

EXPLORING INDIA GUIDE 2022

**A GUIDE FOR ACCESSING
THE INDIAN MARKET**



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PREFACE

India is the fifth largest economy in the world and the most populous democracy¹. This vast country boasts an immensely rich cultural heritage including numerous languages, traditions and people. In the last decade, a stable political environment combined with positive macroeconomic parameters and strong policy reforms have propelled India as a leading destination for global investment. India rose to 62nd place out of 190 nations in the World Bank's Ease of Doing Business 2020 report – up from 142nd place in 2014. Prime Minister Modi aims to make India a USD 5 trillion economy by 2025 and in order to achieve this, the government has focused on 'pro-business policies'.

With this backdrop, India presents many opportunities to global institutions and this has driven a recent influx of foreign investments into the market. To encourage this inflow, Indian regulators continue to make significant modifications to the various laws and regulations that govern the routes for foreign investors to access India. The aim is to position India a favourable market for international investments.

In September 2014 the 'Make in India' campaign was launched with an intention of reviving manufacturing businesses and emphasising key sectors. This campaign identified 25 priority sectors where foreign investment would be of utmost importance and enhance India's attractiveness as an investment destination.

Landscape for foreign investment in India

There are five main routes available to international institutional investors to access investments in India:

- A. Foreign Direct Investment (FDI);
- B. Foreign Portfolio Investment (FPI);
- C. Foreign Venture Capital Investment (FVCI);
- D. External Commercial Borrowings (ECB); and
- E. Investment in Alternative Investment Funds (AIF)

We have provided below a snapshot of each of the above entry route:

A. Foreign Direct Investment (FDI) route

The Foreign Direct Investment (FDI) route is the investment scheme through which a person resident outside India can invest in equity instruments of:

- (a) an unlisted company or
- (b) a listed company in India for 10% or more.

Unlike the other routes, the FDI route does not require registration and any eligible investor is permitted to make investments through this access channel. Foreign investment under the FDI route can be made either under the automatic route or under the approval route depending on the sector/activities in which the Indian entity is engaged. Foreign investment in most sectors is permitted under the automatic route without any ownership restrictions or conditions. Foreign investment caps, minimum capitalisation norms and lock-in requirements are specified for certain sectors/activities and purchase/ transfer of securities is subject to pricing guidelines.

B. Foreign Portfolio Investors (FPI) route

Under the Foreign Portfolio Investors (FPI) route, the foreign investor is required to seek registration from the Securities and Exchange Board of India (SEBI), the securities market regulator for the purpose of making investments into India's capital markets. They are governed by the SEBI (FPI) Regulations introduced in September 2019 replacing the former SEBI (FPI) Regulations, 2014. The FPIs are further categorised as Category I and Category II FPIs on the basis of their characteristics.

An FPI is required to designate a bank in India to route all its investment transactions in India. FPI investment is made through equity instruments where such investment is less than 10 per cent of the post issue paid-up share capital on a fully diluted basis of a listed Indian company or less than 10 per cent of the paid-up value of each series of equity instrument of a listed Indian company.

¹ Source = International monetary fund 2022

C. Foreign Venture Capital Investment (FVCI)

Investors resident outside India can make investments under the C.Foreign Venture Capital Investment (FVCI) route pursuant to obtaining registration with SEBI under the SEBI (FVCI) Regulations, 2000. Investment by an FVCI in equity instruments of an Indian company will be subject to the reporting, sectoral caps, entry routes and associated conditions. However, the key benefits of this route are that it provides exemptions from (a) pricing guidelines stipulated under the FEMA regulations; and (b) pre-issue capital lock-in requirements prescribed under the relevant regulations governing issue of securities. However, an FVCI is permitted to invest in securities (not listed on a recognised stock exchange at the time of issue), of an Indian company that is engaged in only certain specified sectors.

D. External Commercial Borrowings (ECB)

External Commercial Borrowings (ECB) are commercial loans raised by resident entities (eligible to receive FDI) from recognised non-resident entities. In order to qualify under the ECB route, certain parameters must be met (such as minimum maturity, end use of the proceeds of loan, maximum all-in cost ceiling, eligible borrower, recognised lender, currency of borrowing etc.)

ECB loans can be Indian Rupee (INR) denominated or foreign currency denominated. ECBs can be issued in various forms (such as bank loans, Foreign Currency Convertible Bonds (FCCBs), Foreign Currency Exchangeable Bonds (FCEBs), floating/ fixed rate bonds/ debentures, preference shares, trade credits beyond three years, Financial Lease, Rupee Denominated Bonds (RDBs) issued overseas, etc.) depending upon the currency in which the ECB is denominated.

The eligible borrower is required to obtain a loan registration number in order to avail the ECB facility.

ECBs can be converted into equity shares subject to fulfilling certain conditions.

E. Alternative Investment Funds (AIF)

An Alternative Investment Fund (AIF) is any fund established or incorporated in India which is a privately pooled investment vehicle which collects funds from Institutional investors, whether Indian or foreign, for investing in accordance with a defined investment policy for the benefit of its investors. An AIF can be established or incorporated in the form of a trust, a company, a Limited Liability Partnership (LLP) or a body corporate. AIFs are regulated by SEBI and are governed by the SEBI (AIF) Regulations, 2012.

An Introduction to the International Financial Service Center (IFSC) Gujarat International Finance Tec-City (GIFT City)

The IFSC at GIFT City in India's north is a special enclave providing a platform for financial services to operate in a light touch regulatory environment (supported by a favourable tax framework). The IFSC in GIFT City aims to onshore financial services transactions undertaken by overseas financial institutions and overseas branches/ subsidiaries of Indian financial institutions which take place outside of India.

GIFT City is India's first and only operating smart city. The IFSC in GIFT City is being developed as a global financial and information technology services hub on a par with global financial centres. In order to promote ease of doing business, a unified regulator called the International Financial Services Centres Authority (IFSCA) was set-up to regulate financial products, financial services and financial institutions in the IFSC in the areas of banking, insurance, securities and funds management.

What's New in 2022

On the tax and regulatory front, the government and regulators have made various amendments and updates to expand the investment routes and leverage technology to improve efficiency and governance:

Introduction of T+1 rolling settlement on an optional basis

- In order to make the market more efficient and provide investors with more liquidity with the availability of funds and securities, SEBI introduced from January 2022, T (trade date) +1 rolling settlement cycle on an optional basis whereby SEBI has granted the flexibility to stock exchanges to offer either T+1 or T+2 settlement cycle.
- After opting for T+1 settlement cycle for a scrip, the stock exchange is expected to continue with the same for a minimum period of six months. Thereafter, in case, the stock exchange intends to switch back to T+2 settlement cycle, it shall do so by giving one month advance notice to the market. There will be no netting between T+1 and T+2 settlements.

Allowing trading in gold receipts

- In 2022, SEBI notified go live of the Gold Exchange in India by allowing trading in electronic gold receipt (EGR). The EGR shall reflect in the securities account of the beneficial owner maintained with the Depository.
- SEBI issued a circular to clarify various aspects pertaining to the functioning of the gold exchange namely, trade timings, transaction charges by stock exchanges, call auction in pre-open session, block and bulk deal, price bands, investor protection fund and investor service fund and unique client code.
- Relevant amendment has been made in the SCA to include EGR under the definition of 'security'

This latest *India guide* provides a comprehensive view of the **FDI, FPI, FVCI** and **IFSC – GIFT city** policies and what they mean for foreign investors investing into India. The information contained in this document is **updated to 31 March 2022**. For any subsequent updates, readers are advised to consult with their investment advisors/ tax consultants or visit the relevant regulatory websites.

Please contact our award-winning team of experts who will be happy to share their expertise and guide you through the investment routes.

Best regards,



Rohit Dodla Reddy
Head of Securities Services, India
BNP Paribas



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**PART A: REGULATORY
STRUCTURE**

PART A: REGULATORY STRUCTURE AND LEGAL FRAMEWORK

1 INDIA – THUMBNAIL SKETCH

TOTAL AREA	3.30 million square kilometres
CAPITAL	New Delhi
POPULATION	1.38 billion (Source: World Bank)
POLITICAL FRAMEWORK	<ul style="list-style-type: none"> i. World's largest democracy ii. Independent judiciary system iii. Extensive media
TERRITORIES	There are 28 states and 8 Union territories
LANGUAGES SPOKEN	<p>Multilingual society with Hindi as its official language.</p> <p>English is the widely used business language</p>
LITERACY RATE	74.04 percent (2011 census)
TIME ZONE	Greenwich Mean Time (GMT) + 5 ½ hours
CURRENCY UNIT	Indian Rupee (₹/ INR/Rs.)
GROSS DOMESTIC PRODUCT (GDP)	<p>3.7 per cent – FY 2019-20</p> <p>-6.6 per cent – FY 2020-21 (estimate)</p> <p>8.7 per cent – FY 2021-22 (forecast)</p> <p>7.5 per cent – FY 2022-23 (forecast)</p> <p>(Source: The Global Economic Prospects – June 2022 edition)</p>
MARKET CAPITALIZATION OF BSE LISTED COMPANIES	Approximately USD 3.52 trillion (April 2022) ²
MUTUAL FUND ASSET BASE	<p>Approximately USD 500 billion (March 2022)³</p> <p>(Source: The Association of Mutual Funds in India)</p>
INVESTMENT IN INDIA	According to the report of the Department for Promotion of Industry and Internal Trade (DPIIT), India has received foreign remittances inflow worth USD 84.74 billion up to March 2022
SEBI REGISTERED FPIs	More than 10,000 registered FPIs at end of May 2022

² 1 USD = INR 75

³ 1 USD = INR 75

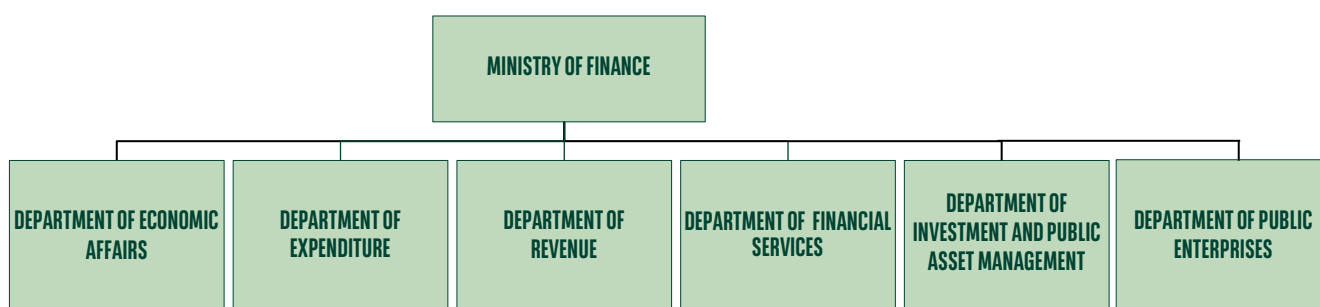
2 REGULATORY STRUCTURE AND LEGAL FRAMEWORK

The government is committed and focused to ensure safe and stable financial markets with world-class processes and governance in order to attract foreign investors to India.

2.1 Regulatory structure

The regulatory system in India is controlled by independent regulators in the field of banking, insurance, capital markets, securities market, etc. The government plays an important role in setting up various legislations, regulatory bodies and ministries for the purpose of effective and efficient operation of the economy and regulating the capital markets.

Ministry of Finance



The Ministry of Finance (MOF) is responsible for the administration of government finances and regulates the expenditure of the central government including transfer of resources to the states. The MOF is involved in taxation, financial legislation and institutions, capital markets, state and central finances and the Union Budget.

- **The Department of Economic Affairs (DEA)**

The responsibility for the formulation and monitoring of the economic policies at a macro level such as policies relating to the functioning of capital markets vests with Department of Economic Affairs ('DEA') within the MOF. It formulates and monitors the country's economic policies and programmes. The primary responsibility of all policy issues related to growth and development of the securities markets and the orderly functioning of SEBI is overseen by the Capital Markets Division within the DEA. The DEA is responsible for advice on economic issues having a bearing on internal and external aspects of the Indian economy including inflation, price control, foreign exchange management, Official Development Assistance domestic finance, the preparation of the Union Budget, and bilateral and multilateral engagement with international financial institutions and other countries.

- **The Department of Revenue (DOR)**

The DOR exercises control in respect of matters relating to all the direct and indirect Union taxes. It exercises its governance through two statutory bodies being the Central Board of Direct Taxes (CBDT) and the Central Board of Indirect Taxes and Customs (CBIC).

The CBDT is the apex tax administration body that functions under the Department of Revenue within the MOF and administers direct taxation in India. This department is also responsible for enforcing the Double Taxation Avoidance Agreements (DTAAs). The main responsibility of the Income Tax Department is to enforce various direct tax laws, most important among these being the Income-tax Act, 1961 (IT Act).

Reserve Bank of India (RBI) – The Central Bank of India

The RBI is India's central bank controlling the monetary and banking policies of the Indian government and promotes the integrity, efficiency, inclusiveness and competitiveness of the financial and payments system. The RBI performs various functions, including:

- As a monetary authority
- As a regulator and supervisor of the financial system
- As a manager of foreign exchange
- As an issuer of currency
- It acts as a banker's bank and also offers various banking solutions

Misistry of Corporate Affairs (MCA)

The Misistry of Corporate Affairs MCA is primarily concerned with regulating the corporate structure in India through the Companies Act, 2013 and other allied Acts and Rules.

Securities and Exchange Board of India (SEBI) – regulatory authority for the securities industry

SEBI was first established in 1988 as a non-statutory body for regulating the securities market. The SEBI Act, 1992 came into force through an Act of Parliament.

SEBI is the regulatory and processing authority for the various intermediaries and Institutional investors connected with the securities market (e.g. brokers, mutual funds (MFs), FPI's, custodians, merchant bankers). The SEBI Act, 1992 empowers SEBI to issue various regulations governing market intermediaries and investors.

SEBI's primary objective is to protect the interest of investors in the stock market and responsible for the orderly functioning of the capital markets. SEBI closely monitors the activities of financial intermediaries including brokers and sub-brokers, etc.

Indian Stock Exchanges

Though the stock exchanges in India are under the overall supervision of SEBI, they are also self-regulatory organisations with their own rules, regulations and by-laws administered by their board of directors. They are also responsible for:

- Ensuring orderly, transparent and fair trading practices
- Controlling the admission and expulsion of members
- Maintaining investor protection funds
- Addressing investor grievances

The two major stock exchanges in India are the National Stock Exchange of India Limited (NSE) and the Bombay Stock Exchange Limited (BSE).



In addition, the Multi Commodity Exchange of India (MCX) and the National Commodities and Derivatives Exchange Limited (NCDEX) are the stock exchanges which facilitate trading in commodities such as precious metals, agricultural products and energy products.



LEGAL FRAMEWORK

Foreign investment into India is primarily regulated by the Foreign Exchange Management Act, 1999 and the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 (NDI Rules) promulgated thereunder. The Master Direction on Foreign Investment consolidating the various notifications and circulars issued by RBI along with other regulations read with the consolidated FDI Policy and various press notes issued by the Department for Promotion of Industry and Internal Trade (DPIIT), Ministry of Commerce and Industry and government. The government makes FDI policy pronouncements through press notes or releases which are notified by the RBI as amendments to the NDI Rules. The procedural instructions are issued by RBI vide A.P (DIR Series) circulars.

2.2 Foreign investment framework

Foreign Direct Investment (FDI)

The government has put an FDI policy framework in place which is transparent, predictable and easily comprehensible. This framework is embodied in the circular on Consolidated FDI Policy, which is updated from time to time to capture the key regulatory changes and keeps pace with the prevailing business context.

For clarity we separately address the compliances/ taxability relating to investment in FDI in **Part B** of this guide.

Foreign Portfolio Investor (FPI)

Under the Foreign Portfolio Investor route, investors are required to seek registration from SEBI. FPIs are governed by FPI Regulations introduced in September 2019 replacing the previous SEBI (FPI) Regulations, 2014.

For clarity we separately address the compliances/ taxability relating to investment in FPI in **Part C** of this guide.

Foreign Venture Capital Investor (FVCI)

Foreign Venture Capital Investor (FVCI) is an investor incorporated and established outside India. Under this route, investors are required to seek registration under SEBI (FVCI) Regulations, 2000.

For clarity we separately address the compliances/ taxability relating to investment in FVCI in **Part E** of this guide.

Companies Act, 2013

The Companies Act 2013 governs the rules and regulations to be followed by corporate entities in India with respect to the issue and transfer of securities, underwriting of securities, the treatment/ use of premium and discount on issues, rights and bonus issues, distribution of dividend and interest, disclosures to be made in documents, and the circulation of the annual report, etc.

Securities and Exchange Board of India (SEBI) Act, 1992

SEBI was established and is regulated under the SEBI Act, 1992 to:

- Safeguard investors
- Prevent unfair trade practices and insider trading
- Develop and regulate the securities market



- Regulate the issuance of capital and transfer of securities
- Regulate intermediaries and participants in securities markets

The SEBI Act grants SEBI with the powers to conduct enquiries, audits, inspection and adjudicate offences under this Act. SEBI issues notifications, guidelines and circulars which need to be complied with by market participants. The orders of SEBI are appealable before the Securities Appellate Tribunal. The FPI regime is also regulated by SEBI.

For listed public companies and public companies proposing to list their securities, the powers under the Companies Act relating to issue and transfer of securities and non-payment of dividend are administered by SEBI.

The powers in respect of the contract for sale and purchase of government securities, gold related securities, money market securities, securities derived from these securities and ready forward contracts in debt securities are exercised concurrently by the RBI.

Securities Contracts (Regulation) Act, 1956 (SCA)

The Securities Contracts (Regulation) Act, 1956 aims to prevent adverse transactions in securities by regulating the business of dealing in the said securities. This Act outlines the provisions for registration, supervision and regulation of the stock exchanges and clearing houses.

Depositories Act, 1996

The Depositories Act of 1996 provides for the regulation of depositories into the securities market. It further provides for the following:

- Dematerialisation (demat) of securities and holding them in a fungible form;
- Enable the depository to be the registered owner of the securities in the books of the issuer (as a registered owner, they do not have any rights in respect of securities held by it); and
- Maintenance of a register and index of beneficial owners.

At present, there are two depositories registered: the National Securities Depositories Ltd (NSDL) and Central Depository Services Limited (CDSL).

The Foreign Exchange Management Act, 1999 (FEMA)

The objective of the Foreign Exchange Management Act of 1999 is to consolidate and amend the law relating to foreign exchange with the motive of facilitating external trade, payments and promoting the orderly development and maintenance of the foreign exchange market in India. It is a regulatory mechanism that enables the RBI and the central government to adopt rules and regulations in relation to foreign exchange.

Prevention of Money Laundering Act, 2002 (PMLA)

The Prevention of Money Laundering Act of 2002 lays out provisions to combat money laundering in India and the primary objectives of PMLA are as follows:

- To prevent money laundering;
- To combat the channelling of money into illegal activities and economic crimes;
- To provide for confiscation of property derived from or involved in money laundering; and

- To deal with any other matters connected with or incidental to act of money laundering in India.

Income Tax Act, 1961

The Income Tax Act provides for charge, levy, administration, collection and recovery of income tax. Securities Transaction Tax (STT) is another direct tax levy which is charged on every purchase or sale of securities that are listed on an Indian stock exchange. This includes shares, futures, options and equity-oriented mutual funds.

Goods and Services Tax Act (GST)

GST is one indirect tax for the whole nation, making India one unified common market. GST came into effect in 2017 and replaced the many indirect taxes in India such as excise duty, value added tax, and service tax.

Foreign Account Tax Compliance Act (FATCA) and Common Reporting Standard (CRS)

The United States Foreign Account Tax Compliance Act requires financial institutions across the world to identify their accounts which have connection with the USA through the enhanced due diligence review and report annually to the internal revenue service or in case of Inter-Governmental Agreement (IGA), to appropriate local government authority.

India and the United States signed the reciprocal version of Model 1 IGA for FATCA in July 2015. The agreement requires both countries to share information from their respective financial institutions.

India signed the Multilateral Competent Authority Agreement for CRS, effective 2016. India is firmly committed to tax transparency and tax information sharing in its capacity as G-20 member.

FATCA-CRS impacts various financial institutions such as banks, custodians, depositories, insurance companies, funds/fund managers, securities traders, brokers and dealers etc. At the time of onboarding, investors and customers are required to self-declare and certify their FATCA and CRS status.

2.3 Permitted instruments – a glimpse

Instruments permissible under the FDI, FPI and FVCI routes:

SR NO.	INSTRUMENT TYPE	FDI	FPI	FVCI
1	EQUITY INSTRUMENTS			
	Listed equity shares (including to be listed)	Yes	Yes	Yes
	Unlisted equity shares	Yes	No	Yes
	Compulsorily convertible preference shares	Yes	Yes	Yes
	Warrants	Yes	Yes	Yes
	Partly paid equity shares	Yes	Yes	Yes
2	DERIVATIVE INSTRUMENTS			
	Exchange traded derivatives (approved by SEBI) [including equity/ index derivatives]	No	Yes	No
	Overnight index swaps/ Interest rate swaps	No	Yes	No
3	DEBT INSTRUMENTS			
	Government securities (including coupons on existing government securities)	No	Yes	No
	Treasury bills	No	Yes	No
	Corporate bonds/ debentures – non convertible	No	Yes	Yes
	Corporate bonds/ debentures – convertible	Yes	Yes	Yes
	Commercial papers	No	Yes	No
	Rupee denominated bonds (RDBs)/units issued by Infrastructure debt funds	No	Yes	No
	Credit enhanced bonds	No	Yes	No
	Securitised debt instruments	No	Yes	No
	Partly paid debt instruments	No	No	No
	Municipal debt instruments	No	Yes	No
	Debt securities issued by InvITs and REITs	No	Yes	No
4	OTHERS (Refer note on SLB⁴)			
	Units of equity-oriented MF	No	Yes	No
	Units of debt-oriented MF	No	Yes	No
	Liquid and money market MF schemes	No	No	No
	Exchange traded funds (ETFs) (investing less than or equal to 50 per cent in equity)	No	Yes	No
	Units of Real Estate Investment Trusts (REIT), Infrastructure Investment Trusts (InvIT) (classified as Hybrid securities) and Category III AIF	Yes	Yes	No

⁴ The SLB scheme has been introduced by SEBI for market participants in 2007 and has been operational since 21 April 2008. SEBI vide circular dated 20 December 2007, has framed the broad mechanism for operationalising of the SLB Scheme under the overall framework of the Securities Lending Scheme, 1997.



SR. No.	INSTRUMENT TYPE	FDI	FPI	FVCI
	Units of Venture Capital Fund (VCF) or of a Category I Alternative Investment Fund (Cat-I AIF) or units of a scheme or of a fund set up by a VCF or by a Cat-I AIF	Yes	No	Yes
	Capital contribution in an LLP	Yes	No	No

2.4 Key statistics

Assets under custody data – Investments under each route:

SR. NO.	INVESTMENT ROUTE	INR (IN MILLIONS)			
		EQUITY	DEBT	DEBT-VRR	HYBRID
1	Foreign Direct Investments	18,478,660	209,120	-	430,490
2	Foreign Portfolio Investments	46,905,140	2,535,330	1,193,670	335,970
3	Foreign Venture Capital Investment	265,410	155,490	-	-
4	Alternate Investment Funds	1,069,030	797,770	-	3,460
5	Financial Institutions	353,310	34,590	-	-

FPI Investments – the top 10 categories of FPIs making investment under FPI route:

CATEGORY OF THE FPI	SUB CATEGORY OF THE FPI	INR (IN MILLIONS)			
		EQUITY	DEBT	DEBT-VRR	HYBRID
Category I	Appropriately regulated fund	25,264,250	459,100	45,000	136,680
Category I	Pension fund	3,862,710	203,150	17,130	8,420
Category I	Unregulated fund whose investment manager is Category I FPI	3,322,710	285,450	79,270	26,470
Category I	Sovereign wealth fund	2,882,840	122,500	440	42,480
Category I	Entity whose Investment manager is Category I FPI from Financial Action Task Force (FATF) member country	2,360,160	78,580	77,440	2,580
Category I	Entity controlled or at least 75% owned by government and government related investor(s)	2,766,700	137,940	21,660	71,700
Category I	Central Bank	1,287,210	467,220	0	2,730
Category II	Appropriately regulated fund not eligible as Category-I FPI	778,770	17,500	1,000	1,250
Category II	Corporate body	164,200	446,000	471,490	15,500
Category I	Appropriately regulated – investment manager	405,390	34,270	115,010	1,890

Source: NSDL FPI monitor updated upto March 2022

Top 10 jurisdictions making investments under FDI route up to March 2022:

SR. NO.	NAME OF THE COUNTRY	AMOUNT OF FOREIGN DIRECT INVESTMENT INFLOWS INR (IN MILLIONS)	PERCENTAGE WITH INFLOWS
1	UNITED STATES OF AMERICA	18,606,310	36.50
2	MAURITIUS	5,547,700	10.88
3	SINGAPORE	4,333,250	8.50
4	LUXEMBOURG	3,906,810	7.66
5	UNITED KINGDOM	2,666,220	5.23
6	IRELAND	2,427,100	4.76
7	CANADA	1,636,660	3.21
8	NORWAY	1,304,230	2.56
9	JAPAN	1,202,120	2.36
10	NETHERLANDS	1,127,800	2.21

Top 10 sector-wise FDI equity inflows from April 2000 to March 2022:

SR. NO.	SECTOR	AMOUNT OF FOREIGN DIRECT INVESTMENT INFLOWS INR (IN MILLIONS)	PERCENTAGE WITH INFLOWS
1	SERVICES SECTOR	5,624,380	16.01
2	COMPUTER SOFTWARE AND HARDWARE	5,780,600	14.53
3	TELECOMMUNICATIONS	2,270,530	6.51
4	TRADING	2,291,320	5.90
5	AUTOMOBILE INDUSTRY	2,074,800	5.58
6	CONSTRUCTION (INFRASTRUCTURE) ACTIVITIES	1,908,010	4.75
7	CONSTRUCTION DEVELOPMENT	1,280,130	4.45
8	CHEMICALS (OTHER THAN FERTILIZERS)	1,120,570	3.31
9	DRUGS AND PHARMACEUTICALS	1,093,820	3.30
10	METALLURGICAL INDUSTRIES	1,013,810	2.89

Source: FDI Factsheet updated up to March 2022





**PART B:
FOREIGN DIRECT
INVESTMENT ROUTE**

PART B: FOREIGN DIRECT INVESTMENT ROUTE

3 INTRODUCTION

3.1 Introduction to Foreign Direct Investment (FDI)

FDI⁵ is investment by a person resident outside India into equity instruments⁶ either in an unlisted Indian company or with 10 per cent or more of the post issue paid-up equity capital on a fully diluted basis⁷ of a listed company in India.

FDI is a major source of non-debt financial resource for the economic development of India. Foreign companies investing in India can benefit from the relatively lower wages and special investment privileges such as tax exemptions.

The government has implemented many initiatives in recent years such as relaxing FDI requirements across sectors such as defence, the public sector undertaking (PSU) oil refineries, telecom, power exchanges and stock exchanges amongst others to ensure that foreign capital keeps flowing into the country.

During the period April 2021 to March 2022, India received FDI equity of USD 58.7 billion. The following are the sectors which attracted the most FDI inflow⁸:

SECTOR	COMPUTER SOFTWARE AND HARDWARE	SERVICES SECTOR ⁹	AUTOMOBILE INDUSTRY	TRADING
Amount (in USD) ¹⁰	14.4 billion	7.1 billion	6.9 billion	4.5 billion

The top countries as a source of FDI during the fiscal year 1 April 2021- 31 March 2022 :

COUNTRY	SINGAPORE	USA	MAURITIUS	NETHERLANDS	CAYMAN ISLANDS
Amount (in USD) ⁶	15.8 billion	10.5 billion	9.3 billion	4.6 billion	3.8 billion

3.2 Legal framework

The FDI policy framework is transparent, predictable and easily comprehensible. This framework is outlined in the circular on the consolidated FDI policy and is updated from time to time. The DPIIT, Ministry of Commerce and Industry, and the government make FDI policy pronouncements through press notes or releases which are notified by the RBI and the MOF.

⁵ Source: NDI Rules i.e. Foreign Exchange Management (Non-debt. Instruments) Rules, 2019

⁶ As defined under NDI Rules, "equity instruments" means equity shares, convertible debentures, preference shares and share warrants issued by an Indian Company

⁷ Fully diluted basis means the total number of shares that would be outstanding if all possible sources of conversion are exercised

⁸ All the data points in the given table have been rounded-off

⁹ Services sector includes Financial, Banking, Insurance, Non-Financial / Business, Outsourcing, Research & Development, Courier, Tech. Testing and Analysis, Other

¹⁰ https://dpiit.gov.in/sites/default/files/FDI_Factsheet_March_2022_23May2022.pdf

4 WHO CAN INVEST

4.1 Eligible Investors

- A non-resident entity can invest in India in accordance with the FDI Policy except in those sectors in which investments are prohibited (refer paragraph 5 below).
- However, an entity of a country which shares borders with India or where the beneficial owner of an investment into India is situated in or is a citizen of any such country, can invest only with the government approval. Further, a citizen of Pakistan or an entity incorporated in Pakistan can invest, only under the government route, in sectors/ activities other than defence, space, atomic energy and sectors/ activities prohibited for foreign investment.
- Also, in the event of the transfer of ownership of any existing or future FDI in an entity in India, directly or indirectly, resulting in the beneficial ownership falling within the above restriction, such subsequent change in beneficial ownership shall also require government approval.
- For the purposes of the above restriction, a Multilateral bank or fund, of which India is a member, shall not be treated as an entity of a particular country nor shall any country be treated as the beneficial owner of the investments of such bank or fund in India.
- Non-resident Indians (NRIs) resident in Nepal and Bhutan as well as citizens of Nepal and Bhutan are permitted to invest in the capital of Indian companies on a repatriation basis, subject to fulfilment of prescribed conditions.
- A company, trust and partnership firm incorporated outside India and owned and controlled by NRIs can invest in India with the special exemption as available to NRIs under the FDI policy.
- Registered FPIs and NRIs, can invest or trade through a registered broker in the capital of an Indian company subject to the fulfilment of prescribed conditions set out under FDI policy .
- SEBI registered FVCIs can make investments using the FDI route in the capital of an Indian company subject to the fulfilment of prescribed conditions set out under FDI Policy..

CAN AN ENTITY WITH FDI INVESTMENTS IN INDIA ALSO REGISTER AND MAKE INVESTMENTS AS AN FPI?

Yes (subject to investment cap and sectoral limits). The entity will have to register itself as an FPI with SEBI. Further, a non-resident entity can hold foreign investments either as FDI or FPI in any particular Indian entity.



4.2 KYC requirements for FDIs

The details/ documents required from a KYC perspective for FDI investments are:

Entry Level	<ul style="list-style-type: none"> • Constitutive documents¹¹ • Proof of address • PAN card • Financials¹² • Board/partner/member resolution or any other relevant document pertaining to investments in the securities market • FATCA/ CRS form • KYC form ¹¹
Senior Management / Authorised Signatories	<ul style="list-style-type: none"> • List of members (full time directors/ partners/ trustees etc. in senior management) and signatures (in case of authorised signatories) • Proof of identity • Proof of address • Photographs
Ultimate Beneficial Owners (Ubo)/ Shareholding Pattern	<ul style="list-style-type: none"> • List of members (required until the UBO) • Proof of Identity (required if UBO with substantial percentage identified) • Proof of address

¹¹ In case of

- Corporates: Copies of the Memorandum and Articles of Association and certificate of incorporation
- Partnership Firm: Copy of Partnership Deed / Certificate of registration (if registered)
- Trust: Copy of Trust Deed / Certificate of registration (if registered)

¹² Copy of the balance sheets for the last two financial years to be submitted every year

5 SECTORAL INVESTMENT LIMITATIONS /CAPS

5.1 Sectors where FDI is not permitted/prohibited

FDI is presently prohibited in the following sectors:

- Lottery business including government/ private lottery, online lotteries, etc;
- Gambling and betting including casinos, etc.;
- Chit funds;
- Nidhi company;
- Trading in transferable development rights;
- Real estate business¹³ or construction of farm houses;
- Manufacturing of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes;
- Activities/ sectors not open to private sector investment e.g. atomic energy and railway operations; and
- Foreign technology collaboration in any form including licensing for franchise, trademark, brand name, management contract is also prohibited for lottery business and gambling and betting activities.

5.2 Entry routes for making permitted FDI investment

FDI in permitted sectors can be made under the following prescribed routes:

- **Automatic route** – Investment is permitted without prior government or RBI approval in all activities/ sectors as specified in the extant consolidated FDI policy, issued by the government from time to time.
- **Government route** – FDI in activities not covered under the automatic route requires prior government approval.

¹³ Real Estate Business' means dealing in land and immovable property with a view to earning profit from there and does not include development of townships, construction of residential or commercial premises, roads or bridges, educational institutions, recreational facilities, city and regional level infrastructure, townships, real estate broking services and Real Estate Investment Trusts (REITs) registered and regulated under the SEBI (REITs) Regulations 2014 and earning of rent or income on lease of the property, not amounting to transfer .

5.3 Composite FDI cap for all sectors¹⁴

SR NO	SECTOR / ACTIVITY	SECTORAL CAP	ENTRY ROUTE	PRESCRIBED CONDITIONS TO BE SATISFIED (Y/N)
1	Agriculture and animal husbandry	100%	Automatic	Y
2	Plantation (tea/coffee/rubber/olive oil/cardamom/palm oil)	100%	Automatic	Y
3	MINING AND PETROLEUM AND NATURAL GAS			
	Mining and exploration of metal and non-metal ores	100%	Automatic	Y
	Coal and lignite mining for captive consumption for certain permitted activities	100%	Automatic	Y
	Setting up coal processing plants like washeries	100%	Automatic	Y
	For sale of coal, coal mining activities including associated processing infrastructure ¹⁵ subject to conditions prescribed under the provisions of coal mines (Special Provisions) Act, 2015 and the mines and minerals (Development and Regulation) Act, 1957 as amended from time to time and other relevant acts on the subject	100%	Automatic	Y
	Mining and mineral separation of titanium bearing minerals and ores, its value addition and integrated activities	100%	Government	Y
	Exploration activities of oil and natural gas fields, infrastructure related to marketing of petroleum products and natural gas, gas pipelines etc.	100%	Automatic	N
	Petroleum refining by public sector undertaking (PSU), without any disinvestment or dilution of domestic equity in the existing PSUs ¹⁶	49%	Automatic	N
4	Manufacturing	100%	Automatic	N
5	Retail trading of food products manufactured and/ or produced in India	100%	Government	N
6	Defence	100%	Automatic up to 74% ¹⁷ , Government route beyond 74% wherever it is likely to result in access to modern technology or for other reasons to be recorded.	Y

¹⁴ Please note that the aforesaid caps may be subject to additional conditions as prescribed. Further, FCCBs and ii. Depository receipts having underlying of instruments which can be issued, being in the nature of debt, shall not be treated as foreign investment. However, any equity holding by a person resident outside India resulting from conversion of any debt instrument under any arrangement shall be reckoned as foreign investment under the sectoral cap

¹⁵ Associated Processing Infrastructure includes coal washery, crushing, coal handling, and separation (magnetic and non-magnetic)

¹⁶ foreign investment up to 100% under the automatic route is allowed in case an 'in-principle' approval for strategic disinvestment of a PSU has been granted by the Government

¹⁷ Investment up to 74 per cent under automatic route shall be permitted for companies seeking new industrial licenses. Infusion of fresh investment up to 49 per cent in a company not seeking industrial license or which already has Government approval for investment in Defence, shall require mandatory submission of a declaration with the Ministry of Defence in case change in shareholding pattern or transfer of stake by existing investor to new foreign investor for investment up to 49 per cent, within 30 days of such change. Proposal for raising investment beyond 49 per cent from such companies will require government approval



SR NO	SECTOR / ACTIVITY	SECTORAL CAP	ENTRY ROUTE	PRESCRIBED CONDITIONS TO BE SATISFIED (Y/N)
7	BROADCASTING CARRIAGE SERVICES			
	Teleports, direct to home, cable networks, mobile TV, head-end-in-the-sky broadcasting service	100%	Automatic	Y
	BROADCASTING CONTENT SERVICES			
	Terrestrial broadcasting FM radio	49%	Government	Y
	Up-linking of 'news and current affairs' TV channels	49%	Government	Y
	Uploading/ streaming of news and current affairs through digital media	26%	Government	Y
	Up-linking of non 'news and current affairs' TV channels/ down-linking of TV channels	100%	Automatic	Y
8	PRINT MEDIA			
	Publishing of newspaper and periodicals dealing with news and current affairs	26%	Government	Y
	Publication of Indian editions of foreign magazines dealing with news and current affairs	26%	Government	Y
	Publishing/ printing of scientific and technical magazines/ specialty journals/ periodicals	100%	Government	Y
	Publication of facsimile edition of foreign newspapers	100%	Government	Y
9	CIVIL AVIATION¹⁸			
	Airports- greenfield and existing projects	100%	Automatic	N
	Scheduled air transport service/ domestic scheduled passenger airline; regional air transport service	100%	Automatic up to 49%, government route beyond 49% (Automatic up to 100% for NRIs)	Y
	Non-scheduled air transport services	100%	Automatic	Y
	Helicopter services/ seaplane services requiring Directorate general of civil aviation approval	100%	Automatic	Y
	Ground handling services	100%	Automatic	Y
	Maintenance and repair organisations, flying training institutes and technical training institutions	100%	Automatic	N
10	Construction development: townships, housing, built-up infrastructure	100%	Automatic	Y
11	Industrial parks – new and existing	100%	Automatic	Y
12	Satellites – establishment and operation	100%	Government	Y

¹⁸ Foreign Investment in M/S Air India Ltd including that of foreign airlines shall not exceed 49 per cent either directly or indirectly. However, in case of investment by NRIs, foreign investment up to 100 per cent is permitted under the automatic route



SR NO	SECTOR / ACTIVITY	SECTORAL CAP	ENTRY ROUTE	PRESCRIBED CONDITIONS TO BE SATISFIED (Y/N)
13	Private security agencies	49% ¹⁹	Government	Y
14	Telecom services (including telecom infrastructure providers category-I)	100%	Automatic	Y
15	TRADING			
	Cash and carry wholesale trading/ wholesale trading (including sourcing from micro and small enterprises)	100%	Automatic	Y
	B2B e-commerce activities	100%	Automatic	Y
	E-commerce activities: marketplace based model of e-commerce	100%	Automatic	Y
	Single brand product retail trading	100%	Automatic	Y
	Multi brand product retail trading	51%	Government	Y
	Duty free shops	100%	Automatic	Y
16	PHARMACEUTICALS			
	Greenfield	100%	Automatic	N
	Brownfield	100%	Automatic up to 74% Government route beyond 74%	Y
17	Railway infrastructure	100%	Automatic	Y
18	FINANCIAL SERVICES			
	Asset reconstruction companies (ARCs)	100%	Automatic	Y
	Banking sector – private sector	74%	Automatic up to 49% Government route beyond 49% and up to 74%	Y
	Banking – public sector	20%	Government	Y
	Infrastructure companies in the securities market	49%	Automatic	Y
	Commodities spot exchange	49%	Automatic	Y
	Power exchanges	49%	Automatic	Y
	Credit information companies	100%	Automatic	Y
	Insurance company	74%	Automatic	Y
	Life Insurance Corporation of India	20%	Automatic	Y

¹⁹ As per the FDI Policy, the sectoral cap in Private Security Agencies is 74 per cent whereby investment upto 49 per cent is under the automatic route and investment beyond 49 per cent but upto 74 per cent is under the Government route. However, as per the NDI Rules, the sectoral cap in Private Security Agencies is 49% under the Government Route. Further, the FDI policy provides that in case of any conflict, the NDI Rules, will prevail. Accordingly, the sectoral cap in Private Security Agencies will be 49 per cent under the Government Route



SR NO	SECTOR / ACTIVITY	SECTORAL CAP	ENTRY ROUTE	PRESCRIBED CONDITIONS TO BE SATISFIED (Y/N)
	Intermediaries and insurance intermediaries including insurance brokers, re-insurance brokers, insurance consultants, corporate agents, third party administrators, surveyors and loss assessors and other insurance intermediaries as may be notified by the Insurance Regulatory and Development Authority of India (IRDA) from time to time	100%	Automatic	Y
	Pension sector	49%	Automatic	Y
	White label automated teller machine operations	100%	Automatic	Y
	Other financial services (registered/ regulated entities)	100%	Automatic where the financial services activities are regulated by a sector regulator i.e. RBI, SEBI, IRDA, Pension Fund Regulatory and Development Authority, National Housing Bank, any other financial service regulator. In any other case, Government approval route.	Y

5.4 Procedure for government approval

- The approval for foreign investments granted by the competent authorities is dependent on the sectors/ activities.
- The approval is to be obtained from the respective administrative ministry/ department.
- In respect of applications in which there is a doubt as to which is the concerned administrative ministry or department, the DPIIT shall identify the relevant authority where the application is to be processed.
- Proposals would be examined by the competent authority according to standard operating procedures laid down by the DPIIT and guidelines for e-filing of applications. Filing of amendment applications and instructions to applicants are available from the Foreign Investment Facilitation Portal (FIFP) (www.fifp.gov.in/Forms/SOP.pdf).
- In case of proposals involving total foreign equity inflow of more than INR 50 billion, the competent authority is required to engage the Cabinet Committee on Economic Affairs (CCEA).
- The CCEA would also consider the proposals which may be referred to it by the minister-in-charge of the concerned competent authority.
- There are certain scenarios whereby government approval is not required
- For activities which have sectoral caps with government approval (as applicable under extant FDI policy), the caps have subsequently been removed/ increased.



6 ELIGIBLE INVESTEEES

6.1 Types of eligible investees

Permissible FDI investments can be made into the following types of entities in accordance with prescribed terms and conditions:

- Indian companies
- Convertible Notes (CNs) in start-up companies (discussed in para 6.3 below)
- Partnership firms and proprietary concerns
- Trusts
- LLPs (discussed in para 6.4 below)
- Investment vehicles²⁰

In addition, specific provisions have been specified for downstream investments by Indian entities with FDI investments (discussed below)

6.2 Downstream investment

- 'Downstream investment' means indirect foreign investment by an eligible Indian entity into another Indian company/ LLP by way of subscription or acquisition. For the purpose of computation of indirect foreign investment in an Indian company all types of foreign investments are to be included (i.e. FDI, FPIs, NRIs, American depository receipts (ADRs), global depository receipts (GDRs), FCCBs, CCDs, CCPS etc.).
- Such downstream investment by a foreign owned and/ or controlled Indian company, into another Indian company, should be in accordance/ compliance with the relevant sectoral conditions on entry route, conditionalities and caps, with regard to the sectors in which the latter Indian company is operating.
- Downstream investments by eligible Indian entities/ LLPs will be subject to the following conditions:
 - Indian entities/ LLP are required to notify the RBI and FIFP of its downstream investment within 30 days of such investment/ capital contribution, even if equity instruments have not been allotted along with the modality of investment in new/ existing ventures (with/ without expansion programme).
 - Downstream investment by way of introduction of foreign investment in an Indian company is required to be duly supported by a resolution of the Board of Directors as also a shareholders agreement, if any
 - Issue/ transfer/ pricing/ valuation of shares will continue to be in accordance with extant SEBI/ RBI guidelines
 - For the purpose of downstream investment, the eligible Indian entities making the downstream investments would have to bring in requisite funds from abroad and not leverage funds from the domestic market. This would, however, not preclude downstream companies/ LLPs, with operations, from raising debt in the domestic market. Downstream investments through internal accruals are also permissible.

²⁰ Please note that Mutual Funds are not included in the definition of investment vehicle.



- Investments by NRIs on a non-repatriation basis as stipulated under Schedule IV of NDI Rules are deemed to be domestic investments at par with the investments made by residents. Accordingly, an investment made by an Indian entity which is owned and controlled by NRIs on a non-repatriation basis shall not be considered for calculation of indirect foreign investment.

6.3 Scheme of issuance of Convertible Notes by an Indian start-up company²¹

- A person resident outside India (other than an individual who is citizen of Pakistan or Bangladesh or an entity which is registered or incorporated in Pakistan or Bangladesh), may purchase convertible notes (CN) issued by an Indian start-up company for an amount of INR 2.5 million or more in a single tranche.
- A start-up company, engaged in a sector where investment by a person resident outside India requires government approval, may issue CNs to a person resident outside India only with such approval. Further, issue of equity shares against such CNs is required to be in compliance with the entry route, sectoral caps, pricing guidelines and other attendant conditions for foreign investment.
- A start-up company shall receive the amount of consideration for issuance of CNs only by way of inward remittance through banking channels or out of funds held in non-resident account or FCNR account or escrow account maintained in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016.
- Repayment or sale proceeds may be remitted outside India or may be credited to a non-resident or FCNR account.
- A NRI or an overseas citizen of India (OCI) may acquire CNs on a non-repatriation basis subject to the fulfilment of prescribed conditions.
- A person resident outside India may acquire or transfer by way of sale, CNs, from or to, a person resident in or outside India, provided the transfer takes place in accordance with the entry routes and pricing guidelines as prescribed for equity instruments.

6.4 Foreign investment in an Limited liability partnership (LLP)²²

- Investment in an LLP is subject to compliance with the conditions specified under the provisions of the LLP Act, 2008.
- A person resident outside India (other than a citizen of Pakistan or Bangladesh) or an entity incorporated outside India (other than an entity in Pakistan or Bangladesh), not being a FPI or FVCI registered in accordance with SEBI guidelines may contribute to the capital of an LLP by way of capital contribution/ acquisition/ transfer of profit shares in an LLP, operating in sectors/ activities where foreign investment up to 100 per cent is permitted under the automatic route and there are no FDI linked performance conditions.
- For the purpose of an LLP, investment means capital contribution or acquisition or transfer of profit shares. Further, investment by way of 'profit share' will fall under the category of 'reinvestment of earnings'.
- FDI in an LLP should not be less than the fair price worked out as per any valuation norm which is internationally adopted as per market practice of capital contribution/ profit share of an LLP. A valuation certificate to this effect is required to be issued by a- CA/ practicing cost accountant/ approved valuer from the panel maintained by the government.

²¹ Rule 18 of NDI Rules

²² Schedule VI to NDI Rules

- In case of transfer of capital contribution/ profit share from a resident to non-resident, the transfer is required to be for a consideration not less than the fair price of the capital contribution/ profit share of an LLP.
- While in case of transfer of capital contribution/ profit share from a non-resident to resident, the transfer is required to be for a consideration which is less than or equal to the fair price of capital contribution/ profit share of an LLP.
- The investment amount towards the capital contribution of an LLP should be paid by way of inward remittance through banking channels or out of funds held in non resident account or foreign currency non-resident (bank) account (FCNR account) maintained in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016.
- The disinvestment proceeds may be remitted outside India or may be credited to non-resident external or FCNR account.

7 ELIGIBLE INVESTMENT INSTRUMENTS

7.1 Eligible instruments for making FDI investments

- FDI investments may be made in the following instruments in accordance with the prescribed terms and conditions:
 - Equity shares
 - Fully, compulsorily and mandatorily Convertible Debentures (CCDs)
 - Fully, compulsorily and mandatorily Convertible Preference Shares (CCPS)
 - Equity shares, CCDs and CCPS having optionality clauses (exercising option/ right), subject to certain conditions
 - Depository receipts
 - FCCBs
 - Warrants and partly paid shares
 - Convertible notes
- All investments under this route are subject to the sectoral caps²³ and conditions prescribed in the FDI policy and notified through the NDI Rules. As indicated earlier, investments can be under the automatic route (i.e. no approval required from any regulatory authority for making investments in a particular sector) or the government approval route (i.e. where a prior approval is required from the relevant ministry/ department of the government for making investment in a particular sector).
- In addition to the above-mentioned conditions, the investment/ investor is required to comply with all relevant laws, regulations and rules applicable to that sector in India.

7.2 Types of FDI transactions

- Subscription to primary issuance of securities
- Secondary acquisitions

²³ Sectoral cap means the maximum investment including both foreign investment on a repatriation basis by persons resident outside India in equity instruments of a company or the capital of a LLP, as the case may be, and indirect foreign investment, unless provided otherwise. This shall be the composite limit for the Indian investee entity

- The secondary market, also called the aftermarket, is the financial market in which previously issued financial instruments such as shares, bonds, options, and futures, etc. are bought and sold. The secondary market includes, transfer of equity instruments from one investor to another i.e. non-resident to resident/ or vice versa, sale of equity instruments on a Recognised Stock Exchange (RSE) by person resident outside India.
- Under the extant FDI policy, a person resident outside India can acquire equity instruments on a RSE in accordance with prescribed conditions and pricing guidelines (discussed below).
- Prior approval from the RBI would be required in certain prescribed transactions (eg: acquisition or transfer of immovable property in India).

7.3 Specific conditions relating to the issue/ transfer of shares

SR NO	CASE	CONDITIONS
1	Rights and Bonus Issue	<p>FEMA provisions allow a person resident outside India and holding an investment in an Indian company to make investments in equity instruments (other than share warrants) issued by such company as a rights issue or a bonus issue.</p> <p>Issuance must be in accordance with other applicable laws/ statutes such as the Companies Act, or for listed companies, the SEBI (Issue of Capital and Disclosure Requirements) Regulations of 2009, other applicable regulations and subject to adherence to the sectoral caps, if any.</p> <p>The shareholding in relation to which the rights or bonus issuance is made must have been acquired and held per the provisions of the extant FEMA regulations.</p> <p>The rights offer to persons resident outside India is:</p> <p>(a) in case of listed companies, at a price as determined by the company.</p> <p>(b) in case of unlisted companies, at a price which is not less than the price at which the rights offer is made to resident shareholders.</p> <p>(c) The aforesaid conditions shall also be applicable in case a person resident outside India who invests in equity instruments (other than share warrants) issued by an Indian company as a rights issue that are renounced by the person to whom it was offered.</p>
2	Acquisition of equity instruments under scheme of compromise or arrangement/ merger/ demerger/ amalgamation of Indian companies	<p>Scheme of compromise or arrangement/mergers/ demergers/ amalgamations of Indian companies are usually governed by an order issued by a competent authority or the National Company Law Tribunal (NCLT) on the basis of the scheme submitted by the companies undergoing merger/ demerger/ amalgamation. Once the scheme of merger or demerger or amalgamation of two or more Indian companies has been approved by a competent authority or the NCLT in India, the transferee company or the new company, as the case may be is allowed to issue equity instruments to the existing shareholders of the transferor company resident outside India, subject to the conditions that:</p> <p>(a) the transfer or issue is in compliance with the entry routes, sectoral caps or investment limits, as the case may be, and the attendant conditionalities of investment by a person resident outside India. Provided, where the percentage is likely to breach the sectoral caps or the attendant conditionalities, the</p>



SR NO	CASE	CONDITIONS
		<p>transferor company or the transferee or new company may obtain necessary approval from the government.</p> <p>(b) the transferor company or the transferee or the new company is not engaged in activities which are prohibited under the FDI policy.</p> <p>Note: government approval would not be required in case of mergers and acquisitions taking place in sectors falling under the automatic route.</p> <p>Where a scheme of compromise or arrangement or merger or amalgamation of two or more Indian companies or a reconstruction by way of demerger or otherwise of an Indian company where any of the companies involved are listed on a RSE in India, then the scheme of arrangement is required to be in compliance with the SEBI (Listing Obligation and Disclosure Requirement) Regulations, 2015.</p>
3	Issue of non-convertible/redeemable bonus preference shares or debentures	<p>Indian companies are allowed to issue non-convertible/redeemable preference shares or debentures to non-resident shareholders, including the depositories that act as trustees for the ADR or GDR holders. The same can be done by Indian companies by way of distribution as a bonus from its general reserves under a scheme of arrangement approved by NCLT or competent authority in India under the provisions of the Companies Act, as applicable. Further, the same is subject to obtaining a no-objection from Income Tax Authorities and the following conditions namely:</p> <p>(a) The original investment made in the Indian company by the non-resident is in accordance with the extant FEMA regulations.</p> <p>(b) The said issuance is in accordance with the provisions of Companies Act, 2013. Further, the terms and conditions, if any, stipulated in the scheme approved by NCLT or competent authority are required to be complied with.</p> <p>(c) The Indian company is not engaged in activities/ sectors wherein investments by non-residents are prohibited.</p>
4	Share swap	<p>In case of investment by way of swap of shares, irrespective of the amount, valuation of the shares will have to be made by a merchant banker registered with SEBI or an investment bank outside India registered with the appropriate regulatory authority in the host country. Government approval will also be a pre-requisite for investments against swap of shares for sectors under the government approval route. Government approval is not required for swap of shares of companies engaged in sectors which are under automatic route.</p>
5	Employee Stock Option Plan (ESOP)/ Sweat Equity/ Share Based Employee Benefits	<p>An Indian company may issue ESOPs and/ or sweat equity shares and/or share based employee benefits to its employees/directors or employees/ directors of its holding company or joint venture or wholly owned overseas subsidiary/ subsidiaries who are resident outside India, provided that:</p> <p>(a) The scheme has been drawn either in terms of regulations issued under the SEBI Act, 1992 or the Companies (Share Capital and Debentures) Rules, 2014 notified by the government under the Companies Act 2013, as the case may be.</p>



SR NO	CASE	CONDITIONS
		<p>(b) The ESOPs/ sweat equity shares/ share based benefits issued to non-resident employees/ directors under the applicable rules/ regulations are in compliance with the sectoral cap applicable to the said company.</p> <p>(c) Issue of ESOPs/ sweat equity shares/ share based benefits by a company where foreign investment is under the approval route requires prior government approval.</p> <p>(d) Issue of ESOPs/ sweat equity shares/ share based benefits under the applicable rules/ regulations to an employee/director who is a citizen of Bangladesh/ Pakistan requires prior government approval.</p> <p>(e) The issuing company is required to furnish Form-ESOP to the relevant RBI regional office under whose jurisdiction the registered office of the company operates, within 30 days from the date of issue of the employee stock options or sweat equity shares.</p>

7.4 Pricing and valuation guidelines

- Pricing and valuation guidelines have been prescribed for:
 - Issue of equity instruments by an Indian company to a person resident outside India;
 - Transfer of equity instruments from a resident to a person resident outside India; and
 - Transfer by a person resident outside India to a person resident in India.

Pricing methodology for each instrument:

SR NO	INSTRUMENT	APPLICABILITY OF PRICING GUIDELINES
1	Equity shares	<p>Issue/ transfer by way of sale/ buy back etc. of equity shares are subject to pricing guidelines.</p> <p>Price of shares issued to a person resident outside India under the FDI route <u>should not be less than</u>:</p> <p>A. the value determined as per internationally accepted pricing methodology on an arm's length basis for the unlisted companies duly certified by a chartered accountant (CA) or a SEBI registered merchant banker or a practicing cost accountant, for unlisted Indian companies;</p> <p>B. the price worked out in accordance with the relevant SEBI guidelines in case of a listed Indian company or of a company going through a delisting process, as per the SEBI (Delisting of Equity Shares) Regulations, 2009.</p> <p>In case of transfer from person resident in India to a person resident outside India, the price <u>should not be less than</u>:</p> <p>A. the price worked out in accordance with the relevant SEBI guidelines a listed Indian company</p>



SR NO	INSTRUMENT	APPLICABILITY OF PRICING GUIDELINES
		<p>B. the price at which a preferential allotment of shares can be made under the SEBI guidelines, as applicable, in case of a listed Indian company or in case of a company going through a delisting process as per the SEBI (Delisting of Equity Shares) Regulations, 2009</p> <p>C. the value determined as per internationally accepted pricing methodology on an arm's length basis for the unlisted companies duly certified by a CA or a SEBI registered merchant banker or a practicing cost accountant, in case of unlisted Indian companies</p> <p>In case of transfer from person resident outside India to a person resident in India, the price <u>should not be more than:</u></p> <p>(a) the price worked out in accordance with the relevant SEBI guidelines in case of a listed Indian company</p> <p>(b) the price at which a preferential allotment of shares can be made under SEBI guidelines, as applicable, in case of a listed Indian company or in case of a company going through a delisting process as per the SEBI (Delisting of Equity Shares) Regulations, 2009</p> <p>(c) the value determined as per Internationally accepted pricing methodology on an arm's length basis for the unlisted companies duly certified by a CA or a SEBI registered merchant banker or a practicing Cost Accountant, in case of unlisted Indian companies</p>
2	CCDs, CCPS and CNs	Price/ conversion formula of convertible equity instruments should be determined upfront at the time of issue of the instruments. The price at the time of conversion should not in any case be lower than the fair value at the time of issuance of such instruments in accordance with FEMA, rules and regulations made thereunder.
3	Swap of shares	Valuation involved in the swap arrangement is required to be made by a SEBI registered merchant or investment bank outside India registered with an appropriate regulatory authority in the host country.
4	Share warrants	Pricing and the price/ conversion formula is determined upfront.
5	Partly paid equity shares	The pricing of the partly paid equity shares is required to be determined upfront.
6	Equity shares of a newly incorporated company	Where shares in an Indian company are issued to a person resident outside India in compliance with the provisions of the Companies Act, 2013, by way of subscription to Memorandum of Association (MOA), such investments are required to be made at face value subject to entry route and sectoral caps.



7.5 Non-applicability of pricing guidelines:

- The pricing guidelines will not apply for investment in equity instruments by a person resident outside India on non-repatriation basis.
- The pricing guidelines will not be applicable for any transfer by way of sale done in accordance with SEBI regulations where the pricing norm is prescribed by SEBI. A CA certificate to the effect that relevant SEBI regulations/ guidelines have been complied with is required to be attached to the Foreign Currency – Transfer of Shares (FCTRS) form filed with the Authorised Dealer (AD) bank.
- The valuation certificate issued by a Chartered Accountant or a SEBI registered merchant banker or a practicing cost accountant must not be more than ninety days old as on the date of the transfer

8 COMPLIANCES – TAX AND REGULATORY

8.1 Basic concepts

- **Scope of income**

Income of a non-resident is taxable in India, if the income is:

- Received in India; or
- Deemed to be received in India; or
- Accrues or arises in India; or
- Deemed to accrue or arise in India.

- **Concept of assessment year and previous year**

- From an income tax perspective, previous year is the year in which a tax payer earns an income, while assessment year is the year following the previous year in which previous year's income is evaluated.
- For example, if the previous year is from 01 April 2021 to 31 March 2022, then the assessment year for income earned during this period would begin after the previous year ends, i.e. on 01 April 2022 till 31 March 2023.

8.2 Types of taxable income

Typically, the following types of income are earned in relation to FDIs in a previous year in Indian securities:

- Dividend
- Interest
- Capital gains/ losses earned on transfer of securities

8.3 Taxation under the provisions of the Income Tax Act

- **Dividend**

Prior to 01 April 2020, recipients earning income through dividend declarations and distributions from an Indian company were exempt from tax under the provisions of the IT Act and the Indian company paying the dividend was subject to dividend distribution tax (DDT) at the specified rate.

However, a significant change to the current system of dividend taxation was introduced in the Finance Act 2020 by abolishing the DDT regime and a shift was made to the classical system of taxing dividends in the hands of shareholders.

Accordingly, with effect from 01 April 2020, dividends paid by Indian companies will now be taxable in the hands of the shareholders at the basic tax rate of 20 per cent²⁴ and Indian companies would be liable to withhold taxes on the such dividend paid to the shareholders.

Further, with effect from 01 April 2019, provisions have been inserted to levy an additional surcharge on income of certain non-corporate assesseees (other than partnership firms and co-operative societies) at the rate of 25 per cent and 37 per cent (super-rich surcharge) where the income of such assesseees (other than specified capital gains) exceeds the prescribed threshold. However, as per the provisions of the Finance Act 2020, the super-rich surcharge shall not be levied on income in the nature of dividend in addition to capital gains earned by FDI and the maximum surcharge leviable in such cases would be 15 per cent.

Further, no deduction for any expenses shall be allowed from the dividend income where the dividend income is taxable on a gross basis.

- **Interest**

Under the provisions of the IT Act, the total income of a foreign company or any other non-corporate foreign entity, includes any income through, interest received, inter alia, from an Indian concern on debt incurred by it in a foreign currency, such income shall be taxable at the rate of 20 per cent (plus applicable surcharge and health and education cess). Non-qualifying interest income would be subject to tax at the rate of 40 per cent (plus applicable surcharge and health and education taxes).

Interest payable in respect of loans obtained in a foreign currency by issue of an RDB²⁵ shall be taxable at a concessional rate of 5 per cent (plus applicable surcharge and health and education cess) under the IT Act.

We have summarised the effective tax rates applicable to FDI entites as provided under the IT Act:

TAXABLE INCOME (IN INR)	NON-CORPORATE ASSESSEE (OTHER THAN FIRMS) (refer note below)	FIRM	CORPORATE ASSESSEE
	Surcharge (%)	Surcharge (%)	Surcharge (%)
Up to 5 million	Nil	Nil	Nil
5 million to 10 million	10%		
10 million to 20 million	15%	12%	2%
20 million to 50 million	25%		
50 million to 100 million	37%		
> 100 million			5%

²⁴ The rates are base tax rates and have to be increased by applicable surcharge and education cess

²⁵ Where bond is issued before 1 July 2023

Note: The Finance Act, 2020 restricted the maximum rate of surcharge to 15 per cent in the case of income derived from capital gains on the transfer of listed securities and income derived from dividends earned by a non-corporate assessee (other than firms). The Finance Act, 2022, capped the surcharge rate at 15 per cent for capital gains arising from transfer of any long term capital asset i.e. not only restricted to listed securities.

- **Tax filing exemptions for specified incomes**

Under the provisions of the IT Act, where the total income of a foreign company or any other non-corporate foreign entity, consists of only income derived from: interest received from an Indian concern on debt incurred by it in foreign currency or interest received from loans obtained in a foreign currency issued by the RDB or income derived from dividends, it is not necessary to file a tax return in India provided taxes are deducted appropriately as prescribed under the IT Act and the rate at which tax is deducted is not lesser than the rates specified under the IT Act.

- **Capital gains**

The taxability of capital gains earned by an FDI on the transfer of Indian securities and derivatives broadly depends on:

- the type of security transferred
- the period for which the securities were held prior to their transfer

In accordance with the provisions of the IT Act, the capital gains or losses are computed by reducing from the sale consideration:

- the cost of acquisition of the asset transferred; and
- any expenditure incurred wholly and exclusively in connection with the transfer

The gains or losses are classified as short-term or long-term depending on the period of holding discussed below:

SOURCE OF INCOME	PERIOD OF HOLDING	TYPE OF GAIN/ LOSS
Capital gains/ losses arising from transfer of unlisted shares	24 months or less before date of sale	Short-term
	More than 24 months before date of sale	Long-term
Capital gains/ losses arising from transfer of listed equity shares/ other listed securities	12 months or less before date of sale	Short-term
	More than 12 months before date of sale	Long-term
Capital gains/ losses arising from transfer of securities other than those mentioned in point (1) and (2) above	36 months or less before date of sale	Short-term
	More than 36 months before date of sale	Long-term



● Tax rates

Effective tax rates applicable to FDI entities on capital gains as provided under the IT Act for the income earned in respect of securities are as follows:

TYPE OF CAPITAL GAINS		TAXABLE INCOME EARNED BY FOREIGN CORPORATE ENTITY		TAXABLE INCOME EARNED BY NON-CORPORATE FDI ENTITY (OTHER THAN PARTNERSHIP FIRMS)				TAXABLE INCOME EARNED BY NON-CORPORATE FDI ENTITY (PARTNERSHIP FIRMS)
		INR 10 million < Total income ≤ INR 100 million	Total income > INR 100 million	INR 5 million < Total income ≤ INR 10 million	INR 10 million < Total income ≤ INR 20 million	INR 20 million < Total income ≤ INR 50 million	Total income > INR 50 million	Total income > INR 10 million
Capital gains on transfer of unlisted shares ²⁶ or listed equity shares where STT is not paid	Long-term	10.61%	10.92%	11.44%	11.96%	11.96%	11.96%	11.65%
	Short-term	42.43%	43.68%	34.32%	35.88%	39.00%	42.74%	34.94%
Capital gains ²⁷ on transfer of listed equity shares (STT is paid)	Long-term	10.61%	10.92%	11.44%	11.96%	11.96%	11.96%	11.65%
	Short-term	15.91%	16.38%	17.16%	17.94%	17.94%	17.94%	17.47%
Capital gains on transfer of debt securities (listed or unlisted)	Long-term	10.61%	10.92%	11.44%	11.96%	11.96%	11.96%	11.65%
	Short-term	42.43%	43.68%	34.32%	35.88%	39.00%	42.74%	34.94%

8.4 Taxation under the provisions of Double Taxation Avoidance Agreement (DTAA)

Where an agreed double taxation treaty exists between India and another country, the provisions of the DTAA if it is more beneficial to the applicable taxpayer will override the provisions of the IT Act.

²⁶ The IT Act provides for foreign exchange fluctuation protection to a non-residents, on short-term gains arising on transfer of shares or debentures

²⁷ Inter-se set-off of capital gains and losses allowed subject to Rules, carry forward of losses allowed up to 8 years

To benefit from the provisions of the DTAA, an FDI entity will have to obtain a Tax Residency Certificate (TRC) confirming its tax residency under the respective DTAA from the home country tax authorities and maintain a self-declaration (in Form 10F) in case the TRC does not contain the prescribed particulars.

Summary of the treaty provisions of the countries from which significant investment is made into India:

PARTICULARS	SINGAPORE	MAURITIUS	JAPAN	NETHERLANDS	USA
Capital gains (Article 13 of the respective tax treaties)	Under Article 13 of the India-Singapore tax treaty, capital gains on equity shares acquired prior to 01 April 2017 are tax exempt and equity shares acquired post 01 April 2017 are taxable as per the provisions of the domestic tax law. For rates please refer to the table above. Capital gains on any other security (except equity shares) is tax-exempt in India.	Under Article 13 of the India-Mauritius tax treaty, capital gains on equity shares acquired prior to 01 April 2017 are exempt and equity shares acquired post 01 April 2017 are taxable as per the provisions of the domestic tax law. For rates please refer to the table above. Capital gains on any other security (except equity shares) is tax-exempt in India.	Under Article 13 of the India-Japan tax treaty, capital gains on the transfer of shares is taxable as per the provisions of the domestic tax law. For rates please refer the table above. Capital gains on any other security (except equity shares) is exempt from tax in India.	Under Article 13 of the India-Netherlands tax treaty, capital gains from transfer of shares of a company where the seller holds at least 10 % of the shares of such company are taxable as per the provisions of the domestic tax law. For rates please refer the table above. Capital gains on any other security (except equity shares) is tax-exempt in India.	Under Article 13 of the India-USA tax treaty, capital gains from transfer of shares and securities is taxable as per the provisions of the domestic tax law. For rates please refer the table above.
Dividend (Article 10 of respective tax treaties)	Dividend income is taxable at the following rates: 1) 10% ²⁸ 2) In cases other than (1) above, 15%	Dividend income is taxable under in India at the following rates: 1) 5% ²⁹ 2) In cases other than (1) above, 15%	Tax rate for dividend income is shall not exceed 10% subject to satisfaction of the beneficial ownership condition	Tax rate for dividend income is shall not exceed 10% subject to satisfaction of the beneficial ownership condition	Dividend income is taxable at the following rates: 1) 15% ³⁰ 2) In cases other than (1) above, 25%
Interest (Article 11 of the respective	Interest income is taxable at following rates: 1) 10% ³¹	The tax rate for interest income shall not exceed 7.5% subject to satisfaction of the beneficial	The tax rate for interest income shall not exceed 10% subject to satisfaction of the	The tax rate for interest income shall not exceed 10% subject to satisfaction of the	Interest income is taxable in India at following rates: 1) 10% ³²

²⁸ Dividend shall be taxable at the rate of 10 per cent if the beneficial owner of the dividend is a company holding atleast 25 per cent of the capital of the company paying the dividend

²⁹ Dividend shall be taxable at the rate of 5 per cent if the beneficial owner of the dividend is a company holding atleast 10 per cent of the capital of the company paying the dividend

³⁰ Dividend shall be taxable at the rate of 15 per cent if the beneficial owner of the dividend is a company holding atleast 10 per cent of the voting stock of the company paying the dividend

³¹ Interest shall be taxable at the rate of 10 per cent if the interest is paid on a loan granted by a bank carrying on a bona fide banking business or by a similar financial institution (including an insurance company)

³² Interest shall be taxable at the rate of 10 per cent if the interest is paid on a loan granted by a bank carrying on a bona fide banking business or by a similar financial institution (including an insurance company)



PARTICULARS	SINGAPORE	MAURITIUS	JAPAN	NETHERLANDS	USA
tax treaties)	2) In cases other than (1) above, 15%	ownership condition	beneficial ownership condition	beneficial ownership condition	2) In cases other than (1) above, 15%

8.5 Securities Transaction Tax (STT) Securities transacted on an RSE in India are subject to STT levied as follows:

TRANSACTION	RATES	PAYABLE BY
Purchase and sale of equity shares on the stock exchange and the contract for purchase and sale is settled by actual delivery or transfer of share	0.1%	Purchaser/Seller
Sale of equity shares on the stock exchange and the contract for sale is settled otherwise than by the actual delivery or transfer of share	0.025%	Seller
Transfer of securities on a RSE in IFSC	NIL	NA

No STT is payable on transaction in debt securities.

8.6 Other relevant tax provisions

- Signing of the Multilateral Convention:

The Multilateral Convention signed in Paris in 2017 implements tax treaty-related measures to prevent base erosion and profit shifting (BEPS). To date, 99 countries³³ including India have signed the Convention with more are expected to sign.

The Convention allows jurisdictions to swiftly implement measures to strengthen existing tax treaties to protect governments against tax avoidance strategies that inappropriately use tax treaties to artificially shift profits to a low or no-tax location.

The measures are intended to put an end to treaty abuse and treaty shopping by transposing in existing tax treaties jurisdictions' commitment to minimally include in their tax treaties tools to ensure these treaties are used in accordance with their intended purpose.

One of the minimum international tax standards applicable to countries who are signatories to the Convention is the Principal Purpose Test (PPT). The PPT is an anti-abuse rule based on the principal purposes of the transaction or arrangements. The PPT provides a general way to address cases of treaty-abuse, including taking advantage of favourable treaty jurisdictions commonly referred as treaty-shopping situation.

The PPT provisions included in the Convention establish that a tax authority may deny the benefits of a tax treaty where it is reasonable to conclude that having considered all the relevant facts and circumstances, one of the principal purpose of the arrangement or the transaction was to obtain the benefits of the tax treaty.

The Convention will operate to modify tax treaties between two or more parties to the Convention. It will not function in the same way as an amending the protocol of a single existing treaty, which would directly amend the text of the covered tax agreement. Instead, it will be applied alongside existing tax treaties, modifying their application in order to implement the BEPS measures.

- General anti-avoidance rule (GAAR)

³³ Status as on 21 April 2022

GAAR provisions were introduced in the IT Act effective from 01 April 2017³⁴. According to the IT Act, GAAR applies to any arrangement where the main purpose is to obtain a tax benefit. In its present shape, GAAR has the power to override DTAA (i.e. where the arrangement qualifies as an impermissible arrangement, treaty benefits could be denied).

- Indirect transfer provisions

Indirect transfer provisions were introduced in the IT Act by the Finance Act, 2012 to clarify that an asset being a share or interest in a company or entity registered or incorporated outside India shall be deemed to be situated in India, if the share or interest derives its value (directly or indirectly) substantially from assets situated in India. Hence, transfer of such a capital asset will be liable to tax in India.

A share or interest in a foreign company or entity is deemed to derive its value substantially from assets (tangible or intangible) located in India, if the value of the Indian assets on a specified date³⁵:

- exceed INR 100 million; and
- represent at least 50 per cent of the value of all the assets owned by such foreign company or entity.

Further, the indirect transfer provisions shall not apply to shareholders not holding the right of management or control of the company or entity registered or incorporated outside India and holding less than 5 per cent of the total voting power, share capital or interest in the company or entity registered or incorporated outside India.

- Minimum Alternative Tax (MAT)

As per the provisions of the IT Act, if the tax payable by a tax payer on the total income computed as per the provisions of the IT Act is less than 15 per cent of its 'book profit', then notwithstanding anything contained in any other provision of the IT Act, the 'book profit' shall be deemed to be the total income of the tax payer. Further, the amount of tax payable shall be the amount of income tax at the rate of 15 per cent (plus applicable surcharge and health and education taxes) on such total income.

It may be noted that the provisions of MAT shall not be applicable and shall be deemed never to have been applicable to foreign company, if:

- The foreign company is a resident of a country or a specified territory with which India has entered into treaty and the foreign company does not have a PE in India in accordance with the provisions of the treaty; or
- The foreign company is a resident of a country with which India does not have a treaty and the foreign company is not required to seek registration under any law for the time being in force relating to companies.

Accordingly, MAT should not ordinarily apply to FDI entities.

- Withholding tax

The IT Act casts an obligation to withhold taxes at source on a person responsible for making a payment to a non-resident where such payment is chargeable to tax in India under the provisions of the IT Act. Given the above, where any capital gains arise on the transfer of shares, the buyer would be required to withhold tax at

³⁴ Investments up to 31 March 2017 are grandfathered from the applicability of GAAR

³⁵ The term "specified date" has been defined under the IT Act to mean: -

- date on which the accounting period of the company or entity ends, preceding the date of transfer of share or interest; or
- date of transfer, if the book value of the assets of the company or entity on the date of transfer exceeds the book value of the assets as on the date referred to in clause above, by 15 per cent.

the rates prescribed above (subject to treaty relief, if any). Similarly, the entity paying dividend or interest income would be required to withhold tax at the rates prescribed above (subject to treaty relief, if any).

- Withholding tax rate on non-furnishing of a permanent account number (PAN)

Where the deductee fails to furnish its PAN or furnishes an incorrect PAN to the deductor, the deductor will be required to withhold taxes at the rate specified under the IT Act or the rates in force or 20 per cent, whichever is higher. However, said provisions shall not apply to a non-resident, inter alia, on the payments derived from interest and payments from the transfer of any capital asset if the non-resident deductee furnishes the specified details and documents to the deductor.

- Withholding tax rate for non-tax return filers of income at higher rates

The Finance Act 2021 introduced a new provision with effect from 01 July 2021 to enable for deduction of taxes at source at higher rates for persons who have not filed their annual income tax return. As per the this provision, any person making payment (other than the payments specifically excluded) to specified persons, the taxes shall be deducted at higher of the following rates:

- Twice the rate as specified in the relevant provision of the IT Act; or
- Twice the rate in force; or
- The rate of 5 per cent

For this purpose, a specified person is defined to mean any person who has not filed the annual income tax return for two previous financial years immediately preceding the previous year; where the time limit of filing of annual income tax return has expired and the amount of tax to be deducted at source is INR 0.05 million or more in each of these two previous years.

However, the term specified person specifically excludes a non-resident who does not have a permanent establishment (PE) in India.

- Certain provisions relating to taxability in case of transfer of shares

Under the provisions of the IT Act, where consideration received on the transfer of shares other than listed shares, is less than its fair market value, then fair market value of such shares determined in the prescribed manner as per the Income-tax Rules, 1962 shall be considered to be sale consideration for the purpose of computing capital gains computation chargeable to tax.

Also, the IT Act, inter alia, provides that where any person receives any property (including shares) without consideration or for inadequate consideration in excess of INR 0.05 million, the fair market value or excess of the fair market value of such property i.e. shares (determined in the prescribed manner as per the Income-tax Rules, 1962) shall be taxed in the hands of person receiving the shares.

9 KEY COMPLIANCES

9.1 Key tax compliances

- **Permanent Account Number (PAN)**

To obtain a PAN, simply fill out Form 49AA and provide proof of identity and address.

- **Payment of taxes on income earned in India**

A taxpayer is required to estimate their tax liability for a financial year and discharge the same by payment of an 'advance tax' on the due dates outlined below:

DUE DATE OF TAX PAYMENT	AMOUNT OF TAX LIABILITY TO BE DISCHARGED BY A TAXPAYER
15 June	15%
15 September	45%
15 December	75%
15 March	100%

Any delay in paying advance tax has interest and penalty implications.

- **Filing of annual income-tax return**

Income earned by the FDI entity in India must be reported in an annual income-tax return filed with the CBDT as per the following schedule:

TAXPAYER	FILING DATE
Non-corporate taxpayer	Before 31 July following the financial year*
Corporate taxpayer	Before 31 October following the financial year*

* Extended to 30 November, following the financial year where transfer pricing (TP) provisions apply to the taxpayer.

Income tax returns may be subject to scrutiny.

- **Withholding tax/ compliance for remittance of proceeds outside India**

The provisions of the IT Act read with the Income-tax Rules, 1962 provides that the person making the payment (the remitter) to a non-resident (recipient) of any sum (whether or not taxable in India) is required to furnish electronically the information relating to the said payment in Form 15CA (Self-Declaration) to the Indian Revenue Authorities (IRA) based on a certificate from a CA in Form 15CB.

- **Application for lower/ NIL withholding certificate**

An application can be made to the IRA under the IT Act for the purpose of issuing a certificate to the effect that, the taxes, if any, on the income of a person, required to be deducted should be deducted at a rate lower than the rate prescribed under the IT Act or at a NIL rate. The said application is required to be made in the manner prescribed under the IT Act and fulfilment of specified conditions.

- **Transfer pricing**

Provisions for transfer pricing (TP) on international transactions between associated enterprises are prescribed within the IT Act. Such transactions between related parties and certain transactions with non-residents are to be reported to the IRA using Form 3CEB. The due date for filing is 31 October following the financial year.

Further, a master file and a local file is required as proof of transfer pricing to substantiate the international transaction between related parties. Details are provided below:

- **Master file**

The master file document contains high level information about the global business operations and TP policy of a group as a whole. The master file will usually include standardised information about the group's organisational structure; significant value drivers; main geographical locations; description of the business activities of members of the group (i.e. products, services, supply chain etc.); information about the group's intangibles; financing activities within the group (including external funding); and financial and tax positions of the group.

- **Local file**

The local file supports the master file and relates to a specific taxpayer in a specific country - usually a single legal entity. The local file is intended to deliver a more detailed overview of the related party's transactions that are entered into by a specific taxpayer and the comparison of the TP policies with the actual (financial) result.

The information provided in the local file would typically supplement the information in the master file and would include a detailed description of; the management structure of the local entity; related party transactions entered in the year; copies of related material inter-company agreements concluded by the local entity; application of TP methodology; and financial information of the local entity.

- **Reporting of Specified Financial Transaction (SFT)**

Under the IT Act, specified persons are required to report details of Specified Financial Transaction (SFT) using Form 61A. The specified person includes, inter alia, a company issuing shares or bonds or debentures. SFT includes, inter alia, receipt from any person of an amount of INR 1 million or more in a financial year for acquiring shares, or INR 1 million or more in a financial year for acquiring bonds or debentures. An Indian company is required to report SFTs for indirect transfers (discussed above).

- **Reporting requirements in case of indirect transfer**

For the purpose of determining the amount of Indian income tax on the transfer of shares of the company or entity registered or incorporated outside India, the Indian concern or the entity whose shares are held by such company or entity registered or incorporated outside India, is required to maintain and furnish to the income tax authority, the information and documents as prescribed under the IT Act. The Indian concern whose shares are indirectly getting transferred are required to undertake reporting obligations in Form 49D.

Further, where indirect transfer provisions are applicable, FDIs are required to furnish a form 3CT (certified by an accountant which should indicate the basis of apportionment of income in accordance with the formula prescribed) along with its return of income.

The list of requirements above are not exhaustive and there may be additional requirements under the IT Act depending on each case.

9.2 Regulatory reporting requirements under FDI³⁶

● **Foreign Currency-Gross Provisional Return (FC-GPR) form**

An Indian Company is required to report using form FC-GPR within 30 days of issue of equity instrument to a person resident outside India.

● **Annual return on foreign liabilities and assets (FLA)**

An Indian company which has received FDI or an LLP which has received foreign investment by way of capital contribution in the previous year(s) including the current year, is required to submit form FLA to the RBI on or before the 15th day of July of each year³⁷.

● **Foreign Currency- Transfer of Shares (FC-TRS) form**

In accordance with NDI rules, form FC-TRS must be completed to report the transfer of equity instruments between:

- A. a person resident outside India holding equity instruments in an Indian company on a repatriable basis and person resident outside India holding equity instruments on a non-repatriable basis; and
- B. a person resident outside India holding equity instruments in an Indian company on a repatriable basis and a person resident in India,

Form FC-TRS must be submitted to the AD bank, within 60 days from the date of transfer of the equity instruments or receipt/ remittance of funds whichever is earlier. The onus to report will be on the transferor/ transferee, resident in India or the person resident outside India holding equity instruments on a non-repatriable basis, as the case may be.

● **Compliance in relation to allotment of equity instruments**

Equity instruments are required to be issued to the person resident outside India making such FDI within 60 days from the date of receipt of the consideration.

In case of partly paid equity shares, 60 days is required from the date of receipt of each call payment.

Where the equity instruments are not issued within 60 days from the date of receipt of the consideration, the same is required to be refunded to the person concerned by outward remittance through banking channels or by credit to his non-resident account or FCNR accounts, as the case may be. The funds are required to be refunded within a period of 15 days from the date of completion of 60 days counted from the date of receipt of the consideration.

● **Compliance for downstream investment**

An Indian company making downstream investment in another Indian company which is considered as indirect foreign investment for the investee company in terms of FDI regulations, is required to notify the Secretariat for Industrial Assistance, and the DPIIT within 30 days of investment³⁸ and file Form DI within 30 days from the date of allotment of the equity instruments.

³⁶ FEMA (Mode of Payment and Reporting of Non-Debt Instruments) Regulations, 2019

³⁷ Year for this purpose shall be reckoned as April to March

³⁸ Filing to DPIIT is required to be made even if equity instruments have not been allotted along with the modality of investment in new/existing ventures (with/without expansion programme)

The first level Indian company making the downstream investment shall be responsible for complying with the NDI provisions for the downstream investment made by it at second level and so on and so forth. The first level company shall obtain a certificate to this effect from its statutory auditor on an annual basis and such compliance of these rules shall be mentioned in the Director's report in the Indian company's annual report.

If a statutory auditor has provided a qualified report, it shall be immediately brought to the notice of the regional RBI office in whose jurisdiction the registered office of the Indian company is located and an acknowledgement from the registered office obtained.

- **LLP (I) and LLP (II) forms**

LLPs are required to make additional declarations using forms LLP (I) and LLP (II). For sums obtained from the acquisition of profit shares, form LLP (I) must be filed within 30 days from the date of receipt of the amount of consideration. Form LLP(II) must be completed for the disinvestment or transfer of capital contribution or profit share between a resident and a non-resident (or vice versa) within 60 days from the date of receipt of funds. The onus of reporting is on the resident transferor/ transferee.

- **Convertible Note (CN) form**

The Indian start-up company issuing CNs to a person resident outside India must file Form CN within 30 days of such issue. A person resident in India, who may be a transferor or transferee of CNs issued by an Indian start-up company must report such transfers to or from a person resident outside India, as the case may be, in Form CN within 30 days of such transfer.



**PART C:
FOREIGN PORTFOLIO
INVESTMENT ROUTE**

PART C: FOREIGN PORTFOLIO INVESTMENT ROUTE

10 INTRODUCTION

10.1 Regulatory framework

Over the last thirty years, India has implemented economic reforms and opened up its economy to allow portfolio investments by foreign institutional investors in Indian securities.

The process of liberalisation of the Indian economy also necessitated for a set of framework/ regulations to provide stability to the Indian capital markets and a regulatory body to monitor the same. Accordingly, the Securities and Exchange Board of India was established as a statutory body in 1992 to protect the interests of investors in securities and to promote the development of, and to regulate, the Indian securities market.

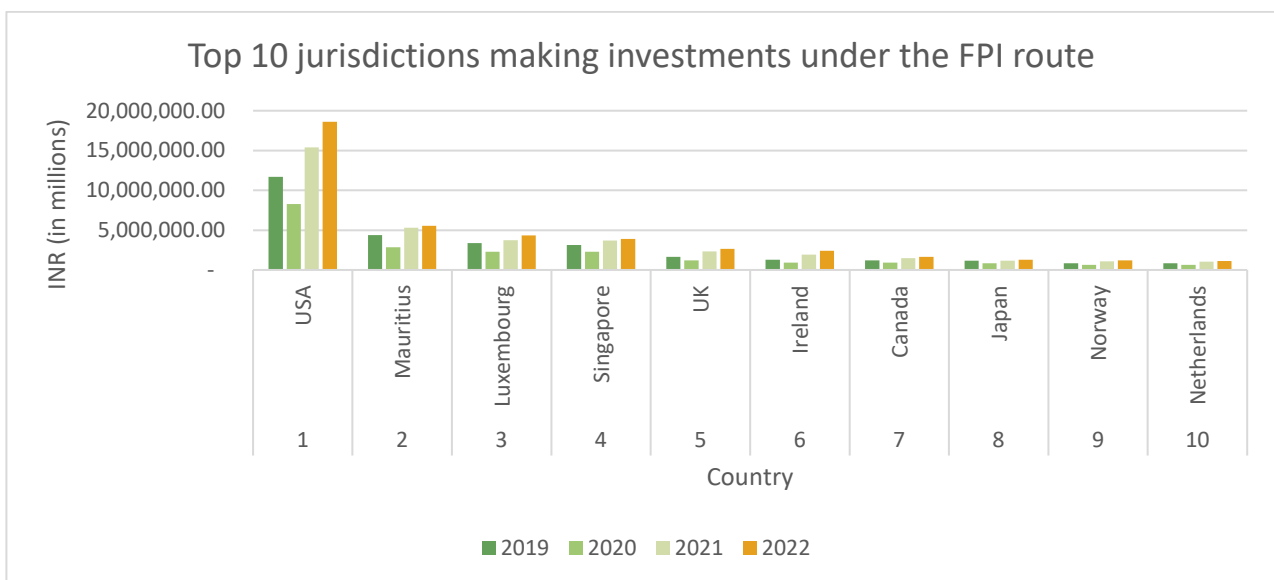
In 1995, the first set of regulations governing foreign portfolio investments into India ie the SEBI (Foreign Institutional Investors) Regulations 1995 were notified. The SEBI FII regulations were updated from time to time and were ultimately replaced by the SEBI (Foreign Portfolio Investors) Regulations, 2014.

Under the FPI regulations, SEBI extended certain administrative powers to Designated Depository Participants (DDPs) to facilitate inter alia the registration of FPIs and the monitoring of their activities such that they are undertaken within the scope of the SEBI regulations.

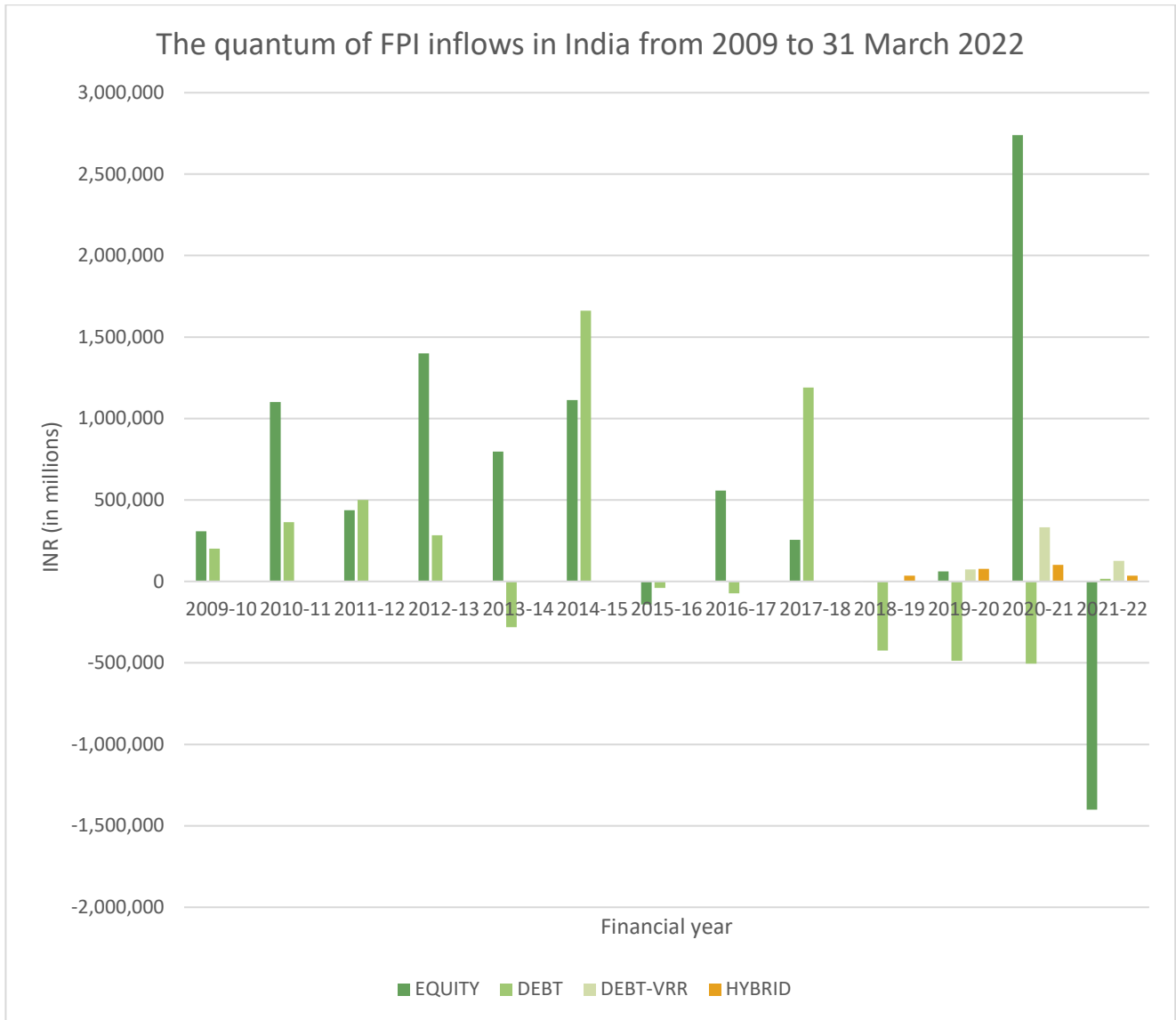
The 2014 regulations were subsequently replaced in 2019, by an updated set of FPI regulations, introduced with effect from 23 September 2019, with the primary objective to provide clarity and transparency to the investors. In addition, on 05 November 2019, SEBI also notified operational guidelines for FPIs and DDPs to facilitate the implementation of the SEBI FPI Regulations, 2019. Thus, presently, the investments made by FPIs in India are governed by the SEBI FPI Regulations, 2019

10.2 KEY STATISTICS

While India has witnessed FPI investments from a host of jurisdictions, the top 10 jurisdictions making investments under the FPI route are depicted below:



The quantum of FPI inflows in India from 2009 to 31 March 2022:



Source: NSDL FPI monitor

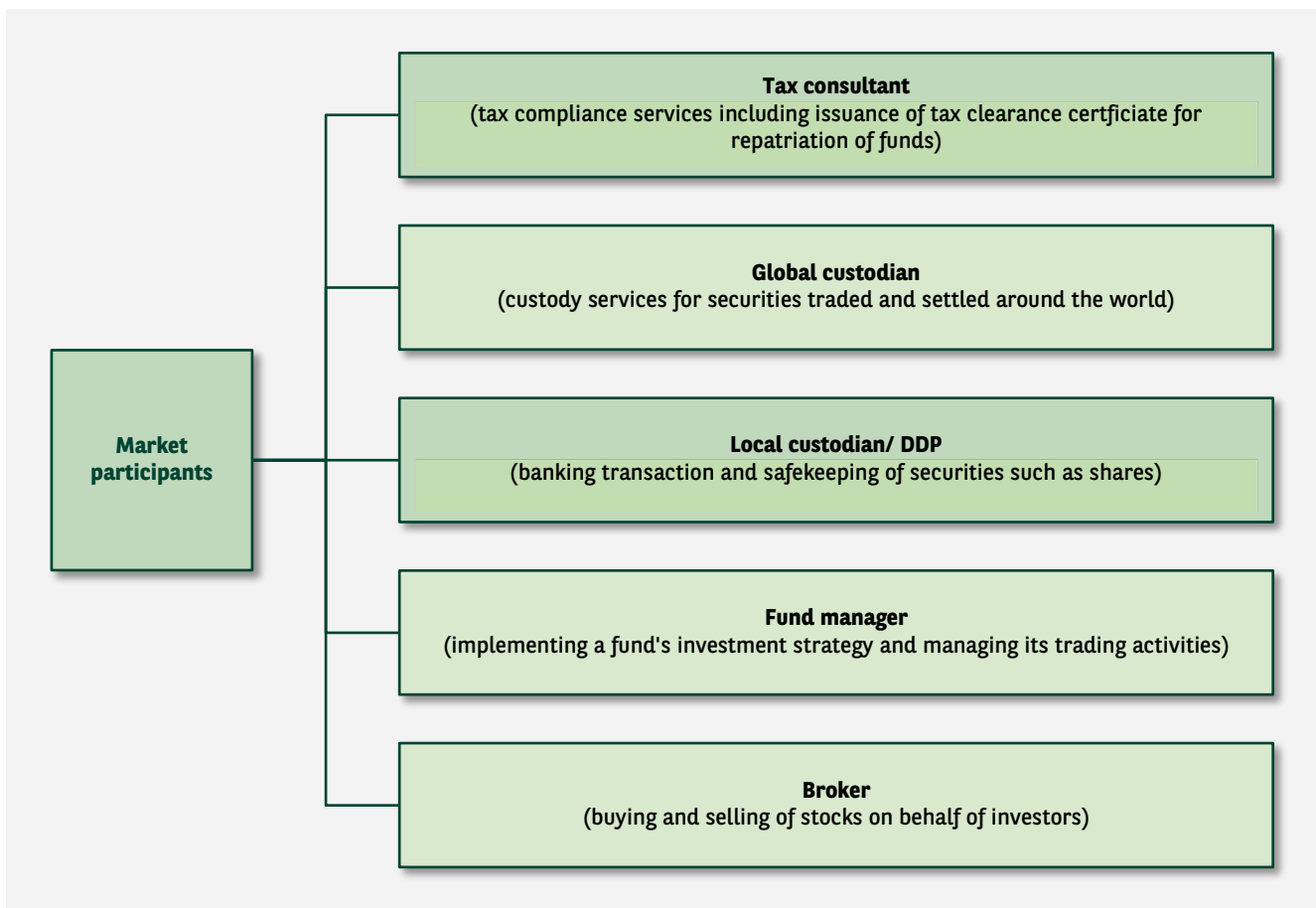
The total cumulative investment by FPIs (at the acquisition cost):

PARTICULARS	APRIL 2021 TO NOVEMBER 2021	APRIL 2020 TO NOVEMBER 2020	INCREASE
Cumulative investment by FPIs ³⁹	288.36 billion	264 billion	9.2%

As at March 31, 2022, over 10,000 FPIs are registered with SEBI.

10.3 Market participants

To invest into India's capital market, FPIs must appoint the following market participants:



³⁹ Economic Survey of India 2021-22

11 REGISTRATION REQUIREMENTS

11.1 Eligibility criteria

To obtain a registration as an FPI, an applicant has to satisfy the following conditions:

- The applicant should not be an RI⁴⁰ (except where the applicant incorporated or established in an International financial services centre (IFSC)) or NRI⁴¹ or an Overseas Citizen of India (OCI⁴²). NRIs or OCIs or RIs may be constituents of the applicant subject to satisfaction of prescribed conditions.
- The applicant should be a resident of a country whose securities market regulator is a signatory to the International Organization of Securities Commission's Multilateral Memorandum of Understanding (MMOU)⁴³ or a signatory to the Bilateral Memorandum of Understanding (BMOU)⁴⁴. The above condition would not apply if the applicant is a government or government-related investor or for applicants incorporated or established in an IFSC.
- The applicant may be a banking company being a resident of a country whose central bank is a member of Bank for International Settlements (BIS). However, central banks of countries are not required to be a member of BIS⁴⁵ to be eligible for FPI registration. Further, this condition is not applicable where the applicant is incorporated or established in an IFSC.
- The applicant or its underlying investors contributing 25 per cent or more in the corpus of the applicant or identified on the basis of control, should not be the persons mentioned in the Sanctions List notified from time to time by the UN Security Council.
- The applicant should meet the 'fit and proper'⁴⁶ criteria specified in SEBI (Intermediaries) Regulations, 2008

⁴⁰ The term RI shall have the meaning assigned to 'person resident in India' under FEMA which means:

- a person residing in India for more than 182 days during the course of the preceding financial year but does not include –
 - a person who has gone out of India or who stays outside India, in either case –
 - for or on taking up employment outside India, or
 - for carrying on outside India a business or vocation outside India, or
 - for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;
 - a person who has come to or stays in India, in either case, otherwise than –
 - for or on taking up employment in India, or
 - for carrying on in India a business or vocation in India, or
 - for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period;
- any person or body corporate registered or incorporated in India,
- an office, branch or agency in India owned or controlled by a person resident outside India,
- an office, branch or agency outside India owned or controlled by a person resident in India.

⁴¹ The term 'NRI' has been defined as per the NDI Rules to mean an individual resident outside India who is a citizen of India.

⁴² The term 'OCI' has been defined as per the NDI Rules to mean an individual resident outside India who is registered as an OCI Cardholder under Citizenship Act, 1955.

⁴³ List of the current signatories to IOSCO's MMOU is available at <https://www.iosco.org/about/?subSection=mmou&subSection1=signatories>

⁴⁴ List of the current signatories to BMOU is available at https://www.sebi.gov.in/sebi_data/internationalAffr/IA_BilMoU.html

⁴⁵ List of the countries whose central bank is a member of BIS is available at <https://www.bis.org/about/member>

⁴⁶ An FPI shall be deemed as a 'fit and proper' after taking into following criteria (but not limited to these criterias only) in relation to the applicant, the principal officer and the key management persons:

- integrity, reputation and character;
- absence of convictions and restraint orders;

- The applicant should not be a resident in the country identified in the public statement of FATF⁴⁷ as –
 - a jurisdiction with an inadequate anti-money laundering or combating the financing of terrorism mechanism; or
 - a jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with the FATF to address the deficiencies.
- Any other criteria as may be specified by SEBI from time to time.

11.2 Prescribed categories of registration

An applicant seeking registration as an FPI may apply in one of the categories indicated below. As per the FPI Regulations, FPIs can be categorised as a Category I or Category II FPI:

SR NO	CATEGORY I	CATEGORY II
1	Government and related investors ⁴⁸	Appropriately regulated funds not eligible as a Category I FPI
2	Pension funds and university funds	Endowments and foundations, charitable organizations, corporate bodies, family offices, individuals
3	Appropriately regulated entities ⁴⁹ such as insurance/ reinsurance entities, banks, asset management companies, investment manager, investment advisor, portfolio managers, broker dealers and swap dealers An applicant incorporated or established in an IFSC shall be deemed to be appropriately regulated	Appropriately regulated entities investing on behalf of the client (private banks, etc)
5	Entities whose investment manager is from FATF member country and registered as a category I FPI; or entities which are at least 75 per cent owned, directly or indirectly, by entities from FATF	

- competence including financial solvency and network.

⁴⁷ List of the countries that are listed in the public statement issued by FATF is available at <http://www.fatf-gafi.org/publications/high-riskandnon-cooperativejurisdictions>

⁴⁸ Central banks, sovereign wealth funds, international or multilateral organizations or agencies and entities controlled or at least 75 per cent, directly or indirectly, owned by the Government and its related investors

⁴⁹ 'Appropriately regulated' means an applicant that means an entity which is regulated by the securities market regulator or the banking regulator of the home jurisdiction.

member countries eligible under second, third and fourth category mentioned above⁵⁰

Impact of registration category

While the registration of an FPI as a Category I or II FPI would largely be dependent on the facts of the case, where an option exists, the following aspects could be relevant in making a decision:

- From a regulatory standpoint, Category I FPIs benefit from:
 - Light-touch Know Your Customer (KYC) requirements (discussed subsequently)
 - Higher trading limits for futures and options (and certain other securities)
- From a taxation standpoint, Category I FPIs and its investors are exempted from the applicability of indirect transfer tax provisions (discussed subsequently).

11.3 Registration process

- SEBI has notified a common application form (CAF)⁵¹ for registration of FPIs, allotment of PAN (tax identification number) and KYC for opening bank and demat account.
- CAF has six sections, which are as under:
 - Part A: KYC Information
 - Part B: FPI Registration number
 - Part C: Information for obtaining PAN
 - Part D: Depository and bank account opening
 - Part E: Declaration and undertaking
 - Part F: Documents uploading

The annexure to CAF further has the following four sections:

- Declaration and undertaking
- Additional information
- Undertaking from the investment manager
- Undertaking from eligible category I entity
- Applicants seeking registration will need to fill CAF and the annexure to the CAF.
- Applications for registration can be made to the DDP along with the applicable fees, which are as follows:

SR NO	CATEGORY OF INVESTORS	SEBI FEES CURRENTLY PRESCRIBED PAYABLE FOR EVERY THREE YEARS ⁵²
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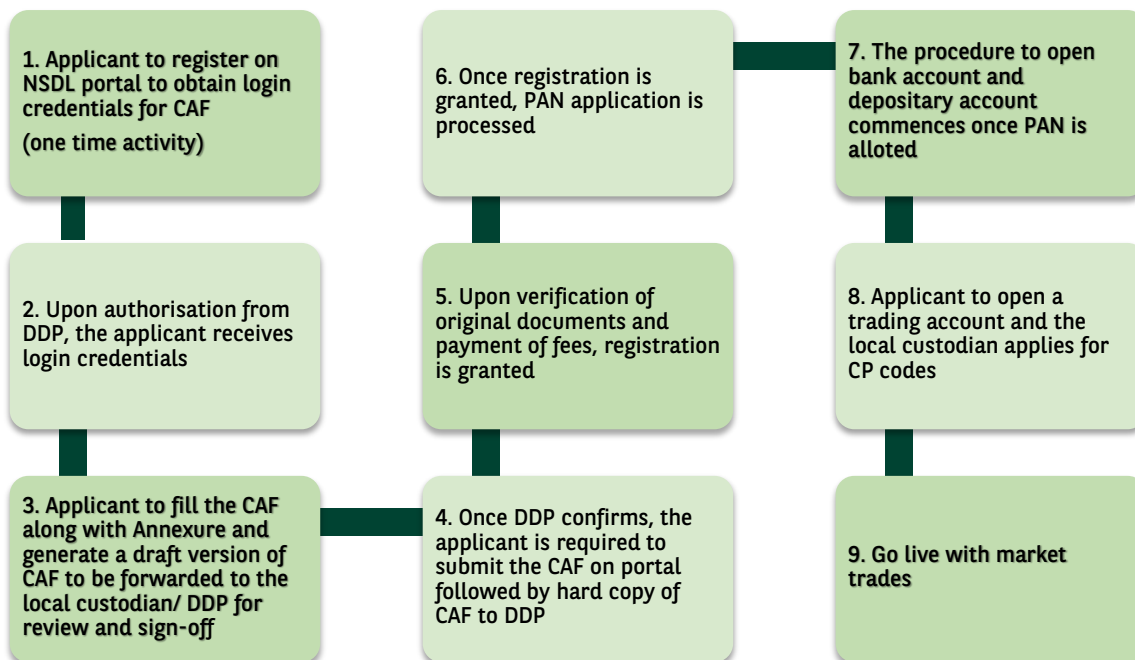
⁵⁰ The Investment Manager or entities mentioned under category no 2, 3 and 4 above are required to provide an undertaking of it being responsible for all the acts of commission or omission of the applicants seeking FPI registration

⁵¹ Circular No IMD/FPI&C/P/2020/022 dated 4 February 2020

⁵² The above fees are excluding fees for Common Application Form/ application of Permanent Account Number (PAN).

1	Category I	USD 3,000
2	Category II	USD 300

- SEBI has issued the operational guidelines to register as an FPI (through the DDP) . As per the applicable guidelines, the DDP would consider an application if the prescribed eligibility criteria (discussed in para 11.1) is satisfied.
- Where the application form is incomplete, or lacks clarity, the applicant would be advised by the DDP to clarify or furnish the desired information within a reasonable time.
- Specific guidance has been provided in the FPI regulations for specific entities including banks/ banking subsidiaries, insurance/ reinsurance entities, pension funds, appropriately regulated entities investing on behalf of their clients, applicants established or incorporated in IFSCs and for Multiple Investment Managers structures.
- A certificate of registration granted to an FPI is permanent unless suspended or cancelled by SEBI or surrendered by the FPI subject to payment of renewal fees which are due every three years.
- Registration is generally granted within 30 days of application.
- FPIs must designate a bank (regarded as AD), broker and custodian/ DDP in India such as BNP Paribas India to route all their investment transactions in the country. They are permitted to freely repatriate their capital after discharge of appropriate Indian income taxes. To start investing, the FPI simply needs simply to remit money from outside India to its Indian bank account and place a trade order with the broker.
- Documents required for FPI registration:
 - Constitutive documents i.e. Memorandum of Association (MOA) and Articles of Association (AOA), prospectus, etc.
 - KYC document as per category of applicant (for detailed discussion refer Para 14.1)
 - Any other document, if prescribed by SEBI
- Step-by-step registration process:



Key points for consideration

CAN AN ENTITY WITH FDI INVESTMENTS IN INDIA ALSO REGISTER AND MAKE INVESTMENTS AS AN FPI?

Yes (subject to investment cap and sectoral limits). While all companies wishing to act as an FPI need registration, no separate registration, per se, is required for FDI investments.

CAN AN ENTITY WITH AN FVCI REGISTRATION ALSO REGISTER AND MAKE INVESTMENTS AS AN FPI?

YES (SUBJECT TO SATISFACTION OF PRESCRIBED CONDITIONS. THE ENTITY WILL BE REQUIRED TO OBTAIN A SEPARATE REGISTRATION AS AN FVCI.



12 INVESTMENT INSTRUMENTS AND LIMITS

12.1 Types of investment instruments under the FPI route

Subject to prescribed terms and conditions, FPIs can generally invest in the following instruments:

INSTRUMENT TYPE	PERMISSIBLE
EQUITY INSTRUMENTS [Refer Note 1 below]	
Listed equity shares/ to be listed equity shares	Yes
Listed CCPS	Yes
Listed CCDs	Yes
Warrants	Yes
Partly paid equity shares	Yes ⁵³
DEBT INSTRUMENTS	
Government securities (including coupons on existing Government securities) (Note 2)	Yes
Treasury bills	Yes
Listed bonds/ Non-Convertible Debentures (NCDs) ⁵⁴ (Note 3)	Yes
Commercial papers	Yes ⁵⁵
RDBs	Yes
Credit enhanced bonds	Yes
Securitised debt instruments ⁵⁶	Yes
Partly paid debt instruments	No
Municipal debt instruments	Yes
Debt instruments issued by banks (eligible for inclusion in regulatory capital)	Yes
Listed non-convertible/ redeemable preference shares or debentures (subject to prescribed conditions)	Yes ⁵⁷
Privately placed bonds (if it is listed within 15 days)	Yes
DERIVATIVE INSTRUMENTS	
Exchange traded derivatives (approved by SEBI) [including equity/ index derivatives]	Yes
Overnight index swaps/ Interest rate swaps	Yes ⁵⁸
OTHERS	

⁵³ Partly paid shares that have been issued to a person resident outside India are required to be fully called-up within twelve months of such issue or as may be specified by the Reserve Bank from time to time. Twenty- five per cent of the total consideration amount (including share premium, if any) are required to be received upfront

⁵⁴ Including NCDs/ Bonds which are under default, privately placed bonds, and those issued by Infrastructure Finance Companies

⁵⁵ FPIs have been permitted to invest in Commercial Papers vide Foreign Exchange Management (Debt Instruments) Regulations 2019 notified on 17 October 2019

⁵⁶ Including any certificate or instrument issued by a special purpose vehicle set up for securitisation of asset/s with banks, Financial Institutions or Non-banking finance companies as originators

⁵⁷ Issued pursuant to an approved scheme of arrangement

⁵⁸ Notification No. FMRD.DIRD.14/2019 issued by RBI

INSTRUMENT TYPE	PERMISSIBLE
Units of equity-oriented MF	Yes
Units of debt-oriented MF	Yes
Liquid and money market MF schemes	No
ETFs (investing less than or equal to 50 per cent in equity)	Yes
Units of infrastructure debt funds	Yes
Units of REIT, InvIT (classified as Hybrid securities) and Category III AIF	Yes
Security receipts issued by ARCs	Yes
Indian Depository Receipt	Yes
Bonus non-convertible/ redeemable preference shares or debentures subject to prescribed conditions	Yes
SLB (Note 4)	Yes
Capital contribution in an LLP	No

Note 1: FPIs are not allowed to short-sell in the Indian market except as allowed under the SLB framework or any other framework specified by SEBI. Further, sales against open purchases are not permitted for FPIs, and FPIs can sell such securities only after their settlement.

Note 2 – FPI investments in government securities, treasury bills, and/or state development loans without any minimum residual maturity requirement should not exceed 30 per cent of the total investment of the FPI in that category⁵⁹. The requirement that these short-term investments should not exceed 30 per cent of total investment by an FPI in that category applies on an end-of-day basis.

Note 3 – FPIs are permitted to invest in corporate bonds with a minimum residual maturity of above one year subject to the condition that short-term investments should not exceed 30 per cent of total investment of the FPI in corporate bonds. The requirement that these short-term investments should not exceed 30 per cent of total investment by an FPI in that category applies on an end-of-day basis. However, these restrictions would not apply to the following securities:

- a. Security receipts and debt instruments issued by ARCs;
- b. Debt instruments issued by an entity under the corporate insolvency resolution process as per the resolution plan approved by the NCLT under the Insolvency and Bankruptcy Code, 2016; and
- c. NCDs/ corporate bonds which are under default, either fully or partly, in the repayment of principal on maturity or principal instalment in the case of amortising bond⁵⁹.

Note 4 – The SLB scheme has been introduced by SEBI for market participants in 2007 and has been operational since 21 April 2008. SEBI vide circular dated 20 December 2007, has framed the broad mechanism for operationalising of the SLB Scheme under the overall framework of the Securities Lending Scheme, 1997.

Note 5: With a view to increase depth and liquidity of the commodity derivative market, SEBI recently released a Consultation Paper allowing FPIs to participate in Exchange Traded Commodity Derivatives (ETCDs) on recognised stock exchanges.

⁵⁹ RBI/2017-18/199 A.P. (DIR Series) Circular No. 31 dated 15 June 2018 (updated upto 26 February 2021)

12.2 Investment limits – Equity and Debt

FPIs can invest in debt or equity securities in India and there is no restriction on the allocation of investments between debt and equity securities. An FPI proposing to invest in debt securities is, however, required to comply with the allocation limits, which are notified by circulars issued by SEBI or the RBI from time to time. In addition, equity investments are also subject to certain limits imposed under the FPI regulations.

- FPI investment limits for equity instruments:

- **Individual limit**

Subject to the overall aggregate limits, the total purchase made by an FPI should be less than 10 per cent of the total paid-up equity capital of the company on a fully diluted basis⁶⁰ or less than 10 per cent of the paid-up value of each series of debentures or preference shares or share warrants issued by an Indian company.

Certain clarifications listed below have been provided on the aspect of clubbing of investment limits for investments made by foreign government and related entities like foreign central banks, sovereign wealth funds and foreign government agencies registered as FPIs:

- In case, two or more FPIs including foreign governments/ their related entities are having direct or indirect common ownership of more than 50 per cent or control, all such FPIs will be treated as forming part of an investor group and the investment limits of all such entities shall be clubbed to a single FPI.
- The investment by foreign government agencies shall be clubbed with the investment by the foreign government / its related entities for the purpose of calculation of 10 per cent limit for FPI investments in a single company, if they form part of an investor group.
- The investment by foreign government/ its related entities from provinces/ states of countries with federal structure shall not be clubbed if the said foreign entities have different ownership and control.
- For the purpose of application of 10 per cent limit for FPI investments in a single company, World Bank Group or the IBRD, IDA, MIGA and IFC are exempted from clubbing of the investment limits.

- **Sectoral limit**

Where there is a composite sectoral cap under the FDI policy, limits for overall FPI investment should be within such overall FDI sectoral caps. FDI/ FPI in almost all sectors is permitted.

- **Aggregate Limit**

Prior to 01 April 2020, the aggregate FPI investment limit in any Indian company was 24 per cent of the total capital of that company.

⁶⁰ 'Fully diluted basis' means the total number of shares that would be outstanding if all possible sources of conversions are exercised

With effect from the 01 April 2020, the aggregate limit for an FPI would be the sectoral caps applicable to the Indian companies with respect to FDI investments

However, the aforesaid limits may be decreased by the Indian companies to a lower threshold, by passing resolution by its Board of Directors, followed by special resolution by its General Body. Once the aggregate limit has been increased to a higher threshold, the Indian company cannot reduce the same to a lower threshold. Further, the aggregate limit with respect to an Indian company in a sector where FDI is prohibited would be 24 per cent.

- FPI investment limits for debt instruments:

- a) Foreign investment limits in Government securities and State Development Loans as on 31 March 2022.

The revised limits for FPI Investments in government securities and state development loans for the financial year 2021-22 has not been announced till date and accordingly till such time the following current limits would continue to prevail:

SR NO	INSTRUMENT TYPE - GOVERNMENT SECURITIES	AMOUNT (INR IN MILLION)
1	Government securities (General)	2,345,310
2	Central government securities (Long term)	1,035,310
3	State Development Loans (General)	676,300
4	State Development Loans (Long term)	71,000

- b) Foreign investment limits in corporate bonds as on 31 March 2022 The limit for FPI Investments in corporate bonds are as under:

SR NO	INSTRUMENT TYPE - CORPORATE BONDS	AMOUNT (INR IN MILLION)
1	Existing FPI Limit	5,414,880
2	Revised Limit for half year ending April 2021 to September 2021	5,742,630
3	Revised Limit for half year ending October 2021 to March 2022	6,070,390

- Additional investment limits/ conditions pertaining to debt investments

A. Concentration limits

Investment by any FPI (including investments by related FPIs), in each of the following three categories of debt: government securities, State Development Loans and corporate debt securities, are subject to the following concentration limits:

- Long-term FPIs: 15 per cent of prevailing investment limit for that category.
- Other FPIs: 10 per cent of prevailing investment limit for that category.



B. FPI investment in government securities and State Development Loans

- The cap on aggregate FPI investments in any government security has been revised to 30 per cent.
- Currently, FPIs are permitted to invest in government securities till the limit utilisation reaches 90 per cent. Once the 90 per cent is crossed, an auction mechanism is used to trigger the allocation of the remaining limit. However, on account of commencing the online monitoring of utilisation of government securities limits, the auction mechanism has been discontinued.
- Utilisation of FPI investments limits in government securities and State Development Loans is being monitored online by Clearing Corporation of India Ltd. The primary responsibility of complying with all limits for investments in government securities and State Development Loans shall lie with FPIs and DDPs.

C. Single/ Group investor-wise limit in corporate bonds:

- Investment by any FPI and its related FPIs, cannot exceed 50 per cent of any issue of a corporate bond. In case an FPI, including related FPIs, has invested in more than 50 per cent of any single issue, it shall not make further investments in that issue until this stipulation is met.
- The requirement of single/ group investor-wise limits in corporate bonds would not be applicable to investments by Multilateral Financial Institutions and investments by FPIs in following securities:
 - Security receipts and debt instruments issued by ARCs;
 - Debt instruments issued by an entity under the corporate insolvency resolution process as per the resolution plan approved by the NCLT under the Insolvency and Bankruptcy Code, 2016; and
 - NCDs/ corporate bonds which are under default, either fully or partly, in the repayment of principal on maturity or principal instalment in the case of amortising bond.

13 OTHER KEY INVESTMENT WINDOWS

13.1 Voluntary Retention Route (VRR)

The RBI in consultation with the government and SEBI introduced on 24 May 2019, a separate investment channel, called the Voluntary Retention Route ('VRR'), to enable FPIs to invest in debt markets in India. Broadly, investments through the VRR route will be free of the macro-prudential and other regulatory norms applicable to FPI investments in debt markets, provided FPIs voluntarily commit to retain a required minimum percentage of their investments in India for a period.

The objective of the VRR is to attract long-term and stable FPI investments into debt markets while providing FPIs with the operational flexibility to manage their investments.

We have listed down the key features of investment under VRR:

- **Eligible instruments**

- **Government:** Government securities, treasury bills and state development loans
- **Corporate:** NCDs, bonds, commercial papers, security receipts issued by ARC, debt instruments issued by banks, eligible for inclusion in regulatory capital, credit enhanced bonds, listed non-convertible/redeemable preference shares or debentures, municipal bonds, securitised debt instruments, units of domestic ETF investing only in debt instruments, RDBs/ units issued by infrastructure debt funds.
- Repo transactions and reverse repo transactions.

● Investment conditions

FPIs are voluntarily required to commit to retain a minimum of 75 per cent of their allocated investments called the committed portfolio size (CPS) for a minimum period of three years (retention period). FPIs are required to invest such 75 per cent of the CPS within three months from the date of allotment. No FPI (including its related FPIs) would be allotted an investment limit greater than 50 per cent of the amount offered for each allotment by tap or auction in case there is a demand for more than 100 per cent of amount offered. The minimum retention period is three years or as may be decided by RBI for each allotment. During this period, FPIs are required to maintain 75 per cent of the CPS in India. The required investment amount should be adhered to an end of day basis.

The investment through this route is in addition to general investment limit and capped at INR 2,500,000 , million or higher as may be decided by RBI. FPIs are required to open a separate Special Non-Resident Rupee (SNRR) Account for funds flowing in relation to investments under this route.

● Disinvestment related provisions

FPIs that wish to exit their investments under this route prior to the end of retention period may do so by selling it to other FPIs subject to buyer FPI abiding by the terms and conditions applicable to the seller FPI.

At the end of the retention period, an FPI may exit by liquidating its portfolio or shift its investments to the general investment limit (subject to availability of limits) or hold the investment until the date of maturity or date of sale, whichever is earlier.

13.2 Fully Accessible Route (FAR)

The RBI, in consultation with the government, introduced a separate channel, called the 'Fully Accessible Route' (FAR), to enable non-residents to invest in specified government-dated securities without any ceiling limits. FPIs also qualify as investors eligible to make investment under the FAR. The investment limits and concentration norms (discussed in Para 12.2 above) shall not apply in case of FPIs investing in specified government securities through the FAR.

We have listed down the key features of investment under FAR:

- **Eligible investors:** Any person resident outside India⁶¹. This would include FPIs.
- **Eligible instruments:** Government securities as may be notified. Currently, the following securities have been notified
 - 6.18% GS 2024
 - 7.32% GS 2024
 - 6.45% GS 2029

⁶¹ Person resident outside India has been defined in FEMA to mean person who is not resident in India

- 7.26% GS 2029
- 7.72% GS 2049
- 7.16% GS 2050
- 5.79% GS 2030
- 5.22% GS 2025
- 5.77% GS 2030
- 6.67% GS 2050
- 5.15% GS 2025
- 5.85% GS 2030
- 5.63% GS 2026
- All new issuance of government securities of 5-year, 10-year and 30-year tenor from the financial year 2020-21.
- **Investment conditions:** There are no quantitative limits on investment by eligible investors in the above-mentioned securities. Further, the investments made under FAR need not adhere to the minimum residual maturity, security-wise limits in government securities and concentration limits as explained above.

13.3 International Financial Services Centre (IFSC)

An IFSC is a jurisdiction that provides financial services to non-residents and residents, to the extent permissible under the current regulation, in any currency except Indian Rupee.

GIFT City, the only place in India which is designated as an IFSC at present, is a central business hub with state-of-the-art infrastructure and a first of its kind development in India. An FPI incorporated or established in IFSC would be deemed to be appropriately regulated.

For better clarity and understanding we have separately discussed the compliances/ taxability relating to investment in IFSC in **Part D** of this guide.



14 KYC REQUIREMENTS

14.1 KYC documentation requirements

PARTICULARS	DOCUMENTS TYPE	CATEGORY - I	CATEGORY - II
Applicant level	Constitutional documents (MOA, AOA, certificate of incorporation, prospectus etc)	Mandatory	Mandatory
	Proof of address	Mandatory ⁶²	Mandatory ⁶³
	PAN	Mandatory	Mandatory
	Board Resolution (BR) ⁶³	Exempt	Mandatory
	FATCA/ CRS form	Mandatory	Mandatory
	Form/ KYC form	Mandatory	Mandatory
Authorised signatories	List and signatures#	Mandatory	mandatory
Ultimate beneficial owner	List of Ultimate beneficial owners including the details of Intermediate beneficial owner ⁶⁴	Mandatory	mandatory
	Proof of identity	Exempt	Mandatory

FPIs are required to provide KYC-related documents based on the category under which it is registered. Once the KYC is completed, the intermediary will upload the form and supporting documents on the KYC Registration Agencies portal for other market intermediaries to access and complete their KYC requirements.

Apart from the KYC requirement stated above, each intermediary may have to complete additional documentation requirements for enhanced due diligence as per their internal policies.

⁶² POA provided to custodian/ DDP stating address acceptable as proof of address

⁶³ FPIs from certain jurisdictions where the practice of passing of BRs is not common practice, the POA provided to global custodian/ local custodian is acceptable. POA granted to global/ local custodian is accepted in lieu of BR. BR and the authorised signatory list is not required if SWIFT is used as a medium of instruction.

⁶⁴ Not required for government and government related entities

14.2 Other key points

- Prospectus and information memorandum are acceptable in lieu of an official constitutional document.
- Valid FATCA/ CRS documentation must be submitted at the time of account opening.
- PAN is not mandatory for United Nations entities/ multilateral agencies exempt from paying taxes/ filing tax returns in India.
- BR and the authorized signatory list is also not required if there is no exchange of physically signed documents/ agreements between the local broker and the FPI or its authorised representative being an Investment Manager regulated in FATF member country.
- If the FPI holds separate depository accounts in both NSDL and CDSL, it may appoint only one DDP/ custodian.
- SEBI recently amended the FPI Regulations to empower itself to grant relaxation from the strict enforcement of any of the FPI Regulations. SEBI can grant such relaxation either suo-moto or on an application made by FPI (along with the prescribed fee) in this regard. The relaxation may be granted where the non compliance could arise due to factors beyond the control of the entity or if the requirement is procedural or technical in nature.

14.3 Identification and verification of beneficial owner

- Beneficial owners are the natural persons who ultimately own or control an FPI. The identification of beneficial owners should be in accordance with Indian anti-money laundering rules⁶⁵. As per the said rules, the materiality threshold for identification of beneficial owners is more than 25 per cent for corporate FPIs and 15 per cent for other FPIs. However, a lower materiality threshold of 10 per cent may be applied for FPIs coming from high risk jurisdictions.
- Beneficial owners of FPIs with general partner/ limited partnership structure are to be identified on an ownership or entitlement basis and control basis.
- FPIs (other than government or government related investors) are required to provide a list of their beneficial owners, inter alia, including the following details:
 - Name and address of beneficial owner (natural person)
 - Date of birth
 - Tax residency jurisdiction
 - Nationality
 - Whether acting alone or together through one or more natural persons as group, with their names and address
 - Beneficial owner group's percentage shareholding/ capital/ profit ownership in the FPIs
 - Tax residency number/ social security number/ passport number of the beneficial owner/ any other government-issued identity document number (not required for Category I FPIs)

⁶⁵ Rule 9 of Prevention of Money Laundering (Maintenance of record) Rules, 2005



- A PAN is not mandatory for ultimate beneficial owners, senior management and authorised signatories of an FPI.

14.4 Periodic KYC review

The DDP may seek confirmation from the FPI whether there is any change in the documents/ information provided earlier. If there is any change, the FPI is required to provide the updated documents/ information to the DDP. We have provided below the periodicity within which an FPI is required to undertake a KYC review.

JURISDICTION	CATEGORY I	CATEGORY II
High risk	For government and government related investors - During continuance of registration i.e. every 3 years For others - Annually	Annually
Non - High risk	During continuance of registration i.e. every 3 years	Regulated entities - during continuance of registration i.e. every 3 years Others - Annually

15 INDIA TAX FRAMEWORK FOR FPI

15.1 Basic concepts

● Scope of income

Income of a non-resident is taxable in India, if the income is:

- received in India; or
- deemed to be received in India; or
- accrues or arises in India; or
- deemed to accrue or arise in India.

● Concept of assessment year and previous year

From an income tax perspective, previous year is the year in which a tax payer earns an income, while assessment year is the year following the previous year in which previous year's income is evaluated.

For example, if the previous year is from 01 April 2021 to 31 March 2022, then the assessment year for income earned during this period would begin after the previous year ends, i.e. on 01 April 2022 till 31 March 2023.

● Types of income

The Indian tax law provide for a special concessional tax framework for investments made by FPIs in India. Typically, the following types of income are earned by FPIs in a financial year on account of investments in securities:

- Dividend
- Interest
- Capital gains earned on transfer of securities

15.2 Taxation under the provisions of the IT Act

A. Dividend

Prior to 01 April 2020, recipients earning income through dividend declarations and distributions from an Indian company were exempt from tax under the provisions of the IT Act and the Indian company paying the dividend was subject to DDT at the specified rate.

However, a significant change to the current system of dividend taxation was introduced vide the Finance Act 2020 by abolishing the DDT regime and a shift was made to the classical system of taxing dividends in the hands of shareholders.

Accordingly, with effect from 01 April 2020⁶⁶, dividends paid by the Indian companies will now be taxable in the hands of the FPIs at the basic tax rate of 20 per cent⁶⁷ and the Indian companies would be liable to withhold taxes on the such dividend paid to the FPIs.

Withholding tax

Prior to 01 April 2021, a 20 per cent²⁷ withholding tax rate was prescribed on dividend income. However, the Finance Act 2021, amended the existing provisions to provide for the withholding of taxes on dividend pay-outs to FPIs at the rate of 20 per cent or the rates provided in the relevant DTAA, whichever is lower. The rates provided in the relevant DTAA is subject to furnishing of TRC and availability of benefits under the relevant DTAA. Accordingly, with effect from 01 April 2021⁶⁸, dividends paid by the Indian companies will now be subject to withholding at the rate of 20 per cent²⁷ or rates provided in the relevant DTAA, whichever is lower.

We have summarised the effective tax rates applicable to FPIs on dividend income earned as provided under the IT Act as under

AMOUNT OF DIVIDEND INCOME EARNED BY FPIs	CORPORATE FPIs	NON-CORPORATE FPIs (OTHER THAN PARTNERSHIP FIRMS)	NON-CORPORATE FPIs (PARTNERSHIP FIRMS)
Up to 5 million	20.80%	20.80%	20.80%
5 million to 10 million	20.80%	22.88%	20.80%
10 million to 20 million	21.22%	23.92%	23.230%
20 million to 50 million	21.22%	23.92%	23.30%
50 million to 100 million	21.22%	23.92%	23.30%
Above 100 million	21.84%	23.92%	23.30%

The aforesaid tax rates are subject to beneficial rates under the provisions of the applicable DTAA, if any.

Where applicable taxes are not withheld on the payment of dividend for any reason, the FPI will need to discharge taxes by itself, prior to remittance or on quarterly advance tax due dates, whichever is earlier, based on tax computed by the tax consultant. Further, where excess taxes are withheld, same could be utilised against other tax liability or can be claimed as a refund.

B. Interest

A concessional tax rate of 5 per cent (plus applicable surcharge and health and education cess) is provided on interest income earned by an FPI from:

- Investment in government securities; or
- Investment in municipal debt securities; or
- Interest distributed by a REIT/ InvIT; or

⁶⁶ Financial Year 2020-21 onwards

⁶⁷ The rates are base tax rates and have to be increased by applicable surcharge and education cess.

⁶⁸ Financial Year 2021-22 onwards

- Investment in RDBs of an Indian company (provided the rate of interest does not exceed the rate notified by the government as mentioned below).

The concessional tax rate of above 5 per cent on interest income earned by FPI from government securities, municipal debt securities and RDBs of an India company is applicable with respect to interest received before 30 June 2023. The rate notified by the government for RDBs issued:

DATE OF ISSUE OF BONDS	MAXIMUM RATE
Prior to 1 July 2010	5% over the SBI Base Rate as on 1 July 2010
After 1 July 2010	5% over the SBI Base Rate as on date of issue of the RDB

Interest earned from other securities (including from RDBs of an Indian company where the rate of interest exceeds the rate notified by the government) would be taxable at 20 per cent (plus applicable surcharge and health and education cess). The payer of interest would, typically, withhold taxes at source on such income.

The interest income will be subject to withholding tax at the same rate. Below is a table summarising the effective tax rates:

TYPE OF INTEREST INCOME	INTEREST ON GOVERNMENT BONDS/ MUNICIPAL DEBT SECURITIES/ REITS/ InvTs/ RDB OF AN INDIAN COMPANY (SATISFYING THE AFORESAID CONDITIONS)			INCOME FROM OTHER SECURITIES		
	Corporate FPIs	Non-Corporate FPIs (Other than firms)	Firm FPIs	Corporate FPIs	Non-Corporate FPIs (Other than firms)	Firm FPIs
Up to INR 5 million	5.20%	5.20%	5.20%	20.80%	20.80%	20.80%
INR 5 million to INR 10 million	5.20%	5.72%	5.20%	20.80%	22.88%	20.80%
INR 10 million to INR 20 million	5.30%	5.98%	5.82%	21.22%	23.92%	23.30%
INR 20 million to INR 50 million	5.30%	6.50%	5.82%	21.22%	26.00%	23.306%
INR 50 million to INR 100 million	5.30%	7.12%	5.82%	21.22%	28.50%	23.306%
Above INR 100 million	5.46%	7.12%	5.82%	21.84%	28.50%	23.30%

The aforesaid tax rates are subject to beneficial rates under the provisions of the applicable DTAA, if any.

Where the issuer of debt securities has not withheld applicable taxes, the FPI will need to discharge taxes by itself, prior to remittance or on quarterly advance tax due dates, whichever is earlier, based on tax computed by the tax consultant.

C. Capital gains



Income earned by an FPI from sale of Indian securities and derivatives will be characterised as 'capital gains' since the securities held by an FPI (in accordance with FPI regulations) are deemed to be capital assets under the provisions of the IT Act.

The taxability of capital gains earned by an FPI on transfer of Indian securities and derivatives broadly depends on:

- type of security transferred; and
- the period for which the securities were held prior to their transfer.

In accordance with the provisions of the IT Act, the capital gains/ loss are computed by reducing from the sale consideration:

- the cost of acquisition of the asset transferred; and
- any expenditure incurred wholly and exclusively in connection with the transfer

No withholding tax applies on capital gains income payable to FPIs. FPIs would have to discharge taxes by themselves, prior to remittance or on quarterly advance tax due dates, whichever is earlier, based on capital gains tax computed by the tax consultant.

The capital gains/ losses are classified as short-term or long-term depending on the period of holding discussed below:

SOURCE OF INCOME	PERIOD OF HOLDING	TYPE OF GAIN/ LOSS
Capital gains/ loss arising from the transfer of listed equity shares/ units of an equity orientated MF/ other listed securities	12 months or less before date of sale	Short-term
	More than 12 months before date of sale	Long-term
Capital gains/ loss arising from the transfer of securities other than those mentioned above (other than unlisted equity shares)	36 months or less before date of sale	Short-term
	More than 36 months before date of sale	Long-term

Effective tax rates (i.e. plus applicable surcharge and health and education cess⁶⁹) applicable to FPIs on capital gains as provided under the IT Act for the income earned in respect of securities are as under⁷⁰:

TYPE OF CAPITAL GAINS		CORPORATE FPIs		NON-CORPORATE FPIs (OTHER THAN PARTNERSHIP FIRMS)		NON-CORPORATE FPIs (PARTNERSHIP FIRMS)
		INR 10 million < Total income ≤ INR 100 million	Total income > INR 100 million	INR 5 million < Total income ≤ INR 10 million	Total income > INR 10 million	Total income > INR 10 million
Income ⁷¹ on transfer of listed equity shares/ equity	Long-term	10.61%	10.92%	11.44%	11.96%	11.65%
	Short-term	15.91%	16.38%	17.16%	17.94%	17.47%

⁶⁹ In case of **corporate taxpayers**, a surcharge of 2 per cent (where total taxable income exceeds INR 10 million but not INR 100 million) or 5 per cent (where total taxable income exceeds INR 100 million) plus a health and education cess of 4 per cent on income-tax and surcharge would be levied

In case of **partnership firms**, a surcharge of 12 per cent (where total taxable income exceeds INR 10 million) plus a health and education cess of 4 per cent on income-tax and surcharge would be levied

In case of **non-corporate taxpayers (other than partnership firms)**, a surcharge of 10 per cent (where total taxable income exceeds INR 5 million but not INR 10 million) or 15 per cent (where total taxable income exceeds INR 10 million) plus a health and education cess of 4 per cent on income-tax and surcharge would be levied

⁷⁰ The tax rates may be amended in subsequent Union Budgets of GOI. Hence, kindly reach out to your Tax Consultant for the most recent tax rates

⁷¹ Inter-se set-off of capital gains and losses allowed subject to Rules; carry forward of losses allowed up to 8 years

oriented MF on market (STT is paid on purchase and sale)						
Capital gains on transfer of debt securities (including debt MF)	Long-term	10.61%	10.92%	11.44%	11.96%	11.65%
	Short-term	31.82%	32.76%	34.32%	35.88%	34.94%
Sale of listed derivatives (listed futures and options)	Short-term	31.82%	32.76%	34.32%	35.88%	34.94%

The taxability and the aforesaid tax rates are subject to beneficial rates under the provisions of the applicable tax treaties, if any.

WHAT ARE THE TAX IMPLICATIONS ON AN FPI FOR UNDERTAKING OFF MARKET TRANSACTIONS?

An FPI is permitted to transfer the securities in an off-market transaction (subject to certain conditions). Long-term and short-term capital gains arising on off market transactions are taxed at the rate of 10 per cent and 30 per cent respectively (plus applicable surcharge and health and education cess⁶⁹). The benefit of indexation is not available to FPIs.

16.3 Taxation under the provisions of DTAA

Where the government has entered into an agreement with the government of any other country for avoidance of double taxation (DTAA), then in relation to a taxpayer to whom such agreement applies, provisions of DTAA to the extent more beneficial will override the provisions of the IT Act.

In order to avail beneficial provisions of the DTAA, FPI will have to obtain a TRC confirming its tax residency under the respective DTAA from the home country tax authorities and maintain a self-declaration (in Form 10F) where the TRC does not contain the prescribed particulars.

We have tabulated below the tax provisions under treaties entered by India with some of the key developed countries⁷² in the world:

NATURE OF INCOME	JURISDICTION				
	SINGAPORE	MAURITIUS	JAPAN	NETHERLANDS	USA
Dividend (Article 10 of respective tax treaties)	Dividend income is taxable at the following rates : 1) 10% ⁷³ 2) In cases other than (1) above, 15%	Dividend income is taxable in India at the following rates: 1) 5% ⁷⁴ 2) In cases other than (1) above, 15%	Tax rate for dividend income shall not exceed 10% subject to satisfaction of beneficial ownership condition	Tax rate for dividend income is shall not exceed 10% subject to satisfaction of beneficial ownership condition	Dividend income is taxable at the following rates: 1) 15% ⁷⁵ 2) In cases other than (1) above, 25%

⁷² These countries are amongst top 10 jurisdictions making investments in India under the FPI route

⁷³ Dividend would be taxable at the rate of 10 per cent if the beneficial owner of the dividend is a company holding atleast 25 per cent of the capital of the company paying the dividend

⁷⁴ Dividend would be taxable at the rate of 5 per cent if the beneficial owner of the dividend is a company holding atleast 10 per cent of the capital of the company paying the dividend

⁷⁵ Dividend would be taxable at the rate of 15 per cent if the beneficial owner of the dividend is a company holding atleast 10 per cent of the voting stock of the company paying the dividend

NATURE OF INCOME	JURISDICTION				
	SINGAPORE	MAURITIUS	JAPAN	NETHERLANDS	USA
Capital gains (Article 13 of the respective tax treaties)	As per Article 13 of the India-Singapore tax treaty, capital gains on equity shares acquired prior to 1 April 2017 are exempt and equity shares acquired post the aforementioned period are taxable as per the provisions of the domestic tax law (for rates please refer the table above). Capital gains on any other security (except equity shares) is exempt from tax in India.	As per Article 13 of the India-Mauritius tax treaty, capital gains on equity shares acquired prior to 1 April 2017 are exempt and equity shares acquired post 1 April 2017 are taxable as per the provisions of the domestic tax law (for rates please refer the table above). Capital gains on any other security (except equity shares) is exempt from tax in India.	As per Article 13 of the India-Japan tax treaty capital gains on transfer of shares is taxable as per the provisions of the domestic tax law (for rates please refer the table above). Capital gains on any other security (except equity shares) is exempt from tax in India.	As per Article 13 of the India-Netherlands tax treaty capital gains from transfer of shares of a company where the seller holds atleast 10% of the shares of such company are taxable as per the provisions of the domestic tax law (for rates please refer the table above). Capital gains on any other security (except equity shares) is exempt from tax in India.	As per Article 13 of the India-USA tax treaty, capital gains from transfer of shares and securities is taxable as per the provisions of the domestic tax law (for rates please refer the table above).
Interest (Article 11 of the respective tax treaties)	Interest income is taxable at following rates: 1) 10% ⁷⁶ 2) In cases other than (1) above, 15%	The tax rate for interest income shall not exceed 7.5% subject to satisfaction of beneficial ownership condition	The tax rate for interest income shall not exceed 10% subject to satisfaction of beneficial ownership condition	The tax rate for interest income shall not exceed 10% subject to satisfaction of beneficial ownership condition	Interest income is taxable in India at following rates: 1) 10% ⁷⁷ 2) In cases other than (1) above, 15%

The benefits under the DTAA may be subject to the LOB article contained in the relevant DTAA. Where the conditions mentioned under the LOB are not satisfied, benefits under the treaty may be denied. Additionally, for applying a beneficial tax rate, the most favored nation clause could be applied which provides for a 'rate lower' or 'scope more restricted' on specified income streams of income.

⁷⁶ Interest would be taxable at the rate of 10 per cent if the interest is paid on a loan granted by a bank carrying on a bona fide banking business or by a similar financial institution (including an insurance company)

⁷⁷ Interest would be taxable at the rate of 10 per cent if the interest is paid on a loan granted by a bank carrying on a bona fide banking business or by a similar financial institution (including an insurance company)



15.4 Securities transaction tax (STT)

Securities transacted on a recognised stock exchange in India are subject to STT which is levied as follows:

TRANSACTION	RATES	PAYABLE BY
Purchase and sale of equity shares or unit of business trust on the stock exchange and the contract for purchase and sale is settled by actual delivery or transfer of share or unit	0.1%	Purchaser/seller
Sale/ redemption of units of equity oriented MF on the stock exchange and the contract for sale is settled by actual delivery or transfer of unit	0.001%	Seller
Sale of equity shares or unit of business trust or unit of equity oriented MF on the stock exchange and the contract for sale is settled otherwise than by the actual delivery or transfer of share or unit	0.025%	Seller
Sale of an option in security on the stock exchange where option is not exercised	0.05% ⁷⁸	Seller
Sale of an option in security where option is exercised on the stock exchange	0.125% ⁷⁹	Purchaser
Sale of a future in securities on the stock exchange	0.01%	Seller
Sale of units of an equity oriented fund to the MF	0.001%	Seller
Sale of unlisted equity shares and unlisted units of a business trust under an offer for sale	0.2%	Seller
Transfer of securities on a recognised stock exchange in IFSC	NIL	Not applicable

No STT is payable on transactions in debt securities/units of debt MF.

⁷⁸ As per NSE website. Further, STT would be computed on the amount of option premium

⁷⁹ STT would be computed on the intrinsic value i.e. difference between the settlement price and the strike price as against the settlement price

15.5 Other relevant tax provisions

● **Signing of the Multilateral Convention:**

In June 2017, India signed the Convention to Implement tax treaty-related measures to prevent BEPS. To date 99 countries have signed the convention.

The Convention allows jurisdictions to swiftly implement measures to strengthen existing tax treaties to protect governments against tax avoidance strategies that inappropriately use tax treaties to artificially shift profits to low or no-tax location.

The measures will put an end to treaty abuse and treaty shopping by transposing in existing tax treaties jurisdictions commitment to minimally include in their tax treaties tools to ensure these treaties are used in accordance with their intended object and purpose.

One of the minimum international tax standards applicable to countries who are signatories to the Convention is the PPT. The PPT is an anti-abuse rule based on the principal purposes of the transaction or arrangements. The PPT provides a general way to address cases of treaty-abuse, including treaty-shopping situation.

The PPT provisions included in the Convention establish that a tax authority may deny the benefits of a tax treaty where it is reasonable to conclude that having considered all the relevant facts and circumstances, one of the principal purposes of the arrangement or the transaction was to obtain the benefits of the tax treaty.

The Convention will operate to modify tax treaties between two or more parties to the Convention. It will not function in the same way as an amending protocol to a single existing treaty, which would directly amend the text of the Covered Tax Agreement. Instead, it will be applied alongside existing tax treaties, modifying their application in order to implement the BEPS measures.

● **General Anti-Avoidance Rules (GAAR)**

GAAR provisions were introduced in the IT Act to be effective from 1 April 2017⁸⁰. According to the IT Act, GAAR applies to any arrangement where the main purpose is to obtain tax benefit. In its present shape, GAAR has the power to override DTAA's.

● **Indirect transfer provisions**

Indirect transfer provisions were introduced in the IT Act vide the Finance Act, 2012 to clarify that an asset being a share or interest in a company or entity registered or incorporated outside India would be deemed to be situated in India, if such a share or interest derives its value (directly or indirectly) substantially from assets situated in India. The transfer of such a share or interest would be liable to tax in India.

A share or interest in a foreign company/ entity is deemed to derive its value substantially from assets (tangible or intangible) located in India, if the value of the Indian assets on a specified date⁸¹:

- exceed INR 100 million; and
- represent at least 50 per cent of the value of all the assets owned by such foreign company or entity.

⁸⁰ Investments up to 31 March 2017 are grandfathered from the applicability of GAAR

⁸¹ The term "specified date" has been defined under the IT Act to mean: -

- date on which the accounting period of the company or entity ends, preceding the date of transfer of share or interest; or
- date of transfer, if the book value of the assets of the company or entity on the date of transfer exceeds the book value of the assets as on the date referred to in clause above, by 15 per cent.



Certain categories of FPIs have been exempted under the IT Act from the indirect transfer provisions. Prior to the amendment of FPI regulations, Category I and Category II FPIs registered under SEBI (FPI) regulations, 2014 were exempted from the provisions of indirect transfer. With the onset of new FPI regulations with effect from 23 September 2019, the IT Act were amended⁸² to provide the same benefit to FPIs recategorised as or newly registered as category I under the new FPI Regulations.

Additionally, a grandfathering benefit has been extended to FPIs (which were previously eligible for the exemption) who have not been recategorised as Category I under the new FPI Regulations. The grandfathering benefit is with respect to the investments made by such FPIs on or before 23 September 2019.

- **Transfer pricing (TP)**

The IT Act prescribes for the applicability of TP provisions on international transactions between associated enterprises. Hence, if an FPI has undertaken any transaction (for example: broking services, custody services, purchase or sale of assets etc.) with any of its associated enterprises, then such transactions are considered as international transactions and are required to be reported to the IRA in the prescribed Form 3CEB.

The due date to file the above form is 31 October following the end of financial year.

- **Minimum Alternative Tax (MAT)**

As per the MAT provisions, if the tax payable by a tax payer on the total income computed as per the provisions of the IT Act is less than 15 per cent of its 'book profit', then notwithstanding anything contained in any other provision of the IT Act, the 'book profit' would be deemed to be the total income of the tax payer. Further, the amount of tax payable would be the amount of income tax at the rate of 15 per cent (plus applicable surcharge and health and education cess) on such total income.

MAT provisions are not applicable and have been deemed never to have been applicable to a foreign company investing in India (including FPIs), if:

- a. the foreign company is a resident of a country or a specified territory with which India has entered into a treaty and the foreign company does not have a PE in India in accordance with the provisions of the treaty; or
- b. the foreign company is a resident of a country with which India does not have a treaty and the foreign company is not required to seek registration under any law for the time being in force relating to companies.

Most FPIs meet the above criterion and therefore MAT does not apply to them.

⁸² Vide Finance Act, 2020

16 TAX AND REGULATORY COMPLIANCES

16.1 Tax compliances

- **Compliance for remittance of proceeds outside India**

Prior to remitting any proceeds outside India arising out of investments made in Indian capital markets, a tax clearance is required from the tax agents of FPIs stating the appropriate taxes on such proceeds, if applicable, have been fully discharged. The local custodian/ DDP of the FPIs typically reach out the tax agents for such clearances. The tax agents issue such clearances on a request made by the local custodian/ DDP of the FPIs on an on-going basis.

- **Payment of advance taxes on income earned in India**

A taxpayer is required to estimate tax liability for a financial year and discharge the same by way of 'advance tax' on the due dates prescribed (mentioned below):

DUE DATE OF TAX PAYMENT	AMOUNT OF TAX LIABILITY TO BE DISCHARGED BY A TAXPAYER
15 June	15%
15 September	45%
15 December	75%
15 March	100%

Delay/ deferment in deposit of advance tax has interest implications. BNP Paribas India sends timely reminders to its investors for advance tax payment.

- **Filing of annual income-tax return**

Income earned by the FPI in India is required to be reported in an annual income-tax return to be filed with the IRA as per the following schedule:

TAXPAYER	FILING DATE
Non-corporate taxpayer	Before 31 July following the financial year*
Corporate taxpayer	Before 31 October following the financial year*

* Extended to 30 November, where TP provisions apply to the taxpayer.

Income tax returns may be subjected to scrutiny proceedings.

- **Reporting requirement in case of indirect transfer**

As discussed above, given that investments by Category I FPIs are granted exemption from indirect transfer, the above reporting requirement would be applicable only in case of investments by FPIs registered/ reclassified as Category II FPIs (subject to grandfathering benefits).

Where indirect transfer provisions are applicable, the FPIs are required to furnish a Form 3CT (certified by an accountant which should indicate the basis of apportionment of income in accordance with the formula prescribed) along with its return of income.

Further, the Indian concern whose shares are indirectly transferred must complete Form 49D.

The compliances discussed above are not an exhaustive list of compliance required and there may be additional compliance documents required under the provisions of the IT Act which are determined based on the specific facts of each case.

16.2 Key regulatory compliances

● **Change in name**

- In case the FPI has undergone a change in name, the request for updation/ incorporation of new name should be submitted by the FPI within six months accompanied by the following documents:
- Original FPI registration certificate granted in the old name;
- Document evidencing change in name (i.e. certified copy of documents from home regulator or Registrar of company or equivalent authority. In absence of above, BR or the equivalent authorising the name change may also suffice;
- Undertaking by the FPI stating that it is a mere name change and does not involve a change in beneficial ownership

● **Change in status of a compliant jurisdiction**

If a jurisdiction, which was a compliant jurisdiction at the time the FPI registration was granted, becomes non-compliant jurisdiction, then the DDP forbids such FPIs to make fresh purchases until the time the jurisdiction is compliant with the regulations. However, the FPI would be allowed to continue to hold any securities already purchased. The relevant DDP would inform SEBI of the details of such FPIs upon such change.

● **Surrender of registration**

If an FPI wants to surrender the certificate of registration, it has to make an application to DDP, who will then seek a 'No Objection Certificate' from SEBI .

While making an application to SEBI, the DDP shall confirm the following:

- The holdings in the security and bank accounts is nil, there are nil outstanding derivative positions, and the accounts held by the FPI are blocked for further transactions;
- There are no dues outstanding to SEBI;
- The Custodial Participant code (CP code) is blocked; and
- There are no actions/ proceedings pending against the FPI

DDP shall process the surrender application after receipt of a No Objection Certificate (NOC) from SEBI and shall ensure the following before issuing a confirmation:

- All the accounts of the FPI are closed; and
- The CP code is deactivated within 10 working days from the date of receipt of NOC from SEBI

Recently, SEBI has allowed FPI's who wish to surrender their registration to write off all shares and debt securities in their beneficiary account which they are unable to sell for any reason.



- **Continuance of registration**

FPIs to pay fees for continuance of its registration and provide additional information, if any, to DDPs at least 15 days prior to current validity of its registration. Where DDP is in receipt of registration fees prior to validity date but the due-diligence including KYC review is not complete by such date due to non-submission of information by the FPI, no further purchases may be permitted to be made by the FPI till the intimation of continuance is given by DDP. Where the FPI has not paid fees for continuance of its registration, the registration would cease to be valid. FPIs cannot apply for continuance of its registration after expiry thereof. However, if such applicant intends to have an FPI registration, it will have to make a fresh application for registration after surrender of its earlier FPI registration.

- **Maintenance of proper books of account, records and documents**

FPIs are required keep or maintain, the following books of accounts, records and documents:

- true and fair accounts relating to remittances of funds to India for buying and selling and realising capital gains or losses on investment made from such remittances;
- bank statement of accounts;
- contract notes relating to purchase and sale of securities; and
- communication including in electronic mode from and to the DDP, stock brokers and depository participants regarding investments in securities.

- **Preservation of books of accounts, records and documents**

Subject to the provisions of any other law, for the time being in force, every FPI is required to preserve the books of accounts, records and documents for a minimum period of five years.

PART D:
**INTERNATIONAL FINANCIAL
SERVICES CENTRES –
GUJARAT INTERNATIONAL
FINANCE TEC-CITY
(IFSC – GIFT City)**

PART D – INTERNATIONAL FINANCIAL SERVICES CENTRES – GUJARAT INTERNATIONAL FINANCE TEC-CITY (IFSC – GIFT City)

17 GIFT CITY – INTRODUCTION

17.1 What is GIFT City⁸³

GIFT city is based in Gandhinagar, capital of the state of Gujarat, India. It covers 886 acres of land with 62 million square feet of built up area (commercial space of 67 per cent, residential space of 22 per cent and social space 11 per cent). It includes office space, residential apartments, schools, hospitals, hotels, clubs, retail and recreational facilities.

GIFT city is an emerging global financial and information technology services hub designed to be at or above par with globally-benchmarked financial centres such as London, Hong Kong, Singapore, Dubai and Labuan.

The idea of setting up an IFSC was first envisioned in 2007, by the then Chief Minister of Gujarat, Mr. Narendra Modi. Further, in 2014 (post general elections), the new government under the leadership of Honorable Prime Minister Mr. Narendra Modi, operationalised the first set of regulations on IFSC in special economic zone (SEZ) specifically targeting GIFT IFSC. In the year 2015, various regulatory bodies such as RBI, SEBI, IRDA opened doors for many players in the financial service sector.

An IFSC is a designated area to provide financial services to residents and non-residents in any currency except local India rupees. GIFT IFSC aspires to become India's gateway for inbound and outbound requirements of international financial services. It aims to attract the top talent in the country by providing the finest quality of life. The IFSC is a joint venture between the Gujarat government and Infrastructure Leasing and Financial Services Limited. It is an agglomeration of financial intermediaries such as banks, insurance companies, insurance brokers, stock exchanges, fund management companies, stock brokers, clearing corporation/ depositories, investment advisors, portfolio managers, AIFs, MF⁸⁴. Various regulators [i.e. SEBI, RBI, IRDA] have issued guidelines and operational frameworks for participants wanting to set-up units in the IFSC.

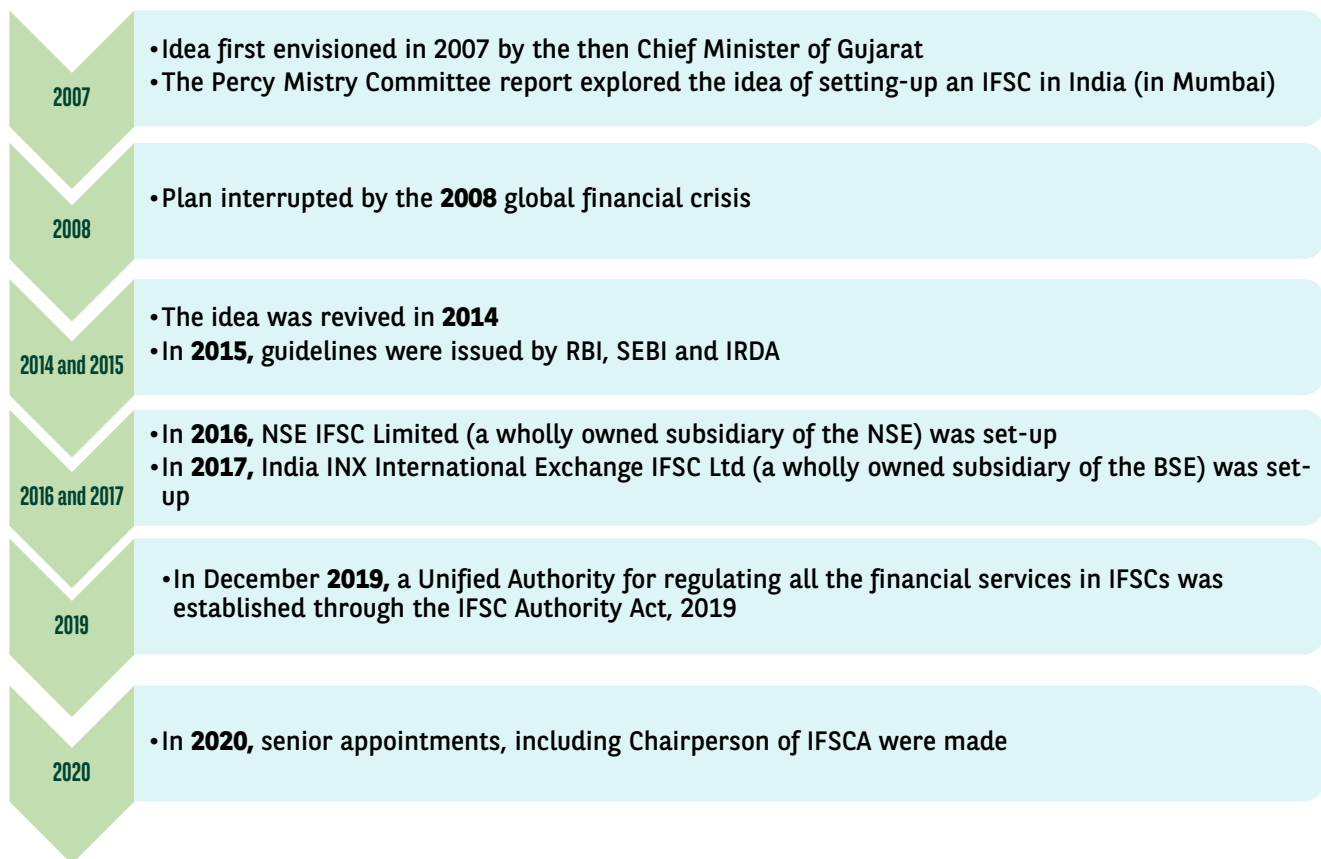
In order to promote ease of doing business, in February 2019, the Union cabinet approved the establishment of a Unified Authority for regulating all the financial services in IFSC through the IFSC Authority bill, 2019. The Unified Authority was to comprise of representatives from national regulators and to be bestowed with all such powers as have been provided to the regulators. The Unified Authority received the assent of the President of India on 19 December 2019 and an Act to provide for the establishment of an Authority to develop and regulate the financial services market in the IFSCs in India and for matters connected therewith or incidental thereto, called the IFSC Authority Act, 2019 was enacted. In December 2020, International Financial Service Center Authority (IFSCA) became an Associate Member of the International Organization of Securities Commissions (IOSCO)⁸⁵. The IOSCO platform enables IFSCA to implement best practices of the regulators of other well established financial centres.

⁸³ In the ensuing paragraphs, we have discussed investments made by foreign investors in IFSC – capital markets.

⁸⁴ It is proposed that MFs be set up in GIFT City IFSC. However, presently SEBI has not issued guidelines for setting up and operating MFs in the IFSC.

⁸⁵ An international organization that brings together the world's securities regulators, covering more than 95 per cent of the world's securities markets.

Key milestones in the set up of IFSC



17.2 GIFT City IFSC – Key features and advantages

Below are some of the strategic objectives/ purpose with which IFSC has been set up:

- To realise the government’s vision to emerge as a major economic power and as a financial hub;
- To entice back to India financial service experts located offshore and transform India as a talent hub;
- To position IFSC as a world-class zone for the long-term provision of office/ service accommodation and high technological, economic and commercial infrastructure.

The benefits of GIFT City:

- State-of-the-art infrastructure at par with other global financial centres;
- Liberal tax regime for 10 years, Gujarat state subsidies and incentives for capital markets and information technology and information technology-enabled services industry;
- International dispute resolution mechanism through the Singapore International Arbitration Centre;
- Strong regulatory and legal environment;
- Integrated ecosystem of banks, insurance, capital markets, law firms and consultancy firms;
- A transparent operating environment, complying with global best practices and internationally accepted laws and regulatory processes;



- Pool of skilled professionals;
- A modern transport, communications and internet infrastructure;
- Potentially lower operating costs;
- Only place in India which allows offshore transactions;
- No stamp duty is chargeable in respect of the instruments listed on RSE and depositories established in IFSC⁸⁶;
- No STT is payable on taxable securities transactions entered into by any person on a RSE located in an IFSC provided the consideration for such transaction is paid or payable in foreign currency⁸⁷;
- No commodities transaction tax is payable on taxable commodity transactions entered into by any person on a RSE located in an IFSC provided the consideration for such transaction is paid or payable in foreign currency

GIFT city targets the following business segments⁸⁸:

BUSINESS	NATURE OF OPPORTUNITY
Offshore banking	corporate banking, servicing joint venture/ wholly owned subsidiary of indian companies registered abroad, factoring/ forfeiting of export receivables, nbfc
Capital markets	exchanges, brokerage services, permissible securities, intermediaries like underwriter, merchant banker, credit rating agency, depository etc
Offshore Asset Management	fund accounting, alternative investment fund, investment services, custodian services, trust services, etc.
Offshore insurance	general/ life insurance, co-insurance, reinsurance, captive insurance, etc.
Ancillary services	legal, accounting and audit, research and analytics etc., compliance, recruitment, risk management
Information technology services	software development, artificial intelligence, robotics, internet of things, business intelligence, mobile platforms, communications technology, consulting, data analytics, data/ information management, research and development, web development, games
Information Technology enabled services/ Business Process Outsourcing	back-office operations, call centres, content development or animation, data processing engineering and design geographic information system services, human resource services, insurance claim processing, legal databases, medical transcription, accounting support centres, website services, aviation finance company.

⁸⁶ Section 9A of the Indian Stamp Act, 1899 as amended by the Finance Act, 2020

⁸⁷ "Foreign Currency" shall have the meaning assigned to it in clause (m) of section 2 of the FEMA, 1999 (42 of 1999)

⁸⁸ <http://www.giftgujarat.in/genesis>

17.3 Present participants in GIFT City IFSC

Below is an indicative list of companies that have established their presence in GIFT city:

SECTOR	PARTICIPANTS
Banking sector ⁸⁹	<p>Indian banks</p> <p>Axis Bank, IDBI Bank, State Bank of India, Bank of Baroda, Federal Bank, HDFC Bank, Bank of India, Yes Bank, RBL Bank, ICICI Bank, IndusInd Bank, Kotak Mahindra Bank</p> <p>Foreign Banks</p> <p>Standard Chartered Bank, HSBC Bank, Barclays Bank Plc, Deutsche Bank, JP Morgan Chase NA, New Development Bank.</p>
Insurance sector ⁹⁰	<p>New India Assurance, Export Credit Guarantee Corporation, ICICI Lombard GIC, J B Boda Insurance and Reinsurance Brokers, Pioneer Insurance and Reinsurance Brokers, Xperitius Insurance Brokers, Risk Care Insurance Brokers, Trinity Reinsurance Brokers, Aditya Birla Insurance Brokers.</p>
Capital Markets sector	<p>Stock Exchange⁹¹</p> <p>India International Exchange INX (INDIA INX), NSE IFSC, International Bullion Exchange</p> <p>Brokers⁹²</p> <p>BSE Broker's Forum, Edelweiss Securities (IFSC) Limited</p> <p>Portfolio Managers⁹³</p> <p>ASK Investment Managers Limited, Axis Asset Management Company Limited, Phillip Ventures IFSC Private Limited, SBI Funds Management Private Limited, Unifi Investment Management LLP.</p>
Others ⁹⁴	<p>Oracle, Tata Communication, World Trade Centers Association, Reliance Capital, Narsee Monjee Education Trust, Sterling Hospitals, Aircraft Leasing and Finance, Alternative Investment Funds (AIFs).</p>

⁸⁹ www.ifsc.gov.in/Banks

⁹⁰ www.ifsc.gov.in/InsuranceAndReinsuranceCompanies

⁹¹ www.ifsc.gov.in/StockExchanges

⁹² www.ifsc.gov.in/BrokerDealers

⁹³ www.ifsc.gov.in/PortfolioManager

⁹⁴ These are in non-IFSC area

18 CAPITAL MARKETS IN GIFT CITY IFSC

18.1 Background and overview

SEBI issued guidelines to facilitate and regulate financial services relating to securities market in an IFSC set up under Section 18(1) of SEZ Act, 2005. The Guidelines, dated 27 March 2015, may be called as SEBI (IFSCs) Guidelines, 2015, which came into effect from 1 April 2015, and amended from time to time.

18.2 Type of securities to be traded on the stock exchanges

The stock exchanges operating in IFSC may permit dealing in following types of securities and products in such securities in any currency other than INR, with a specified trading lot size on their trading platform subject to prior approval of the Board:

1. Equity shares of a company incorporated outside India;
2. Depository receipt(s);
3. Debt securities issued by eligible issuers;
4. Currency derivatives [including derivatives involving INR (with settlement in foreign currency)]⁹⁵ and interest rate derivatives;
5. Index based derivatives;
6. Commodity derivatives⁹⁶;
7. Derivatives on equity shares⁹⁷; or
8. Units of InvITs and REITs⁹⁸; and
9. Such other securities as may be specified by the Board.

Currently, there are at least 132 Indian equity derivatives, two Index derivatives, 11 commodity futures, three global currency derivatives and two Indian currency derivatives that are traded on Stock Exchanges in the IFSC. The exhaustive list of products can be seen on the official websites⁹⁹ of the respective Stock Exchanges in the IFSC.

18.3 Guidelines for participation/functioning of EFIs in IFSC¹⁰⁰

Eligible Foreign Investor (EFIs) operating in IFSC shall not be treated as entities regulated by SEBI. Further, SEBI registered FPIs, proposing to operate in IFSC, are permitted, without undergoing any additional documentation and/or prior approval process. The following are the eligibility and KYC norms for EFIs:

Eligibility norms:

EFIs are those foreign investors who are eligible to invest in IFSC by satisfying the following conditions:

- A. the investor is not resident in India;

⁹⁵ SEBI Circular: SEBI/HO/MRD2/DCAP/CIR/P/2020/17 dated 3 February 2020

⁹⁶ SEBI Circular: CIR/MRD/DSA/41/2016 dated 17 March 2016

⁹⁷ SEBI Circular: SEBI/HO/MRD/DRMNP/CIR/P/2017/31 dated 13 April 2017

⁹⁸ SEBI Circular SEBI/HO/DDHS/DDHS/CIR/P/2020/174 dated 16 September 2020

⁹⁹ <https://www.indiainx.com/static/productsnapshot.aspx>

¹⁰⁰ SEBI Circular: IMD/FPI&C/CIR/P/2019/124 dated 5 November 2019

- B. the investor is not resident in a country identified in the public statement of FATF as:
 - i. a jurisdiction having a strategic Anti-Money Laundering or Combating the Financing of Terrorism deficiencies to which counter measures apply; or
 - ii. a jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with the FATF to address the deficiencies; and
- C. the investor is not prohibited from dealing in securities market in India.

KYC norms:

Intermediary operating in IFSC needs to ensure that records of their clients are maintained as per Prevention of Money-laundering Act, 2002 and Rules made thereunder. The following KYC norms may be made applicable to EFIs:

- A. In case of participation of an EFI, not registered with SEBI as an FPI, but wishing to operate in IFSC, a trading member of the RSE in IFSC, may rely upon the due diligence carried out by a bank, which is permitted by RBI to operate in IFSC, during the account opening process of EFI;
- B. In case of EFIs that are not registered with SEBI as FPI and also not having bank account in IFSC, KYC as applicable to Category II FPI as per the new FPI categorisation shall be made applicable. However, PAN shall not be applicable for KYC of EFIs in IFSC; and
- C. In case of participation of FPI in IFSC, due diligence carried out by SEBI registered intermediary at the time of account opening and registration shall be considered.

Segregation of accounts:

FPIs, who presently operate in the Indian securities market and also propose to operate in the IFSC, are required to ensure clear segregation of funds and securities. Custodians shall, in turn, monitor compliance of this provision for their respective FPI clients. Such FPIs shall keep their respective custodians informed about their participation in IFSC.

18.4 Segregated Nominee Account Structure¹⁰¹

With a view to further facilitate ease of market access for foreign investors in the IFSC, SEBI permits a Segregated Nominee Account (SNA) Structure in IFSC wherein orders of foreign investors may be routed through an eligible SNA or (hereinafter referred to as 'Providers'), for trading on stock exchanges in IFSC while adhering to regulatory requirements, inter alia, relating to identification of end-client, Unique Client Code, order placement at client level, client level margining and position limits.

The following entities are eligible to register with the Stock Exchange/ Clearing Corporation to offer SNA services to foreign investors:

1. SEBI-registered brokers in IFSC;
2. SEBI registered FPIs (Category I and II); and
3. Trading/ clearing members of international stock exchanges/ clearing corporations that are regulated by a member of FATF.

¹⁰¹ SEBI Circular: SEBI/HO/MRD/DRMNP/CIR/P/2018/83 dated 24 May 2018

18.5 Position Limits for cross-currency futures and options contracts¹⁰² on exchanges in IFSC¹⁰³

The position limits for cross-currency futures and options contracts (including cross-currency futures and options contracts involving INR) on exchanges in IFSC, for eligible market participants, per currency pair per stock exchange, are as follows:

Institutional Investors – Gross open position across all contracts not to exceed 15 per cent of the total open interest or USD 1 billion equivalent, whichever is higher.

Eligible Foreign Investors – Gross open position across all contracts not to exceed 15 per cent of the total open interest or USD 1 billion equivalent, whichever is higher.

18.6 Key differences between trading on domestic stock exchanges vis-à-vis India INX¹⁰⁴

PARTICULARS	INDIAN INX	DOMESTIC INDIAN EXCHANGES
Access process	Short	Long
Trading timings	22 hours	6.30 hours
Market structure	Single	Multiple
Taxation	Less taxes on account of certain tax exemption benefits	Comparatively taxes are high
Custody account	Not mandatory (subject to certain exceptions)	Mandatory
Currency risk	No	Yes
Position limits	Enhanced	Limited
Transaction cost	Low	High
Bank account	Not mandatory (subject to certain exceptions)	Mandatory
Issuance on foreign currency bonds	Allowed	Not allowed

18.7 Key developments for promotion of GIFT IFSC

With a view to promote IFSC, following key developments have been announced:

- A unified authority (IFSCA) was established to regulate all financial services in IFSC.

¹⁰² Including contracts involving INR (SEBI Circular: SEBI/HO/MRD2/DCAP/CIR/P/2020/17 dated 3 February 2020)

¹⁰³ SEBI Circular: SEBI/HO/MRD/DRMNP/CIR/P/2017/43 dated 17 May 2017

¹⁰⁴ India International Exchange (IFSC) Limited (India INX) is India's first international exchange in IFSC

- Trading of rupee derivatives in IFSC is permitted provided the settlement is in foreign currency.
- With a view to create a bullion ecosystem within the IFSC, trading in bullion depository receipts, bullion financing, bullion-based loans, bullion loans against collateral, clearing and settlement services, etc. can be transacted in IFSC and is regulated by IFSCA.
- Listing and trading of units of InvITs and REITs from permissible jurisdictions (such as the USA, UK, France, etc.) on RSE in the IFSC are permitted (subject to fulfilling prescribed conditions). IFSCA issued a circular prescribing the regulatory framework for the same.
- 'Aircraft leasing' is notified as a financial product, in the list of permissible activities in an IFSC, which includes operating/ financial lease/ hybrid of operating and financial lease of aircraft/ helicopter (including engines or any other parts).

IFSCA issued a framework for aircraft leasing in IFSC. The framework includes activities permitted in the aircraft leasing, minimum capital requirements, etc. The development of framework will attract more financial services players (including banking and insurance companies) to participate in the overall leasing ecosystem.

- IFSCA issued a framework for enabling ancillary service providers to operate in IFSC in India. Ancillary services shall include legal, compliance and secretarial services; auditing, accounting, book keeping and taxation services; professional and management consultancy services; administration, asset management support and trusteeship services, and other services approved by IFSCA.
- In order to facilitate a vibrant capital market ecosystem in IFSC and to attract investors and foreign capital, the IFSCA has introduced a NLT (Negotiated Large Trade) facility for derivatives on the stock exchanges. For this purpose, an operational framework was issued which prescribes for the trading hours, minimum order size, position limits and certain other conditions in this regard. IFSCA issued International Financial Services Centres Authority (Finance Company) Regulations, 2021 to provide a framework for finance companies in IFSC. The Regulations are aimed at providing a competitive regulatory environment to non-banking financial institutions to complement the role of banking in providing finance, innovative products and services from IFSC.
- IFSCA issued regulations on the issuance and listing of securities in IFSC 1. The framework proposed by IFSCA provides for the issuance and listing of securities by start-ups, small and medium enterprises, etc.
- SEBI (Issue and Listing of Non-Convertible Securities) Regulations, 2021 ("NCS Regulations") have been notified which has the effect of merging SEBI (Issue and Listing of Debt Securities) Regulations, 2008 and SEBI (Issue and Listing of Non-Convertible Redeemable Preference Shares) Regulations, 2013 into a single regulation.
- The RBI issued a notification whereby resident individuals are permitted to make remittances under the Liberalised Remittance Scheme in IFSCs set up in India under the SEZ Act, 2005. Such remittance shall only be made for making investment in IFSCs in securities, other than those issued by entities/companies resident (outside IFSC) in India.
- The IFSCA issued a circular in December 2020 on Over-The-Counter (OTC) derivative transactions in IFSC, which inter alia provided that the RBI's Circular on "Comprehensive Guidelines on Derivatives" is applicable for OTC derivative transaction in the IFSC subject to certain modifications as below:
 - All the IFSC banking units can issue OTC derivatives in the IFSC subject to meeting other specified norms
 - ODIs on Indian government bonds and state development loans can be issued by the IFSC banking units with an FPI registration. However, the issue of ODIs in other securities such as corporate bonds, equity instruments, etc is yet to be addressed.



19 ALTERNATIVE INVESTMENT FUNDS IN IFSC (AIFs)

19.1 Introduction

- With the success of the AIF regime and with a view to encourage such a fund regime in the IFSC, in 2015, SEBI issued detailed guidelines to facilitate and regulate the securities market in IFSC. These guidelines provided the basic framework for AIFs.
- The IFSCA has recently issued IFSCA (Fund Management) Regulations, 2022¹⁰⁵ to regulate the fund management activity in GIFT IFSC, repealing the former regulations issued by IFSCA with SEBI¹⁰⁶. The broad theme of these regulations are –
 - (i) to regulate the fund manager instead of the fund;
 - (ii) provide single registration for multiple activities (such as a registered Fund Management Entity (FME) which can offer Portfolio Management Services (PMS) to clients);
 - (iii) risk-based approach based on the activity to be undertaken.
- Below is a quick snapshot of types of fund management entities¹⁰⁷ and schemes¹⁰⁸:

PARAMETERS	AUTHORISED FME	REGISTERED FME (NON-RETAIL)	REGISTERED FME (RETAIL)
Investment strategy	Start-ups, early-stage VC undertakings, family investment funds	Registered scheme, PMS, multi family offices, REITs / INVITS (private)	Retail or restricted schemes, ETFs, REITs / INVITS (public)
Legal structure	Company, LLP, branch	Company, LLP, branch	Company
Min net worth	USD 75,000	USD 500,000	USD 1,000,000
Min Key Management Personnels (KMPs)	1 Principal officer (PO)	2 (PO + compliance & risk officer)	3 (PO + Compliance & Risk officer + an additional KMP). To have atleast 4 directors (50% to be independent)
Fund management activity	As specified for an Authorised FME	Allowed to undertake all activities of Authorised FMEs	Allowed to undertake all activities of Authorised FMEs & Registered (Non-Retail)

¹⁰⁵ Notified on 19 April 2022

¹⁰⁶ SEBI AIF Regulations 2012; Operating Guidelines for AIF in IFSC dated 26 November 2018 and other circulars issued by IFSCA and SEBI in relation to AIF in IFSC

¹⁰⁷ Erstwhile referred to as "Fund/ AIF Manager"

¹⁰⁸ Erstwhile referred to as "Fund/ AIF"



PARAMETERS	VENTURE CAPITAL SCHEMES	RESTRICTED SCHEMES (NON-RETAIL)	RETAIL SCHEMES
Launched by	FMEs	Registered FME	Registered FME (Retail)
Types of investors	Pooling of monies from accredited investors or investors investing above USD 250,000	Pooling of monies from accredited investors or investors investing above USD 150,000	All investors including retail investors
Permissible investments	Listed and unlisted securities, debt, securitized debt instruments, money market securities, unit of MF, investment in LLP ¹⁰⁹ etc. Units of any investment schemes/ AIFs and derivatives can be done by non-retail and retail schemes.		
Corpus of the Scheme	Min: USD 5 million Max: USD 200 million	Min: USD 5 million Max: NA	
Time period for launch	'Green channel' ¹¹⁰ for subscription by investors	'Green channel' if subscription is to be raised only from accredited investors, else 21 days	Can be launched only after filing with regulator and incorporating their comments
Category of AIF as per existing laws (income-tax FEMA etc.)	Category I	Category I, II and III	Category III AIF

- The IFSCA has provided tax and regulatory incentives to encourage fund management regime in the IFSCA. Amongst others, it provides an attractive tax regime for Category-III AIFs in GIFT City with tax benefits at par vis-à-vis available under various tax treaties entered by India with other jurisdictions (discussed in detail in section 20 of this chapter).

¹⁰⁹ Retail scheme cannot invest in LLPs

¹¹⁰ Green Channel route means that the schemes filed shall be open for subscription by investors immediately upon filing



20 TAXATION SCHEME FOR INVESTMENT IN CAPITAL MARKETS IN IFSC

20.1 Basic concepts

Scope of income

Under the provisions of the IT Act, income of a non-resident is taxable in India, if the income is:

- Received in India; or
- Deemed to be received in India; or
- Accrues or arises in India; or
- Deemed to accrue or arise in India.

Concept of assessment year and previous year

From an income tax perspective, previous year is the year in which a tax payer earns an income, while assessment year is the year following the previous year in which previous year's income is evaluated.

For example, if the previous year is from 1 April 2021 to 31 March 2022, then the assessment year for income earned during this period would begin after the previous year ends, i.e. on 1 April 2022 till 31 March 2023.

20.2 Tax framework and taxation under the provisions of the IT Act

Typically, the following types of income could be earned by EFIs in a financial year on account of investments in securities listed on RSE in IFSC:

- **Dividend¹¹¹**
 - With effect from 1 April 2020, under the provisions of the IT Act, dividends received will be taxable in the hands of the shareholder at the basic tax rate of 20 per cent (plus applicable surcharge and health and education cess).
 - Dividend income earned by Category III AIFs in IFSC is taxable at concessional rate of 10 per cent.

- **Interest**

To boost the number of bond listings on the IFSC exchange, the Finance Act 2020, provided a concessional withholding tax rate of 4 per cent on interest payments made to a non-resident, not being a company or to a foreign company, by an Indian company. The concessional withholding tax rate is available, in respect of monies borrowed by an Indian company, by way of issue of any long-term bond or RDB on or after the 01 April 2020 but up to 01 July 2023, which is listed on a RSE located in any IFSC.

Further, the actual tax liability on such interest income will correspond to the amount of tax withheld.

- **Capital gains**
 - An EFI which operates in accordance with the SEBI circular (on guidelines of participation of EFIs in IFSC) shall be deemed as an FPI for the purposes of transactions in securities made on a RSE located in any IFSC where the consideration for such transaction is paid or is payable in foreign currency¹¹². Further, since the securities held by an FPI (in accordance with FPI Regulations) are deemed to be capital assets under the provisions of the IT Act, the consideration received from sale of Indian securities and derivatives will be characterised as 'capital gains' in the hands of such EFIs.

¹¹¹ Currently, shares are not listed but only depository receipts having underlying as shares are listed on the RSE in the IFSC

¹¹² CBDT Notification No. 17/2020/ F. No. 173/10/2014-ITA-I dated 13 March 2020

- **Certain transfers are exempt and not chargeable to capital gains tax in India**

According to the IT Act, any transfer of capital asset such as:

- (i) a bond or GDR;
- (ii) a RDB of an Indian company;
- (iii) a derivative;
- (iv) a foreign currency denominated bond¹¹³;
- (v) a unit of a MFs²⁰;
- (vi) a unit of a business trust (REIT/ InvIT)¹¹³⁰;
- (vii) a foreign currency denominated equity shares of a company¹¹³⁰;
- (viii) a unit of AIF¹¹³⁰;
- (ix) other securities as may be notified by the government in this behalf, made by a non-resident on a RSE located in any IFSC and where the consideration for such transaction is paid or payable in foreign currency^{Error! Bookmark not defined.}, is not considered as a transfer and as a result, the capital gains earned by a non-resident from the transfer of any assets mentioned above would be exempt from capital gains tax in India.

- The CBDT has prescribed the rules and conditions to be adhered for tax exemption of income of a non-resident from non-deliverable forward contracts. Key conditions are as follows :
 - (i) the non-deliverable forward contract should be entered into by the non-resident with an offshore banking unit (OBU) in the IFSC and registered with the IFSC Authority; and
 - (ii) such contract is not entered into by the non-resident through or on behalf of its permanent establishment in India - The OBU shall ensure that this condition is observed.

- There are exemption for certain income earned by Category-III AIF, unitholders of Category-III AIF and relocation of offshore funds in IFSC:

- The Act provides an exemption to income accrued or arisen from or received by a Category-III AIF located in IFSC and all units of which are held by non-residents in respect of the following:
 - (i) Transfer of specified capital asset as specified above (points (i) to (ix)) of the IT Act, on a recognized stock exchange located in the IFSC where the consideration of such transaction is paid/ payable in convertible foreign currency; or
 - (ii) Transfer of securities (other than shares in a company resident in India¹¹⁴) ; or
 - (iii) Income from securities issued by a non-resident (not being a permanent establishment of a non-resident in India) where such income does not accrue/ arise in India; or
 - (iv) Income from securitisation trust which is chargeable under the head ' profits and gains from business or profession'.
- Exemption and benefits to unitholders (being non-residents) of Category-III AIF
 - (i) The IT Act exempts income accruing or arising to or received by a unitholder from Category-III AIF located in IFSC;
 - (ii) Additionally, the distribution of income to the unitholders is not subject to tax withholding;

¹¹³ Notification No. 16 of 2020, dated 5 March 2020

¹¹⁴ Capital gains on equity shares of Indian company shall be chargeable to tax at prescribed rates as per the IT Act.



- (iii) They are exempted from requirement of obtaining a PAN (subject to providing requisite information/ documents); and
- (iv) Also exempted from the requirement of filing of return of income (only if the unitholders do not earn any income in India, except the income from investments in the AIF in IFSC).
- **To confer a comprehensive tax exemption for relocation¹¹⁵ of an offshore Fund to IFSC (i.e. relocation of 'Original Fund¹¹⁶' to 'Resultant Fund¹¹⁷'), following tax incentives are provided:**
 - (i) **Capital gains income earned on the transfer of a capital asset by the original fund to a resulting fund would not be considered as a transfer under the Act;**
 - (ii) **Capital gains income earned on the transfer of a share or unit or interest held by an investor in the original fund in consideration for the share or unit or interest in the resultant fund would not be considered as transfer under the Act;**
 - (iii) **Capital gains arising or received by a non-resident or the resultant fund to the extent units are held by non-residents (not being a PE of the non-resident in India) on transfer of shares of an Indian company by the resultant fund shall be exempt under the Act, . This exemption is available if capital gains on such shares were not chargeable to tax had the relocation not taken place;**
 - (iv) **Cost of acquisition of shares of an Indian company acquired by the resultant fund upon relocation is deemed to be cost of previous owner i.e. cost base of shares of Indian company in the hands original fund;**
 - (v) **The period of holding of units of resultant fund acquired by unitholders upon relocation is deemed to include the period for which the unitholders held the units of the original fund; and**
 - (vi) **Benefit of set-off and carry forward of losses to the extent the change in shareholding has taken place on account of relocation.**

4.3 Taxation under the provisions of DTAA

Where the government has entered into an agreement with the government of any other country for avoidance of double taxation, then in relation to a taxpayer to whom such agreement applies, provisions of DTAA to the extent more beneficial will override the provisions of the IT Act.

¹¹⁵ Relocation means a transfer of assets of the original fund to a resultant fund on or before 31 March 2023, where consideration for such transfer is discharged in the form of share or unit or interest in the resulting fund.

¹¹⁶ Original fund means a fund establish outside India which collects funds from its members for investing such funds for their benefits and fulfills the following condition: (i) the fund is not a person resident in India; (ii) the fund is resident of a country with which India has a treaty; (iii) the fund and its activities are subject to applicable investor protection regulations in the country where it is established or incorporated; and fulfills such other conditions as may be prescribed.

¹¹⁷ Resultant fund means a fund established or incorporated in India in the form of a trust or a company or a limited liability partnership, which (i) has been granted a certificate of registration as a Category III AIF and is regulated by SEBI or IFSCA; and (ii) is located in IFSC.



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PART E:

**FOREIGN VENTURE CAPITAL
INVESTOR ROUTE**

PART E: FOREIGN VENTURE CAPITAL INVESTOR ROUTE

21 FOREIGN VENTURE CAPITAL INVESTOR (FVCI) – INTRODUCTION AND OVERVIEW

21.1 Introduction

To attract foreign investment in India and boost investments into venture capital and start ups, the Indian government has liberalised the regime applicable to foreign venture capital investors (FVCI).

The formalisation of the Indian venture capital community began in 1993 when India Venture Capital Association was formed. In 1996, SEBI introduced the SEBI (VCF) Regulations, 1996 to regulate and promote domestic venture capital funds. Subsequently, SEBI introduced the FVCI Regulations in 2000 which have subsequently been amended. In 2012, the SEBI (AIF) Regulations, 2012 were introduced replacing the SEBI (VCF) Regulations, 1996.

The FVCI route is typically preferred by certain sectors on account of various regulatory benefits discussed in detail in this chapter.

Investing in VCFs can be valuable return-enhancing tool for investors while the increase in risk at the portfolio level is minimised by regulations.

21.2 Who is FVCI

An FVCI is defined as:

- An investor incorporated and established outside India;
- Registered under FVCI regulations; and
- Proposes to make investments in accordance with FVCI regulations.

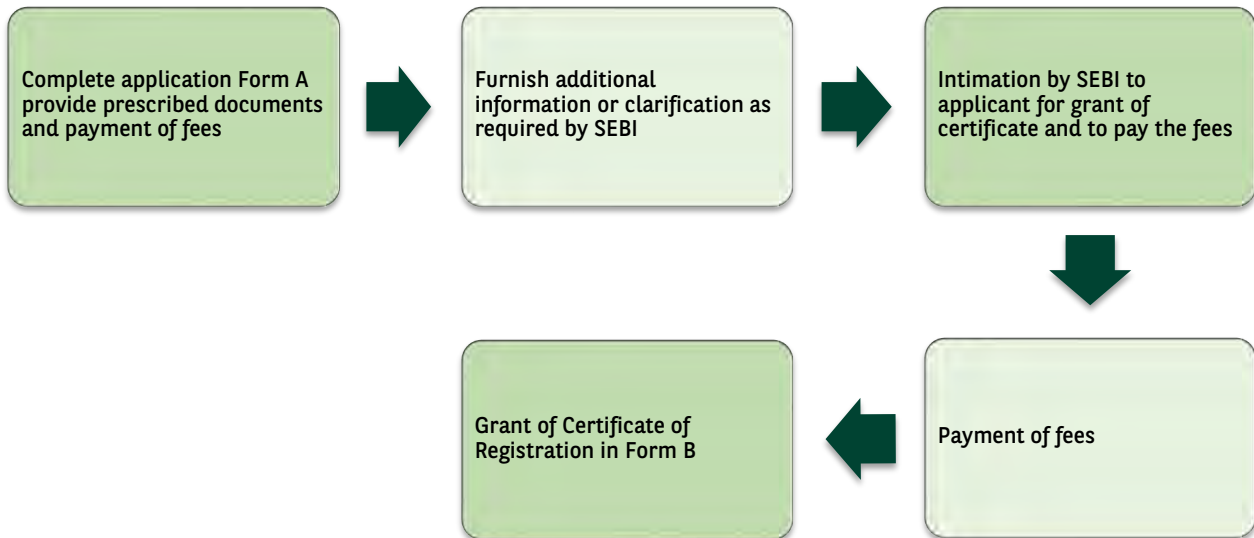
21.3 What is a VCF ?

An VCF means a fund registered under SEBI (VCF) Regulations, 1996 or under SEBI (AIF) Regulations, 2012 in the sub category of VCF under Category I AIF.



22 REGISTRATION OF FVCIs

22.1 Registration Process



22.2 Eligibility Criteria

Applicant's BACKGROUND	<ul style="list-style-type: none"> Track record Professional competence General reputation of fairness and integrity Financial soundness Experience.
RBI APPROVAL	Necessary RBI approval received for making investments in India ¹¹⁸
STATUS OF APPLICANT	<ul style="list-style-type: none"> Investment company Investment Trust Investment Partnership Pension fund/ MF/ endowment fund/ university fund Charitable institution Asset management company Investment manager or Investment management company Any other entity/ investment vehicle incorporated outside Indi;
AUTHORISED TO INVEST	Applicant should be authorised to invest in VCF or carry on activity as FVCI or AIF

¹¹⁸ Practically, no separate RBI approval is obtained as SEBI internally gets an approval from RBI.



REGULATED ENTITY	<p>The applicant should be:</p> <ul style="list-style-type: none"> i. Regulated by an appropriate foreign regulatory authority; or ii. Income-tax payer; or iii. Submits a certificate from its banker of its or its promoter's track record where applicant is neither a regulated entity nor an income tax payer.
EARLIER REGISTRATION NOT GRANTED	Applicant should not have been refused registration by SEBI.
FIT AND PROPER PERSON	<p>For the purpose of determining whether any person is a 'fit and proper person' SEBI may take into account any criteria as it deems fit, including but not limited to:</p> <ul style="list-style-type: none"> i. integrity, honesty, ethical behaviour, reputation, fairness and character; and ii. Absence of any disqualifications¹¹⁹ against the applicant; in relation to : <ul style="list-style-type: none"> • the applicant or the intermediary, or persons exercising direct or indirect control over the applicant or intermediary, • principal officer, • directors or managing partners, • the compliance officer • key management persons, • any person holding twenty percent or more voting rights for controlling interest or exercise control of an unlisted applicant or intermediary
FIRM COMMITMENT	Applicant required to obtain firm commitment from investors for contributing at least USD 1 million at the time of submission of application.

22.3 Conditions of certificate

The registration certificate granted to the FVCI shall be inter alia subject to the following conditions

- FVCI shall abide by the provisions of the SEBI Act, 1992 and FVCI regulations;
- FVCI shall appoint a domestic custodian for purpose of custody of securities;
- FVCI shall enter into arrangement with a designated bank for the purpose of operating a SNRR or foreign currency account; and
- FVCI shall forthwith inform SEBI if any information/ particulars previously submitted to SEBI are found to be false or misleading or if there is any change in the information already submitted.

¹¹⁹ I. Pending criminal complaint or information under section 154 of the Code of Criminal Procedure, 1973 (2of 1974) filed by SEBI;

II. Filed and pending charge sheet by any enforcement agency in matters concerning economic offences;

III. In force order of restraint, prohibition or debarment passed by SEBI or any other regulatory authority or enforcement agency in any matter concerning securities laws or financial markets

IV. Recovery proceedings

V. Passed order of conviction by a court for any offence involving moral turpitude

VI. Winding up proceedings

VII. Declared insolvent and not discharged;

VIII. Found to be of unsoundmind by a court of competent jurisdiction

IX. Categorized as a wilful defaulter;

X. Declared a fugitive economic offender; or any other disqualification as may be specified by the SEBI from time to time

22.4 Fees

To apply for registration, the fee can be paid electronically or by bank draft to “The Securities and Exchange Board of India” payable at Mumbai:

SR NO	NATURE OF FEES	AMOUNT
1	Application fees	USD 2,500
2	Registration fees	USD 10,000

23 INVESTMENT – INSTRUMENTS, LIMITS AND CONDITIONS/ RESTRICTIONS

23.1 Instruments in which FVCIs can invest

- Investments by an FVCI must comply with SEBI regulations, FEMA and sectoral caps under the FDI policy;
- An FVCI may invest in securities listed on a recognised stock exchange subject to the provisions of the FVCI regulations;
- An FVCI can invest in securities issued by an Indian company engaged in various sectors¹²⁰ and whose securities are not listed on a recognised stock exchange at the time of issue of said securities;
- An FVCI can invest in an equity or an equity-linked or debt instrument issued by an Indian startup¹²¹, irrespective of the sector in which it is engaged;
- An FVCI can invest in units of a VCF or of a Category I Alternative Investment Fund (Cat-I AIF) or units of a scheme or of a fund set up by a VCF or a Category-I AIF;
- FVCIs can also make investments under FDI route as non-resident entities, in other companies, subject to FDI policies and FEMA regulations. AN FVCI can hold an FPI license at the same time as holding an FPI licence. as well.

23.2 Investment – limits and conditions/ restrictions

- An FVCI cannot invest in an LLP.
- An FVCI is required to disclose its investment strategy and duration of life cycle of the fund to SEBI.
- A FVCI's investment should be paid out of inward remittance from abroad through normal banking channels or out of funds held in a foreign currency or SNRR account account maintained in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016.
- The sale or maturity proceeds (net of taxes) of the securities may be remitted outside India or may be credited to the foreign currency or a SNRR account of the FVCI.
- An FVCI may also receive the proceeds of the liquidation of VCFs or of Cat-I AIFs or of schemes/ funds set up by the VCFs or Cat-I AIFs.
- Following are the investment restrictions:

¹²⁰ Biotechnology, IT related to hardware and software development, Nanotechnology, Seed research and development, Research and development of new chemical entities in pharmaceutical sector, Dairy industry, Poultry industry, Production of bio-fuels, Hotel-cum-convention centers with seating capacity of more than three thousand, Infrastructure sector (The term 'Infrastructure Sector' has the same meaning as given in the Harmonised Master List of Infrastructure sub-sectors approved by Government of India vide Notification F. No. 13/06/2009-INF dated March 27, 2012 as amended/ updated).

¹²¹ A 'startup' is an entity incorporated in India not more than -10 years back with an annual turnover not exceeding INR 1000 million in any preceding financial year, working towards innovation, development or improvement of products or processes or services, or if it is a scalable business model with a high potential of employment generation or wealth creation.

PER CENT OF INVESTMENT	MODE OF INVESTMENT
100 percent	Committed in one VCF or an AIF
At least 66.67 per cent of investible funds ¹²²	In unlisted equity shares or equity linked instruments of Venture Capital Undertaking (VCU) ¹²³ or investee company ¹²⁴
Upto 33.33 per cent of investible funds ¹²²	<p>As prescribed under the guidelines, including:</p> <ul style="list-style-type: none"> • Subscription to Initial Public Offer of a VCU or investee company; • Debt or debt instrument of a VCU or investee company in which FVCI has already invested by way of equity; • Preferential allotment of equity shares of a listed company subject to lock in period of one year; • Special purpose vehicles which are created for the purpose of facilitating or promoting investment in accordance with these regulations.

23.3 Certain benefits

- An FVCI may acquire by purchase or transfer by sale of securities at a price mutually acceptable to the buyer and seller and are exempted from pricing norms at the time of entry as well as exit. The pricing guidelines under NDI rules are not applicable to investment under FVCI route.
- In the case of an initial public offer, an FVCI is not subject to lock-in restrictions on the pre-issue equity shares held by an FVCI provided it is not a promoter and has held such shares for a period of six months.

¹²² Investible funds means the fund committed for investments in India net of expenditure for administration and management of the fund.

¹²³ Venture Capital undertaking" means a domestic company:

- Which is not listed on a recognised stock exchange in India at the time of making investment; and
- Which is engaged in the business for providing services, production or manufacture of article or things and does not include following activities or sectors:
 - non-banking financial companies, other than Core Investment Companies in the infrastructure sector, Asset Finance Companies, and Infrastructure Finance Companies registered with RBI;
 - gold financing;
 - activities not permitted under industrial policy of GOI;
 - any other activity which may be specified by SEBI in consultation with GOI from time to time.

¹²⁴ As per the AIF regulations, an Investee company means any company, special purpose vehicle or limited liability partnership or body corporate or real estate investment trust or infrastructure investment trust in which an AIF makes an investment.

Taxation and regulatory compliance requirements for FVCIs

23.4 FVCI taxation

- Taxation of income earned by a FVCI would depend upon whether the VCF/ VCU in which the FVCI has made an investment is set up as an AIF, trust or company. For more details on taxation please visit FDI section (part B of this document).
- The IT Act provides that the provisions of the IT Act or the relevant tax treaty with the respective country will apply to the extent it is more beneficial to the non-resident.
- In order to be eligible to claim relief under tax treaty, a non-resident is required to produce a TRC issued by the government of the respective country or the specified territory in which it is resident along with additional information in Form 10F. However, additional information prescribed in Form 10F may not be required if it already forms a part of TRC. Additionally, the FVCI would also need to satisfy the provisions of Indian GAAR and Multilateral Instruments to be eligible to claim relief under a tax treaty (if applicable).

23.5 SEBI compliance

- FVCIs are required to submit a quarterly report on venture capital activity to SEBI in the prescribed format.
- The report is to be uploaded to the SEBI portal within seven days from the end of respective quarter. Physical copies of the report do not need to be submitted.
- The FVCI's domestic custodian shall be responsible for the timely submission of these reports.

23.6 FEMA compliance

- FVCIs are required to comply with reporting requirements prescribed under FEMA regulations.

24 OBLIGATIONS AND RESPONSIBILITIES OF FVCIs

24.1 Maintenance of books and records

- An FVCI is required to maintain for eight years the accounts, records and documents reflecting a true and fair picture.
- An FVCI is required to inform SEBI of where such books, records and documents are kept.

24.2 Appointment of domestic custodian

- An FVCI or global custodian acting on behalf of the FVCI is required to enter into agreement with domestic custodian to act as a custodian of securities for FVCI.
- The domestic custodian is required to:
 - Monitor the FVCI's investments in India;
 - Furnish periodic records to SEBI;
 - Furnish required information to SEBI.

24.3 Appointment of a designated bank

- An FVCI must open a foreign currency denominated account or SNRR account with an RBI-approved designated bank. The account is to be used exclusively for transactions specified under the FEMA regulations.

25 KYC FOR FVCI

KYC documents clarifications

<p>ENTRY LEVEL</p>	<ul style="list-style-type: none"> • Constitutive Documents¹²⁵ • Proof Of Address • PAN Card • Financials¹²⁶ • SEBI Registration Certificate • Board/Partner/Member Resolution Or Any Other Relevant Document Pertaining To Investments In The Securities Market • FATCA/ CRS Form • KYC Form 11
<p>SENIOR MANAGEMENT / AUTHORISED SIGNATORIES</p>	<ul style="list-style-type: none"> • List of Members (Whole time Directors/ Partners/ Trustees etc. in Senior Management) and Signatures (In case of Authorised Signatories) • Proof of Identity • Proof of Address • Photographs
<p>ULTIMATE BENEFICIAL OWNERS (UBO)/ SHAREHOLDING PATTERN</p>	<ul style="list-style-type: none"> • List of Members (Required until the UBO) • Proof of Identity (Required if UBO with substantial percentage identified) • Proof of Address

¹²⁵ In case of

- Corporates: Copies of the Memorandum and Articles of Association and certificate of incorporation
- Partnership Firm: Copy of Partnership Deed / Certificate of registration (if registered)
- Trust: Copy of Trust Deed / Certificate of registration (if registered)

¹²⁶ Copy of the balance sheets for the last two financial years to be submitted every year



COMMONLY USED TERMS AND GLOSSARY

26 COMMONLY USED TERMS

Commonly used terms

TERM	MEANING
IT Act	The Law in India dealing with, <i>inter alia</i> , taxation of income earned on investments made into India and matters incidental thereto.
CDSL/ NSDL	CDSL/ NSDL are depositories in India offering depository services in respect of Indian securities
DTAA	An international treaty entered into between India and the other contracting jurisdiction for the purpose of eliminating situations of double taxation of income earned, <i>inter alia</i> , on investments made into India.
FDI	One of the entry routes for making investments into India.
FPI	One of the entry routes for making investments into India.
Form FC-GPR	A form required to be submitted by the recipient with RBI on receipt of consideration from a foreign investor for allotment of securities (shares, debentures, etc.).
Form FC-TRS	A form required to be submitted with RBI in case of transfer of securities (shares, debentures, etc.) of an Indian concern by a resident to a foreign investor or by a foreign investor to a resident.
PAN	A tax identification number issued by the IRA. The same is required for the purposes of making investments into India, filing of return of income in India, etc
RBI	India's exchange control and banking regulator
SEBI	India's securities market regulator formed with the objective of protecting the interests of investors in securities and to promote the development of and to regulate the securities market in India.
Sectoral Cap	The limit up to which an investment can be made in a particular sector by a non-resident
STT	A tax levied in India on transaction undertaken in securities (shares, debentures) on a RSE.



27 GLOSSARY

ABBREVIATION	MEANING
%	Percent
AD	Authorised Dealer
ADR	American Depository Receipt
AIF	Alternative Investment Fund
AOA	Articles of Association
ARC	Asset Reconstruction Company
BEPS	Base Erosion Profit Shifting
BIS	Bank for International Settlements
BMOU	Bilateral Memorandum of Understanding
BO	Beneficial Owner
BR	Board Resolution
BSE	Bombay Stock Exchange
CA	Chartered Accountant
CAF	Common Application Form
CBDT	Central Board of Direct Taxes
CCD	Compulsorily Convertible Debentures
CCEA	Cabinet Committee on Economic Affairs
CCPS	Compulsorily Convertible Preference Shares
CDSL	Central Depository Services Limited
CN	Convertible Notes
CP Code	Custodial Participant Code
CPS	Committed Portfolio Size
CRS	Common Reporting Standard
DDP	Designated Depository Participants
DDT	Dividend Distribution Tax
DEA	Department of Economic Affairs
DPIIT	Department of Promotion of Industry and Internal Trade
DTAA	Double Tax Avoidance Agreement
ECB	External Commercial Borrowing
EFI	Eligible Foreign Investor
ESOP	Employee Stock Option Plan
ETF	Exchange Traded Funds
FAR	Fully Accessible Route
FATCA	Foreign Account Tax Compliance Act
FATF	Financial Action Task Force
FCCB	Foreign Currency Convertible Bond
FCEB	Foreign Currency Exchangeable Bond
FC-GPR	Foreign Currency Gross-Provisional Return
FCNR	Foreign Currency Non-Resident (Bank) Account
FC-TRS	Foreign Currency-Transfer of Shares
FDI	Foreign Direct investment



FEMA	Foreign Exchange Management Act
FIFP	Foreign Investment Facilitation Portal
FLA	Foreign Liabilities and Assets
FPI Regulations	SEBI (FPI) Regulations, 2019
FPI	Foreign Portfolio Investors
FVCI	Foreign Venture Capital Investor
FVCI Regulations	SEBI (FVCI) Regulations, 2000
GAAR	General Anti Avoidance Rule
GDR	Global Depository Receipt
GIFT City	Gujarat International Finance Tec-City
GOI	Government of India
GST	Goods and Services Tax
IFSC	International Financial Services Centre
IFSCA	International Financial Services Centre Authority
IGA	Inter-Governmental Agreement
INR	Indian Rupee
InvIT	Infrastructure Investment Trust
IOSCO	International Organization of Securities Commission
IRA	Indian Revenue Authorities
IRDA	Insurance Regulatory and Development Authority of India
IT Act	Income-tax Act, 1961
KYC	Know Your Customer
LLP	Limited Liability Partnership
LOB	Limitation on Benefits
MAT	Minimum Alternative Tax
MF	Mutual Funds
MMOU	Multilateral Memorandum of Understanding
MOA	Memorandum of Association
MOF	Ministry of Finance
NCDs	Non-Convertible Debentures
NCLT	National Company Law Tribunal
NDI Rules	Foreign Exchange Management (Non-debt Instruments) Rules, 2019
NOC	No Objection Certificate
NRI	Non-Resident Indian
NSDL	National Securities Depository Limited
NSE	National Stock Exchange
OCI	Overseas Citizen of India
PAN	Permanent Account Number
PE	Permanent Establishment
PFRDA	Pension Fund Regulatory and Development Authority
PMLA	Prevention of Money Laundering Act
POA	Power of Attorney
PPT	Principal Purpose Test
PSU	Public Sector Undertaking



RBI	Reserve Bank of India
RDB	Rupee Denominated Bond
REIT	Real Estate Investment Trust
RI	Resident Indian
RSE	Recognised Stock Exchange
Rules	Income-Tax Rules,1962
SBI	State Bank of India
SEBI	Securities and Exchange Board of India
SEZ	Special Economic Zone
SFT	Specified Financial Transaction
SLB	Securities Lending and Borrowing
SNA	Segregated Nominee Account
SNRR	Special Non-Resident Rupee Account
STT	Securities Transaction Tax
TP	Transfer Pricing
TRC	Tax Residency Certificate
UBO	Ultimate Beneficial Owner
UK	United Kingdom
UN	United Nations
USA	United State of America
VCF	Venture Capital Fund
VCU	Venture Capital Undertaking
VRR	Voluntary Retention Route



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