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By

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CONTENTS

Dear Readers,

In this 98hedition, we bring you articles covering the recent supreme court judgment under the service tax law, wherein it was held that only provisions of updates to already sold subjected to VAT software is not again subjected to service tax.

The next article is part of the series of various facets of taxability of management support services. In this part, we have analysed the impact of arm's length principle qua the management support services vis-à-vis low value adding intra group services.

The next article is on the recent release of change in ODI Regulations. The readers may recall that draft ODI regulations for public comments have released a year ago. Now, the final version of regulations has been released. We tried to compare the old vs. draft vs. new regulations and its implications.

I hope that you will have good time reading this edition and please do share your feedback. I will also urge clients to mail us topics or issues on which you want us to deliberate in our future editions, so that we can contribute to the same.

Thanking You,

Suresh Babu S
Founder & Chairman

GST

NO SERVICE TAX ONLY FOR REASON UPDATES ARE GIVEN - SC IN QUICK HEAL TECHNOLOGIES

Contributed by CA Sri Harsha

The Supreme Court in the recent matter of Quick Heal Technologies Limited[1] has rejected the tax authorities claim of service tax on the amounts that are collected towards sale of anti-virus software. The Supreme Court followed its previous decision of Tata Consultancy Services[2] in reaching the above conclusion. In this article, we deal with the approach adopted by Supreme Court in arriving at the conclusion.

Issue:

The assessee (Quick Heal Technologies Limited) was engaged in development of anti-virus software under the brand of 'Quick Heal'. The same is supplied along with the license code/product code either online or on the replicated CDs/DVDs to the end-customers in India. The tax authorities has demanded service tax on such sale of anti-virus software for the period 01.03.2011 to 31.03.2014 (covering both the positive and negative list regime). The main contention of the tax authorities to demand the service tax is that the assessee, apart from the sale of the above software in canned form, also provides periodical electronic updates and such provision of periodical electronic updates to the software already sold is subjected to service tax.

The matter when reached Tribunal, the same was held against the tax authorities. The Tribunal stated that the anti-virus software which was sold by assessee does not have an element of interactivity and hence does not fall under the definition of 'information technology software' provided in both positive and negative list and accordingly not taxable. The Tribunal then proceeded to reject the claim of the tax authorities by placing reliance on the decision of Tata Consultancy Services (supra), wherein it was held that the sale of canned software or pre-packaged software would be treated as sale of goods. The final leg on which the Tribunal's rejection stood is the CBEC[3] guidelines which clarified that pre-packaged/canned software would not be goods even if there was a license. Accordingly, the Tribunal has rejected the entire tax demand which was confirmed by the tax authorities. The tax authorities were in appeal before the Supreme Court.

Arguments of Revenue before Supreme Court:

The revenue argued that the decision in Tata Consultancy Services (supra) was erroneously applied to the facts of the instant case by Tribunal. They have argued that the issued before Supreme Court in Tata Consultancy Services (supra) was whether canned software which was 'intangible property' would fall under the definition of 'goods'? and not whether the canned software can be called as 'goods' or 'service'. Since there was no argument that the canned software being 'service', the Supreme Court in Tata Consultancy Services (supra) did not make any comment as to possibility that canned software can also be called as 'service'. Hence, the reliance by Tribunal is clearly misplaced and accordingly prayed that the order need to be set aside.

[1] [2022] 141 taxmann.com 146 (SC)
[2] (2005) 1 SCC 308
[3] Central Board of Excise and Customs

The revenue contended that entire transaction of selling or trading of software can be divided into two stages:

a. Upto replication of master CD by the replicators under the terms of agreement
b. **Supply to end-users under a separate EULA[4] , which consists of two parts:**
   i. **Supply of Anti-virus software in CD**
   ii. **Providing Electronic Updates to software originally provided**

It was contended that present dispute is one relating to part (b) in the above transaction. The revenue agrees that the part (a) in the above transaction is covered by the judgment of Tata Consultancy Services (supra) and not part (b). The revenue placed reliance on the judgment of Madras High Court in M/s Infotech Software Dealers Association [5], wherein it was held that sale of packaged anti-virus software to the end user by charging licensee fee as per the end user license agreement amounts to service and not sale, based on the nature of transaction.

Arguments by Assessee before Supreme Court:

The assessee argued that the Tribunal is right in holding that the software sold is not interactive and hence there cannot be any tax since it does not fall under the definition of 'information technology software'. The Tribunal holding that a programme could be said to be interactive only when it involves the user to have exchange of information or when there is action and communication between the user and software, cannot be faulted with. The assessee argued that the transaction cannot be bifurcated into two components as argued by revenue. The reason being that when pre-packaged anti-virus software which is sold in the box has a condition of sale that updates for the period of license would also be provided to the person who has purchased the goods without any further consideration. Hence, it argued that these updates are part and parcel of the sale of software itself and cannot be divorced from the transaction and treated separately as a service. The assessee placed reliance on the decision of BSNL (supra)and argued that the contract cannot be vivisected or split out and once a lumpsum has been charged for the sale of CD and sales tax has been paid thereon, the revenue cannot levy service tax on the entire sale consideration once again on the ground that the updates are being provided. Placing reliance on Imagic Creative Private Limited[6] , they have argued that the service and VAT are mutually exclusive and since, VAT is already paid, there cannot be demand of service tax.

Analysis by Supreme Court:

The Supreme Court after referring to the order of Tribunal stated that the Tribunal has laid much emphasis on the fact that in accordance with the agreement the licensee has the right to use the software subject to conditions laid therein. The fact that the licensee is entitled for the updates and technical support from the assessee post sale of the anti-virus software has made the Tribunal to reach a conclusion that the above is a 'deemed sale' and hence would be out of the definition of 'service'. The revenue on the other hand argued that the said transaction does not fall under the ambit of 'deemed sale'.

[4]End User Licensing Agreement
[5]2010 (20) STR 289 (Mad)
[6](2008) 9 STR 337 (SC)

The Supreme Court after referring to the judgments of Tata Consultancy Services (supra), Associated Cement Companies Limited , 20th Century Finance Corporation Limited and BSNL (supra) has culled out the principles as to what constitutes right to use under Article 366(29)(d) of Constitution and held that the sale of anti-virus software falls under the ambit of the said article to be called as 'deemed sale'. The Supreme Court by placing reliance on BSNL (supra) concluded stating that once a lumpsum has been charged for the sale of CD and sale tax has been paid thereon, the revenue thereafter cannot levy service tax on the entire sale consideration once again on the ground that the updates are being provided. The Court rejected the artificial segregation of the transaction, as done by revenue in the instant case, by stating that in substance the transaction is sale of software and once it is accepted that the software put in CD is 'goods', there cannot be any separate service element in the transaction. The Court concluded by stating that even otherwise the user is put in possession and full control of the software making it a 'deemed sale', which is out of ambit of service tax. Accordingly, the Supreme Court rejected the contention of the revenue.

Remarks:

It appears that the main reason for rejection of the demand of service tax was that there was no separate consideration charged for provision of the updates. If there is a separate consideration charged, whether the above decision will hold good? Alternatively, if there is a period during which the updates are provided free of cost and later updates being chargeable, then whether, the above decision will hold good? In such cases, whether the consideration appears to be different, will that be subjected to service tax? These are important questions which will come up in due course of time before the Supreme Court.

This article is contributed by CA Sri Harsha. The author can be reached at harsha@sbsandco.com

DIRECT TAX

MANAGEMENT SUPPORT SERVICES - ALP

Contributed by CA Sri Harsha & CA Narendra

Introduction:

In first two parts of Article (Part I[1] and Part II[2]), the concept of taxability of management support services ('MSS') under treaty and Income Tax Act ('IT Act') has been analysed in detail.

Further, through the third part, consequences of such transaction under transfer pricing provisions have been discussed.

In part III[3], it is concluded that payment to non-resident associate enterprise in relation to management support services as intra group services. Now, in this part, let us proceed to analyse determination of remuneration for those services under Arm's Length Principle.

Let us proceed to continue with the same example considered in the previous Parts.

ABC Inc a company incorporated in USA has entered into license agreement with ABC India Private Limited for manufacturing of goods in India. Subsequent to such license agreement, ABC Inc has entered into another agreement for providing various MSS.

Now, let us proceed, to understand computation of Arm's Length Price under the Indian TP Regulations.

[1]Management Support Services vis-à-vis Ancillary and Subsidiary Clause–An Analysis on position under Treaties - Taxmann

[2]Management Support Services vis-à-vis Other Income – An Analysis on position under Treaties – Part II - Taxmann

[3]Management Support Services vis-à-vis Intra Group Services – An Analysis under Transfer Pricing – Part III - Taxmann

The above services are termed as 'intra group services' under the TP Regulations. Section 92 of IT Act provides that any income or expense arising from international transaction shall be computed having regard to the Arm's Length Price ('ALP'). Section 92 further provides that allocation, apportionment or contribution of any allowance, expenses between the AE shall be computed having regard to the ALP. However, such computation of income or allocation of expense or allowance shall not reduce the total income or increase in loss computed by the assessee under normal provisions of the IT Act.

The issue arises qua intra group services is substantiating the fact that services are actually provided by the AE and benchmarking the payment made for such services under arm's length principle. Hence, the questions:

i. Whether intra group services are actually provided?

ii. Whether payment to such services is at ALP?

This possible solution to the first question has been discussed in our Part -III. Let us proceed to examine the second question, which is the subject matter of the current article.

Whether payment to such services is at ALP?

A special attention may have to been drawn while arriving at ALP for intra group services when compared to other transactions.

In order to determine the ALP for intra group services, it is required to understand that basis of charge for such intra group services.

OECD in its TP Guidelines has discussed both direct and indirect charge methods.

Direct Charge Method:

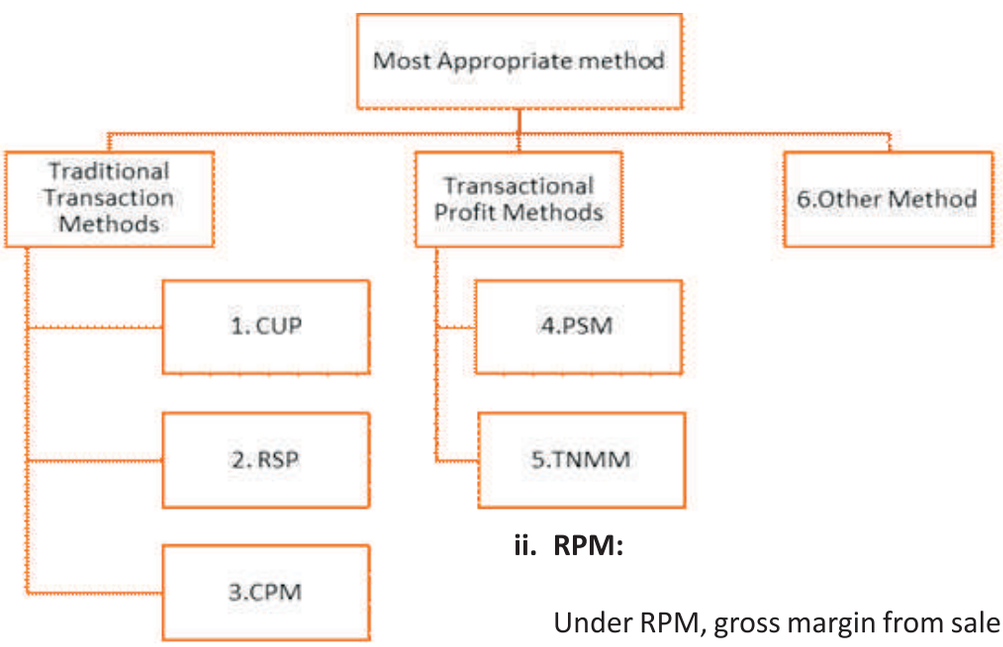
Under this method, arrangements made for charging for intra group services can be readily identified and there would not be any apportionment of expense based on any allocation key.
This method can be used when similar services are also provided to independent enterprise. When such similar services are provided to independent enterprise, assessee is in a position to demonstrate that services provided to associated enterprise are at ALP.

Indirect Charge Method:

Under this method, unlike to direct charge method, assessee may adopt cost allocation and apportionment method which often necessitate some degree of estimation or approximation. However, this method may not be accepted when those services are main business functions of the services provider.

Determination of ALP:

ALP in respect of intra group services is to be computed by using the 'most appropriate method' specified under Section 92C and such method has to be computed having regard to the procedure provided in Rule 10C of IT Rules.



i. CUP Method:

Under CUP method, transaction with AE has to be compared with uncontrolled transaction and such comparison is with respect to value of transaction. The assessee may use external comparable if such comparable data is available or use internal comparable. Internal comparable is nothing but transaction entered with third party for transfer of same property or service by the assessee, or transaction by AE with third party.

ii. RPM:

Under RPM, gross margin from sale of goods to third parties which are acquired from AE is to be compared with comparable margins. This method is applied when there is no significant value addition to the products by the assessee and it acts as mere distributor.

iii. CPM:

Under the CPM, gross profit margin is the basis for comparison. Under this method, gross profit is computed by considering both direct and indirect cost incurred by the assessee for

providing services. The gross profit margin as computed above shall be compared with the comparable margin. However, the main difficulty with this method is availability of data as data relating to gross margins is generally not available in public domain. However, internal CPM may be applied if such data is available.

iv. PSM:

PSM provides distribution of profits between two or more enterprises. This method is typically used under circumstances wherein the assessee and AE has entered into transactions jointly.

v. TNMM:

TNMM is similar to CPM and the major difference between CPM and TNMM is that under the CPM, gross profit margin is compared with the comparable company margins whereas under the TNMM, net profit is compared with the comparable margins. Further, details of net margin for comparable companies would be available in public domain.

vi. Other Method:

Rule 10AB provides that any method which takes into account the price which has been charged or paid, or would have been charged or paid, for the same or similar uncontrolled transaction, with or between non-AEs, under similar circumstances, considering all the relevant facts.

In order to compute ALP, most appropriate method has to be selected on factual basis after considering the parameter provided in Rule 10C. In most cases, judicial fora have held that once the basics tests are fulfilled (which are discussed in part III), revenue cannot consider ALP as Nil and upheld TNMM as most appropriate method for benchmarking MSS. However, depending on the facts of each case, other methods may also be selected as most appropriate method for computing of ALP. In each case, performing a functional analysis plays a vital role in selection of appropriate method.

Low Value Adding Intra Group Services:

Low value adding intra group services have been discussed by OECD in its TP Guidelines[4] in detail. As name suggests, low value intra group services are supportive services in nature which does not involve use of intangible assets, does not assume significant risk by the services provider, which are not core business activities of the services provider.

Further, OECD has provided examples of services which can be termed as low value adding intra group services and which cannot be termed as low value adding intra group services. According to the OECD TP Guidelines, following services may be considered as low value adding intra group services:

- Accounting and Auditing,
- Processing and management of accounts receivables/payables,
- Human resource activities,
- Monitoring and compilation of data relating to health, safety, environmental and other standards,
- IT support services,
- Internal and external communication services,
- Legal services,
- Tax support services
- General administrative services.

[4]OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations

However, if above services are performed by services provider as a core business activity, such services may not be considered as low value adding intra group services.

Simplified Approach for Low Value Adding Intra Group Services:

As mentioned above that low value intra group services do not involve use of intangible and do not contain significant risk, in order to reduce the compliance burden in respect of low value adding intra group services, OECD has proposed a simplified approach to determined ALP for those intra group services. Following are the benefits of adopting simplified approach:

- It reduces compliance effort of meeting the benefit test and in demonstration of ALP.
- Provides greater certainty for MNE group that the price charged for intra group services will be accepted by tax administrations.
- Provides tax administrations with targeted documentation enabling efficient review of compliance risk.

Benefit test to Low Value Intra Group Services:

As discussed in part III, benefits test needs to be satisfied in order to substantiate that intra group services are actually received by the assessee.

However, in respect of low value adding intra group services, it may be difficult or may require more efforts to demonstrate that services are actually received.

In this regard, OECD in its TP Guidelines states that when MNE maintains documentation as mentioned in simplified approach, it would be sufficient to demonstrate that the benefit test is satisfied.

Determination of remuneration to Low Value Intra Group Services:

In order to determine remuneration to low – value adding intra group services, following steps need to be followed:

- Determination of cost pools.
- Allocation of cost to members.
- Inclusion of profit markup.

Determination of Cost Pools:

The initial step involved in determination of remuneration is determination of cost pools. In this step, cost incurred by all members of the group in performing each category of services has to be pooled which shall included both direct and indirect cost incurred in performing those services. However, cost that are attributable to an activity which benefits solely the company performing the activity should be excluded.

Further, cost which are incurred by an entity to provide services to a particular member in a group shall also be excluded from cost pool.

Allocation of Cost to members:

Once total cost incurred by all members are pooled, next step is allocation of such cost to members in the group.

Such costs have to be allocated to members in the group based on an allocation key. However, there is pre-determined formula in selection of allocation key and such selection shall be based on relevant facts. However, such allocation shall be utilized consistently.

Inclusion of Profit Markup:

Once costs are allocated based on allocation key, group company may add mark-up to those costs. OCED in its TP Guidelines provides a standard markup of 5 percent for low value adding intra group services.

Finally, remuneration to low value adding intra group services has to be determined by aggregating costs allocated to members and profit markup:

Cost incurred solely for the purpose of providing services to specific members plus markup + cost allocated to members plus markup.

Arm's Length Price for Low Value Intra Group Services:

As stated above, OECD in its TP Guidelines provides that a mark up of 5% can be considered for low value adding intra group services. The proposed mark up must be applied on cost allocated to such low value adding intra group services. As the ALP for low value adding intra group services is determined at 5% markup, TP Guidelines states that such services need not be benchmarked separately through a study.

Further, TP Guidelines states that tax administrations have to setup a threshold to avail the benefit of simplified approach.

Documentation:

In respect of low value adding intra group services, group adopting simplified approach has to maintain following documentations:

- A description of the categories of low value adding intra group services provided and identity of the beneficiaries.
- Reasons justifying that each category of services constitute low value adding intra group services.
- A description of benefits to members and selection of allocation key.
- Written contracts/agreements for the provision services.
- Documentation and computation of cost pools and markup added thereon.
- Calculation showing the application of the specified allocation keys.

India's Approach:

In India, low value adding intragroup services have been discussed in safe harbour rules. Rule 10TD of IT Rules[5] states that where an eligible assessee has entered into eligible international transaction, such transaction shall be accepted by income tax authorities if such transaction is in accordance with the limits and conditions specified therein.
Rule 10TC defines that term 'eligible international transaction' which inter alia includes receipt of low value-adding intra-group services from one or more members of its group. Further, eligible assessee has been defined under section 10TB which inter alia includes a person who has received low value-adding intra-group services from one or more members of its group and opted for safe harbour provisions by filing Form 3CEFA.

Rule 10TA of IT Rules defines the term 'low value adding intra group services' to mean services that are performed by one or more members of a multinational enterprise group on behalf of one or more other members of same multinational enterprise group and which

i. are in the nature of support services;

ii. are not part of the core business of the multinational enterprise group, i.e., such services neither constitute the profit-earning activities nor contribute to the economically significant activities of the multinational enterprise group;

[5] Income Tax Rules, 1962

iii. are not in the nature of shareholder services or duplicate services;

iv. neither require the use of unique and valuable intangibles nor lead to the creation of unique and valuable intangibles;

v. neither involve the assumption or control of significant risk by the service provider nor give rise to the creation of significant risk for the service provider; and

vi. do not have reliable external comparable services that can be used for determining their arm's length price, but does not include the following services, namely:

   a. research and development services;
   b. manufacturing and production services;
   c. information technology (software development) services;
   d. knowledge process outsourcing services;
   e. business process outsourcing services;
   f. purchasing activities of raw materials or other materials that are used in the manufacturing or production process;
   g. sales, marketing and distribution activities;
   h. financial transactions;
   i. extraction, exploration, or processing of natural resources; and
   j. insurance and reinsurance.

Threshold and Markup:

In respect of low value adding intra group services, Rule 10TD states that safe harbour provisions would be applicable only when such value of transaction does not exceed Rs.10 Crore and markup does not exceed 5percent.

Further, Rule 10TD states that provisions of section 92D (maintenance of documentation) and section 92E (submission of Form 3CEB) are applicable irrespective of the fact that the assessee exercises his option for safe harbour in respect of such transaction.

Having understood implications under the Income Tax Act, the next aspect would be understanding implications of MSS under other legal Acts which be discussed in next part.

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FEMA

ARTICLE ON NEW OVERSEAS INVESTMENT REGIME

Contributed by CA Sri Harsha & CS D V K Phanindra & CA Narendra

Under the pre-amended/old regulations, overseas investment, in respect of investment in foreign securities, is governed by Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 and, overseas investment, in respect of investment in immovable property, is governed the Foreign Exchange management (Acquisition and Transfer of Immovable Property Outside India) Regulations, 2015.

Government of India, in order to improve its standards in ease of doing business by way of relaxations, simplifications or exemptions, is making many changes to various laws and regulations which inter alia includes changes to taxation laws, Foreign Exchange Management Regulations, Corporate and other laws etc.

Under the old regulations, overseas investment is considered to be investment in joint venture or investment in wholly owned subsidiary which has created some sort of confusion in relation to overseas investment by various persons in other overseas entities. Further, overseas investment by individual, investment by way of loan/ debt securities, round tripping concept were also topics of discussion under old regulations.

Now, in order to make overseas investment regulations simpler, and to provide certain clarifications/relaxations, Government of India has made changes to overseas investment regulations and rules thereunder. In this regard, Reserve Bank of India ('RBI') has notified Foreign Exchange Management (Overseas Investment) Regulations, 2022 ('OI Regulations') and Central Government has notified Foreign Exchange Management (Overseas Investment) Rules,2022 ('OI Rules') with effective from 22.08.2022 which are applicable to OI in securities as well as immovable properties.

In this Article, we shall discuss various changes made by overseas investment Regulation/Rules In order to understand the new Regulations, following aspects has to be understood.

❖OI Regulations and OI Rules shall not be applicable to following investments:

- Any investment made outside India by financial institution in an IFSC.

- Acquisition or transfer of any investment outside India made,-
  i. Out of RFC Account
  ii. Out of foreign currency resources held outside India by a person who is employed in India for a specific duration irrespective of length or for a specific hob or assignment, duration of which does not exceed 3 years.
  iii. In accordance with section 6(4) of FEMA,1999 i.e., acquisition of foreign security or immovable property outside India if such security or property is acquired when such person was a resident outside India or inherited from a person who is resident outside India.

❖ OI by person resident in India has been divided into six parts in brief:

Part	Details
Part I	Schedule I to OI Rules deals with ODI by an Indian entity
Part II	Schedule II to OI Rules deals with OPI by an Indian entity
Part III	Schedule III to OI Rules deals with OI by resident individual
Part IV	Schedule IV to OI Rules deals with OI by a person other than Indian entity or resident individual
Part V	Schedule V to OI Rules deals with OI in IFSC by a person resident in India
Part VI	Rule 21 of OI Rules deals with investment in immovable property outside India

Particulars	New Provisions
Overseas Direct Investment ('ODI') **Rule 2(q)**	**ODI means-** • Investment by way of acquisition of unlisted equity capital of a foreign entity ('FE'). • Subscription to the Memorandum of Association of a FE. • Investment in 10 percent or more of the paid-up equity capital of listed FE. • Investment with control where investment is less than 10 percent of the paid-up equity capital of a listed FE. Further, once the investment made by a person resident in India in the equity capital of a FE is treated as ODI, such investment shall continue to be a ODI even if the investment falls below 10 percent threshold specified or such person loses control in the FE.
Rule 2 (e)	**"Equity capital' means:** • equity shares. • Perpetual capital/instruments that are irredeemable. • Contribution to non-debt capital that are fully and compulsory convertible.

Author's Comments:

- The old regulation states that investment in capital of a FE is considered as direct investment outside India. However, new regulations inserted a word 'equity capital' in its definition making other than equity capital ineligible for ODI (preference shares are also not considered).

- However, investment in perpetual capital/instruments that are irredeemable or contribution to non-debt capital that are fully, and compulsory convertible is treated ODI.

- Old regulation does not provide more details about portfolio investment however, the new regulations provide more clarity for portfolio investment by providing specific definition, terms and conditions for such investment etc. which will be discussed in subsequent paras.

Financial Commitment ('FC') **Rule 2(f)**	FC means aggregate amount of investment made by resident in India by way of ODI, or debt other than OPI in which ODI is made and includes non-fund-based facilities.

Author's Comments:

- Above definition states that that non-fund based facilities shall also be reckoned for computing the FC. However, in the case of performance guarantee, Regulation 5 states that only 50 percent of the guarantee shall be considered. Further, if guarantee is issued by a group company, such guarantee is to be reckoned towards the utilisation of limits separately. However, if such guarantee is issued by individual promotor, same shall be considered towards computation of limits by such Indian entity.

- Further, in respect of investment by Indian entities, Schedule I to OI Rules states that capitalization of retained earnings shall not be considered for computing the FC limit however, utilisation of ADR/GDR including stock swap of such receipts and utilisation of ECB has to be considered for such computation.

- The need to determine FC arises when Indian entity is making ODI in a FE and for OPI, there may not be any requirement to compute FC.

FC by Indian entity by modes other than equity capital **Regulation 3**	**General Permission:** The Indian entity may lend or invest in any debt instrument issued by a FE or extend non-fund-based commitment to or on behalf of a FE including overseas stepdown subsidiary of such Indian entity subject to following conditions: • Indian entity is eligible to make ODI. • Indian entity has made ODI in the FE. • Indian entity has acquired control in such FE at the time of making such FC. **FC by way of debt:** An Indian entity may lend or invest in debt instruments issued by a FE subject to the condition that such load is backed by a loan agreement and interest is charged on AL basis. **FC by way of Guarantee:** An Indian entity may issue following guarantees: • Corporate or performance guarantee. • Corporate or performance guarantee by a group company. **FC by way of pledge or Charge:** An Indian entity which has made ODI is eligible to make pledge. Investment in debt securities/extending non-fund based facilities have been discussed in Schedule I in subsequent paras.

Author's Comments:
New OI Regulations provide more clarity in terms of investment by a resident in debt instruments of FE. New Regulations states that investment in debt instruments is not permitted unless such investment is preceded by equity investment. Further, investment by way of OPI is excluded from the ambit of FC as such investment is not considered as ODI.

Regulation 3 of OI Regulation deals with investment in FE by means other than by equity capital. It provides certain conditions subject to which such investment can be made. It states that only Indian entity is allowed to make investment in debt securities issued by FE subject to the primary condition that there should be an ODI by the Indian entity and such Indian entity has acquired control in such FE.

Further, the term debt instrument is defined under Rule 5 of OI Rules to mean Government Bonds, corporate Bonds, all tranches of securitization structure which are not equity tranche, borrowings by firms through loans and depository receipts whose underlying securities are debt securities.

Overseas Investment ('OI')	OI means FC and OPI by a person resident in India.

Author's Comments:

- The definition of OI states that FC and OPI is treated asoverseas investment.

- FC has been expressly defined to mean investment by way of ODI and debt investment in FE in which such ODI has been made and included non-fund-based facilities extended to such FE and investment by way of OPI is not considered as FC.

S.No.	Definition	Explanation
1	OI	FC + OPI.
2	FC	ODI + Debt[1] + non-Fund based facilities[2].
3	ODI	Equity investment in unlisted + Subscription to MOA of FE + Equity investment in 10 percent or more of capital of listed FE + Equity investment (with control) in less than 10 percent of capital of listed FE.
4	OPI	Investment in foreign security which is not considered as ODI.

[1]Debt is allowed only when Indian entity has already made ODI in FE.
[2]Non fund-based facilities may be extended only when Indian entity has already made ODI in FE.

Overseas Portfolio Investment ('OPI') **Rule 2(s)**	• OPI means investment in foreign securities but does not include any unlisted debt instruments or any security issued by a person resident in India who is not in an IFSC.Investment which is treated as ODI above shall not be considered as OPI. • The definition of OPI further states that the investment which is considered as OPI shall continue to be treated as OPI even after delisting until any further investment made in the entity.

Author's Comments:

- The definition of OPI has been inserted in the ODI regulation for providing similar treatment as provided in FDI regulations.

- Under the new OI Rules, in addition to investment in unlisted equity capital of FE, investment in listed equity capital is treated as ODI if such investment is 10 percent or more of the paid-up equity capital,or investment with control, where the investment is less than 10 percent of the paid-up equity capital of the listed FE. The definition of ODI further states that such investment shall continue to be ODI even if the investment falls below 10 percent.

- On the other hand, if such investment in listed equity capital is less than 10 percent, such investment is treated as OPI if there is no investment by way of control. Further, in future if such shares are delisted, such investment shall continue to be an OPI until any further investment made by the Indian entity in such FE. Which means that such OPI may be treated ODI, only if any fresh investment has been made by the Indian entity post delisting of shares.

- From the reading of above definitions, it may be understood that an ODI may not become OPI, however, an OPI may become ODI. Further, the definition of FC excludes the investment by way of OPI from its ambit. If such investment becomes ODI in future by virtue of delisting, such investment would be included in the ambit of FC.

- Procedure for making investment through OPI is discussed in subsequent paras.

ODI vs OPI:

Nature of investment / FE	Unlisted FE	Listed FE
Investment in 10 percent or more of equity capital	ODI	
Investment in less than 10 percent of equity capital	ODI	If investment is coupled with control, ODI
		Other than above, OPI

General Permission to OI **Rule 11 to Rule 15**	**A person resident in India is permitted to make overseas investment as under:** • An Indian entity may make ODI in the manner and subject to the terms and conditions prescribed in Schedule -I to the OI Rules. • An Indian entity may make OPI in the manner and subject to the terms and conditions prescribed in Schedule -II to the OI Rules. • A resident Individual may make OI in the manner and subject to the terms and conditions prescribed in Schedule – III to the OI Rules. • A person resident in India, other than an Indian entity or a resident Individual, may make OI in the manner and subject to the terms and conditions prescribed in Schedule – IV to the OI Rules. • A person resident in India may make OI in an IFSC in India in the manner and subject to the terms and conditions prescribed in Schedule – V to the OI Rules.

Author's Comments:

The new rules and regulations provide for manner in which ODI/OPI/OI as the case may be are to be made, and also the obligations of the parties and the reporting requirement in each of the case.

Under the old Regulations, general permission is given to make OI from RFC account and when not permanently resident in India, from foreign currency sources outside India. Under the new Regulations, Rule 4 of OI Rules states that OI out of RFC Account is outside the scope of new OI Regulations and those investment are permitted without complying with these Regulations.

RBI approval – Ceiling Amount **Rule 9 (3)**	• Reserve Bank of India may, in consultation with the Central Government, stipulate the ceiling for the aggregate out flow during the financial year on account of FC or OPI. • RBI may, in consultation with the Central Government, stipulate the ceiling beyond which the amount of FC by Indian entity in a financial year shall require its prior approval.

Author's Comments:

- The new rules confer powers on RBI, to fix the limits as to the total outflow in a FY, on account of FC or OPI, and with prior approval in case of FC. Rule 3 of OI Rules states that RBI may issue directions, circulars, instructions and clarifications for effective implementation of OI Rules.

- In this regard, Master Direction states that FC by an Indian entity exceeding USD 1 billion in a financial year requires prior approval of RBI even when such FC is within the eligible limit under the automatic route.

Approval from Central Government **Rule 9**	• Any overseas investment or transfer of such investment in any entity formed, incorporated or registered in Pakistan or any other jurisdiction as may be advised by the Central Government shall require prior approval Central Government. • Investment in strategic sectors or geographies, above the limits prescribed in the OI Rules requires approval from Central Government.

Author's Comments:

- Under the new rules, investment in strategic sectors or geographies above limits specified in OI Rules shall require approval of the CG. The strategic sector has been defined to mean energy and natural resources sectors such as Oil, Gas, Coal and Mineral Ores, submarine cable system and start-ups and any other sector as may be specified by the CG.

- However, Schedule I to OI Rules states that investment by specified PSUs and its subsidiaries in strategic sector is allowed without considering the limit of 400% networth.

Prohibited investments
 	
Rule 19
	• A person resident in India is prohibited from making ODI in a FE engaged in:
	  • Real Estate activity.
	  • Gambling in any form.
	  • Dealing with financial products linked to Indian Rupee without specific approval of RBI.
	
	• ODI in any start-ups recognized under the laws of host country shall be made by an Indian entity only from its internal accruals or from the internal accruals of its group or associate entities in India, and in the case of resident individual only from own funds of such individual.
	
	• No person resident in India shall make FC in a FE that has invested in or invests into India, at the time of making such FC or at any time thereafter, either directly or indirectly, resulting in a structure with more than two layers of subsidiaries However, such restriction is not applicable to banking company, NBFC, insurance company and Government company.

Author's Comments:

- Under old Regulations, investment inprohibited activities were allowed with the prior approval of the RBI. However, no such provision of approval is found in new rules/regulation.Further, the prohibited list has been expanded to include gambling. However, Rule 19 deals with only ODI and silent about investment through OPI.

- Further, the concept of round tripping is always an undiluted matter under overseas investments. Even though such concept is not expressly dealt with by the provisions of FEM Act, 1999, there are many instances wherein the RBI has held such transactions are not permitted and accorded approval on a case to case to basis.

- With the new OIRegulations, it may be considered that these regulations have allowed the round tripping transactions subject to satisfaction of above conditions.

- In draft Rules, it is provided that round tripping is allowed subject to the condition that such investment is not for the purpose of tax evasion/avoidance. However, in final OI Rules, such condition of tax evasion/avoidance has been taken out and restriction of two-layer subsidiary has been brought in. Further, Rule 9 of OI Rules states that any investment outside India shall be in FE which is engaged in bonafide business activity.

Pricing guidelines **Rule 16**	Issue or transfer of any equity capital: • from a person resident outside India to a person resident in India • from a person resident in India to another person resident in India. • from a person resident in India to a person resident outside India, shall be subject to a price arrived on an arm's length basis. AD Bank shall ensure that such compliance with arm's length pricing taking into consideration the valuation as per any internationally accepted pricing methodology for valuation.

Author's Comments:

- Under the old Regulations, transfer of existing shares or securities shall be based on the price on stock exchange if such share are listed and based on the valuation report obtained from merchant/investment banker or CA in the case of acquisition and from a CA in the case of transfer.

- However, under the new OI Rules, without any limit, price for issue / transfer of shares shall be arrived on arm's length basis. Further, Master Direction3 states that AD bank shall put in place its policy in order to comply with arm's length pricing. It states that policy has to provide scenarios where the valuation report may not be insisted upon viz. transfer on account of merger, amalgamation or demerger or liquidation if price is approved by the competent authority/Tribunal or if price is readily available on stock exchange etc.

Mode of payment **Regulation 8**	The person resident in India making OI shall make payment for such acquisition by way of: • Remittance made through banking channels • Out of funds held in an account maintained in accordance with provisions of the Act • Swap of securities. Further, in respect of following investments, payment may be made out of proceeds of ADR, GDR, stock swap raised on account of ADR/GDR and ECB: • In respect of ODI by Indian entity. • In respect of FC by way of debt investment by Indian entity.

Author's Comments:

- As under new OI Regulations/Rules, OPI has been brought in separately, it is specifically provided that proceeds of ADR/GDR including stock swap has to be utilized for investment by way of ODI or in respect of FC by way of debt.

- Even though new OI Regulations prescribe limited options, other options have been provided in respective Schedules of OI Rules. Even under new OI Regulations/Rules, person resident in India may invest in FE by way of capitalization of exports subject to conditions prescribed in Schedules.

- Further, Indian entity may make ODI, on account of merger, demerger, amalgamation or any scheme of arrangement, on account of issue of rights issue/bonus issue.

- Similarly, a resident induvial may make investment in FEaccount of merger, demerger, amalgamation, or liquidation, or on account of issue of rights or bonus shares, or by of inheritance, gift, acquisition of sweat equity shares, ESOPs without involving payment of consideration.

Deferred Payment **Regulation 7**	In respect of investment by way of ODI in the equity capital of FE by a person resident in India by way of • By a person resident in India by way of subscription to an issue or Purchase of shares from a resident outside India or • By a person resident outside India by way of Purchase of shares from a person resident in India, The payment of consideration may be deferred for such period as provided in the agreement subject to the following: • The foreign securities equivalent to the total consideration, shall be transferred (or issued) upfront by the seller to the buyer. • The final consideration paid shall be in compliant with the pricing guidelines. Such deferred part of the consideration in the case of acquisition of equity capital of a FE shall be treated as non-fund-based commitment.

Author's Comments:

- Under old Regulations, deferred payment is not allowed. However, under new OI Regulations/Rules a person may agree for deferred payment option.

- Under this option, both resident in India and outside India may acquire shares on deferred payment option provided period within which remittance is to be made for such acquisition has to be defined upfront and should be recorded in underlying agreement/document and valuation of such acquisition shall be determined upfront.

- Such acquisition by deferred payment is considered as non-fund based FC and has to be reported accordingly and once payment is completed, reporting Form has to be submitted again to convert it from non-fund based FC to equity.

- Under draft Regulations, it is provided that in case of advance payment is made, buyer may be indemnified by the seller. However, in the final OI Regulations, such option of payment in advance is removed. However, clarity is required in which case, such indemnity is required.

Part I – ODI by an Indian entity **Schedule – I**	An Indian entity may make ODI in equity capital of a FE for the purpose of bona fide business activities: **Modes of acquisition:** An India entity may make ODI by way of: • Subscription to/purchase of equity capital (listed/unlisted). • Acquisition through bidding or tender process. • Acquisition of equity capital by way of rights issue or allotment of bonus shares. • Capitalisation of any dues from FE to Indian entity subject to other conditions. • The swap of securities. • Merger, demerger, amalgamation, or any scheme of arrangement as per the laws in India/host jurisdiction. **ODI in financial services activity:** An Indian entity which is engaged in financial services activity in India may make ODI in a FE which is engaged in financial services activity subject to the following: • Such Indian entity has posted net profits during the preceding three financial years. • Such Indian entity is registered with or regulated by financial services regulator in India. • Indian entity shall obtain approval from such regulators in India and host country if required. An Indian entity not engaged in financial services activity in India may make ODI in a FE which is not engaged in financial services activity (except banking or insurance) subject to the condition that the Indian entity has posted net profits during the preceding 3 financial years[4]. However, Indian entity not engaged in insurance sector may make ODI in general or health insurance subject to conditions.

[4]If Indian entity does not meet the net profits requirements on account of COVID -19 for FY 2020-21 to 2021-22, then such period may be excluded.

Limit on FC: The total FC made by Indian entity shall not exceed 400 percent or as directed by RBI from time to time of its networth as per the latest audited balance sheet.

- Capitalisation of retained earnings need not to be considered while computing the threshold.
- FC by 'Maharatna' PSUs or 'Navaratna' PSUs or subsidiary of such PSUs in a FE which is engaged in strategic sector shall not be subject to above threshold.
- Utilisation of ADR/GDR and ADR/GDR stock swap shall also be reckoned for the purpose of computation of limit.
- Utilisation of proceeds from ECB for making FC shall be reckoned for the above limits.

Investment in Debt Instruments/extending guarantee:

- An Indian entity, which has made ODI in equity capital of a FE and also acquired control in such FE, is eligible to undertake FC by modes other than equity capital.
- Such FC includes lending or investing in debt instruments, extending non-fund-based commitments including its SDS. Further, such FC shall be within the limits specified above.
- In respect of investment by way of lending or investing in debt instruments, loans shall be backed by appropriate agreements and interest shall be charged on arm's length basis.
- An Indian entity may extend non-fund facilities to FE or its SDS (Operating) viz:
  - Corporate/performance guarantee by Indian entity.
  - Corporate/performance guarantee by holding/subsidiary of Indian entity or promotor company for such Indian entity.
  - Personal guarantee by resident individual being promotor of Indian entity.
  - Bank guarantee by AD bank which is backed by a counter guarantee or collateral by the India entity.
- Where guarantee is issued by a holding company, subsidiary company or promotor company, such guarantee shall be counted independently towards utilisation of FC limit.
- Where guarantee is issued by an Individual promotor, such guarantee shall be counted within the limits of Indian entity.

	• When the guarantee is invoked by the other party, same shall cease to be a non-fund facility and considered as lending.
	
	• Where guarantee is extended by jointly by two or more Indian entities, 100 percent of the amount of such guarantee shall be reckoned towards the individual limits of each of such Indian entities.
	
	• In case of performance guarantee, 50 percent of the amount of guarantee shall be reckoned towards FC.
	
	FC by way of Pledge/Charge:
	• Pledge of foreign company shares: An Indian entity which has made ODI may pledge equity capital of the FE or of its SDS in favour of an AD bank, public financial institution in India or overseas lender for availing fund based or non-fund-based facilities for itself or any FE in which ODI is made or to its SDS, or in favour of a debenture trustee registered with SEBI for availing fund based facilities.
	
	• **Charge on assets:** An Indian entity which has made ODI may create charge by way of mortgage, pledge, hypothecation or other identical mode on
	  • its assets in India in favour of overseas lender for availing fund/non-fund-based facilities for FE or SDS.
	
	  • Assets outside India of FE or SDS in favour of AD bank or public financial institution in India or overseas lender for availing fund/non-fund-based facilities for itself, FE or SDS or in favour of a debenture trustee registered with SEBI for availing fund based facilities.
	
	The amount of pledge or the amount of facility whichever is lower shall be considered for counting the FC excluding cases where such facility is availed by Indian entity for itself.

Author's Comments:

- With the introduction of new OI Regulations, the concept of JV/WOS has been taken away and precise definition/clarification has been provided in respect of investment in FE.

- Under the old Regulations, Indian party allowed to make ODI in JV/WOS. The term JV/WOS has been defined under old Regulations to mean entity formed, registered or incorporated in accordance with the laws and regulations of the host country in which the Indian party makes a direct investment. However, under the new OI Regulations, Schedule I to OI Rules states that Indian entity may make ODI in equity capital and such equity capital has been defined under Rule 2(e) of OI Rules to mean equity shares, perpetual equity or instruments that are irredeemable or contribution to debt capital which is fully and compulsory convertible. In this regard, much clarity is required in respect of investment in registered partnerships outside India.

- Under the old Regulations, FC without equity investment is allowed with the prior approval of the RBI. However, under the new regulations, such facility has not been provided.

- Under the old Regulations, guarantee may be given by sister concern and associated enterprise in addition to the Indian Party including its promotors (corporate/individual). Under the new regulations, it has been clearly statedthat such guarantee, in addition to the Indian party including its promotors, may be given by holding company and subsidiary company with specific shareholding conditions. Further, under the new regulations, guarantee given by group company is to be considered independently for the purposes of counting limit of FC.

- Under the old Regulations, Indian party is permitted to extend guarantee to FE, SDS (whether it is operating SDS or SPV) under automatic route and subsequent SDS (Operating) under approval route. In the new OI Regulations, it is mentioned that Indian entity is permitted to extend guarantee facility to SDS (operating) in which Indian entity has acquired control through FE under automatic route.In the draft Rules, it was provided that SDS of SDS is also to be considered as SDS. However, such definition is not provided in final OI Rules.

- Under the old regulations, investment through proceeds of ADR/GDR are outside the networth limits. However, under the new regulations, it is specifically mentioned that such proceeds need to be reckoned for the purpose of computation of limits. It is clarified that FC made through these resources under old Regulations shall not reckoned.

- Further, a relaxation is provided in respect of capitalization of retained earnings. Under new Regulations, an Indian entity can invest in FE by capitalizing the retained earnings and such investment is outside the limit specified for FC.

Part II – OPI by an Indian entity
 	
Schedule – II
	An Indian entity may make OPI:
	• An Indian entity may make OPI including by way re-investment within the limit of 50 percent of its net worth as per latest audited balance sheet.
	
	• An unlisted Indian entity may make OPI only by way of:
	  • Acquisition of equity capital by way of rights issue or allotment of bonus shares.
	  • Capitalisation of any dues from FE to Indian entity subject to other conditions.
	  • The swap of securities.
	
	Merger, demerger, amalgamation, or any scheme of arrangement as per the laws in India/host jurisdiction.

Author's Comments:

- Under the new regulations, a specific schedule is inserted with regard to investment by Indian entity by way of OPI. The regulations provide thatboth listed and unlisted companies are permitted to invest by way of OPI.However, listed entities may invest through OPI without any restriction whereas unlisted entities can invest through OPI only by way of rights/bonus shares, capitalization of any dues, swap of shares, or under restructuring arrangements.

- However, such restriction is not provided in the case of investment by resident Individual. Schedule - III states that resident Individual may make overseas investment by way of ODI and OPI.

Part III – OI by resident individual **Schedule – III**	A resident individual may make ODI by way of investment in equity capital or OPI, subject to conditions, within the ceiling limits prescribed under LRS. A resident individual may make ODI in an operating FE not engaged in financial services activities and which does not have subsidiaries and stepdown subsidiaries where the residential individual has control in FE.A resident individual may make OPI including by way of re-investment. A resident individual may make ODI or OPI by way of: • Capitalisation of any amount due from FE. • Swap of securities on account of merger, demerger, amalgamation or liquidation. • Acquisition of equity capital through rights issue or allotment of bonus shares. • Gift. • Inheritance[5] . • Acquisition of sweat equity shares[5]. • Acquisition of minimum qualification shares issued for holding a management post in a FE[5]. • Acquisition of shares/interest under ESOP[5]. Further, investment in equity capital by way of last three options provided above, whether listed or unlisted, shall be considered as OPI if value of investment is less than 10 percent and there is no control in such FE. **Inheritance/Gift subject to the conditions:** • A resident Individual may acquire foreign securities by way of inheritance from a person resident in India who has acquired such shares in accordance with the ODI regulations or from a person resident outside India without any limit. • A resident individual may acquire foreign securities by way of gift from a person resident in India, who is a relative without any limit. • A resident individual may acquire foreign securities by way of gift from a person resident outside India in accordance with the provisions of FCRA,2010. Acquisition under ESOP[6] : A resident individual who is an employee or a director of: • An office or branch of overseas entity • Subsidiary in India of overseas entity • Indian entity in which overseas entity has direct or indirect equity holding May acquire without any limit[7] shares or interest under ESOP offered by such overseas entity provided that such ESOPs are offered globally on uniform basis.

[5]May make ODI whether or not such entity is engaged in financial services activity, or whether or not such entity has subsidiary or stepdown subsidiary where the resident individual has control.

[6]Includes sweat equity shares.

[7]Master direction states that such amount shall be reckoned towards the LRS limit of the person concerned.

Author's Comments:

- Under the old Regulations, the concept of investment by resident Individual was not allowed from the inception. By a notification in 2013, such investment by resident Individual was allowed subject to conditions. However, as permission is given separately, there are some gaps in terms of eligibility, mode of acquisition, nature of payment, amount to be included for the purpose of computation of limit etc.

- Under the new Regulations, such issues have been expressly dealt with by incorporating separate Schedule -III to the regulations.

- Under the old Regulations, investment in SDS is allowed by Indian party by specific mention. However, such investment by resident Individual is not expressly permitted/prohibited (indirectly it is prohibited). However, under new Regulations, individual is barred from making ODI if such FE has subsidiary/step down subsidiary where such individual has control in the FE. Which means that if individual does not have control in FE, there is not restriction in making step down subsidiary.

Relief from investment in SDS by Individual: As stated above, investment by resident individual is restricted under the old Regulations. However, under new Regulations, only certain type of investments by resident individual are restricted and following investments are not restricted in respect of investment by individual in SDS.

- If investment is considered as ODI and there no control in FE.

Nature of investment / FE	Unlisted FE	Listed FE
Investment in 10 percent or more of equity capital	If investment with control – Restricted	If investment with control – Restricted
	If investment without control – NotRestricted	If investment without control – NotRestricted
Investment in less than 10 percent of equity capital	If investment with control – Restricted	If investment with control – Restricted
	If investment without control – NotRestricted	If investment without control – not to be considered as ODI and hence, NotRestricted

- If investment is considered as OPI then, restriction of making SDS is not applicable.

- Further, investment by individual by way of inheritance, sweat equity shares, acquisition of qualification shares or ESOPs is not restricted whether or not such FE is engaged in financial services activity or has subsidiary where the resident individual has control.

- Further, where investment by way of sweat equity shares, acquisition of qualification shares or ESOPs, if investment is less than 10 percent, are considered as OPI.

- **Investment in debt securities by resident Individual:** Regulation 3 of OI Regulations deals with investment in foreign entities by means other than equity capital. It states that only Indian entity is eligible to make investment in debt securities. Which means that resident individual cannot make OI by debt investment. However, under LRS, a resident individual may remit the amount towards extending loans to non-residents subject to other conditions specified therein.

- **Round Tripping Transactions:** Rule 19 of OI Rules states that person resident in India is restricted from making FC in a FE that has invested into India resulting in a structure with more than two layers of subsidiaries.

- On reading of Rule 19 and Schedule III to OI Rules, a resident individual is allowed to make investment in FE which in turn invests into India. However, resident individual shall not acquire control in such FE.

Gift/Inheritance:

- Under old Regulations, there is no restriction for an individual resident in India to acquire foreign securities as a gift from a person resident outside India. However, under new OI Regulations, Schedule III to OI Rules states that such acquisition shall be subject to provisions of FCRA,2010.Further, Schedule III to states that resident individual may also acquire foreign securities by way of gift from a person resident in India subject to the condition that such transferor shall be a relative of the transferee.

- In respect of inherence, old as well as new Regulations states that resident individual may acquire foreign securities by way of inheritance from any person whether resident or non-resident.

- Master Direction3 clarifies that resident individuals are not permitted to transfer any OI by way of gift to a person resident outside India.

Part – IV OI by other than above	• A registered trust or society engaged in the educational sector or which has setup hospitals in India may make ODI in FE with the prior approval of the RBI subject to conditions specified.
Schedule – IV	• Mutual funds or venture capital funds or AIF can make overseas investment in specified securities subject to conditions mentioned in these regulations. Such investments by mutual fund, venture capital fund or AIF shall be considered as OPI notwithstanding to the definition of ODI. • Clearing corporations and clearing members may open and maintain Demat accounts with foreign depositories, remit proceeds, liquidate such foreign securities and repatriate proceeds to India. Domestic depository, and AD Bank including its overseas branch can acquire, hold or transfer foreign securities subject to conditions specified in these regulations.

Author's Comments:

- The new regulations provide for detailed modalities of acquiring, holding and transfer of foreign securities by a person other than Indian entity or resident individual.

Part – V OI in IFSC by person resident in India **Schedule – V**	A person resident in India may make OI in an IFSC in India in manner as laid down in Schedule I, Schedule II, Schedule III or Schedule IV mentioned above, and subject to the following; • In case ODI is made in IFSC, approval of the Financial Services Regulator concerned, shall be decided within 45 days from the date of application, failing which it shall be deemed to be approved. • An Indian Entity not engaged in Financial Services activity in India, making ODI, in a FE not directly or indirectly engaged in financial services activity, except banking or insurance, who does not meet the net profit condition as required under the rules, may make ODI in an IFSC. • A person resident in India may make contribution to an investment funds or vehicle set-up in an IFSC as OPI. • A resident individual may make ODI in a FE, including an entity engaged in financial services activity (except in banking and insurance) in IFSC, if such entity does not have subsidiary or stepdown subsidiary outside IFSC where the resident individual has control in the FE.

Author's Comments:

- It is clarified that listed, unlisted and resident individual may make investment in an IFSC subject to restrictions provided in Schedule I to Schedule IV.

- A resident individual may make investment in investment in IFSC which may have SDS within the IFSC (whether or not such individual has control in entity in IFSC).

Procedure for making ODI	• A person resident in India who is intending to make ODI shall approach AD bank for obtaining UIN before sending outward remittance or acquisition of equity capital in a FE whichever is earlier.
	
	• A person resident in India making ODI shall designate a branch of AD Bank and route all transactions pertaining a particular UIN through such designated branch.
	
	• Where more than one person resident in India making FC in the same FE, all such persons shall route all transactions relating to that UIN through the branch of the AD bank designated for that UIN.
	
	• A person resident in India which has made ODI shall submit, share certificates or any other relevant document as per laws of host country, to the AD Bank within 6 months from the effective date.
	
	• A person resident in India which has made ODI shall realise and repatriate to India:
	  • All dues receivable from FE.
	  • Amount of consideration on transfer/disinvestment of such ODI.
	  • Net realisable value of assets on liquidation of such FE.
	within a period of 90 days from the relevant date.

Author's Comments:

- Under the old regulation, in case acquisition of shares, valuation report needs to be obtained from merchant/investment banker if such value is more than USD 5 million and from CA in other cases. However, under the new regulations, such valuation needs to be obtained from registered valuer under the Companies Act,2013.

- Further, the time limit for realization of dues from FE has been increased from 60 days to 90 days which significantly provides relief to the Indian investors.

Reporting Requirement	**Form FC:** A person resident in India who has made ODI or making FC or undertaking a disinvestment in a FE shall report the following: • FC, whether or not such amount is reckoned for limit specified, at the time of outward remittance or making such FC whichever is earlier. • Disinvestment within 30 days of receipt of disinvestment proceeds. • Restructuring within 30 days of from the date of such restructuring. **Form OPI:** A person resident in India other than individual, making OPI or transfer of such investment by way of sale, shall report such transaction in Form OPI within 60 days from the end of half year (half year ending at Sept/March). **Form APR**: A person resident in India which has made ODI shall file APR with respect to each FE every year by 31st December [8]. However, APR is not required to be reported in the following situation:

[8] If accounting year of such FE ends on 31st December, APR shall be submitted by 31st December of the next year.

	• A person resident in India is holding less than 10 percent of the equity capital without control in the FE and there is no further FC other than by way of equity capital. • In the case where, FE is under liquidation. • The APR shall be based on the audited financial statements. However, where the person resident in India does not have control in the FE and laws of host country does not provide for mandatory auditing of the books of accounts, APR may be submitted based on the unaudited financial statements certified as such by the statutory auditor of Indian entity or by a CA where statutory audit is not applicable. • In case more than one person resident in India has made ODI, such APR needs to be submitted by a person who is having highest stake in the FE and in the case of equal holding, APR may be filed jointly. **Form FLA:** An Indian entity which has made ODI shall submit FLA within dates as may be specified by RBI [9]. **Changes in ODI:** An Indian entity which has made ODI shall report details regarding acquisition or setting up or winding up or transfer of an SDS or alteration in the shareholding in FE during the year in the APR. **Delay in reporting[10] :** Where there is a delay in reporting of above Forms or submission of share certificate, a person resident in India is liable for 'late submission fee' subject to the conditions mentioned. However, such facility can be availed within a maximum period of three years from the due date of such submission or filing. Further, until and unless such delay is regularised, no further FC whether fund based or not shall be made.

Author's Comments:

- A new set of Forms has been notified replacing old Form ODI. Under new OI Regulations, Form FC has to be filed for investment and disinvestment and Form APR and Form FLA has to be filed annually. Further, Form OPI is notified for investment by way of OPI. However, individual making investment, which is considered OPI, need not to file Form OPI.

- Under the old regulations, in a case where audit is not applicable to FE, APR needs to be submitted based on the unaudited financial statements subject to obtaining of certificate from statutory auditor of the Indian party to state that audit is not applicable. However, in respect of some of the persons viz. partnerships firms, it may not be possible to obtain certificate from statutory authorities as such audit may not be applicable to them.

[9] 15th July of every year.

[10] These provisions are also applicable to compliances which are pending under old regulations

- Under the new OI Regulations, it is provided that certificate needs to be obtained from statutory auditor if such audit is applicable or by CA in other cases.

- Further, under the old regulations, APR may be submitted by stake holder having maximum stake or another person as may be designated. However, under the new regulations, such APR may be submitted by person having highest person and the option of filing by another person is not provided.

Transfer/ Liquidation/ Restructuring	• A person resident in India may transfer equity capital by way of sale to a person resident in India who is eligible to make such investment, or to a person resident outside India.
	
	• A person resident in India may transfer such investment on account of merger, demerger, amalgamation, buyback or liquidation which have approval from competent authority in host country and in India.
	
	• **Disinvestment of ODI:**
	  • In the case of disinvestment of ODI, there should not be any outstanding dues from FE (unless liquidation)
	
	  • Disinvestment shall not be made within in period of 1 year from the date of investment (can be converted into loan).
	
	However, above conditions shall not be applicable in the case merger, demerger or amalgamation between two or more foreign entities that are wholly owned by the Indian entity or where there is no change or dilution in aggregate equity holding of the Indian entity in the merged or demerged or amalgamated entity.
	
	• Further, where the original investment is not permitted under these regulations, subsequent transfer of such investment is treated as contravention of regulations.
	
	Restructuring: An Indian entity which has made ODI may permit restructuring of balance sheet subject to following conditions:
	
	• Restructuring is permitted when such FE is incurring losses from last two years, subject to ensuring compliances with reporting, documentation requirements.
	
	• Diminution in the value of amount due to Indian entity including investment value shall not exceed proportionate amount of accumulated losses.
	
	Where the investment is more than USD 10 million or diminution exceeds 20 percent of the total dues, such diminution in value shall be certified on arm's length basis by a registered valuer under the Companies Act, 2013 or similar valuer registered in the host country.

Author's Comments:

The requirement of certification relating to diminution in value on arm's length basis from a registered valuer under the Companies Act, 2013 or similar valuer registered in the host country, has been brought in in relation to the restructuring..

Part – V Investment in Immovable Property Outside India
 	
Rule 21
	No person resident in India shall acquire or transfer any immovable property located outside India without general or special permission of RBI.
	
	General Permissions:
	• A person resident in India may acquire immovable property outside India by way of inheritance or gift or purchase from a person resident in India who has acquired such property as per the foreign exchange provisions.
	
	• A person resident in India may acquire immovable property located outside India from a person resident outside India:
	  • By way of inheritance.
	  • By way of purchase of such property out of funds held in RFC account.
	  • By way of purchase out of remittance sent under LRS.
	  • Jointly with a relative who is a person resident outside India.
	  • Out of income or sale proceeds of assets, other than ODI, acquired overseas under the provisions of FEM Act,1999.
	
	• An Indian entity having overseas office may acquire immovable property outside India for the business and residential purposes of its staff.
	
	Transfer of immovable property:
	A person resident in India who has acquired immovable property outside India, may transfer such property
	• By way of gift to a person resident in India who is eligible to acquire such property.
	
	• By way of sale.
	
	• Create charge on such immovable property in accordance with Regulations.
	
	Further, where the original investment is not permitted under these regulations, subsequent transfer of such immovable property is treated as contravention of regulations.

	Transactions not covered: In respect of following transaction, these regulations are not applicable: • Immovable property held by a resident in India who is a national of a foreign state. • Immovable property acquired by a resident in India on or before 8th July 1947 and continued to be held by such person with the permission of RBI. • Immovable property acquired by a resident in India on a lease not exceeding 5 years.

Author's Comments:

Provisions relating to Investment in Immovable Property Outside India, have been brought in to the ambit of OI Rules.

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