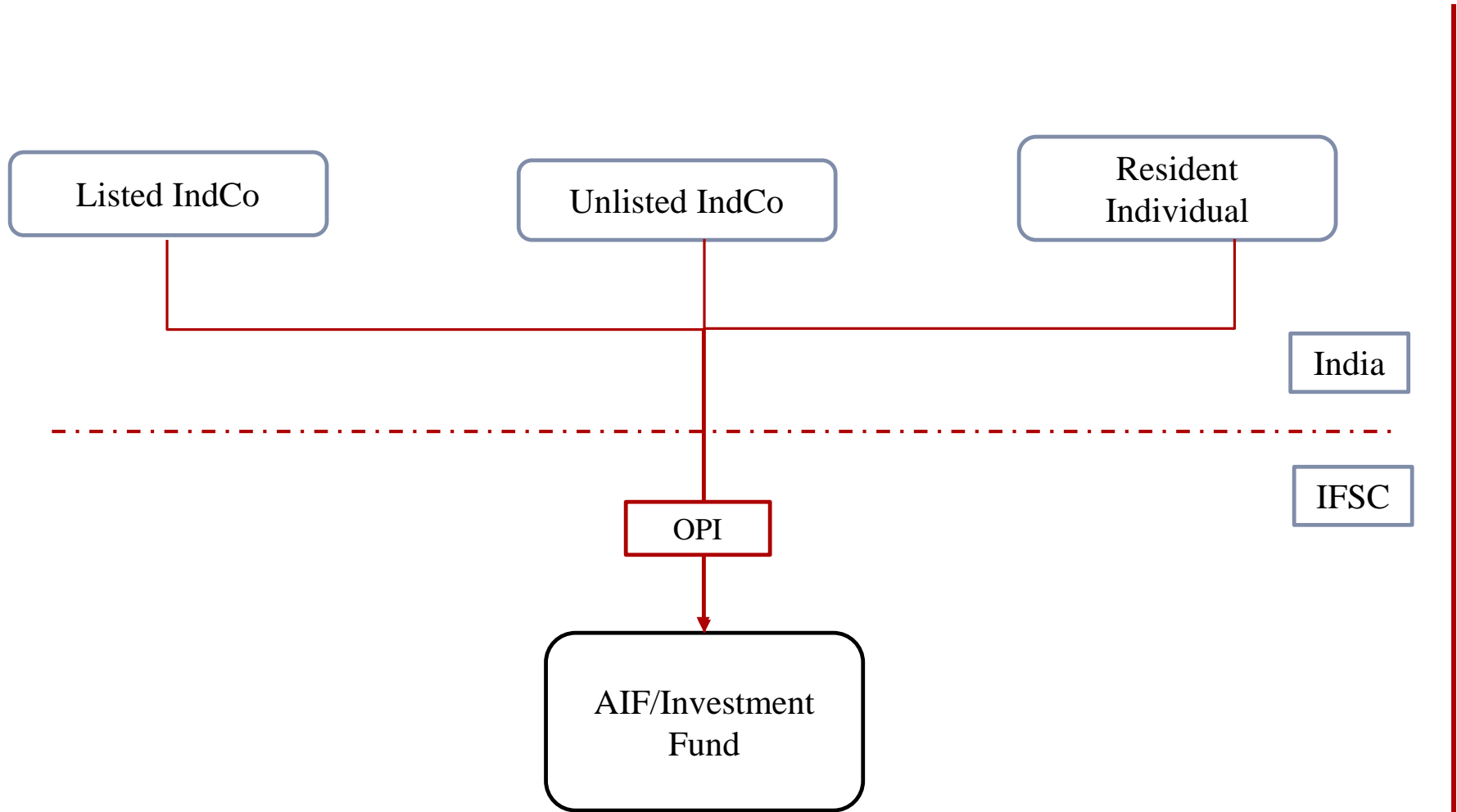
ODI in IFSC – approval of FS regulator to be decided in 45 days. Failing which construed as deemed approval

IE not engaged in FS activity in India and making ODI in foreign entity directly/ indirectly engaged in FS activity (except banking/ insurance) – permitted to make ODI in IFSC even when does not meet NP condition

PRI permitted to make OPI as a contribution to an investment fund or vehicle setup in an IFSC

RI permitted to make ODI in a foreign entity (even engaged in FS activity) in IFSC if such entity does not have SDS o/s IFSC in case RI has control in the such foreign entity

Sch V – Overseas Investment in IFSC



Financial Commitment by IE – Other than equity

- ❖ The Indian entity **may lend or invest in any debt instrument** issued by a foreign entity or extend the non-fund-based commitment to or on behalf of a foreign entity including overseas SDS **within the financial commitment limit** subject to the following conditions:
 - Indian entity is **eligible to make ODI**;
 - Indian entity **has made ODI** in the foreign entity;
 - Indian entity **has acquired control** in the such foreign entity at the time of making such financial commitment.
- ❖ Lending and investing in debt instruments subject to the condition that such **loans are duly backed by a loan agreement where the rate of interest is charged at ALP.**
- ❖ Financial Commitment by way of guarantee as well as by way of pledge or charge permitted subject to the terms & conditions if any provided under the Overseas Investment Regulations issued by RBI.
- ❖ **In the new ODI Regulations, approval for issuance of corporate guarantees to or on behalf of 2nd or subsequent SDS has been dispensed with.**

Financial Commitment - Guarantee

- ❖ Following guarantees may be issued to or on behalf of FE or any SDS in which IE has acquired control:
 - Corp/ Performance guarantee by IE;
 - Corp/ performance guarantee by a group company of such Indian entity in India, being a holding company or a subsidiary company or a promoter group company, which is a body corporate;
 - Personal guarantee by the RI promoter of such IE;
 - Bank guarantee, which is backed by a counter-guarantee or collateral by IE or its group company, and issued, by a bank in India.
- ❖ Guarantee extended by group Co – Utilisation of FC limit of such group co.
- ❖ Guarantee extended by RI– Utilisation of FC limit of IE
- ❖ No guarantee shall be open-ended
- ❖ Amount invoked - cease to be a part of the non-fund based commitment but be considered as lending
- ❖ Joint Guarantee – 100% amount towards individual limit; Perf. Guarantee – 50%
- ❖ Rollover of Guarantee – Not a fresh FC if amt does not exceed original guarantee
- ❖ Remittance towards invocation of guarantee – Not fresh FC.

Financial Commitment - Pledge

Security by Indian entity	In whose favour	Facility availed	Amount reckoned towards financial commitment
A) Pledge the equity capital of the foreign entity /its SDS outside India.	AD bank or a public financial institution in India or an overseas lender.	Fund/non-fund based facilities for Indian entity.	NIL
		Fund/non-fund based facilities for any foreign entity/its SDSs outside India.	The value of the pledge or the amount of the facility, whichever is less.
	A debenture trustee registered with SEBI in India.	Fund based facilities for Indian entity.	NIL
B) Create charge on its assets (other than A above) in India [inc. assets of its group company or associate company, promoter and / or director].	AD bank or a public financial institution in India or an overseas lender.	Fund/non-fund based facility for any foreign entity/its SDS outside India	The value of charge or the amount of the facility, whichever is less
	Overseas or Indian lender.	fund/non-fund based facilities for Indian entity.	NIL

Financial Commitment - Pledge

Security by Indian entity	In whose favour	Facility availed	Amount reckoned towards financial commitment
C) Create charge on the assets outside India of the foreign entity/ its SDS outside India.	An AD bank in India or a public financial institution in India.	Fund/non-fund based facility for any foreign entity/its SDS outside India.	The value of the charge or the amount of the facility, whichever is less.
		Fund/non-fund based facility for Indian entity.	NIL
	a debenture trustee registered with SEBI in India.	fund based facilities for Indian entity.	NIL

Reinvestment - ODI?

Erstwhile Notification No. FEMA 120	New FEMA Rules
<ul style="list-style-type: none"> All dues receivable from the foreign entity, like dividend, royalty, technical fees etc. – Repatriate within 60 days of its falling due. Sale Proceeds – Repatriate within 90 days for Indian party / 60 days for RI from the date of sale. 	<ul style="list-style-type: none"> PRI shall realise & repatriate within 90 days in the following cases: <ul style="list-style-type: none"> ✓ all dues receivable with respect to investment in a such foreign entity; ✓ consideration received on transfer/disinvestment; ✓ realisable value of assets on account of liquidation.

Reinvestment - LRS?

Erstwhile LRS Master Direction	Updated LRS Master Direction
<ul style="list-style-type: none"> Investor who has remitted funds are LRS are permitted to retain, reinvest the income earned on investment and thus, not required to repatriate funds or income to India. 	<ul style="list-style-type: none"> Income can be retained and reinvested. However, funds or income unless reinvested shall be repatriated and surrendered within a period of 180 days.

Obligation of PRI

- ❖ PRI is required to submit the **share certificate or any relevant document** as evidence of investment **within 6 months** from the date of effecting remittance/ date when dues are capitalized etc.
- ❖ PRI to **obtain a Unique Identification Number (UIN)** before sending outward remittance or acquisition of equity capital, whichever is earlier.
- ❖ PRI to **route all transactions** relating to a particular UIN through designated AD. Routing of transactions through the same AD even in a case where > 1 PRI makes the financial commitment.
- ❖ PRI shall **realise & repatriate within 90 days** in the following cases:
 - all dues **receivable with respect to investment in a such foreign entity**;
 - consideration received on **transfer/ disinvestment**;
 - relaisable value of assets on account of **liquidation**.
- ❖ PRI permitted to make remittance towards earnest money deposit or obtain bid bond guarantee for participation in bidding/ tender procedure.

Reporting Requirement for OI

- ❖ PRI who has made **ODI needs to report** the same in Form FC in case:
 - At the time of **sending outward remittance or making a financial commitment, whichever is earlier;**
 - **Disinvestment** within 30 days of receipt of disinvestment proceeds;
 - **Restructuring** within 30 days of such restructuring.
- ❖ **PRI other than RI making OPI or transferring OPI** to report such investment. Transfer **within 60 days** from the **end of half-year**.
- ❖ In case of OPI by way of ESOP scheme – reporting by Indian counterpart.
- ❖ PRI making ODI required to submit Form APR by end of 31st December every year.
 - No reporting is required in cases where PRI is holding < 10% without control and there is no other financial commitment other than by way of equity.
 - Control + not mandatory audit in host country – even then APR based on audited FS
 - In case ODI by 1 or more PRI – the person holding the highest stake may file.
 - Details of set up/ acquisition/ winding up of SDS or alteration in SH pattern of the foreign entity to be reported in Form APR.
- ❖ **Indian entity** who has made ODI required to **submit Form FLA before 15th July of every year.**

Delay in reporting

- ❖ **Delay post date of publication of these rules:** Submission can be made subject to payment of Late Submission Fees (LSF). However, the facility of payment of LSF can be availed within a period of 3 years from the due date of such submission.
- ❖ **Delay - Pre-date of publication of these rules:** Submission can be made subject to payment of Late Submission Fees (LSF). However, the facility of payment of LSF can be availed within a period of 3 years from the date of publication of these regulations in the Official Gazette i.e. 22nd August 2022.
- ❖ LSF mechanism/ calculation provided by RBI vide the directions issued in this regard.

Restriction of Further Investment/ Transfer

- ❖ PRI who has made a financial commitment in a foreign entity **shall not be permitted** to make any further financial commitment, whether fund-based or non-fund-based, directly or indirectly **till any delay in reporting is regularized.**

Late Submission Fees

- ❖ In case of delay in filing/submitting the requisite form/return/document - Pay the Late Submission Fee (LSF)
- ❖ The LSF for delay in reporting of overseas investment related transactions shall be calculated (per return) as per the following matrix:

Sr. No.	Type of Reporting delays	LSF Amount (INR)
1	Form ODI Part-II/ APR, FLA Returns, Form OPI, evidence of investment or any other return which does not capture flows or any other periodical reporting	7,500/-
2	Form ODI-Part I, Form ODI-Part III, Form FC, or any other return which captures flows or returns which capture reporting of non-fund based transactions or any other transactional reporting	[7500 + (0.025% × A × n)]

- ✓ “n” is the number of years of delay in submission rounded-upwards to the nearest month and expressed up to 2 decimal points.
- ✓ “A” is the amount involved in the delayed reporting.
- ❖ Maximum LSF: 100% of amount involved
- ❖ LSF Payment within 30 days

Case Studies



Case Study - I

Facts: Big Bull Inc., a company incorporated in the USA owns and operates the global investment platform that allows Indian HNIs to invest in stocks & ETFs listed in NASDAQ. Big Bull Inc. offers model portfolios on its platform, however, they don't advise on which models, stock, or ETFs HNIs should invest in. Big Bull Inc. will charge a platform fee and a model portfolio access fee to its clients. Further, Big Bull Inc. is also intending to incorporate a company in India to provide marketing services. Roar Enterprise Limited, an Indian company is in talks to acquire 25% of the share capital of Big Bull Inc.



Question: Whether Roar Enterprise Limited is permitted to acquire shares of Big Bull Inc. under FEMA?

Case Study - II

Facts: Mr. Intelligent Investor, a resident of India who is a follower of Mr. Warren Buffet's investing principles had made portfolio investments into the listed US stocks under LRS of RBI during the year 2015. However, since the financial results of some of the stocks were consistently poor on account of corporate governance issues and thus, Mr. Intelligent Investor sold a few of the stocks as under:

- Sale of A company's shares during the month of January 2022;
- Sale of B company's part shares during the month of July 2022.

Further, he is intending to sell balance shares of company B during the last week of March 2023. Moreover, Mr. Intelligent Investor has not utilized the sale proceeds of company A & B's shares till now since he is unable to find investment opportunities owing to the recession and business slowdown talks in the US.



Question: Is there any FEMA violation considering the above fact pattern?

Case Study - III

Facts: Esports Gaming Ltd, a company incorporated in Singapore is engaged in the business activity of Esports such as BGMI, Free Fire, Valorant, Counter Strike, FIFA, etc. Under this business model, Esports Gaming Ltd buys out players from different parts of the world and forms a team that will contest in global multi Esports events. Apart from receiving a monthly salary, players will also receive a split in ad revenue, prize money, etc in the agreed %. Gamer Limited, an Indian company intends to acquire 35% of Esports Gaming Ltd. since the founders are esports enthusiasts and also because the Olympic Esports Series event is to be held soon.



Question: Whether Gamer Limited is permitted to acquire shares of Esports Gaming Ltd under FEMA?

Case Study - IV

Facts: Mr. Bond, a resident Indian is of the view that the interest rates will fall in the near future which will result in an increase in the prices of bonds. With this investment philosophy, he already invests into bonds of HUDCO, REC, NTPC, SBI that are listed in India. Now he wants to invest abroad with this same philosophy. He plans to take exposure in overseas listed bonds as follows: ;

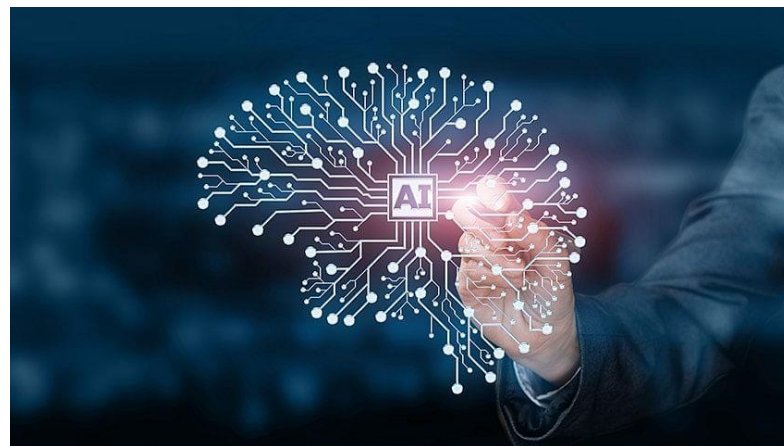
- Bonds issued by Vedanta Resources Finance II PLC, SBI (London Branch), Bank of Baroda (London Branch) listed outside India
- Investments in the listed overseas funds which will in turn invest in above overseas bonds
- Investments in overseas funds (not listed) which will in turn invest in above overseas bonds



Question: Whether Mr. Bond is permitted to invest in above capital assets?

Case Study - V

Facts: AI Technology Inc., a company incorporated in the USA is engaged in the new-age technology business of Artificial Intelligence, Machine Learning, etc. It is being claimed as the probable rival of OpenAI's ChatGPT. Algorithms Private Limited, an Indian company engaged in similar kinds of businesses is contemplating investing in an instrument of AI Technology Inc. which gives them the right to acquire shares of AI Technology Inc. in the future. In this arrangement, if there is any equity financing round, the instrument will be automatically converted into shares of AI Technology Inc. However, in case of any liquidity event such as a change of control or IPO, Algorithms Private Limited will receive the cash-out amount and the instrument will stand cancelled.



Question: Whether Algorithms Private Limited is permitted to invest in such an instrument issued by AI Technology Inc.?

Case Study – VI

Facts: Mr. A is engaged in the business activity of manufacturing of food & dairy products in India through its Indian company. Indian company of Mr. A makes almost all its export sales to the Gulf region. Now, Mr. A in his individual capacity plans to open an onshore distribution company in Dubai. MOA of onshore LLC would provide for sharing of profits between the shareholders on 80:20 basis with 80% profits attributed to Mr. A. However, the capital contribution would be 49:51% with 49% being that of Mr. A.



Question: Is the formation of such an overseas company permitted under FEMA?

Contravention of Overseas Direct Investment (ODI)



Notification No. FEMA 120 - ODI

❖ RIR Enterprises [C.A. No. 4096/2016]

Facts

- RRI International Limited in Mauritius was the WOS of the applicant incorporated on 5th Dec 2007. Applicant issued corporate and personal guarantees on behalf of its WOS, to ICICI bank, Bahrain so that WOS can raise a loan
- The financial commitment exceeded limit of 400% of net worth of the applicant.
- The WOS invested the loan proceeds in CCPS of an Indian company.

Relevant Regulation

- Regulation 6(2)(i), Regulation 6(2)(ii) and Regulation 6(2)(vi) of Notification No. 120/2004-RB dated 7th July 2004 - ODI subject to 400% of the financial commitment, ODI in JV/WOS engaged in bonafide business activity (ODI – FDI Structure) & Investment in JV/ WOS when the IP is under investigation

Key Takeaway

- Benefit due to round tripping of funds was neutralized: Difference between CCPS coupon rate (–) PLR.

Notification No. FEMA 120 - ODI

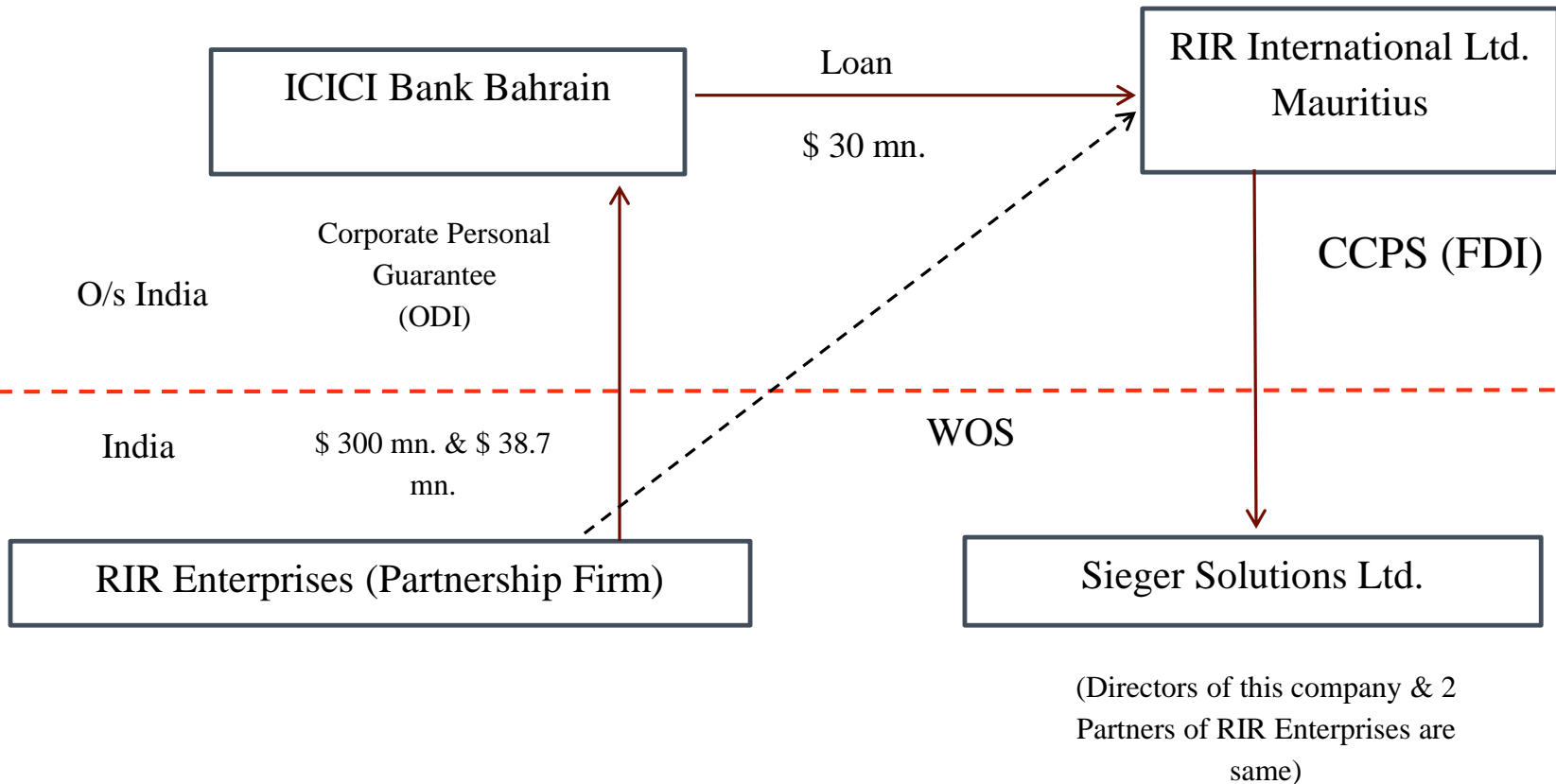
❖ RIR Enterprises [C.A. No. 4096/2016]

Key Takeaway (cont..)

- RBI had returned the application since matter had been referred to ED. However, applicant filed petition No. 652 of 2014 before Bombay HC. HC disposed of the petition by directing RBI to process the application and put show cause notice of DOE on hold for 4 weeks.
- Applicant argued that late filing of Form ODI was because AD didn't guide appropriately. RBI has stated in the order that such argument can be sustained to certain extent but primary onus lies on applicant to comply with FEMA. For other contraventions, RBI rejected the plea for leniency since an elaborate financial engineering for economic gain had been resorted to.

Notification No. FEMA 120 - ODI

RIR Enterprises – Round Tripping Issue



Notification No. FEMA 120 - ODI

❖ Reno Mercantile Private Limited [C.A. No. 4629/2018]

Facts

- The applicant provides back office support service to companies in India & abroad.
- Applicant acquired stake in M/s Vikasa Pte, a Singapore based company on 29th March 2017 when its net worth was Rs.0.93/- Crores.
- After the capital infusion in the applicant company from its shareholders, the investment came within 400% of net worth as on 15th June 2017.

Relevant Regulation

- Regulation 6(2)(i) - ODI in JV/ WOS shall not exceed 400%

Key Takeaway

- Regularization of Reg. 6(2)(i) can be under two alternative approaches:
 - Make disinvestment to extent of amount in excess of 400% of net worth of IP.
 - Infuse capital in IP equivalent to amount required to bring financial commitment within 400% of net worth of IP.
- The amount of contravention is only the excess of financial commitment over and above 400% of net worth of Indian Party.

Notification No. FEMA 120 - ODI

❖ PC Jeweller Limited [C.A. No. 4619/2018]

Facts

- The applicant is engaged in the business of manufacturing and exporting of jewellery. It had set up a WOS namely, PC Jeweller Global DMCC in UAE.
- Applicant was under investigation by DRI so it was not eligible to undertake ODI under the automatic route pending disposal of the appeal. Also, prior approval of RBI was required in such case.

Relevant Regulation

- Regulation 6(2)(iii) - Investment in JV/WOS is permitted, inter alia, if the Indian Party is not under any investigation

Key Takeaway

- Whether investigation initiated by DRI relates to a serious contravention suspected of money laundering/terror financing/affecting sovereignty & integrity of the nation is not expressed clearly.
- When a particular investigation can be said to be completed by investment/enforcement agency/regulatory body? - Reg. 6(2)(iii) is unclear.

Notification No. FEMA 120 - ODI

❖ Pyramid Consulting Engineers Private Limited [C.A. No. 4673/2018]

Facts

- The applicant made a remittance of USD 2,75,000 on 17th August 2007 towards investment in overseas JV viz. Pyramid Engineering & Consulting LLC in Oman. However, the plan to open the JV could not materialize.
- The aforesaid amount of investment was returned to the applicant after the deduction of bank charges. The applicant received partial amount within 6 months of initial investment and balance amount beyond 6 months of initial investment.

Relevant Regulation

- Regulation 15(i) – Submission of share certificate/ any other proof of investment within 6 months of effecting remittance

Key Takeaway

- RBI regards such timeline of 6 months as being applicable to receiving refund of share application money also. If share application money is returned within 6 months, then it may not amount to contravention of Reg. 15(i).
- An application for cancellation of the allotted UIN may be made upon receipt of refund of entire share application money when the transaction is not to be undertaken.

Notification No. FEMA 120 - ODI

❖ **Modular Power Private Limited [C.A. No. 4707/2018]**

Facts

- The applicant acquired 0.5% stake in the overseas JV viz. Energy Age Group Ltd, Germany in January 2008.
- Due to global recession, there was delay in forming the JV and subsequently, delay in getting confirmation of share allotment.
- A letter dated 22nd Jan 2010 was issued by the overseas JV certifying allotment of 0.5% of shares to the applicant which was submitted to AD in March 2010.
- As the company was a minority stakeholder holding 0.5% stake in the JV, it found it very difficult to obtain financial data by due dates.

Relevant Regulation

- Regulation 15(i) - Submission of share certificate/ any other proof of investment within 6 months of effecting remittance
- Regulation 15(iii) - An IP shall submit an Annual Performance Report in form ODI Part III in respect of each JV/WOS & other reports / documents
- Regulation 16(1)(v) - An IP may disinvest from its overseas JV with / without any write-offs of its initial investment provided it has been in operation for atleast one year and has submitted all APRs that were due

Notification No. FEMA 120 - ODI

❖ **Modular Power Private Limited [C.A. No. 4707/2018]**

Key Takeaway

- Share certificates are not the only acceptable evidence of investment under Reg. 15(i).
- Reg. 15(i) allows furnishing of any other document as evidence of investment in the foreign entity to the satisfaction of RBI.
- A minor stake of 0.5% in a foreign entity has been considered to satisfy Reg. 2(e) r.w. Reg. 2(m).

Notification No. FEMA 120 - ODI

❖ **Dynemic Products Limited [C.A. No. 4587/2017]**

Facts

- The applicant (DPL) had set up WOS i.e. Dynemic USA Inc., USA in the year 2005.
- In this case, there was disinvestment of ODI as the WOS was liquidated in Nov 2009 and it involved write off of a major component of equity investment and other receivables (loan) of DPL from WOS.
- Some proceeds from disinvestment were received in the form of cash & physical asset.

Relevant Regulation

- Regulation 16 - It lays down the conditions under which the Indian Party may transfer, by way of sale any share / security held by it in a joint venture (JV) or WOS outside India - under automatic route.
- Regulation 16(1)(iii) - An Indian party having made ODI in JV/WOS whose shares are not listed on the stock exchange, can disinvest under automatic route after submission of a certificate indicating the fair value of the shares based on the latest audited financial statements of the JV/ WOS, as certified by a CA /CPA.

Notification No. FEMA 120 - ODI

❖ **Dynamic Products Limited [C.A. No. 4587/2017]**

Key Takeaway

- Disinvestment proceeds not realized & repatriated to India by the way of inward remittance through the designated AD - contravention under Reg. 16. It partially received disinvestment proceeds in the form of cash & laptop.
- It is a unique case where value of cash & laptop has been adopted as the amount of contravention of Reg. 16.
- Period of contravention in this case is the length of period from the date of receipt of cash & laptop till date of submission of compounding application.

Notification No. FEMA 120 - ODI

❖ Gharda Chemicals Limited [C.A. No. 4226/2016]

Facts

- The applicant had a WOS named Gharda USA Inc. The applicant had remitted around USD 1,43,17,995.33 to WOS.
- As the WOS had substantial losses, the applicant decided to liquidate the WOS & write-off an amount of USD 18,51,411 upon liquidation.
- The applicant, an unlisted company was required to take prior permission from RBI for writing off the amount when investment exceeded USD 10 million. However, the applicant had failed to take approval from RBI before writing off the amount.
- Also, the remaining assets & liabilities were not repatriated, instead it was taken over in the books of the applicant in the form of Intellectual Property Rights.

Relevant Regulation

- Reg. 16(1A)(i)(c) – An IP may disinvest, if the repatriation proceeds on disinvestment is less than the amount of the original investment: where the Indian party is an unlisted company and the investment in the overseas venture does not exceed USD 10 million.
- Reg. 16(2) – Repatriation proceeds on sale of shares/securities immediately /any case not later than 90 days from the date of sale of the shares/securities.

Notification No. FEMA 120 - ODI

❖ **Gharda Chemicals Limited [C.A. No. 4226/2016]**

Key Takeaway

- Transfer of IPR can result in various issues like registration of IPR, valuation of IPR, transfer of ownership from one country to another.
- Reg. 16 provisions were contravened as the disinvestment proceeds are not realised & repatriated to India by way of inward remittance through AD - **Dynemic Products Limited (C.A. No. 4587/2017)**.
- The disinvestment proceeds are received in kind, in the form of IPR.

Notification No. FEMA 120 - ODI

❖ Shantanu Pande [C.A. No. 4766 / 2018]

Facts

- The applicant, a resident individual remitted USD 3,253 on Feb 2013 towards setting up a overseas, OM Exports (FZC). The investment was repatriated on 1st June 2018 & not capitalized.

Relevant Regulation

- Regulation 5(1) of FEMA Notification 120/2004-RB dated 7th July, 2004 – PRI shall make direct investment outside India only with prior RBI approval.
- Notification no. FEMA 263/RB-2013 dated 5th March, 2013 effective from 5th August 2013 permitted the ODI by resident individuals.

Key Takeaway

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

Notification No. FEMA 120 - ODI

❖ Mr. Rajesh Gilbert Salins [C.A. No. 4991/2019]

Facts

- The applicant, an Indian resident invested AED 50,000 & AED 22,000 on 20th November 2017 & 19th Jan 2018 respectively in an overseas JV in UAE.
- The share certificates for AED 1,00,000 on 21st June, 2017 were issued to the applicant by Dubai World Central (DWC) Free Zone.

Relevant Regulation

- Regulation 5 (1) – Receipt of share certificates without making remittance/ deferred payment basis not permitted under the notification

Key Takeaway

- Shares acquisition prior to making remittance for ODI transaction would amount to acquisition of shares on deferred payment basis - not permitted without prior RBI approval.
- FAQ No.63 on ODI states that an IP cannot acquire shares of a foreign entity without upfront payment/ deferred payment basis as it would be contravention of Reg. 5(1).

Notification No. FEMA 120 - ODI

❖ Tavisca Solutions Pvt Ltd [C.A. No. 4727/2018]

Facts

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

Relevant Regulation

- Regulation 6(3) – Permissible sources of funds – Drawal of foreign exchange shall not exceed 400% of the net worth of the IP

Key Takeaway

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

Notification No. FEMA 120 - ODI

❖ Mahajan Overseas Private Limited [C.A. No. 4853/2018]

Facts

- A WOS was incorporated by the applicant in Hong Kong on 19th May 2008. The WOS had incorporated a Step down subsidiary in Canada on 9th October 2008.
- SBLC was extended by the applicant amounting to USD 5,00,000 in favour of SDS on 6th January 2010. It was renewed four times beginning 30th August, 2012.

Relevant Regulation

- Reg. 6(3)(ii)(i) - Issuance of bank guarantee is not permissible w/o prior approval of RBI

Key Takeaway

- FAQ No. 18 on ODI - SBLC is akin to bank guarantee.
- Reg. 6(4)(i), the guarantee can be issued to JV/WOS but not to SDS of JV/WOS under the automatic route.
- As SBLC was renewed four times without prior approval of RBI, it resulted into four contraventions.
- Each renewal of SBLC would amount to another contravention starting from the date of issue of original SBLC.

Notification No. FEMA 120 - ODI

❖ Maheshwari Foods and Hospitality Private Limited [C.A. No. 4970/2019]

Facts

- The applicant made an investment in an overseas JV to acquire a 50% stake.
- The project was abandoned as the overseas JV failed to arrange visas for the Indian staff & although some expenses were already incurred.
- The applicant received the partial refund of USD 50,000 in Jan 2016. Balance USD 50,000 was not received by the applicant and was considered as a part of the loss due to expenses being incurred.
- USD 510 was retained as shares issued and USD 49,490 was retained as share application money.
- A share certificate was produced for USD 510 with a delay on 24th March, 2017. The overseas JV was wound up in April, 2017 involving write-offs.

Notification No. FEMA 120 - ODI

❖ Maheshwari Foods and Hospitality Private Limited [C.A. No. 4970/2019]

Relevant Regulation

- Reg. 15(i) – Submission of share certificate/ any other proof of investment within 6 months of effecting remittance
- Reg. 16(1)(iii) – An IP may disinvest any share / security held by him in a JV/WOS outside India provided the share price is not less than the value certified by a CA/CPA as the fair value of the shares based on the latest audited financial statements of the JV/WOS

Key Takeaway

- Within 6 months the evidence of investment should be submitted to RBI under Reg. 15(i). The remittance for USD 50,000 was received as a refund within 6 months so it was not a contravention under Reg. 15(i).
- Outstanding amount for USD 49,490 – Neither the shares were issued nor the refund was granted.
- Applicant was compounded for the delay beyond 6 months for submission of the said share certificate for USD 510.

Notification No. FEMA 120 - ODI

❖ Ms. Pratibha Agarwal [C.A. No. 4958/2019] & Mr. Virendra Agarwal [C.A. No. 4852/2018]

Facts

- Mrs. Pratibha and her spouse Virendra Agarwal are resident individuals in India. Mr. Virendra was awarded 8000 shares of Vedanta Resources PLC, London in March 2004 to be issued in 2 tranches.
- The consideration equivalent to FV of Rs.17,532 was deducted from Virendra's salary in Feb 2005.
- Option available in the reward plan – Mr. Virendra Agarwal nominated Mrs. Pratibha Agarwal for 3000 shares out of the 4000 shares to be received in the 2nd tranche and were then allotted to Mrs. Pratibha on 8th September, 2006. These shares were considered as a gift in the hands of Mrs. Pratibha from Mr. Virendra.

Relevant Regulation

- Regulation 22(1)(i) – A person resident in India being an individual may acquire foreign securities by way of gift from a person resident outside India
- Regulation 22(4) – A person resident in India may transfer by way of sale, the shares acquired in terms of sub-regulations (2) and (3)

Notification No. FEMA 120 - ODI

❖ **Ms. Pratibha Agarwal [C.A. No. 4958/2019] & Mr. Virendra Agarwal [C.A. No. 4852/2018]**

Key Takeaway

- RBI recognised the nomination of shares by Virendra to his wife as gift transaction.
- Although the contravention relates to the same shares, it cannot be said that same transaction has been compounded twice.
- Mr. Virendra could not transfer shares under Reg. 22(4) and Mrs. Pratibha could not acquire shares by way of gift from a person resident outside India under Reg. 22(1)(i).
- The fair value of the gift can be taken as contravention amount in the case of Mrs. Pratibha. The period of contravention has been considered from the date of allotment i.e. 8th Sept, 2006.

Credits – Naisar Shah

Thank you



Contact Information



P. R. BHUTA & Co.
CHARTERED ACCOUNTANTS

Address	2-I, Jeevan Sahakar, 2nd Floor, Sir P. M. Road, Fort, Mumbai – 400001, India.
Telephone	+91 22 22660010/3427; 43471727
Mobile	+91 9930114418;
E-mail	harshal.bhuta@bhutaco.com
Website	www.bhutaco.com
LinkedIn	https://in.linkedin.com/in/harshalbhuta