

Between the lines...

December, 2015

Highlights

- i. Reforms in FDI Policy
- ii. Amendment to FEMA regulations to include investment vehicles
- iii. Introduction of e-Biz platform

I. Reforms in FDI Policy

The Department of Industrial Policy and Promotion (DIPP) released Press Note No. 12 of 2015 (Press Note) on 24 November 2015 introducing major reforms to the Consolidated Foreign Direct Investment Policy of India. The reforms majorly focus on enhancing FDI limits in certain sectors, boosting of investment by setting forth automatic route instead of obtaining Government approval,

reducing unnecessary hassles including Government intervention, and opening up of new sectors, etc.

The major changes including sector specific reforms brought through Press Note 12 are summarized hereunder-

FDI in LLP- FDI in LLP has been allowed and downstream investment by LLP into another Indian LLP is permitted provided that LLP is operating in those sectors/activities where 100% FDI is allowed through the automatic route and there are no FDI- linked performance conditions. *[Previously, FDI in LLPs was allowed only with prior government approval, with a blanket restriction on downstream investments.]*

Swap of shares- Approval of the Government will continue to be a prerequisite for investment by swap of shares for sectors under Government approval. No approval of the Government is required for investment in automatic route sectors by way of swap of shares. *[However prior to this press note, approval of the Government was mandatory for investment by way of Swap of Shares even in the automatic route sectors.]*

Infusion of Foreign Investment in an Indian Company which does not have any operation and also does not have any downstream investment-For undertaking activities which are under automatic route and without FDI linked performance conditions, Indian company which does not have any operations and also does not have any downstream investments, will be permitted to have infusion of foreign investment under automatic route. However approval of the Government will be required for such companies for infusion of foreign investment for undertaking activities which are under Government route, regardless of the amount or extent of foreign investment. *[Prior to this Press note, Government/FIPB approval was mandatory for such companies. No clarity has been provided regarding undertaking of activities which are under automatic route and require FDI linked performance conditions.]*

Incorporated entities owned and controlled by non-residents-A company, trust and partnership firm incorporated outside India and owned and controlled by non-resident Indians can invest in India with the special dispensation as available to Non-Resident Indians under the FDI policy. Investments (other than under the Portfolio Investment Scheme) by companies, trusts and partnership firms owned and controlled by NRIs, will be treated as domestic investments.

Levels of Approvals for cases under the Government Route- FIPB would consider FDI proposals with total foreign equity inflow of and below ₹ 50 billion. The recommendations of FIPB on proposals with total foreign equity inflow of more than ₹ 50 billion would be placed for consideration of Cabinet Committee on Economic Affairs (CCEA). *[These limits have been increased from ₹ 30 billion to ₹ 50 billion for FIPB and above ₹ 50 billion for CCEA.]*

‘Manufacturing’ and Foreign Investment in Manufacturing sector- Hitherto, the term Manufacturing had not been defined in the FDI policy. DIPP has resolved this issue by defining the term ‘manufacture’ in the current FDI policy as follows: *“Manufacture”, with its grammatical variations, means a change in a non living physical object or article or thing- (a) resulting in transformation of the object or article or thing into a new and distinct object or article or thing having a different name, character and use; or (b) bringing into existence of a new and distinct object or article or thing with a different chemical composition or integral structure.*

Furthermore, it has been clarified that foreign investment in manufacturing sector is under automatic route, subject to provisions in the FDI policy. A manufacturer is also permitted to sell its products in India through wholesale and/or retail or through e-commerce without requirement of Government approval.

Liberalization of FDI in certain sectors- Press note 12 has liberalized the investment cap/route/conditions for FDI in the following sectors/activity-

- (A) 100% FDI has been allowed under the automatic route in Tea sector including tea plantations, Coffee plantations, Rubber plantations, Cardamom plantations, Palm oil tree plantations, Olive oil tree plantation.
- (B) 49% FDI has been allowed under the automatic route in the Defence Industry. Proposals above 49% would be considered under the government route on case to case basis, wherever it is likely to result in access to modern and ‘state-of-art’ technology in the country. The earlier conditions have been relaxed and license applications would be considered by DIPP, Ministry of Commerce and Industry, in consultation with Ministry of Defense and Ministry of External Affairs. Further, foreign investment in the sector is subject to security clearance and guidelines of the Ministry of Defense.
- (C) FDI limit in broadcasting carriage services has been increased to 100% (automatic approval up to 49% and subject to government approval thereafter). In the broadcasting content sector, FDI limit in terrestrial broadcasting (FM radio) and up-linking of 'news and current affairs' TV channels has been increased to 49%

subject to government approval. Up-linking 'non news and current affairs' TV channels is now under the automatic approval route with 100% FDI permitted.

- (D) In respect of Air transport Services under Civil Aviation, 49% (100% for NRIs) FDI has now been provided for under the automatic route. Further, FDI cap for non-scheduled Air Transport Service has now been increased to 100% under the automatic route from 74%. In the Ground Handling Services, FDI limit has been increased to 100% under the automatic route from 74%.
- (E) FDI cap in respect of 'Satellites-establishment and operation' has been increased from 74% to 100% under the Government Route.
- (F) FDI cap in respect of Credit Information Companies has now been made 100% under the automatic route from 74% previously.
- (G) In respect of Construction-development projects, requirement of minimum floor area to be developed (20,000 sq. meters) has now been done away with. Further, the requirement of minimum investment to be made by the investee company (US\$ 5 Million within six months of the commencement of the project) has also been done away with.

Now, subject to a lock-in period of 3 years with respect to each tranche of foreign investment, any investor could exit and repatriate foreign investment before completion of the project under foreign investment. It has now also been provided that the transfer of stake from one non-resident to another non-resident will not be subject to any lock-in or Government approval. *[Previously, the investor was permitted to exit only on completion of the project or on development of trunk infrastructure i.e. roads, water supply, street lighting etc.]*

- (H) In respect of wholesale/cash and carry trading, a wholesale/cash and carry trader can now undertake single brand retail trading also subject to satisfaction of conditions laid down for FDI in single brand retail trading. Further, any entity undertaking both the activities is required to maintain separate books of accounts for these two arms of the business which must also be duly audited by the statutory auditors.
- (I) In respect of single brand retail trading, a single brand retail trading entity operating through brick and mortar stores is now permitted to undertake retail trading through e-commerce. Further, it is provided that in case of "state-of-art" and "cutting-edge technology" segment, the extant condition of mandatory local sourcing (of 30 percent of value of goods purchased) can be dispensed by the Government.
- (J) FDI in Duty Free Shops has now been permitted to the extent of 100% under the automatic route and is subject to compliance of conditions stipulated under the Customs Act, 1962 and other laws, rules and regulations.

Further, Duty Free Shop entity is mandated to not engage into retail trading activity in the Domestic Tariff Area of the country.

- (K) In respect of investment in Banking- Private Sector, with regard to the permissible limits under portfolio investment schemes through stock exchanges for FIIs/FPIs, individual FII/FPI holding is restricted to below 10% of the total paid up capital, aggregate limit for all FIIs/FPIs/QFIs cannot exceed 24% of the total paid up capital, which can be raised up to sectoral limit of 74% of the paid-up capital by the bank concerned through a resolution by its Board of Directors followed by a special resolution to that effect by its General Body.

Source: http://dipp.nic.in/English/acts_rules/Press_Notes/pn12_2015.pdf

VA View

The sectors that benefited from the relaxation include defence, real estate, defence, civil aviation, single brand retail and news broadcasting. The policy had also clearly spelled out the rules for e-commerce, laying down expressly that companies that manufactured goods in India were free to sell them online. It has defined manufacturing but it is unclear whether contract manufacturing will constitute manufacturing. The new rules provide for easier exit from investment in the construction sector. Palm, coffee and rubber plantations have been opened up for the first time.

The crux of these reforms is to further ease, rationalize and simplify the process of foreign investments in the country and to put more and more FDI proposals on automatic route instead of Government route. These reforms and further liberalization would go a long way in ensuring that India becomes a favourable destination for foreign investments.

II. Amendment to FEMA regulations to include investment vehicles

The Reserve Bank of India, vide its notification dated 16th November, 2015 (Notification No. FEMA 355/2015-RB) has amended the Foreign Exchange (Transfer and Issue of Securities by Person Resident Outside India) Regulations, 2000 ("Regulations") and has allowed foreign investment to be carried out in Investment Vehicles including Alternative Investment Funds(AIF), Real Estate Investment Trusts(REITs), Infrastructure Investment Trust(InvIts) by persons resident outside India including NRIs, RFPIs registered and regulated under the respective SEBI Regulations. Pursuant to the amendment, a new Schedule (Schedule 11) has been added to the Regulations which provides for the conditions on which investment can be done by a person resident outside India in an Investment Vehicle.

Accordingly, the Schedule inter alia provides that downstream investments by an investment vehicle will be regarded as a foreign investment, where neither the sponsor, the manager nor the investment manager is an Indian "owned and controlled" as defined in the Regulations. Further, such investments will have to conform to applicable sectoral

caps/ conditions/ restrictions, if any. In case of sponsor, manager or investment manager which are organized in a form other than companies, SEBI shall have the power to determine whether ownership and control is with a foreign entity. Further, according to the Explanation to the Schedule, ownership and control is to be determined as per the extant FDI policy. The Explanation further provides that AIF is a pooled investment vehicle. 'Control' of the AIF should be in the hands of 'sponsors' and 'managers/investment managers', with the general exclusion of others. *In case the 'sponsors' and 'managers/investment managers' of the AIF are individuals, for the classification of downstream investment by such AIF as domestic investment, 'sponsors' and 'managers/investment managers' should be resident Indian citizens.* As ownership and control cannot be determined in LLP under the extant FDI policy, a LLP shall not act as sponsor or manager/investment manager.

Another Explanation to the Schedule makes it clear that the extent of foreign investment in the corpus of the Investment Vehicle will not be a factor to determine as to whether downstream investment of the Investment Vehicle concerned is foreign investment or not.

Source: RBI Notification No. FEMA. 355/2015-RB

VA View

This amendment would encourage long-term capital and fund management in India. The new rules say that a fund will be considered as 'domestic' in nature as long as its sponsors or managers are Indian. This could lead to bypassing of several FDI related caps, conditionalities and prohibitions under the FDI Policy.

Also, subsequent to the release of this amendment, the DIPP vide press note 12 dated 24th November 2015, defined ownership and control in case of LLPs, and thus suitable amendment may be required to the effect that LLPs can now act as sponsor or manager/investment manager.

III. Introduction of e-Biz platform

With a view to promoting the ease of reporting of transactions under foreign direct investment, the Reserve Bank of India (RBI), under the aegis of the e-Biz project of the Government of India, has enabled online filing of the Advance Remittance Form, which is used by the companies to report the foreign direct investment (FDI) inflow to RBI, FCGPR Form, which a company submits to RBI for reporting the issue of eligible instruments to the overseas investor and Form FC-TRS for reporting transfer of shares, convertible debentures, partly paid shares and warrants from a person resident in India to a person resident outside India or vice versa.

The design of the reporting platform enables the customer to login into the eBiz portal, download the reporting form, complete and then upload the same onto the portal using their digitally signed certificates. The Authorised Dealer

Banks (ADs) will be required to download the completed forms, verify the contents from the available documents and if necessary, call for additional information from the customer and then upload the same for RBI to process and allot the Unique Identification Number (UIN).

The Reserve Bank of India further intends to stop the reporting for FCGPR-A and FC-TRS in the physical form and enable online reporting for all the transactions processed tentatively by the end of 2015. Existing reporting's in physical form would continue till further instructions are received from Reserve Bank of India. The ADs will be required to access the e-Biz portal [which is hosted on the National Informatics Centre (NIC) servers] using a Virtual Private Network (VPN) Account obtained from NIC.

Source: <https://rbi.org.in/Scripts/NotificationUser.aspx?Id=9993&Mode=0>



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Contact Details :

www.vaishlaw.com

NEW DELHI

1st, 9th & 11th Floor
Mohan Dev Bldg. 13 Tolstoy Marg
New Delhi - 110001, India
Phone: +91-11-4249 2525
Fax: +91-11-23320484
delhi@vaishlaw.com

MUMBAI

106, Peninsula Centre
Dr. S. S. Rao Road, Parel
Mumbai - 400012, India
Phone: +91-22-4213 4101
Fax: +91-22-4213 4102
mumbai@vaishlaw.com

GURGAON

803, Tower A, Signature Towers
South City-I, NH-8
Gurgaon - 122001, India
Phone: +91-124-454 1000
Fax: +91-124-454 1010
gurgaon@vaishlaw.com

BENGALURU

Unit No. 305, 3rd Floor
Prestige Meridian-II, Building No. 30
M.G. Road, Bengaluru - 560001, India
Phone: +91-80-40903581/ 88 /89
Fax: +91-80-40903584
bangalore@vaishlaw.com