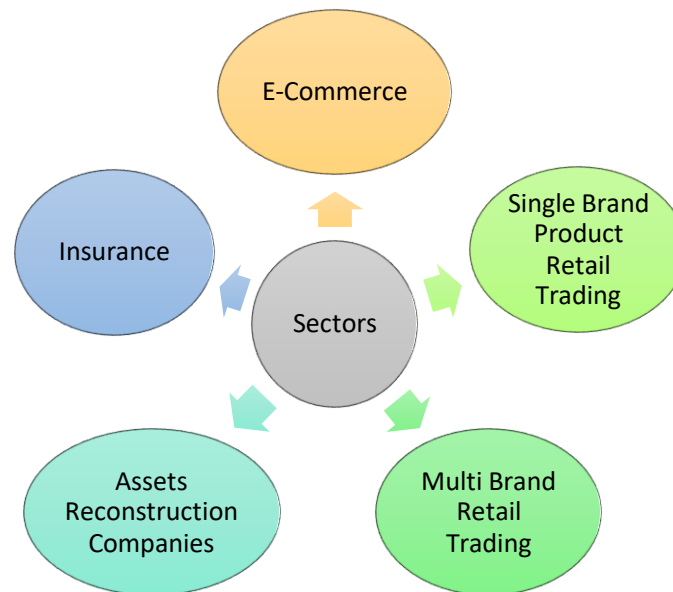


Foreign Direct Investment – Regulation & Policy

Conditions of FDI in Major Sector – Part – 2



FDI in E-Commerce Activities –

A) Meaning of E-commerce –

E-commerce means buying and selling of goods and services including digital products over digital & electronic network.

B) Meaning of E-commerce entity –

E-commerce entity means a company or an office, branch or agency owned or controlled by a person resident outside India and conducting the e-commerce business.

C) Inventory based model –

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.

D) Marketplace based model –

Marketplace based model of e-commerce means providing of an information technology platform by an e-commerce entity on a digital & electronic network to act as a facilitator between buyer and seller.

Conditions for Investment –

- 1) E-commerce entities engage only in Business to Business (B2B) e-commerce will be eligible for FDI.
- 2) E-commerce entities engaged in Business to Consumer (B2C) e-commerce will not be eligible for FDI.
- 3) 100% FDI under automatic route is permitted in marketplace model of e-commerce.
- 4) FDI is not permitted in inventory-based model of e-commerce.

- 5) E-commerce marketplace may provide support services to sellers in respect of warehousing, logistics, order fulfillment, call centre, payment collection and other services.
- 6) E-commerce entity will not have any ownership rights on the inventory.
- 7) E-commerce entity will have to provide full details of the sellers such as name, address and other contact details.
- 8) Post sales, delivery of goods to the customers and customer satisfaction will be responsibility of the seller.
- 9) Any warrantee/ guarantee of goods and services sold will be responsibility of the seller.
- 10) Payments for sale should be in conformity with the guidelines of the RBI.
- 11) An e-commerce entity will not permit more than 25% of the sales value on financial year basis affected through its marketplace from one vendor or their group companies.
- 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.
- 13) E-commerce marketplace entity will not make it mandatory for any seller to sell any product exclusively on its platform only.
- 14) Audit Report of statutory auditor should be submitted confirming that all the guidelines have been followed.

FDI in Single Brand Product Retail Trading –

FDI allowed in Single Brand Product Retail Trading –

100% FDI is allowed under Automatic route



Conditions for Investment –

- 1) Products to be sold should be of a 'Single Brand' only.
- 2) Products should be sold under the same brand internationally (This condition is not applicable on Indian brands)
- 3) 'Single Brand' product-retail trading would cover only products which are branded during manufacturing.
- 4) There should be a legally tenable agreement with the brand owner for undertaking single brand product retail trading (This condition is not applicable on Indian brands).
- 5) A single brand retail trading entity operating through brick and mortar stores, is permitted to undertake retail trading through e-commerce.
- 6) In respect of proposals involving foreign investment beyond 51%, sourcing of 30% of the value of goods purchased, will be done from India
- 7) Application seeking permission of the Government for FDI exceeding 49% in a company should be made to DIPP (SIA)

FDI in Multi Brand Retail Trading –

In Multi Brand Retail Trading, 51% FDI allowed under Government route.

Conditions for Investment –

- ✓ Fresh agricultural produce, including fruits, vegetables, flowers, grains, pulses, fresh poultry, fishery and meat products, may be unbranded.

- ✓ Minimum amount as FDI by the foreign investor would be US \$ 100 million.
- ✓ At least 50% of total FDI brought in the first tranche of US \$ 100 million, shall be invested in 'back-end infrastructure' within 3 years
- ✓ At least 30% of the value of procurement of manufactured/processed products purchased shall be sourced from Indian micro, small and medium industries, which have a total investment in plant & machinery not exceeding US \$ 2.00 million.
- ✓ Retail sales outlets may be set up only in cities with a population of more than 10 lakh as per 2011 Census and may cover an area of 10 kms.
- ✓ Government will have the first right to procurement of agricultural products.
- ✓ Retail trading by e-commerce, would not be permissible, for companies with FDI, engaged in the activity of multi-brand retail trading.
- ✓ State / Union Territory government have freedom to formulate their own policies.

Note –

List of States/Union Territories who have already formulated their policies –

1. Andhra Pradesh
2. Assam
3. Delhi
4. Haryana
5. Himachal Pradesh
6. Jammu & Kashmir
7. Karnataka
8. Maharashtra
9. Manipur
10. Rajasthan
11. Uttarakhand
12. Daman & Diu and Dadra and Nagar Haveli (Union Territories)

FDI in ARC –

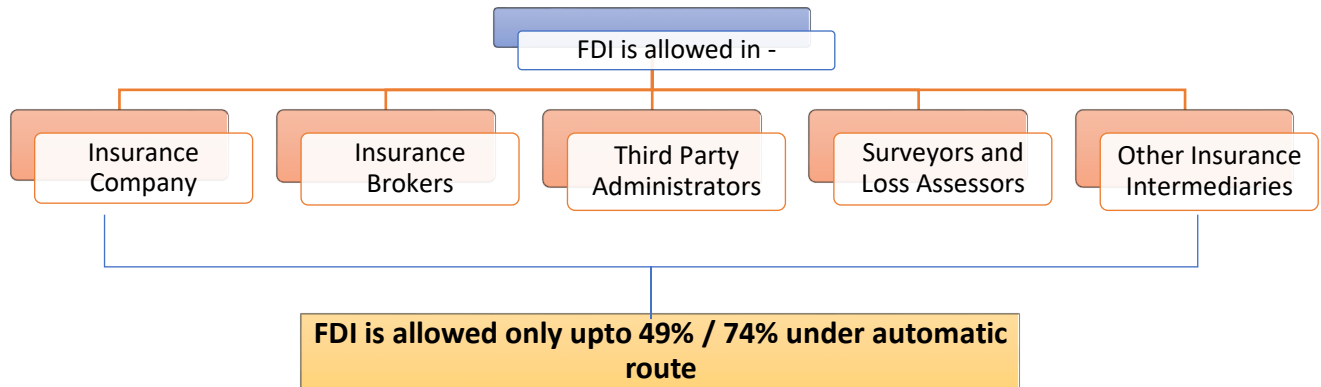
Meaning of ARC –

'Asset Reconstruction Company' (ARC) means a company registered with the Reserve Bank of India under Section 3 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act). **100 % FDI allowed in ARC under automatic route.**

Conditions for Investment –

- Persons resident outside India can invest in the capital of ARCs registered with RBI, up to 100% on the automatic route.
- **Investment from a single FII/FPI** shall be below 10% of the total paid-up capital.
- FIIs/FPIs can invest in the Security Receipts (SRs) issued by ARCs.
- Guidelines of FEMA, FDI as well as SARFAESI Act, should be followed.

FDI in Insurance –



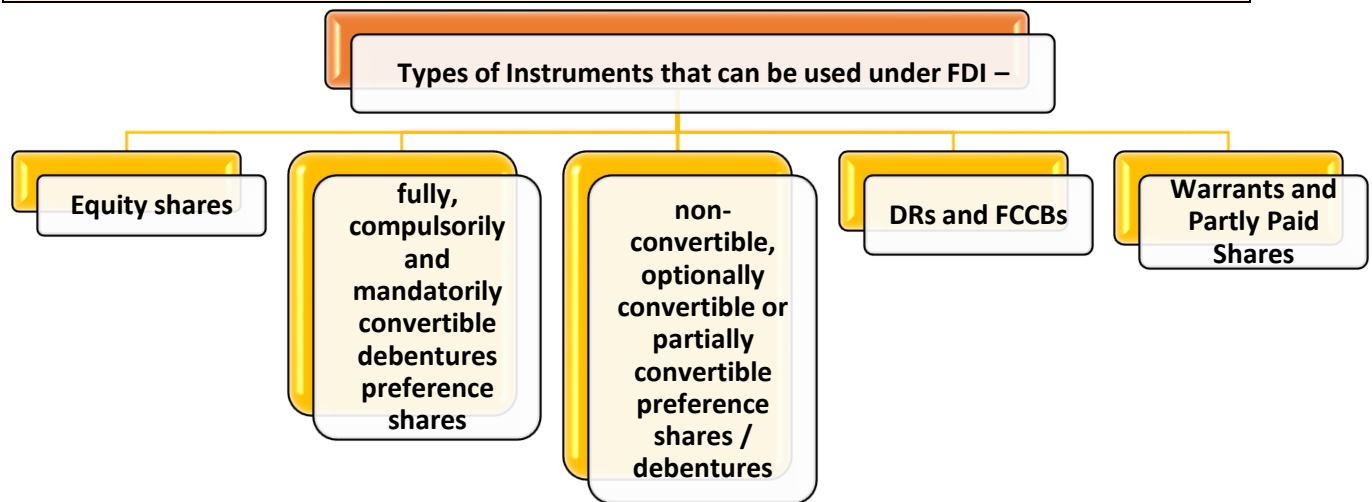
Note –

49% / 74% FDI is allowed under automatic route that means no approval of RBI will be required. However, approval of sectoral regulator i.e. IRDA will be required.

Conditions for Investment –

- Maximum 49% of investment can be received by way of Total Foreign Investment (FDI + FPI).
- Insurance companies receiving FDI should be registered with IRDA.
- Control and ownership at any point of time should be with Resident Indian entity.
- Foreign portfolio investment in an Indian Insurance company shall be governed by FEMA Regulations as well as by SEBI (Foreign Portfolio Investors) Regulations, 2014.
- Any increase in foreign investment in an Indian Insurance company shall be in accordance with the pricing guidelines of RBI.
- Bank who is acting as insurance company will also be allowed only 49% / 74% FDI subject to the condition that the revenues from banking business is more than 50% of their total revenues in any financial year

Types of Instruments that can be used under FDI –



1) Equity shares, fully, compulsorily and mandatorily convertible debentures / preference shares

–

Indian companies can issue Equity shares, fully, compulsorily and mandatorily convertible debentures / preference shares subject to following conditions –

- The price/conversion formula of convertible capital instruments should be determined upfront at the time of issue of the instruments as per FEMA and SEBI (if the company is listed) guidelines.
- Minimum **lock-in period of 1 year** from the date of allotment.
- Shares / Debentures / Preference shares can be sold after the lock-in period subject to FDI guidelines.

2) Non-convertible, optionally convertible or partially convertible preference shares / debentures –

Non-convertible, optionally convertible or partially convertible for issue of which funds have been received on or after May 1, 2007 are considered as debt.

Since it is considered as debt, interest should be paid and interest should be based on LIBOR and ECB guidelines.

3) DRs and FCCBs –

The inward remittance received by the Indian company vide issuance of DRs and FCCBs are treated as FDI and counted towards FDI.

4) Acquisition of Warrants and Partly Paid Shares –

An Indian Company may issue warrants and partly paid shares to a person resident outside India subject to terms and conditions as stipulated by the RBI.

Sponsored ADR/GDR issue –

An Indian Company can also sponsor an issue of ADR/GDR. Under this mechanism, the company offers its resident shareholders a choice to submit their shares back to the company so that on the basis of such shares, ADRs/GDRs can be issued abroad. The proceeds of the ADR/GDR issue are remitted back to India and distributed among the resident investors who had offered their Rupee denominated shares for conversion.

Issue of Shares –

A) Issue of capital instruments –

- 1) The capital instruments should be issued within 60 days from the date of receipt of the inward remittance.
- 2) In case, the capital instruments are not issued within 60 from the date of receipt of the inward remittance then the amount of consideration received shall be refunded within next 15 days.

Please note –

Time allowed by RBI is 180 days and time allowed by MCA is 60 days. In a nutshell, the time limit to issue/allot the shares comes down to 60 days as per the MCA.

B) Price at which share are to be issued –

Price of shares issued to persons resident outside India under the FDI Policy, shall not be less than –

- a) If the company is listed, then as per SEBI guidelines.

- b) If the company is unlisted, then as per the valuation done by –
 - registered Merchant Banker or a Chartered Accountant
 - as per any internationally accepted pricing methodology
 - on arm's length basis.
- c) where the issue of shares is on preferential allotment, the price as applicable to transfer of shares from resident to non-resident as per the pricing guidelines laid down by the RBI.

C) Foreign Currency Account –

Indian companies which are eligible to issue shares to person's resident outside India under the FDI Policy may be allowed to retain the share subscription amount in a Foreign Currency Account, with the prior approval of RBI.

Transfer of shares and convertible debentures –

- 1) Non-resident investors can also invest in Indian companies by purchasing/acquiring existing shares from Indian shareholders or from other non-resident shareholders.
- 2) General permission has been granted to non-residents/NRIs for acquisition of shares by way of transfer subject to the following conditions –

- **Approval / Automatic –**

Government approval is not required for transfer of shares in the investee company from one non-resident to another non-resident in sectors which are under automatic route.

Note –

Approval of Government will be required for transfer of stake from one non-resident to another non-resident in sectors which are under Government approval route.

- **PROI to PROI -**

person resident outside India (other than NRI and erstwhile OCB) may transfer by way of sale or gift, the shares or convertible debentures to any person resident outside India (including NRIs).

- **NRI to NRI –**

NRIs may transfer by way of sale or gift the shares or convertible debentures held by them to another NRI.

- **PROI to PRI –**

A person resident outside India can transfer any security to a person resident in India by way of gift.

- **PROI selling shares through Indian stock exchange –**

A person resident outside India can sell the shares and convertible debentures of an Indian company on a recognized Stock Exchange in India through a stock broker registered with stock exchange or a merchant banker registered with SEBI.

- **PRI to PROI under private placement –**

A person resident in India can transfer by way of sale, shares/ convertible debentures (including transfer of subscriber's shares), of an Indian company under private arrangement to a person resident outside India, subject to the guidelines.

- **PROI to PRI under private placement –**

General permission is also available for transfer of shares/convertible debentures, by way of sale under private arrangement by a person resident outside India to a person resident in India, subject to the guidelines.

- **Form FC-TRS –**

- a) Form FC-TRS should be submitted to the AD Category-I Bank, within 60 days from the date of receipt of the amount of consideration.
- b) The onus of submission of the Form FC-TRS within the given timeframe would be on the transferor/transferee resident in India.

Note –

Where the NR investor, including an NRI, acquires shares on the stock exchanges under the FDI scheme, the investee company would have to file form FC-TRS with the AD Category-I bank.

Issue of Rights/Bonus Shares –

- 1) FEMA provisions allow Indian companies to freely issue Rights/Bonus shares to existing non-resident shareholders, subject to adherence to sectoral cap, if any.
- 2) Necessary SEBI regulations should also be complied.
- 3) The offer on right basis to the person's resident outside India shall be –
 - a) **In case of listed company –**
at a price as determined by the company
 - b) **In case of unlisted company –**
at a price which is not less than the price at which the offer on right basis is made to resident shareholders.

Note –

The investee company can allot the additional rights share out of unsubscribed portion, subject to the condition that the overall issue of shares to non-residents in the total paid-up capital of the company does not exceed the sectoral cap.

Acquisition of Shares Under Scheme of Merger/Demerger/Amalgamation –

Once the scheme of merger or demerger or amalgamation of two or more Indian companies has been approved by a Court in India, the transferee company or new company is allowed to issue shares to the shareholders of the transferor company resident outside India, subject to the conditions that –

- A) the percentage of shareholding of persons resident outside India in the transferee or new company does not exceed the sectoral cap, and
- B) the transferor company or the transferee or the new company is not engaged in activities which are prohibited under the FDI policy.

Issue of Employees Stock Option Scheme (ESOPs) / Sweat Equity –

- 1) An Indian company may issue “employees’ stock option” and/or “sweat equity shares” to its –
 - employees/ directors or
 - employees/directors of its holding company or
 - employees/directors of joint venture or
 - employees/directors of wholly owned overseas subsidiary,
 who are resident outside India
- 2) Following conditions should be fulfilled –
 - Scheme is in compliance with the provisions of SEBI and Companies Act, 2013
 - Issue of ESOPs / Sweat Equity are in compliance with the sectoral cap applicable to the company.

- Issue of “employee’s stock option”/ “sweat equity shares” by a company where foreign investment is under the approval route shall require prior approval of Government of India.
- Issue of “employee’s stock option”/ “sweat equity shares” to an employee/director who is a citizen of Bangladesh/Pakistan shall require prior approval of the Government of India
- The issuing company shall furnish to the RBI within 30 days from the date of issue of employees’ stock option or sweat equity shares, a return as per the Form-ESOP.

Share Swap –

- 1) Valuation of the shares will have to be made by a Merchant Banker registered with SEBI or an Investment Banker outside India registered with the appropriate regulatory authority in the host country
- 2) Approval of the Government will also be a prerequisite for investment by swap of shares for sector under Government approval route
- 3) No approval of the Government is required for investment in automatic route sectors by way of swap of shares.

Pledge of Shares –

- 1) **Pledge by a promoter of a company registered in India –**
 - a) **A person being a promoter of a company registered in India (borrowing company)** which has raised ECB, may pledge the shares of the borrowing company or that of its associate resident companies for the purpose of securing the ECB raised by the borrowing company provided that a no objection for the same is obtained from a bank which is an authorised dealer.
 - b) **AD will issue no objection after making sure that following conditions are satisfied –**
 - ✓ ECB is raised as per FEMA Regulations.
 - ✓ the loan agreement has been signed by both the lender and the borrower,
 - ✓ there exists a security clause in the Loan Agreement requiring the borrower to create charge on financial securities, and
 - ✓ the borrower has obtained Loan Registration Number (LRN) from the Reserve Bank; and the said pledge would be subject to the following conditions –
 - a) the period of such pledge shall be co-terminus with the maturity of the underlying ECB;
 - b) in case of invocation of pledge, transfer shall be in accordance with the FDI Policy and directions issued by the Reserve Bank;
 - c) the Statutory Auditor has certified that the borrowing company will utilized/has utilized the proceeds of the ECB for the permitted end use/s only.
- 2) **Non-residents holding shares of an Indian company pledging shares with AD –**

Non-residents holding shares of an Indian company, can pledge these shares in favour of the AD bank in India to secure credit facilities being extended to the resident investee company for bonafide business purpose, subject to the following conditions –

 - a) in case of invocation of pledge, transfer of shares should be in accordance with the FDI policy existing at the time of creation of pledge;

- b) submission of a declaration/ annual certificate from the statutory auditor of the investee company that the loan proceeds will be / have been utilized for the declared purpose;
 - c) the Indian company has to follow the relevant SEBI disclosure norms; and
 - d) pledge of shares in favour of the lender (bank) would be subject to Section 19 of the Banking Regulation Act, 1949.
- 3) **Non-residents holding shares of an Indian company pledging shares with overseas bank – Non-residents holding shares of an Indian company**, can pledge these shares in favour of an overseas bank to secure the credit facilities being extended to the non-resident investor/non-resident promoter of the Indian company or its overseas group company, subject to the following conditions –
- a) loan is availed of only from an overseas bank;
 - b) loan is utilized for genuine business purposes overseas and not for any investments either directly or indirectly in India;
 - c) overseas investment should not result in any capital inflow into India;
 - d) in case of invocation of pledge, transfer should be in accordance with the FDI policy in existing at the time of creation of pledge; and
 - e) submission of a declaration/annual certificate from a Chartered Accountant/ Certified Public Accountant of the non-resident borrower that the loan proceeds will be / have been utilized for the declared purpose.

Remittance and Repatriation –

A) Remittance of sale proceeds –

- Sale proceeds of shares and securities and their remittance is 'remittance of asset' governed by The Foreign Exchange Management (Remittance of Assets) Regulations under FEMA.
- AD Category-I bank can allow the remittance of sale proceeds of a security to the seller of shares resident outside India, provided –
 - a) the security has been held on repatriation basis,
 - b) the sale of security has been made in accordance with the prescribed guidelines and
 - c) NOC/tax clearance certificate from the Income Tax Department has been produced.

B) Remittance on Winding Up/Liquidation of Companies –

- AD Category-I banks have been allowed to remit winding up proceeds of companies in India, which are under liquidation.
- AD Category-I banks shall allow the remittance provided the applicant submits –
 - a) No objection or Tax clearance certificate from Income Tax Department for the remittance
 - b) Auditor's certificate confirming that all liabilities in India have been either fully paid or adequately provided for.
 - c) Auditor's certificate to the effect that the winding up is in accordance with the provisions of the Companies Act, as applicable.
 - d) In case of winding up otherwise than by a court, an auditor's certificate to the effect that there are no legal proceeding pending in any court in India against the applicant or

the company under liquidation and there is no legal difficulties in permitting the remittance.

C) Repatriation of Dividend –

- Dividends are freely repatriable without any restrictions
- The repatriation is governed by the provisions of the Foreign Exchange Management (Current Account Transactions) Rules, 2000

D) Repatriation of Interest –

- Interest on fully, mandatorily & compulsorily convertible debentures is also freely repatriable without any restrictions
- The repatriation is governed by the provisions of the Foreign Exchange Management (Current Account Transactions) Rules, 2000

Modes of Payment allowed for receiving FDI in an Indian Company –

An Indian company issuing shares/ convertible debentures to a person resident outside India shall receive the amount of consideration by –

1. inward remittance through normal banking channels;
2. debit to NRE/ FCNR account of a person concerned maintained with an AD Category I bank;
3. debit to non-interest bearing escrow account in Indian Rupees in India which is opened with the approval from AD Category – I bank and is maintained with the AD Category I bank on behalf of residents and non-residents towards payment of share purchase consideration;
4. conversion of royalty/ lump sum/ technical know-how fee due for payment or conversion of ECB;
5. conversion of pre-incorporation/ pre-operative expenses incurred by the a non-resident entity up to a limit of five percent of its capital or USD 500,000 whichever is less;
6. conversion of import payables/ pre incorporation expenses/ can be treated as consideration for issue of shares with the approval of FIPB;
7. against any other funds payable to a person resident outside India, the remittance of which does not require the prior approval of the Reserve Bank or the Government of India: and
8. Swap of capital instruments, provided where the Indian investee company is engaged in a Government route sector, prior Government approval shall be required.

If the shares or convertible debentures are not issued within 180 days from the date of receipt of the inward remittance or date of debit to NRE/ FCNR (B)/ escrow account, the amount shall be refunded

Reporting of FDI –

A) Reporting of Inflow –

- 1) An Indian company receiving investment from outside India for issuing shares/convertible debentures/preference shares under the FDI Scheme, should report the details of the amount of consideration to the Regional Office concerned of the Reserve Bank within 30 days from the date of receipt in the Advance Reporting Form
- 2) Indian companies are required to report the details of the receipt of the amount of consideration through an AD Category-I bank.

- 3) The report would be acknowledged by the Regional Office concerned, which will allot a Unique Identification Number (UIN) for the amount reported.
- 4) An Indian company issuing partly paid equity shares, shall furnish a report not later than 30 days from the date of receipt of each call payment.

B) Reporting of issue of shares –

- 1) Indian company has to file **Form FC-GPR**, within 30 days from the date of issue of shares.
- 2) Form FC-GPR should be signed by Managing Director/Director/Secretary of the Company and submitted to the Authorized Dealer of the company who will forward it to the RBI.
- 3) following documents have to be submitted along with Form FC-GPR –
 - a) **A certificate from the Company Secretary of the company certifying that –**
 - all the requirements of the Companies Act have been complied with;
 - terms and conditions of the Government of India approval have been complied with;
 - the company is eligible to issue shares; and
 - the company has all original certificates issued by authorized dealers in India evidencing receipt of amount of consideration.

Note –

Companies which are not required to appoint CS may get the above certificate from a PCS.

- b) A certificate from SEBI registered Merchant Banker or Chartered Accountant indicating the manner of arriving at the price of the shares issued to the persons resident outside India.
- c) The report of receipt of consideration as well as Form FC-GPR have to be submitted by the AD Category-I bank to the Regional Office concerned of the Reserve Bank under whose jurisdiction the registered office of the company is situated.
- d) Annual return on Foreign Liabilities and Assets should be filed on an annual basis by the Indian company, directly with the Reserve Bank.
- e) Issue of bonus/rights shares or stock options to persons resident outside India directly or on amalgamation/merger/demerger with an existing Indian company, as well as issue of shares on conversion of ECB/royalty/lumpsum technical know-how fee/import of capital goods by units in SEZs, has to be reported in Form FC-GPR.

C) Reporting of transfer of shares –

- ✓ Reporting of transfer of shares between residents and non-residents and vice- versa is to be done in Form FC-TRS
- ✓ The Form FC-TRS should be submitted to the AD Category-I bank, within 60 days from the date of receipt of the amount of consideration
- ✓ The onus of submission of the Form FC-TRS within the given timeframe would be on the transferor/transferee, resident in India.

D) Reporting of Non-Cash –

Details of issue of shares against conversion of ECB have to be reported to the Regional Office concerned of the RBI as follows –

- 1) In case of full conversion of ECB into equity, the company shall report the conversion in Form FC-GPR to the Regional Office concerned of the Reserve Bank as well as in Form ECB-2 to the Department of Statistics and Information Management (DSIM), Reserve Bank of India, Bandra-Kurla Complex, Mumbai- 400 051, within 7 working days from the close of month to which it relates.
- 2) In case of partial conversion of ECB, the company shall report the converted portion in Form FC-GPR to the Regional Office concerned as well as in Form ECB-2 clearly differentiating the converted portion from the non-converted portion.

Adjudication and Appeals –

- For the purpose of adjudication of any contravention of FEMA, MoF appoints officers of the Central Government as the Adjudicating Authorities.
- Before imposing penalty and opportunity of being heard should be given.
- CG may also appoint an Appellate Authority/ Appellate Tribunal to hear appeals against the orders of the adjudicating authority.

Compounding Proceedings –

- ✓ Central Government may appoint 'Compounding Authority' who will be an officer either from Enforcement Directorate or Reserve Bank of India.
- ✓ The Compounding Authorities are authorized to compound the amount involved in the contravention to the Act made by the person
- ✓ Any second or subsequent contravention committed after the expiry of a period of 3 years from the date on which the contravention was previously compounded shall be deemed to be a first contravention.
- ✓ The Compounding Authority shall pass an order of compounding within 180 days from the date of application made to the Compounding Authority