

Regulatory Alert

August 17, 2021



Draft rules/regulations on Overseas Direct Investment

The Reserve Bank of India, on 09th August 2021 issued draft rules/regulations regarding Overseas Direct Investment and has sought feedback on the same or before 23 August 2021.

Background

- Presently, Overseas Direct Investment (ODI) is governed by the Foreign Exchange Management (Transfer Or Issue Of Any Foreign Security) Regulations, 2004¹
- Post the amendment to Section 6 to Foreign Exchange Management Act, 1999 by the Finance Act, 2015 the power to issue regulations for other than debt instruments had been shifted to the Central Government.
- In exercise of those powers, Central Government issued new rules relating to Foreign Direct Investment (FDI) in 2019. Since then discussions have been going on to revamp the regulations governing ODI.
- On 09 August 2021, the Reserve Bank of India issued draft Foreign Exchange Management (Non-debt Instruments - Overseas Investment) Rules, 2021 and the draft Foreign Exchange Management (Overseas Investment) Regulations, 2021 and has sought comments on or before 23 August 2021.
- As per the RBI, the objective of these changes is “to further liberalise regulatory framework and also to promote ease of doing business, it has been decided to rationalize the existing provisions governing overseas investment”. Following are the salient features of changes proposed in the draft Rules/Regulations.

¹ As amended from time to time



The Proposed Changes

Changes in definition

- The definition of Overseas Direct Investment has been expanded to include (i) investment of more than 10% in a listed foreign entity, (ii) foreign entity where a person resident in India has invested and has control or has acquired control.
- The existing regulations did not define what constitutes a '**portfolio investment**'. The draft rules define Overseas Portfolio Investment (**OPI**) as investment, other than ODI, in foreign securities, units of ETF, Depository receipts which are listed on an overseas stock exchange.

Extension of loan to overseas Entity

- Going forward lending by an Indian entity to a foreign entity must be backed by a loan agreement and the interest thereon must be at Arms' Length Price (**ALP**).

Round Tripping

- The draft rules also provide that investment by a resident person in a foreign entity that has invested or invests into India (directly or indirectly) – popularly known as "**Round Tripping structure**" will be prohibited if the transaction is designed for tax evasion or tax avoidance.

Requirement of NoC for ODI

- Where a person resident in India desirous to make any investment or disinvesting such investment has an account appearing as a Special Mention Account-1/2 or non-performing asset or wilful defaulter or is under investigation by a regulatory body or investigative agencies in India, an NoC from the concerned authorities would be necessary before making an investment or undertaking disinvestment. If the NoC is not provided within 60 days it will be presumed that they do not have any objections. Such investigative agency includes the income-tax department.

Restricted sectors and clarification on leasing activity

- The investment in a foreign entity engaged in (i) Real estate activity; (ii) Gambling in any form; and (iii) Offering financial products linked to Indian Rupee except for products offered in IFSC is prohibited.
- Under the extant regulations, the leasing of real estate abroad by an overseas entity was considered as "real estate activity" even when the definition of Real Estate Business was silent. The draft rules now clarify that real estate activity will not include leasing.

Investment through a Special Purpose Vehicle (SPV)

- As per the current regulation ODI can be done through a SPV abroad, however, a view is prevalent that the investment can be routed only through one SPV (*because of the use of 'a' before the term SPV*) in an operating entity. The draft Rules/Regulations seems to have done away with such condition.

The price band of 5% while computing fair value

- The draft Rules/Regulations also provides that in the case of acquisition or disinvestment of shares of a overseas unlisted company by a person resident in India, the transaction price can be within the 5% range of fair value arrived on ALP basis.

Deferred Consideration

- The extant regulations do not provide for deferred consideration. The draft Rules/Regulations have introduced a concept of deferred payment in ODI transactions.

Restructuring balance sheet

- In the current regulations, the permission to restructure the balance sheet of a foreign entity is available only for listed entities under automatic route. In the draft



Rules/Regulations, the said permission has been extended to all Indian entities (*listed as well as unlisted limited*).

Change-related to Forms and reporting

New Form

- Form ODI will be replaced with Form FC – the content of the form is not yet provided.
- Form OPI has been introduced for Overseas Portfolio Investment.

Changes in Filing of APR form:

- Going forward Form APR will have to be filed within 6 months from the end of the accounting period of the foreign entity.
- Filing of Form APR is not required where (i) where there is only one Indian resident investor in a foreign entity and (ii) such resident investor neither has control nor holds more than 10% equity shares.
- In case more than one Indian resident has invested in the same foreign entity the Form APR has to be filed by a person resident in India having the highest stake in the foreign entity.

Delay in reporting and Late Submission Fee (LSF)

- The draft Rules/Regulations provide that additional overseas investments are not permissible until the delay in reporting (if any) is regularized.
- To regularize the delay in reporting the option of Late Submission Fee (LSF) is proposed. The matrix for computation of LSF is yet to be prescribed.

Changes for investment by resident Individuals

- In the case of investment by resident Individuals, there are no substantial changes except it is now clarified that remittance towards ESOP or sweat equity shares will be within the overall limit of LRS.

- Gift of shares by a non-resident to an Indian individual – As per the current regulations, an individual resident in India can receive shares of a foreign company by way of a gift from a non-resident. However, in the draft rules, this has been restricted and the gift of foreign shares is permitted only from non-resident relatives.

Dhruva Comments

The changes proposed by the draft Rules/Regulations are welcome and provide much-needed clarification on quite a few issues such as real estate leasing, permitting deferred consideration, the five per cent range for valuations, including on 'round-tripping'; however, clarity on what constitutes Tax Avoidance/Evasion, who determines it and does this mean round trip structures are now under the automatic route, require further clarity.

There are also a few questions around the use of LRS for properties and securities by individuals and whether the same is now exclusively covered by the draft Rules/Regulations or whether the LRS route remains unaffected, that require clarification. One will need to review the final Rules/Regulations duly updated after factoring in the feedback from the stakeholders.

If you have any points on which clarification is required, do reach out to us.

Contributors:

[Venkatraman Iyer \(Principal\)](#)

[Sagar Joshi \(Senior Associate\)](#)

For any queries in relation to this regulatory alert, please feel free to reach out.



ADDRESSES

Mumbai

One World Center, 11th floor,
Tower 2B, 841, Senapati Bapat Marg,
Elphinstone Road (West),
Mumbai 400013
Tel: +91 22 6108 1000 / 1900

Ahmedabad

B3, 3rd Floor, Safal Profitaire,
Near Auda Garden,
Prahlanagar, Corporate Road,
Ahmedabad 380015
Tel: +91-79-6134 3434

Bengaluru

Prestige Terraces, 2nd Floor
Union Street, Infantry Road,
Bengaluru 560001
Tel: +91-80-4660 2500

Delhi / NCR

101 & 102, 1st Floor, Tower 4B
DLF Corporate Park
M G Road, Gurgaon
Haryana 122002
Tel: +91-124-668 7000

Pune

305, Pride Gateway, Near D-Mart, Baner,
Pune 411 045
Tel: +91-20-6730 1000

Kolkata

4th Floor, Unit No 403, Camac Square,
24 Camac Street, Kolkata
West Bengal 700016
Tel: +91-33-66371000

Singapore

Dhruva Advisors (Singapore) Pte. Ltd.
20 Collyer Quay, #11-05
Singapore 049319
Tel: +65 9105 3645

Dubai

WTS Dhruva Consultants
Emaar Square Building 4, 2nd Floor,
Office 207, Downtown,
P.O. Box 127165
Dubai, UAE
Tel: +971 4 240 8477

KEY CONTACTS

Dinesh Kanabar

Chief Executive Officer
dinesh.kanabar@dhruvaadvisors.com

Mehul Bheda (Mumbai/Ahmedabad)

mehul.bheda@dhruvaadvisors.com

Ajay Rotti (Bengaluru)

ajay.rotti@dhruvaadvisors.com

Vaibhav Gupta (Delhi/NCR)

vaibhav.gupta@dhruvaadvisors.com

K. Venkatachalam (Pune)

k.venkatachalam@dhruvaadvisors.com

Aditya Hans (Kolkata)

aditya.hans@dhruvaadvisors.com

Mahip Gupta (Singapore)

mahip.gupta@dhruvaadvisors.com

Nimish Goel (Dubai)

nimish.goel@dhruvaadvisors.com

Dhruva Advisors has been consistently recognised as the **“India Tax Firm of the Year”** at the ITR Asia Tax Awards in 2017, 2018, 2019 and 2020.

Dhruva Advisors has also been recognised as the **“India Disputes and Litigation Firm of the Year”** at the ITR Asia Tax Awards 2018 and 2020.

WTS Dhruva Consultants has been recognised as the **“Best Newcomer Firm of the Year”** at the ITR European Tax Awards 2020.

Dhruva Advisors has been recognised as the **“Best Newcomer Firm of the Year”** at the ITR Asia Tax Awards 2016.

Dhruva Advisors has been consistently recognised as a **Tier 1 Firm in India for General Corporate Tax** by the International Tax Review's in its World Tax Guide.

Dhruva Advisors has been consistently recognised as a **Tier 1 Firm in India for Indirect Taxes** in International Tax Review's Indirect Tax Guide.

Dhruva Advisors has also been consistently recognised as a **Tier 1 Firm in India for its Transfer Pricing** practice ranking table in ITR's World Transfer Pricing guide

Disclaimer:

This information contained herein is in summary form and is therefore intended for general guidance only. This publication is not intended to address the circumstances of any particular individual or entity. No one should act on such information without appropriate professional advice after a thorough examination of the particular situation. This publication is not a substitute for detailed research and opinion. Before acting on any matters contained herein, reference should be made to subject matter experts and professional judgment needs to be exercised. Dhruva Advisors LLP cannot accept any responsibility for loss occasioned to any person acting or refraining from action as a result of any material in this publication