Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 - FDI Part 4B

Transfer of Equity Instrument by Pledge –

Transfer of Equity Instrument by Pledge

By promoter of Indian Company

⇩

Promoter holding shares of Indian company may pledge his shares for raising External Commercial Borrowings (ECB)

⇩

Conditions –

- Loan shall be utilized for permitted end use activities of the company
- Tenure of the pledge should be equal to the tenure of ECB
- statutory auditor should certify that loan has been utilized for the permitted end-use only
- NOC should be obtained from authorized dealer bank
- in case of invocation of pledge, transfer shall be made as per the directions issued by the Reserve Bank

By PROI holding shares in Indian Company

⇩

PROI may pledge his shares for raising loan which should be utlised for company only

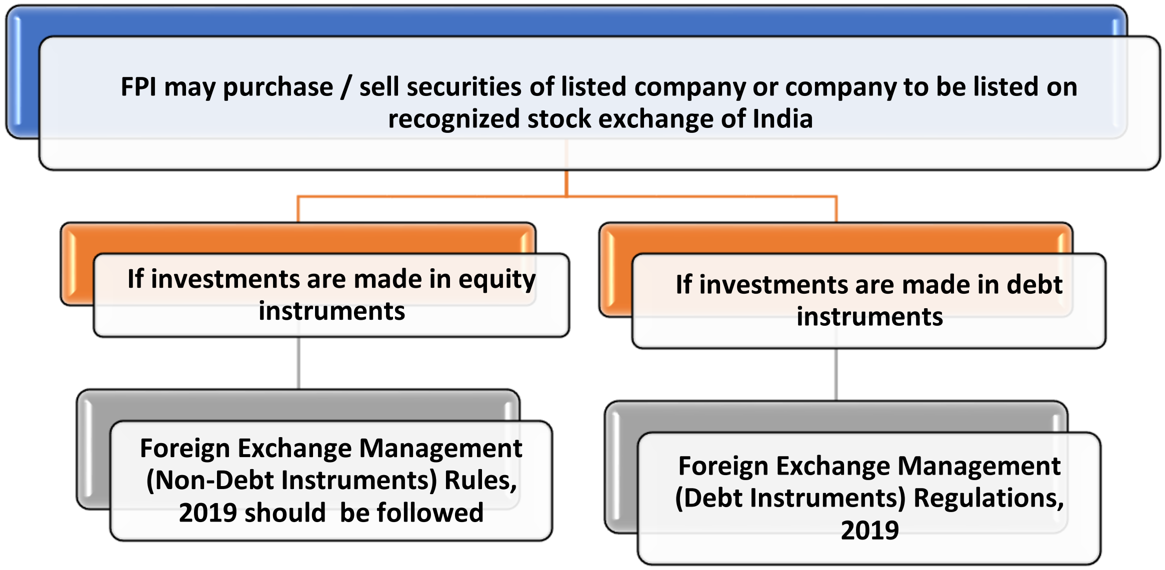
⇩

Shares may be pledged with –

- Indian Bank;
- Overseas Bank;
- NBFC

in case of invocation of pledge, transfer shall be made as per the directions issued by the Reserve Bank

Investment by Foreign Portfolio Investor (FPI) – Rule 10



Limits of Investment by FPI –

Investment	Limits
Individual Limit (single FPI)	Less than 10% of total paid-up equity capital on a fully diluted basis; or Less than 10% of the paid-up value of each series of debentures or preference shares or share warrants
Aggregate Limit (All FPI)	Maximum 24% of total paid-up equity capital on a fully diluted basis; or Maximum 24% of the paid-up value of each series of debentures or preference shares or share warrants

Can the above limit be increased?

- Yes, above limits can be increased subject to overall limits of sectoral cap

What are the conditions to increase the limits?

- Pass board resolution
- Pass Special resolution

Can the above limit be decreased?

- Yes, above limits can be decreased.

What are the conditions to decrease the limits?

- Pass board resolution
- Pass Special resolution

Note –
Once the limits are increased, it cannot be decreased.

Breach of investment limits by FPI –

In case FPI breaches the above limits the FPI has 2 options -

Option 1 - To divest excess holding within 5 days

Option 2 - If does not divest the excess holding then subject to sectoral limits -

Entire shareholding shall be treated as FDI and FPI shall not make any further investments

Notice of Breach –

FPI shall disclose the breach of limits through its custodian to the Depository Bank within 7 days of settlement of trade due to which breach was caused.

Effect of Breach –

Period between breach and sale / conversion into FDI shall not be treated as contravention of these rules.

Other Important Points –

1) FPIs are allowed for short selling, lending and borrowing of securities subject to RBI and SEBI Regulations.
2) Purchase or sale of securities other than equity instruments by FPIs –
   FPIs are allowed to purchase following instruments other than equity instruments –
   a) Units of domestic mutual fund;
   b) Category III Alternative Investment Fund;
   c) Off shore funds which in turn invest more than 50% in equity instruments on repatriation basis
   d) Units of REITs and InVITs
   e) IDRs

Transfer by way of sale or gift of securities –

- A FPI may transfer by way of sale or gift the equity instruments of an Indian company or units held by him to any PROI;
- Such transfer shall also include transfer resulting from merger, demerger, amalgamation of company.
- If company is under approval route, prior government approval should be obtained

Investment by Non-Resident Indian or an Overseas Citizen of India – Rule 12

NRIs or OCI can invest on REPATRIATION BASIS

In equity instruments

Conditions –
- NRIs or OCI may purchase / sell equity instruments of Listed company.
- Limits –
  Individually = 5% (Total paid-up equity capital on full diluted basis)
  Aggregate = 10% (Total paid-up equity capital on full diluted basis)
- Limits can be increased to 24% after passing BR and SR.

Shares of Public Sector Undertakings

Conditions –
NRIs or OCI may purchase / sell shares without any limits in disinvestment programme by government

Units of domestic mutual funds

NRIs or OCI may purchase / sell units without any limits. The only condition is that mutual fund should invest more than 50% in equity instruments

Subscription to national pension system

NRIs or OCI may subscribe to NPS if the NPS is governed by PFRDA

Note –
- Investment can be done on REPATRIATION BASIS if done as explained above.
- All investments should be done with the mode of payment prescribed by RBI

NRIs or OCI can invest on NON - REPATRIATION BASIS

- In equity instruments of Indian Company
- Units of Mutual Funds
- Capital contribution to LLP
- Capital contribution to firm / proprietory firm

1) Investments in Indian company, mutual funds or LLP –

NRIs or OCIs or a trust or firm incorporated by NRIs / OCIs are allowed to invest in –

a) Equity instrument of listed / unlisted company without any limits;

b) Units of mutual funds or investment vehicle without any limits;
c) Convertible notes of start-up company without any limits;
d) Capital contribution in LLP without any limits.

All investments made as above shall be treated at par with the resident investors.

2) Investments by NRIs / OCIs is not allowed in -
a) Nidhi company;
b) company engaged in agricultural or plantation activities;
c) company engaged in real estate business or construction of farm houses
d) dealing in transfer of development rights (TDRs).

3) Investment in a firm or a proprietary concern –
A NRI or an OCI may invest in capital of a firm or a proprietary concern without any limits. Provided, such firm or a proprietary concern should not be engaged in agricultural or plantation activity or print media or real estate business.

Note –
NRIs / OCIs may also invest in derivative contracts and IDRs.
Mode of payment should be such as prescribed by RBI.

Issue of Convertible Notes by an Indian Start-Up Company –

PROI may purchase convertible notes issued by an Indian start-up company.

⇩

Citizen of Pakistan or Bangladesh or an entity which is registered or incorporated in Pakistan or Bangladesh cannot purchase convertible notes issued by an Indian start-up company

⇩

Conditions –
- Minimum amount shall be 25 lakh rupees in a single tranche
- If start-up company is engaged in activity covered under approval route then prior approval shall be required.
- Mode of payment should be such as prescribed by RBI.
- All the other guidelines of RBI shall be followed.

Merger or Demerger or Amalgamation of Indian Companies –

In case of equity instruments issued by new company or transferor company because of amalgamation, merger, demerger or reconstruction then it can be issued to PROI

⇩

Conditions –
- Scheme of amalgamation, merger, demerger or reconstruction shall be approved by NCLT / competent authority.
- In case of listed companies, SEBI Regulations shall be followed;

- Other guidelines of RBI should also be followed

Pricing Guidelines –

If the company is governed under SEBI Regulations then in such case, pricing shall be done as per SEBI Regulations.

Minimum pricing for <u>issue of instruments</u> –

For listed companies

Minimum price of the instruments shall be as per SEBI Regulations

In case of Delisting also, SEBI Regulations shall apply

For Unlisted companies

the valuation of equity instruments should be done as per internationally accepted pricing methodology for valuation on an arm's length basis

Valuation should be certified by –
Merchant Banker; or
PCA; or
PCMA

<u>Non-Applicability of pricing guidelines –</u>

If PROI has invested in the instruments on non-repatriation basis then pricing guidelines shall not apply.

Minimum pricing for <u>transfer of instruments</u> –

Transfer (by sale / gift) can be between

PROI to PRI

PRI to PROI

Maximum Price shall be –

1) In case of listed companies –
   Pricing shall be as per SEBI Regulations

2) In case of unlisted Companies –
   The valuation of equity instruments should be done as per internationally accepted pricing methodology for valuation on an arm's length basis
3) Valuation should be certified by –
   a) Merchant Banker; or
   b) PCA; or
   c) PCMA

Minimum Price shall be –

1) In case of listed companies –
   Pricing shall be as per SEBI Regulations

2) In case of unlisted Companies –
   The valuation of equity instruments should be done as per internationally accepted pricing methodology for valuation on an arm's length basis
3) Valuation should be certified by –
   a) Merchant Banker; or
   b) PCA; or
   c) PCMA

Non-Applicability of pricing guidelines –

If PROI has invested in the instruments on non-repatriation basis then pricing guidelines shall not apply.

Taxes and Remittances of Sale Proceeds –

Sales proceeds can be remitted if the following conditions are satisfied –

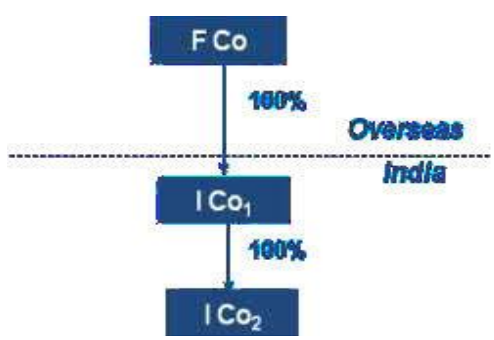
1) All transactions should be done through normal banking channels;
2) All the applicable taxes should have been paid;
3) The security should have been held on repatriation basis
4) RBI rules and regulations have been satisfied.

Note –

If securities are held on non-repatriation basis then prior RBI approval shall be obtained.

Downstream Investment –

A) What is Downstream Investment?



Downstream investment **is** investment **made by an Indian entity which has total foreign** investment **in it or an** Investment **Vehicle in the capital instruments or the capital of another Indian entity.**

B) What is Indirect Foreign Investment?

1) Downstream investment by an Indian Entity and such investing Indian Entity is –
   a) Not owned or controlled by PRI;
   b) Owned and controlled by PROI

2) If such investing Indian Entity whose sponsor or manager or Investment manager is –
   a) Not owned or controlled by PRI;
   b) Owned and controlled by PROI

Ownership of an Indian Entity –

On the basis of Shareholding –

a) In case of company = more than 50% of equity instruments should be held by PROIs.
b) In case of LLP = more than 50% of capital and majority of profit share should be held by PROIs.

OR

On the basis of Control –

a) Right to appoint majority of BOD or DP (for LLP);
b) Right to control management or policy discussion.

C) What is Total Foreign Investment –

Total foreign investment means total of foreign investment and shall include indirect foreign investment on fully diluted basis

Calculation of Total Foreign Investments held by PROI–

Guidelines for calculating total foreign investment in Indian companies are as follows –

1) Convertible debt instruments shall be treated as total foreign investment;
2) FCCBs and DRs shall not be treated as total foreign investment;
3) Investment under portfolio route shall also be covered;
4) Indirect foreign investment in wholly owned subsidiary of Indian company shall be taken upto the amount received by company making investments

D) Conditions for downstream investments –

1) Approval of BOD and shareholders should be obtained.
2) Funds should be brought from outside India and should not be borrowed from domestic markets.
3) Funds can be arranged through internal accruals lying in reserve account after taxes.
4) All the compliances shall be the responsibility of the first level Indian company making downstream investments.
5) first level Indian company shall obtain certificate regarding compliances from statutory auditor on annual basis.

Acquisition and Transfer of Immovable Property in India –

Acquisition and transfer of property in India by a NRI or an OCI – Rule 24

1) **NRI or an OCI can acquire property in India.**
2) NRI or and OCI cannot acquire agricultural land or farm house or plantation property:
3) Consideration shall be paid out of –

a) funds received in India through banking channels from any place outside India ; or
b) funds held in any non-resident account maintained

4) **Following modes for paying consideration is not allowed –**
Payment through traveller's cheque or by foreign currency notes will not be allowed for paying consideration

5) **Gift –**
NRIs / OCIs can acquire immovable property in India by way of gift from PRI or other NRI / OCI provided they should be relative as per Companies Act, 2013.

6) **Inheritance –**
NRIs / OCIs can acquire immovable property in India by way of inheritance from PROI who had acquire such property –
a) As per foreign exchange law; or
b) From PRI

7) **Transfer –**
NRIs / OCIs can transfer property in India –
a) to a person resident in India; or
b) to NRIs / OCIs.

Joint acquisition by the spouse of a NRI or an OCI – Rule 25

1) A PROI who is spouse of NRI / OCI may acquire immovable property jointly with NRI/OCI in India if –
- they are married for atleast 2 years;
- marriage is registered;
- spouse is not prohibited from acquisition.

2) Consideration shall be paid out of –
a) funds received in India through banking channels from any place outside India ; or
b) funds held in any non-resident account maintained

3) Following modes for paying consideration is not allowed –
Payment through traveller's cheque or by foreign currency notes will not be allowed for paying consideration.

Acquisition of immovable property for carrying on a permitted activity – Rule 26

PROI who has established branch office in India or any other place of business in India excluding liaison office may –

1) Acquire immovable property necessary for or incidental to carrying on such activity.
Form IPI should be filed within 90 days of acquisition with RBI
2) Mortgage to authorised dealer as security for payment.

Restrictions –

Citizens of following countries cannot acquire or transfer immovable property in India and if they want to acquire or transfer immovable property then prior RBI approval is required –
- Pakistan,
- Bangladesh,

- Sri Lanka,
- Afghanistan,
- China,
- Iran,
- Nepal,
- Bhutan,
- Hong Kong
- Macau
- Democratic People's Republic of Korea (DPRK)

When Prior approval is not required?
Prior approval of RBI is not required when the citizens of these countries are acquiring property for lease for maximum 5 years.

Citizens include natural person + Legal Entities

Purchase or sale of immovable property by Foreign Embassies or Diplomats or Consulate Generals – Rule 27

Not allowed
⇩
To purchase agricultural land, plantation property, farmhouse

Allowed –
⇩
a) Only after clearance from MEA, CG.
b) Consideration only through banking channels

Acquisition by a long-term visa holder – Rule 28

⇩

Citizens of Afghanistan, Bangladesh or Pakistan belonging to minority communities in those countries such as Hindus, Sikhs, Buddhists, Jains, Parsis and Christians; and

⇩

who is residing in India and has been granted a Long Term Visa (LTV) by the Central Government

⇩

may purchase only one residential immovable property in India as dwelling unit for self-occupation and only one immovable property for carrying out self-employment

⇩

<u>Conditions –</u>

- Property should not be situated in restricted area;
- Declaration should be submitted specifying the source of funds and that he or she is residing in India on LTV to the Revenue Authority of the district where the property is located,
- the registration documents of the property shall mention the nationality and the fact that such person is on LTV
- the property of such person may be attached or confiscated in the event of his or her indulgence in anti-India activities;
- Copy of documents should be submitted to –
    a) DCP; or

b) Foreigners Registration Office (FRO); or c) Foreigners Regional Registration Office (FRRO) • If such person becomes citizen of India then he can buy / sell property in any manner

Repatriation of sale proceeds – Rule 29

Seller of Immovable property	Conditions
PROI	Can transfer sale proceeds of property with general or specific permission of RBI
NRIs / OCIs	• Allowed to transfer through authorized dealer • Property was acquired as per the rules • the amount for acquisition of the immovable property was paid in foreign exchange received through banking channels. • In case of residential property = maximum 2 property's consideration is allowed
Sale in case of property secured for ECB	• authorised dealer may permit the overseas lender to sell the immovable property only to a PRI and to repatriate the sale proceeds

Prohibition on transfer of immovable property in India – Rule 30

No PROI can transfer immovable property in India unless –

a) RBI permits transfer;
b) For creating charge, it should be created through authorized dealer;
c) Funds of ECB should only be used for core business outside India;
d) in case of invocation of charge, the Indian bank shall sell the immovable property to an eligible acquirer and remit the sale proceeds to the overseas lender

Prohibition on acquisition or transfer of immovable property in India by citizens of certain countries – Rule 31

Citizens of following countries cannot acquire or transfer immovable property in India and if they want to acquire or transfer immovable property then prior RBI approval is required –

- Pakistan,
- Bangladesh,
- Sri Lanka,
- Afghanistan,
- China,
- Iran,
- Nepal,
- Bhutan,
- Hong Kong
- Macau
- Democratic People's Republic of Korea (DPRK)

When Prior approval is not required?
Prior approval of RBI is not required when the citizens of these countries are acquiring property for lease for maximum 5 years.

Citizens include natural person + Legal Entities