

FAQs on Overseas Direct Investments

(Updated as on 22nd April, 2019)

Esha Chakraborty

esha@vinodkothari.com

Abhirup Ghosh

abhirup@vinodkothari.com

Table of Contents

1.	<i>What are the governing regulations for making overseas investment?</i>	3
2.	<i>What is Overseas Direct Investment?</i>	3
3.	<i>Can an Indian Party or a resident Individual make investment in any activity?</i>	3
4.	<i>How can an Indian Party make direct investment outside India?</i>	4
5.	<i>What are the limits of ODI?</i>	4
6.	<i>What should be reckoned under 'Total Financial Commitment' by an Indian Party?</i>	5
7.	<i>Whether there are any sub-limits of the ceiling of the total financial commitment?</i>	5
8.	<i>What are the various sources of funding ODI?</i>	5
9.	<i>Can the net worth of subsidiary/holding company of the Indian party be utilized for investing in a JV/WOS abroad?</i>	6
10.	<i>What are the various filing requirements in ODI?</i>	6
11.	<i>Can Indian Parties invest through special purpose vehicles (SPV)?</i>	7
12.	<i>Can Indian Parties set up step-down overseas subsidiaries under the Automatic route?</i>	7
13.	<i>Is ODI in Agricultural Operations permissible?</i>	7
14.	<i>Can an Indian party make overseas investment in Financial Services Sector?</i>	7
15.	<i>Can any Registered Trusts or Societies in India make ODI?</i>	8
16.	<i>Is an Indian Party permitted to extend loan/guarantee on behalf of its overseas JV/WOS?</i>	8
17.	<i>Is an Indian Party permitted to extend loan/guarantee on behalf of step down subsidiaries of its overseas JV/WOS?</i>	8

18.	<i>Can resident individual promoters issue personal guarantee on behalf of the overseas JV/ WOS?</i>	9
19.	<i>Is an Indian Party allowed to invest in any foreign security without the limits?</i>	9
20.	<i>Is an Indian Party allowed to undertake financial commitment, without equity contribution?.....</i>	9
21.	<i>Are there any separate requirements for making investment by way of exchange for shares of a foreign company?</i>	9
22.	<i>What all parameters does RBI consider while evaluating such applications?.....</i>	10
23.	<i>How to make investments by way of capitalisation?</i>	10
24.	<i>Can an Indian Party transfer its holding in an overseas JV/WOS?</i>	11
25.	<i>Can the Indian Party transfer any holding in an overseas JV/WOS, involving write-offs?</i>	11
26.	<i>Can an Indian Party create charge on its properties or financial assets in favour of overseas JV/WOS?.....</i>	12
27.	<i>What are the obligations of an Indian party making ODI?</i>	12
28.	<i>Can resident individuals, in any manner, invest in foreign entities?.....</i>	13
29.	<i>How can resident Individuals make direct investments in overseas JVs and WOS?13</i>	
30.	<i>How are Compulsorily Convertible Preference Shares (CCPS) treated for the purpose of ODI?</i>	14
31.	<i>Can investment be made in overseas JV/WOS by way of Share Swaps?.....</i>	14
32.	<i>Can overseas investments be made by Domestic Venture Capital Funds (VCF)? .14</i>	
33.	<i>Can Indian Parties invest in foreign entities other than by way of direct investments?.....</i>	14

The very concept of Overseas Direct Investments has been looked upon with a lot of curiosity and apprehension, at the same time! The governing body, Reserve Bank of India has also never failed to surprise us with the intricacies in its guidelines.

While each case of such investment(s) has to be dealt separately based on its structure; with the following questions, we seek to understand the basic ground rules -

1. What are the governing regulations for making overseas investment?

Direct investments outside India by residents in Joint Venture (JV)/ Wholly Owned Subsidiary (WOS) are allowed in terms of Section 6(3)(a) of the Foreign Exchange Management Act, 1999 read with Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 (“**FEMA Regulations**”), as amended from time to time.

Further, on 1st January, 2016, RBI came up with the [Master Directions- Direct Investment by Residents in Joint Venture \(JV\) / Wholly Owned Subsidiary \(WOS\) Abroad](#) (“**Master Directions**”) as amended from time to time, that consolidates all Notifications/ Circulars issued earlier in this regard as mentioned in the Appendix to the Master Directions.

2. What is Overseas Direct Investment?

Overseas Direct Investments (ODI) refers to the investments made in the overseas entities by way of contribution to their capital or subscription to the Memorandum of Association of a foreign entity (JV/ WOS) or by way of purchase of existing shares of a foreign entity (JV/ WOS) either by market purchase or private placement or through stock exchange signifying a long-term interest in the foreign entity (JV/ WOS), but it does not include portfolio investment.

3. Can an Indian Party¹ or a resident Individual make investment in any activity?

Yes, with effect from 5th August, 2013, a resident individual satisfying the conditions mentioned in the Master Direction may make overseas investment in the equity shares and compulsorily convertible preference shares of a JV or WOS outside India with the ceiling limits mentioned in the Liberalised Remittance Scheme, as prescribed by the RBI from time to time.

Further, an Indian party shall not make any direct investment in a foreign entity engaged in real estate or banking sector.

¹ “‘Indian Party’ means a company incorporated in India or a body created under an Act of Parliament or a partnership firm registered under the Indian Partnership Act, 1932 or a Limited Liability Partnership (LLP) registered under the Limited Liability Partnership Act, 2008 making investment in a Joint Venture or Wholly Owned Subsidiary abroad, and includes any other entity in India as may be notified by the Reserve Bank: - Provided that when more than one such company, body or entity make an investment in the foreign entity, all such companies or bodies or entities shall together constitute the ‘Indian Party’”.

Investments in Real estate sector would include buying and selling of real estate or trading in Transferable Development Rights (TDRs) but does not include development of townships, construction of residential/commercial premises, roads or bridges.

4. How can an Indian Party make direct investment outside India?

An Indian Party can make direct investment in a Joint Venture² or Wholly Owned Subsidiary³ outside India. The conditions for making such investment are as under:

- (i) The total financial commitment of the Indian Party in Joint Ventures / Wholly Owned Subsidiaries shall not exceed 400%, or as decided by the Reserve Bank from time to time, of the net worth of the Indian Party as on the date of the last audited balance sheet;
- (ii) The direct investment should be made in an overseas JV or WOS engaged in a bonafide business activity;
- (iii) The Indian Party should not be on the Reserve Bank's Exporters caution list /list of defaulters to the banking system circulated by the Reserve Bank or Credit Information Bureau (India) Ltd. (CIBIL) or any other credit information company or under investigation by any investigation /enforcement agency or regulatory body;
- (iv) The Indian Party must have submitted its Annual Performance Report in respect of all its overseas investments in the format given in Part III of the Form ODI;
- (v) The Indian Party must route all transactions relating to the investment in a Joint Venture/Wholly Owned Subsidiary through only one branch of an authorised dealer⁴ to be designated by it.
- (vi) The Indian Party must submit Part I of the Form ODI, duly completed, to the designated branch of an authorised dealer.

5. What are the limits of ODI?

The 'Total Financial Commitment' by an Indian Party in its Joint Venture company (JV) /Wholly-owned subsidiary (WOS) outside India should not exceed 400% of net worth of the Indian Party. The 'net worth' should be as per the last audited balance sheet of the Indian Party.

² means a foreign 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

³ means a foreign entity formed, registered or incorporated in accordance with the laws and regulations of the host country, whose entire capital is held by the Indian party

⁴ The Indian Party may designate different branches of authorised dealers for different Joint Ventures/Wholly Owned Subsidiaries outside India.

6. What should be reckoned under 'Total Financial Commitment' by an Indian Party?

For the purpose of determining 'Total Financial Commitment' within the said limit of net worth, the following should be considered –

- a. 100% of the amount of equity shares and/ or Compulsorily Convertible Preference Shares (CCPS);
- b. 100% of the amount of other preference shares;
- c. 100% of the amount of loan;
- d. 100% of the amount of guarantee (other than performance guarantee) issued by the Indian Party;
- e. 100% of the amount of bank guarantee issued by a resident bank on behalf of JV or WOS of the Indian Party provided the bank guarantee is backed by a counter guarantee / collateral by the Indian Party.
- f. 50% of the amount of performance guarantee issued by the Indian Party provided that if the outflow on account of invocation of performance guarantee results in the breach of the limit of the financial commitment in force, prior permission of the Reserve Bank is to be obtained before executing remittance beyond the limit prescribed for the financial commitment.

7. Whether there are any sub-limits of the ceiling of the total financial commitment?

No, there are no sub-limits of the total financial commitment. The overall ceiling of the total financial commitment is 400% of the net worth of the Indian Party which may consist of equities, preference shares, loans, guarantees, etc.

8. What are the various sources of funding ODI?

Indian Parties may invest out of one or more of the following sources –

- i. Out of balance held in the Exchange Earners Foreign Currency account of the Indian Party maintained with the Authorised Dealer.

Provided that the ceiling of 400% of net worth shall not apply where the investment is made out of balances held in its EEFC account, maintained in accordance with the Master Directions.

- ii. Drawal of foreign exchange from an authorised dealer in India

- iii. Capitalisation of exports;
- iv. Utilisation of the amount raised by issue of ADRs/GDRs by the Indian party;
- v. External Commercial Borrowing in conformity with other parameters of the ECB guidelines;
- vi. Proceeds of Foreign Currency Convertible Bonds (FCCBs);
- vii. Swap of shares;
- viii. ADR/GDR Stock Swap subject to the valuation norms and sectoral cap;

9. Can the net worth of subsidiary/holding company of the Indian party be utilized for investing in a JV/WOS abroad?

For the purpose of determining the net worth of an Indian party, the net worth of its holding company (at least 51% stakeholding in the Indian Party) or its subsidiary company (at least 51% stakeholding by the Indian party) may be taken into account to the extent not availed of by the holding company or the subsidiary independently and has furnished a letter of disclaimer in favour of the Indian Party.

10. What are the various filing requirements in ODI?

Following are the filing requirements in ODI:

- a. Form ODI Part I – Application for making overseas direct investments and reporting of Remittances/ Transactions to be submitted by the applicant to the RBI.
- b. Form ODI Part II – Annual Performance Report (APR) – To be submitted, certified by Statutory Auditors of the Indian party, through the designated AD Category– I bank every year by June 30th as long as the JV / WOS is in existence.
- c. Form ODI Part III – Report on disinvestment by way of closure/ voluntary liquidation, winding up of the JV/WOS abroad/ sale / transfer of the shares of the overseas JV/ WOS to another eligible resident or non-resident/ Buy back of shares by the overseas JV/ WOS of the IP / RI .

- d. Annual Return on Foreign Liabilities and Assets – All the Indian Parties having ODI have to file the FLA return every year by July 15⁵.

11. Can Indian Parties invest through special purpose vehicles (SPV)?

Direct Investments for the sole purpose of investing in overseas JV/WOS are allowed to be made through SPV under the Automatic route provided the Indian Party is not under the caution list of RBI or under any investigation by the Directorate of Enforcement or included in the list of defaulters to the banking system/ any other Credit Information company.

12. Can Indian Parties set up step-down overseas subsidiaries under the Automatic route?

Yes, within the prescribed investment limits, the Indian Parties can set up overseas step down subsidiaries under the Automatic route. But where the Indian Party wishes to set up overseas subsidiaries in financial services sector, it also has to comply with additional requirements, as stated hereunder in [FAQ 14](#).

13. Is ODI in Agricultural Operations permissible?

Yes. However, the following should be ensured while making ODI in Agricultural Operations:

- a) A person resident in India, being a company incorporated in India or a partnership firm registered under the Indian Partnership Act, 1932, are permitted to undertake agricultural operations including purchase of land incidental to such activity either directly or through their overseas offices;
- b) The Indian Party is otherwise eligible to make the ODI and such investments is within the prescribed limits;
- c) For the purpose of acquisition of land, the same should be valued by certified valuers registered with the appropriate valuation authority in the host country.

14. Can an Indian party make overseas investment in Financial Services Sector?

Yes. Only an Indian Party rendering financial services, subject to the following conditions, may invest in overseas Financial Service Sector:

- a) has earned net profits in preceding 3 financial years from financial services activities;

⁵ The format went for a revision vide RBI's circular dated 18th June, 2014 and the same can be viewed here: https://rbidocs.rbi.org.in/rdocs/Forms/PDFs/FLR180614FL_A.PDF

- b) is registered with the regulatory authority in India to conduct financial services activities;
- c) approvals have been accorded from the regulatory authorities of both the countries, India and abroad, for venturing into such financial services sector;
- d) has complied with the prudential norms relating to capital adequacy, as set by the regulatory authority in India.

It's to be noted, any additional investment by an existing JV / WOS or its step down subsidiary in the financial services sector is also required to comply with the above conditions.

15. Can any Registered Trusts or Societies in India make ODI?

Essentially, no.

Only the registered Indian Trusts and Societies engaged in manufacturing/educational activities and which have set up hospital(s) in India, as per the criteria laid down under the Regulations, may invest in the same sector(s) through overseas JV/WOS after taking RBI's approval.

16. Is an Indian Party permitted to extend loan/guarantee on behalf of its overseas JV/WOS?

Yes. The Indian Party may extend loan or a guarantee to or on behalf of its JV/WOS abroad, subject to the following –

- i. the same should be within the permissible financial commitment limits;
- ii. the Indian Party has made the investment by way of contribution to the equity capital of the Joint Venture.

17. Is an Indian Party permitted to extend loan/guarantee on behalf of step down subsidiaries of its overseas JV/WOS?

An Indian Party may extend corporate guarantee on behalf of its first generation step down operating company within the prevailing limit for overseas direct investment.

Explanation: Issue of corporate guarantee on behalf of second level or subsequent level step down operating subsidiaries will be considered under the Approval Route, provided the Indian Party indirectly holds 51 per cent or more stake in the overseas subsidiary for which such guarantee is intended to be issued.

18. Can resident individual promoters issue personal guarantee on behalf of the overseas JV/ WOS?

The indirect resident individual promoters of the Indian party may issue personal guarantee on behalf of the overseas JV / WOS of the Indian party provided the provisions under para B. 1 of the Master Directions are fulfilled by the Indian party and further provided that:

a) total 'financial commitment' including all forms of guarantees remains within the overall ceiling stipulated for overseas investment by an Indian Party and

b) no guarantee is 'open ended'

19. Is an Indian Party allowed to invest in any foreign security without the limits?

Where an Indian Party utilizes the proceeds of its international offering of shares through the mechanism of ADR and/or GDR, it is allowed to make direct investment without any limit in any foreign security with such proceeds. Provided, that –

(a) the ADR/GDR issue has been made in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (through Depository Receipt Mechanism) Scheme 1993 and the guidelines issued thereunder from time to time by the Central Government;

(b) the Indian Party files with the designated Authorized dealer full details of such investment proposal.

20. Is an Indian Party allowed to undertake financial commitment, without equity contribution?

An Indian party may, with prior approval of RBI, undertake financial commitment⁶ without equity contribution in JV / WOS provided it is as per the business requirement of the Indian party and also as per the legal requirement of the host country.

21. Are there any separate requirements for making investment by way of exchange for shares of a foreign company?

Application is to be made in Part I of the Form ODI.

⁶ means the the amount of direct investment by way of contribution to equity, loan and 100 per cent of the amount of guarantees and 50 per cent of the performance guarantees issued by an Indian party to or on behalf of its overseas Joint Venture Company or Wholly Owned Subsidiary.

(a) for the purpose of investment by way of remittance from India, in an existing company outside India, shall be accompanied, by the valuation of shares of the company outside India, made-

(i) where the investment is more than USD 5 (five) million, by a Category I Merchant Banker registered with SEBI or an Investment Banker/Merchant Banker registered with the appropriate regulatory authority in the host country; and

(ii) in all other cases, by a Chartered Accountant or a Certified Public Accountant.

(b) for the purposes of investment by acquisition of shares of an existing company outside India where the consideration is to be paid fully or partly by issue of the Indian party's shares, shall be accompanied by the valuation carried out by a Category I Merchant Banker registered with the SEBI or an Investment Banker/Merchant Banker registered with the appropriate regulatory authority in the host country.

22. What all parameters does RBI consider while evaluating such applications?

The parameters for evaluation have been mentioned below:

- a. Prima facie viability of the Joint Venture/Wholly Owned Subsidiary outside India;
- b. Contribution to external trade and other benefits which will accrue to India through such investment;
- c. Financial position and business track record of the Indian Party and the foreign entity;
- d. Expertise and experience of the Indian Party in the same or related line of activity of the Joint Venture or Wholly Owned Subsidiary outside India.

23. How to make investments by way of capitalisation?

Subject to the Regulations, the Indian Party may invest outside India by way of capitalisation of amount due to the Indian Party from the foreign entity, partly or fully towards –

- a. Payment for export of plant and machinery, equipment and other goods/services to the foreign entity;
- b. Fees, royalty, commission or other entitlements due to the Indian Party from the foreign entity for the supply of the technical knowhow, consultancy, managerial and other services.

In this regard, an Indian software exporter may receive upto 25% of the value of exports in the form of shares to an overseas software startup company without entering into JV agreement by filing an application with the RBI, through the Authorized Dealer.

But, where such export proceeds have remained unrealized beyond the prescribed time limit of realization and fees, royalties, commissions or other entitlements of the Indian Party have remained unutilized from the date on which such payment is due, any such proceeds shall not be capitalised except prior approval of the RBI.

24. Can an Indian Party transfer its holding in an overseas JV/WOS?

Yes. An Indian Party may transfer, by way of sale, any share or security held by it in an overseas JV or WOS to another Indian Party which complies with the provisions of the Regulations or to a person resident outside India, subject to the following conditions:

- i. the sale does not result in any write off of the investment made;
- ii. the sale is to be effected through a stock exchange where the shares of the overseas JV/ WOS are listed;
- iii. if the shares are not listed on the stock exchange and the shares are disinvested by a private arrangement, the share price is not less than the value certified by a Chartered Accountant / Certified Public Accountant as the fair value of the shares based on the latest audited financial statements of the JV/WOS;
- iv. the Indian Party does not have any outstanding dues by way of dividend, technical know-how fees, royalty, consultancy, commission or other entitlements and/or export proceeds from the JV or WOS;
- v. the overseas concern has been in operation for at least one full year and the Annual Performance Report together with the audited accounts for that year has been submitted to the Reserve Bank;
- vi. the Indian party is not under investigation by CBI / DoE / SEBI / IRDA or any other concerned regulatory authority in India.

Where an Indian party does not satisfy the criteria specified above, it shall apply to RBI for permission to transfer by way of sale of shares of a JV/WOS outside India.

25. Can the Indian Party transfer any holding in an overseas JV/WOS, involving write-offs?

Where the transfer by way of sale of shares or security as referred in [FAQ 24](#) by any Indian Party listed on any Indian stock exchange(s), is for a price lesser than the amount invested in

the share or the security transferred, the Indian party may write-off capital invested subject to the following circumstances –

- i. where the difference between the said value and the sale price does not exceed the percentage approved by the RBI, from time to time, of the Indian Party's actual export realisation of the previous year, the Indian party may write-off to the extent of the difference, the capital invested in the overseas JV/WOS;
- ii. where such difference is more than the percentage approved by the RBI, from time to time, of the Indian Party's actual export realisation of the previous year, the Indian Party shall apply for prior approval of RBI to write-off the capital invested.

26. Can an Indian Party create charge on its properties or financial assets in favour of overseas JV/WOS?

Yes. The Indian Party may create a charge, by way of mortgage/ pledge/ hypothecation, on its movable/ immovable properties or financial assets (*except shares of JV/WOS*) or that of its Group companies in favour of the overseas JV/WOS, to avail financial/non-financial facility from an authorised dealer bank or a public financial institution in India or to an overseas lender, subject to the following –

- i. the Indian Party is required to obtain prior permission from the RBI;
- ii. the lender is regulated and supervised as a bank;
- iii. the total financial commitment of the Indian Party remains within the limit stipulated by the RBI for overseas investments in JV/WOS; and
- iv. a 'No Objection' is submitted by the Indian party and its Group companies from their resident lenders.

27. What are the obligations of an Indian party making ODI?

An Indian Party which has made ODI in securities of the overseas JV/WOS shall –

- a. receive the share certificates within 6 months from the date of making investments;
- b. repatriate to India, all dues receivable from the foreign entity, like dividend, royalty, technical fees etc., within 60 days of its falling due, or such further period as the Reserve Bank may permit;

- c. submit to the RBI, through an Authorised Dealer, on or before a specified date, an Annual Performance Report in respect of each overseas JV/WOS of the Indian Party based annual audited accounts of the preceding years;
- d. have to submit an Annual Return on Foreign Assets and Liabilities in specified format by a specified time to the RBI.

28. Can resident individuals, in any manner, invest in foreign entities?

Individuals resident in India may invest by way of purchasing/acquiring shares of a foreign entity as a part/full consideration for rendering professional services or in lieu of director's remuneration.

However, the aforesaid manner of acquiring such shares in terms of value shall be within the overall ceiling limit as prescribed for the resident individuals under the Liberalized Remittance Scheme (LRS) in force at the time of acquisition.

In case the value of shares exceeds the limit mentioned under the LRS, such shares are to be acquired after the consent of the RBI.

29. How can resident Individuals make direct investments in overseas JVs and WOS?

An Individual resident in India may also invest directly through equity or compulsorily convertible preference shares in overseas JVs/ WOS either singly or in association with other resident individuals or with an Indian Party, subject to the following conditions:

- a. investments made abroad should not be in entities engaged in the business of real estate, banking or business of providing financial services.
- b. investments should not be made in the entities situated in the countries identified as "non-co-operative countries and territories" by the Financial Action Task Force (FATF).
- c. the Individual should not be on the Exporter's Caution List or List of Defaulters to the banking system.
- d. investments should be made within the ceiling of LRS. The investments made out of the balance in the EEFC/ RFC account shall also be counted while considering the ceiling under the LRS.
- e. the Individual is allowed to make investments in an operating entity only and no step down subsidiary is allowed to be acquired or set up by the JV/ WOS.

30. How are Compulsorily Convertible Preference Shares (CCPS) treated for the purpose of ODI?

The CCPSs are treated at par with equity shares and the Indian Parties are allowed to make ODI in overseas JV/WOS by way of investments in CCPSs.

However, apart from the CCPS, all other types of preference shares are to be treated as loan extended by the Indian party to its JV/WOS abroad and compliance to the provisions of FEMA Regulations needs to be adhered to.

31. Can investment be made in overseas JV/WOS by way of Share Swaps?

Yes. Direct investment outside India in a JV/WOS by way of share swap arrangement can be made under the automatic route after complying with the valuation norms prescribed i.e. valuation of the shares is done by a Category I Merchant Banker registered with the SEBI or an Investment Banker outside India registered with the appropriate Regulatory Authority in the host country are satisfied, and the shares are duly issued / transferred in the name of the Indian investing company.

32. Can overseas investments be made by Domestic Venture Capital Funds (VCF)?

VCFs registered with SEBI may invest in the overseas VCFs by way of subscribing to the equity or equity linked instruments and such other terms and conditions prescribed by the SEBI from time to time.

33. Can Indian Parties invest in foreign entities other than by way of direct investments?

Yes, a Listed Indian Company may invest up to 50% of their net worth, as per its last audited balance sheet, in overseas companies listed on a recognised stock exchange or in rated debt securities issued by such overseas companies.

To view our other articles on this matter, click [here](#)

To view our other articles, click [here](#)