Introduction to Overseas Direct Investment

Complied by: Mousam Kothari

Topics Covered

- What is the meaning of Direct Investment outside India?
- What is Automatic & Approval Route?
- What is a JV/WOS & what are prohibited activities for ODI?
- Process of making an application under Approval Route?
- Concept of Designated Authorized Dealer?
  (Can there be more than one designated Authorized Dealer for the same JV/WOS incase it has more than one Indian Promoter?)
  (What if one promoter has more than one JV in either the same or different countries)?
- Who is eligible to make ODI investment under Automatic Route?
- Monetary Limits of ODI?
- Are overseas investments freely allowed in all the countries?
- Is prior registration with the Reserve Bank necessary for direct investments under the Automatic Route?
- Importance of UIN?
- Does ODI encompass acquiring an existing company either partially or wholly?
- Permissible Sources of Investment
- Obligations of Indian Party
- Annual Performance Report
- Summary of Form ODI
- Queries

A. Meaning of ODI :-

Direct investment outside India means investments, either under

Automatic Route | **Approval Route**

by way of contribution to the capital or subscription to the Memorandum of a foreign entity or by way of purchase of existing shares of a foreign entity either by market purchase or private placement or through stock exchange, signifying a long-term interest in the foreign entity (JV or WOS).

B. Automatic & Approval Route:-

Under the ***Automatic Route***, an Indian Party does ***not*** require any **prior approval** from the **RBI** for making overseas direct investments in a **JV/WOS** abroad. The Indian Party should approach an Authorized Dealer Category – I bank with an application in Form ODI and the prescribed enclosures / documents for effecting the remittances towards such investments.

Form ODI is available as an Annex to the Master Direction titled ***'Master Direction on Reporting under Foreign Exchange Management Act'.***

Proposals not covered by the conditions under the automatic route require prior approval of the Reserve Bank for which a ***specific application*** in Form ODI with the documents prescribed therein is required to be made through the Authorized Dealer Category – I banks.

C. WOS/JV & Prohibited Activities:-

"Joint Venture (JV)"/ "Wholly Owned Subsidiary (WOS)" means a foreign entity formed, registered or incorporated in accordance with the laws and regulations of the host country in which the Indian party makes a direct investment. A foreign entity is termed as **JV** of the Indian Party when there are **other foreign promoters** holding the stake along with the Indian Party. In case of **WOS** entire capital is held by the ***one or more Indian Company.***

PROHIBITED ACTIVITIES

Real Estate Business | **Banking Business**

Real estate business means buying and selling of real estate or trading in Transferable Development Rights (TDRs) but does ***not include*** development of townships, construction of residential/commercial premises, roads or bridges, educational institutions, recreational facilities, city and regional level infrastructure, townships. Further, ***earning of rent income on lease of the property, not amounting to transfer, will not amount to real estate business***.

However, Indian banks operating in India ***can set up*** JVs/WOSs abroad provided they obtain clearance under the Banking Regulation Act, 1949, from the Department of Banking Regulation (DBR), CO, RBI.

D. Process of Making an application under Approval Route

The applicant should **approach** their designated **Authorized Dealer (AD)** with the ***proposal*** which shall be submitted to Reserve Bank after due scrutiny and with the specific recommendations of the designated AD bank along with supporting documents (as mentioned below) to the following address:

The Chief General Manager,
Reserve Bank of India,
Foreign Exchange Department,
Overseas Investment Division,
Amar Building, 5th Floor,
Sir P. M. Road, Fort,
Mumbai 400001.

The designated AD ***before forwarding the proposal should submit the Form ODI in the on-line OID application*** under approval route and the transaction number generated by the application should be mentioned in the letter. In case the proposal is approved, the AD bank should effect the remittance under advice to Reserve Bank so that the ***UIN is allotted.*** Documents need to be submitted along with Section D and Section E of Form ODI - Part I by the designated Authorized Dealer:

a) A ***letter*** from the designated **AD** of the IP in a sealed cover mentioning the following details:

- Transaction number generated by the OID application.
- Brief details of the Indian entity.
- Brief details of the overseas entity.
- Background of the proposal, if any.
- Brief details of the transaction.
- Reason/s for seeking approval mentioning the extant FEMA provisions.
- Observations of the designated AD bank with respect to the following:
    - Prima facie viability of the JV/ WOS outside India;
    - Contribution to external trade and other benefits which will accrue to India through such investment;
    - Financial position and business track record of the IP and the foreign entity;
    - Expertise and experience of the IP in the same or related line of activity of the JV/

WOS outside India.
• Recommendations of the designated AD bank.

b) A letter from the IP addressed to the designated AD bank.
c) Board resolution for the proposed transaction/s.
d) Diagrammatic representation of the organizational structure indicating all the subsidiaries of the IP horizontally and vertically with their stake (direct & indirect) and status (whether operating company or SPV).
e) Incorporation certificate and the valuation certificate for the overseas entity (if applicable).
f) Other relevant documents properly numbered, indexed and flagged.

E. Designated AD:-

The Indian party/ Resident Individual is required to route all transactions in respect of a ***particular overseas*** JV/WOS only through **one branch** of an Authorized Dealer. This branch would be the 'designated Authorized Dealer' in respect of that JV/WOS and **all transactions** and communications relating to the investment in that particular JV/WOS are to be reported only through this 'designated' branch of an Authorized Dealer. In case the JV/WOS is being set up abroad by two or more Indian promoters, then all Indian ***promoters collectively called the Indian*** *party* and the Resident Individual, would be required to route all transactions in respect of that JV/WOS only through one 'designated Authorized Dealer'. In case the Indian Party/ Resident Individual wants ***to switch over*** to another AD, an application by way of a letter may be made to the Reserve Bank after obtaining an NOC from the existing Authorized Dealer.

The Indian promoters are free to designate ***different branches*** of the same Authorized Dealer or branches of other Authorized Dealers for their separate JVs/WOSs. ***The only requirement is that regardless of the number of promoters, one JV/WOS will have only one 'designated Authorized Dealer' to route*** all its transactions

Note:- Choose your AD Bank wisely, although switch over option is available still why get into the hassle of paper work with RBI.

F. Eligible Persons:-

An Indian Party is eligible to make overseas direct investment under the Automatic Route. An Indian Party is a company incorporated in India or a ***body created*** under an Act of Parliament or a partnership firm registered under the Indian Partnership Act 1932 or a Limited Liability Partnership (LLP) incorporated under the LLP Act, 2008 and any other entity in India as may be notified by the Reserve Bank. When more than one such company, body or entity makes investment in the foreign JV / WOS, such combination will also form an "Indian Party".

G. Monetary Limit of ODI:-

i. The Indian Party can invest up to the ***prescribed limit of its net worth*** (as per the last audited Balance Sheet) in JV / WOS for any bonafide activity permitted as per the law of the host country.

The prescribed limit vis-a-vis the net worth will **not be** applicable where the investment is made out of balances held in the ***EEFC account of the Indian party or out of funds raised through ADRs/GDRs;***

ii. The Indian Party is not on the Reserve Bank's exporters' caution list / list of defaulters to the banking system published/ circulated by the Credit Information Bureau of India Ltd. (CIBIL) /RBI or any other credit information company as approved by the Reserve Bank or under investigation by the Directorate of Enforcement or any investigative agency or regulatory authority; and

iii. The Indian Party routes all the transactions relating to the investment in a JV/WOS through only one branch of an authorized dealer to be designated by the Indian Party.

H. Freely Allowed:-

Investment *in **Pakistan is allowed*** under the ***approval route***. Investments in **Nepal** can be **only** in Indian **Rupees**. Investments in **Bhutan** are allowed in Indian Rupees and in freely convertible currencies.

I. Prior Registration with RBI?

Per se ***no prior registration*** with the Reserve Bank is necessary for making direct investments under the automatic route. After the online report of the first remittance / investment in Form ODI for a JV / WOS in terms of A.P. (DIR Series) Circular No.62 dated April 13, 2016, a Unique Identification Number (UIN) for that particular JV/WOS is generated automatically and instantaneously. Subsequent investments in the same JV / WOS can be made only after allotment of the UIN

J. Issuance of UIN amount to approval?

No, the allotment of UIN does not constitute an approval from the Reserve Bank for the investment made/to be made in the JV/WOS. The issue of UIN ***only signifies taking on record*** of the investment for maintaining the database. The onus of complying with the provisions of FEMA regulations rests with the AD bank and/or the Indian party.

Further, with effect from June 01, 2012 an **auto generated e-mail**, giving the details of UIN allotted to the JV / WOS under the automatic route, is forwarded to the AD / Indian party as confirmation of allotment of UIN, and no separate letter is issued by the Reserve Bank to the Indian party and AD Category - I bank confirming the allotment of UIN.

K. Acquiring of Existing Company

An eligible Indian party is free to acquire either a ***partial*** stake (JV) or the entire stake (WOS) in an already existing entity overseas, provided the ***valuation is as per the laid down norms***.

L. Permissible Sources of Funding ODI

Funding for overseas direct investment can be made by one or more of the following sources:

i. Drawal of foreign exchange from an AD bank in India.

ii. Swap of shares (***refers to the acquisition of the shares of an overseas JV / WOS by way of exchange of the shares of the Indian party***).

iii. ***Capitalization of exports*** and other dues and entitlements. (***Capitalization of Exports is when an eligible Indian party exports outside India, it shall be entitled to receive consideration, instead of receiving it, same can be capitalized as ODI***)

iv. Proceeds of ***External Commercial Borrowings*** / Foreign Currency Convertible Bonds.

v. In exchange of ***ADRs / GDRs*** issued in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993 and the guidelines issued by Government of India in the matter.

vi. Balances held in Exchange Earners Foreign Currency account of the Indian Party maintained with an Authorized Dealer.

vii. Proceeds of foreign currency funds raised through ADR / GDR issues.

M. Obligations of Indian Party

An Indian Party will have to comply with the following: -

i. ***receive share certificates*** or any other documentary evidence of investment in the foreign JV / WOS as an evidence of investment and submit the same to the designated AD within 6 months;

ii. ***Repatriate*** to India, all dues receivable from the foreign JV / WOS, like dividend, royalty, technical fees etc.;

iii. ***Submit*** to the Reserve Bank through the designated Authorized Dealer, every year, an ***Annual Performance Report*** in ***Part III of Form ODI*** in respect of each JV or WOS outside India set up or acquired by the Indian party. Revised Instructions for APR filing has been issued vide A.P. (DIR Series) Circular No.61 dated April 13, 2016.

iv. ***Report*** the details of the decisions taken by a JV/WOS regarding ***diversification*** of its activities /setting up of step down subsidiaries/alteration in its share holding pattern ***within 30 days of the approval*** of those decisions by the competent authority concerned of such JV/WOS in terms of the local laws of the host country. These are also to be included in the relevant Annual Performance Report; and

v. in case of ***disinvestment***, sale proceeds of shares/securities shall be repatriated to India immediately on receipt thereof and in any case ***not later than 90 days*** from the date of sale of the shares /securities and documentary evidence to this effect shall be submitted to the Reserve Bank through the designated Authorised Dealer.

N. Annual Performance Report

An Indian Party (IP) / Resident Individual (RI) which has made an Overseas Direct Investment (ODI) has to submit an Annual Performance Report (APR) in Form ODI Part III to the Reserve Bank by ***30th of June every year*** in respect of each Joint Venture (JV) / Wholly Owned Subsidiary (WOS) outside India set up or acquired by the IP / RI (as prescribed under Regulation 15 of FEMA Notification, ibid).

With effect from April 13, 2016, the ***AD bank,*** before undertaking / facilitating any ODI related transaction on behalf of the eligible applicant, should necessarily check with its nodal office to ***confirm that all APRs*** in respect of all the JV / WOS of the applicant have been ***submitted***. ***Further, certification of APRs by the Statutory Auditor or Chartered Accountant may not be insisted upon in the case of Resident Individuals. Self-certification may be accepted.***

With effect from April 13, 2016, where ***multiple IPs*** / RIs have invested in the same overseas JV / WOS, the obligation to submit APR shall lie with the IP / RI having ***maximum stake*** in the JV / WOS. ***Alternatively***, the IPs / RIs holding stake in the overseas JV / WOS ***may mutually agree*** to assign the responsibility for APR submission to a designated entity which may acknowledge its obligation to submit the APR in terms of Regulation 15 (iii) of Notification, ibid, by furnishing an appropriate undertaking to the AD bank.

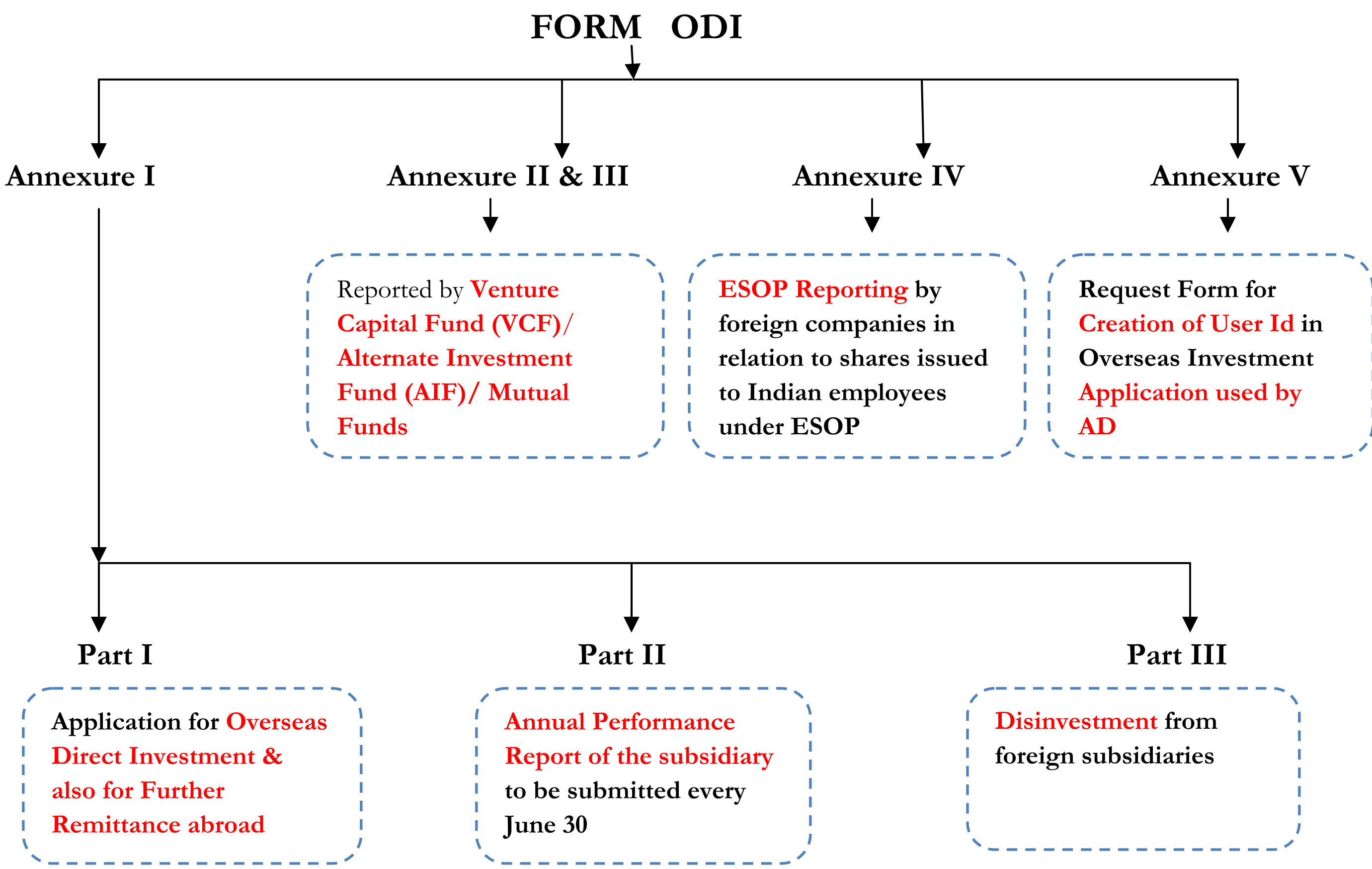
Where the law of *the* ***host country does not*** mandatorily require auditing of the books of accounts of JV / WOS, the Annual Performance Report (APR) may be submitted by the Indian party based on the ***un-audited annual*** accounts of the JV / WOS ***provided***:

a) The ***Statutory Auditor*** of the Indian party ***certifies*** that 'The un-audited annual accounts of the JV / WOS reflect the true and fair picture of the affairs of the JV / WOS' and

b) That the un-audited annual accounts of the JV / WOS has been adopted and ***ratified by the Board*** of the Indian party.

O. SUMMARY OF FORM ODI

As per RBI notification A.P. (DIR Series) Circular No. 62 dated April 13, 2016, the new form ODI has been amended and would have ***FIVE Annexure*** instead of six. The rationalized and revised Form ODI will now comprise of following parts:-



P. Queries

In case of any further queries you can write us at Email: mousam.kothari@gmail.com

Thank You

Source: RBI Website