Ministry of Commerce and Industry releases
Draft Press Note (2010) on FDI Regulatory Framework

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Over the last few months, all the legislations, regulations and regulatory guidelines are being recasted and redrafted. After the redrafting of SEBI DIP Guidelines, it was the need of the hour to bring out some developments in the area of Foreign Investment also. Union Minister of Commerce and Industry has released the Draft Press Note (2010) encompassing significant aspects of FDI Policy and FDI Regulatory Framework on 25th December 2009. The full text of the draft is available at http://www.dipp.nic.in/FDI_Manuals/FDIRegulatory_Framework_24December2009.pdf

Comments are invited on the said draft Press Note by 31st January, 2010, so that the Govt. of India can take a consolidated view on the same and come out with the final note on 31st March / 1st April, 2010.

This draft Press Note is mere a consolidation exercise for facilitating comprehensive reading by the investors and it does not aim at bringing out changes in the extant policies and procedures. It enlists all prior regulations on FDI. However, areas left out will continue to be dealt in the current way where it is listed. The motive is to ensure transparency and clarity in the understanding of regulations and to promote investment friendliness by reducing unnecessary strains.

This Press Note (rescinding all earlier press notes on FDI) will have a sunset clause of 6 months and will be replaced by a new Press Note at the end of every 6 months. It will incorporate and reflect all the changes in the regulations during the last intervening period of six months.

FDI Regulatory Framework- A synopsis:

Foreign Direct Investment in India is governed by the Government of India and Reserve bank of India under the FEMA 1999 and its various regulations. To keep pace with the dynamic scenario, Govt. of India and RBI from time to time bring about necessary amends in the extant regulatory framework by way of new Acts, Regulations, Press Notes, Press Releases, Clarifications, etc.

The said draft is divided into 5 Chapters:

- Chapter 1 of the said draft lays down various definitions of the terms used therein.
- Chapter 2 deals with Source, Type, Eligibility, conditions and Issue/ Transfer of Investment

- Chapter 3 encompasses Calculation, Entry route, Caps, Conditions, etc. of Investment
- Chapter 4 enlists Policy on Route, Caps and Conditions
- Chapter 5 covers Remittance, Reporting, Violation and Acquitition of Immovable Property

Some of the significant aspects are summarized hereinbelow:

Chapter 2: Source, Type, Eligibility, conditions and Issue/ Transfer of Investment

Persons eligible:
All non- resident entities or entities incorporated outside India (other than that of Pakistan) is eligible to make investment under the FDI route. However citizens of Bangladesh and entities incorporated in Bangladesh can invest the FDI- Government route only. Further, NRI's, resident in Nepal and Bhutan as well as citizens of Nepal and Bhutan are permitted to invest in shares and convertible debentures of Indian companies on repatriation basis, subject to the conditions specified.

An FII may invest in a particular share issue of an Indian company either under the FDI Scheme or the Portfolio Investment Scheme.

Types of instruments:
Issue of equity shares, fully and mandatorily convertible debentures and fully and mandatorily convertible preference shares, which are in the nature of equity are covered within the ambit of FDI. However, issue of other types of preference shares such as non-convertible, optionally convertible or partially convertible, have to be in accordance with the guidelines applicable for External Commercial Borrowings (ECBs).

Provisions relating to Issue of shares by companies under FCCB/ ADR/ GDR are also covered.

Issue of Equity Instruments:
The equity instruments should be issued within 180 days from the date of receipt of the inward remittance or by debit to the NRE/FCNR (B) account of the non-resident investor or the amount of consideration so received should be refunded immediately.

Issue price of shares:
Price of shares issued to persons resident outside India under the FDI Regulations, shall be on the basis of SEBI guidelines in case of listed companies. In case of unlisted companies, valuation of shares has to be done by a Chartered Accountant in accordance with the guidelines issued by the erstwhile Controller of Capital Issues (CCI).

Foreign Currency Account:
Indian companies which are eligible to issue shares to persons resident outside India under the FDI Regulations will be allowed to retain the share subscription amount in a Foreign Currency Account, with the prior approval of RBI.

Other Areas:
This chapter further discusses-
- Eligibility criteria for investment in resident entities as Indian Company/ Partnership Firm / Proprietary Concern/ Trusts and other Entities.
- Conditions on Transfer of Shares and convertible debentures
- Conversion of ECB/Lumpsum Fee/Royalty/Import of capital goods by SEZs into Equity.
- Issue of Rights/Bonus Shares
- Acquisition of shares under Scheme of Merger/Amalgamation
- Issue of shares under Employees Stock Option Scheme (ESOPs)

Chapter 3: Calculation, Entry Route, Caps, Conditions, etc. of Investment

Calculation of total foreign investment i.e. Direct and indirect foreign investment in Indian companies:
Investment in Indian companies can be made both by non-resident as well as resident Indian entities. Any non-resident investment in an Indian company is direct foreign investment. Investment by resident Indian entities could again comprise of both resident and non-resident investment. Thus, such an Indian company would have indirect foreign investment if the Indian investing company has foreign investment in it. The indirect investment can be a cascading investment i.e. through multi-layered structure also. Guidelines for calculation of total foreign investment i.e. direct and indirect foreign investment in an Indian company have been detailed therein.

Entry routes for investment:
Investments can be made by non-residents in the shares/convertible debentures/preference shares of an Indian company, through two routes;
- Automatic Route
- Approval Route.

Under the Automatic Route, the foreign investor or the Indian company does not require any approval from the Reserve Bank or Government of India for the investment. Under the Government Route, prior approval of the Government of India through Foreign Investment Promotion Board (FIPB) is required.

Caps on Investments
Investments can be made by non-residents in the capital of an Indian entity only to the extent of the percentage of the total capital. Thus investment can be prohibited in some sectors/activities or their can be a restriction through a CAP on the investment for other sector/activities ,while in others there may not be any restrictions and the total 100% capital can be held by non resident entities.

Other areas:

- Guidelines for Downstream Investment by Indian Companies
- Guidelines for consideration of FDI proposals by FIPB
- Constitution of FIPB

Chapter 4: Policy on Route, Caps and Conditions:

This chapter lays down the areas wherein FDI is prohibited and the Sectoral Caps.

Chapter 5: Remittance, Reporting, Violation and Acquitition Of Immovable Property

Repatriation of Dividend:
Dividends are freely repatriable without any restrictions.

Reporting of Inflow

(i) An Indian company receiving investment from outside India for issuing shares / convertible debentures / preference shares under the FDI Scheme, should report the details of the amount of consideration to the Regional Office concerned of the Reserve Bank not later than 30 days from the date of receipt in the Advance Reporting Form enclosed in Annex.

(ii) Indian companies are required to report the details of the receipt of the amount of consideration for issue of shares / convertible debentures, through an AD Category – I bank, together with a copy/ies of the FIRC/s evidencing the receipt of the remittance along with the KYC report (enclosed as Annex) on the non-resident investor from the overseas bank remitting the amount. The report would be acknowledged by the Regional Office concerned, which will allot a Unique Identification Number (UIN) for the amount reported.

Reporting of issue of shares
After issue of shares (including bonus and shares issued on rights basis) and shares issued under ESOP)/fully and mandatorily convertible debentures / fully and mandatorily convertible preference shares, the Indian company has to file Form FCGPR, enclosed in Annex, not later than 30 days from the date of issue of shares.

Other Areas:
Further it details the Guidelines/ Orders and Consequences of Violation, Penal provisions, provisions relating to Adjudication & Appeals and Compounding Proceedings.

Surely, this is an attempt worth appreciating.