

Foreign Exchange Management Act, 1999 (FEMA)

FDI in Petroleum & Natural Gas - Public Sector Undertakings & Foreign Investment in Telecom Sector increased to 100% from 49% under automatic route

[Press notes no. 4 \(2021 series\) dated 6th October 2021](#) and [Press notes no. 3 \(2021 series\) dated 29th July 2021](#)

Ministry of Commerce and Industry has declared that Foreign Investment up to 100% under the automatic route is now allowed in Telecom services sector which erstwhile required government approval beyond 49% and Foreign Investment in Petroleum & Natural Gas – Public sector Undertaking is now allowed, where an 'in-principle' approval for strategic disinvestment of a PSU has been granted by the Government.

The RBI has provided LIBOR +100 basis point rate for advance against exports received by the exporter

[Notification No. FEMA 23\(R\)/\(5\)/2021-RB dated 8th September 2021](#) and [RBI/2021-2022/101](#)

'The RBI' has vide above notification made amendments in FEM (Export of Goods and Services) (Amendment) Regulations, 2021,

wherein it has provided that in case of the advance payment received against exports, the rate of interest, if any, payable against such advance shall not exceed 100 basis points above the LIBOR or other applicable benchmark as may be directed by 'the RBI'.

Ministry of Finance (MoF) has pronounced amendments in FEM (Non-Debt Instrument) Rules 2019 ('NDI' rules) of – Insurance sector so as to bring it in line with the amended sectoral limit from 49% to 74%, along with the changes in the sectoral conditions.

[MoF notification no. S.O. 3411\(E\) dated 19th August 2021](#)

The MoF has in NDI rule, vide the above FPIs notification has pronounced following amendments in sectoral conditions of Insurance sector, such as:

- It has replaced the sectoral limit from 49% to 74% wherever applicable.
- The definition of Equity Share Capital, "Foreign Direct Investment" (FDI), Foreign Investors, "Foreign Portfolio Investment," "Indian Insurance Company", "Indian

Company,” “Non-resident Entity,” “Public Financial Institution,” “Resident Indian Citizen”, “Total Foreign Investment” shall have the same meaning as provided in Indian Insurance Companies (Foreign Investment) Rules, 2015 issued by Department of Financial Services and regulations issued by Insurance Regulatory and Development Authority of India from time to time, along with the newly introduced term Key Management Person (KMP).

- c. The term ‘control’, ‘Indian Control of an Indian Insurance Company’, ‘Indian Ownership’ have been deleted.
- d. The majority of boards composition consisting of directors, KMP, Chairman, MD, CEO of such Insurance companies and its intermediaries having foreign investment shall be of Resident Indian Citizens.

Draft Foreign Exchange Management (Non-debt Instruments - Overseas Investment) Rules, 2021 and Foreign Exchange Management (Overseas Investment) Regulations, 2021

[Draft FEM \(NDI - OI\) Rules, 2021](#)

[Draft - FEM\(OI\) Regulations, 2021](#)

Background

‘The RBI’ vide its press release dated 9th August 2021 has issued Foreign Exchange Management (Non-debt Instruments - Overseas Investment) Rules, 2021 (‘FEM (OI)’) and the draft Foreign Exchange Management (Overseas Investment) Regulations, 2021. The objective behind the release of the said draft rules and regulations on Overseas Direct Investments (‘ODI’) – was to obtain feedback on the same. Mentioned below are the salient features of changes proposed in the draft Rules/Regulations-

Changes/Insertion of new definition

There has been insertion of a few definitions which did not form part of the extant rules and regulations such as “Write off”, “Step Down Subsidiary (‘SDS’)”, “Foreign entity”, “Relative”, “Overseas Portfolio investment”, “Control”,

“Sweat equity shares”. Clarification on a few definitions is also provided.

Further, the scope of ODI has been enlarged to include investment beyond 10% in listed foreign entity and where person resident in India has invested in foreign entity and has acquired control.

Bonafide Business Activity (Round Tripping)

The draft rules have included the concept of round tripping which will be prohibited; where investment by a resident person in a foreign entity that has invested or invests into India (directly or indirectly). It further clarifies that said inclusion is specifically to avoid transactions designed for tax evasion or tax avoidance.

Mandatory requirement of No objection Certificate (NOC)

Where a person resident in India intends to make any investment or disinvestment, then NOC from concerned authorities is necessary in case of investment having Special Mention Account or Non-Performing Assets/willful defaulter or it is under investigation by a regulatory body or investigative agencies.

The price band of 5% while computing fair value

The draft rules provides that in case of Overseas Investment other than listed foreign securities, the price should be within 5 % range of the fair value arrived on an arm’s length basis as per any internationally accepted pricing methodology for valuation duly certified by a registered valuer (‘RV’) as per the Companies Act 2013. The concept of RV has been brought in for the first time.

Transfer/Liquidation

A person holding equity capital may transfer such investment / divestment, in compliance with rules & FEM(OI) regulations. In following case of disinvestment:

- That is other than liquidation – there shall be no dues outstanding receipt from foreign entity.

- That is other than by way of conversion to loan- Should have stayed invested for at least 1 year from making ODI.
- That is by way of conversion to loan- Person resident in India shall not lose control & should be compliant with the provisions for lending / investment.

Restructuring Balance Sheet

In the draft Rules/Regulations, restructuring of the Balance Sheet of a listed / unlisted foreign entity is allowed which has been incurring losses for previous 2 years as against only listed entity in existing regulations. Subject to:

- Compliance with the extant regulations.
- Total value of the outstanding dues towards the Indian entity including investment in equity and debt, after such restructuring not exceeding the proportionate amount of the accumulated losses.
- In case original investment > USD 10 million or diminution exceeds 10% of the total value of the outstanding dues towards the Indian entity. Then the diminution to be certified by a registered valuer certificate (not older than 6 months) as per the Companies Act 2013 or by similar valuer registered with the regulatory authority in the host jurisdiction.

Restricted sectors and clarification on leasing activity

Overseas investment in a foreign entity engaged in-

- Real estate activity;
 - Gambling in any form; and
 - Offering financial products linked to Indian Rupee except for products offered in International Financial Services Centre (IFSC)
- is prohibited. The draft rules now clarify that real estate activity does not cover development of townships, construction of residential/commercial premises, roads or bridges for selling or leasing.

Also, overseas investment (OI) all not be made in countries/jurisdictions that are not Financial Action Task Force ('FATF') and International

Organization of Securities Commissions (IOSCO) compliant country.

Immovable Property

Acquisition/Transfer:

There is restriction to acquire or transfer any immovable property situated outside India without general or special permission of 'the RBI' barring a few exceptions. The draft also states a list of ways and persons who may acquire immovable property outside India.

Transfer:

A person resident in India who has acquired any immovable property outside India may transfer such property by way of gift, inheritance or sale. He can also create a charge on such property.

Limit for financial commitment

The draft rule clarifies that the 400% of net worth limit is to be applied at the time of undertaking financial commitment and not annually, thereby removing the ambiguity.

ODI in Financial Services Activity

It is now specifically provided that an entity engaged in financial services activity in India may make ODI in a foreign entity which is engaged in the same activity.

Overseas Portfolio Investment (OPI)

'OPI' is recently added which states a listed Indian entity may make 'OPI' (incl reinvestment) within 50% limit of its net worth. Also, a software exporting entity is allowed to receive foreign securities up to 25% of the value of exports made to a foreign software company.

Acquisition by way of gift or inheritance

There is no limit on a resident individual acquiring 'OI' by inheriting from a person resident in/outside India. He may also acquire foreign securities by way of gift under limit prescribed from a relative who is a resident outside India or person mentioned under section 6(4) of the FEMA Act.

Modes for undertaking financial commitment other than equity capital

Acquiring Control is an additional prerequisite to make ODI by equity investment. Financial

commitment by way of Debt also shall be considered in the 400% limit. A welcome change is that in the draft regulations, financial commitment by way of guarantee can now be provided to all levels of 'SDS' which under the existing rules is available only to Joint Venture and Wholly Owned Subsidiary.

Mode of Payment

For making OI, mode of remittance shall be made through banking channels, out of funds held in an account maintained in accordance with the FEMA rules and regulations or Swap of securities.

The new Forms and Reporting

Reporting shall be done under:

- **Form FC** in case of financial commitment.
- **Form OPI** in case of Overseas Portfolio Investment which has been recently inserted.
- **Form APR** (Annual Performance report) will have to be filed within 6 months from the end of the accounting period of the foreign entity.
- Filing of Form APR is not required where-
 - i. Financial commitment is only in equity capital
 - ii. where there is only one Indian resident investor in a foreign entity and
 - iii. such resident investor neither has control nor holds more than 10% equity shares.

In case more than one Indian resident have made ODI in the same foreign entity the Form APR has to be filed by a person resident in India having the highest stake in the foreign entity.

Delay in reporting and Late submission fee

To regularize the delay in reporting, the draft Regulations proposed the option of Late Submission Fee (LSF) that additional overseas investments are not permissible until the delay in reporting (if any) is regularized.

Reserve Bank of India (RBI)

Resolution Framework for COVID-19-related Stress – Financial Parameters – Revised timelines for compliance

[RBI/2021-22/80 dated 6th August 2021](#)

Please refer to the [Circular dated 7th September 2020](#) *inter alia* advising the key ratios and their sector specific thresholds to be considered by lending institutions while finalising the resolution plans in respect of eligible borrowers under Part B of the Annex to the Resolution Framework issued on 6th August 2020.

In view of the resurgence of the Covid-19 pandemic in 2021 and recognising the difficulties it may pose for the borrowers in meeting the operational parameters, it has been decided to defer the target date for meeting the specified thresholds in respect of the 4 operational parameters, viz. Total Debt / EBITDA, Current Ratio, Debt Service Coverage Ratio (DSCR) and Average Debt Service Coverage Ratio (ADSCR), to 1st October 2022.

The target date for achieving the ratio Total Outside Liabilities/Adjusted Tangible Net Worth as crystallised in terms of the resolution plan, will remain unchanged as 31st March 2022

Prudential Norms for Off-Balance Sheet Exposures of Banks – Restructuring of derivative contracts

[RBI/2021-22/81 dated 6th August 2021](#)

The RBI has clarified that change in the terms of a derivative contract on account of change in reference rate necessitated due to transition from LIBOR to an alternative reference rate should not be treated as restructuring of the derivative contract provided all other parameters of the original contract remain unchanged.

Master Direction on Financial Statements - Presentation and Disclosures

[RBI/DOR/2021-22/83 dated 30th August 2021](#)

This Master Direction incorporates all the guidelines, instructions and directives issued by 'the RBI' to the banks which will enable banks to have all current instructions on presentation and disclosure in financial statements at one place for reference. Some of the key features are as follows-

- These Directions will be applicable to:
 - all banking companies, corresponding new banks, regional rural banks (RRBs) and State Bank of India (collectively referred to as Commercial Banks)
 - Urban Co-operative Banks (UCBs).
- Commercial Banks should ensure strict compliance with the Accounting Standards (AS) notified under the Companies (AS) Rules, 2006, as amended from time to time, subject to Directions/Guidelines issued by 'the RBI'. UCBs will be guided by the announcements of the Institute of Chartered Accountants of India (ICAI) regarding applicability of AS
- In Consolidated Financial Statement, (CFS) where different entities in a group are governed by different accounting norms laid down by the concerned regulator/s, the Balance Sheet size may be used to determine the dominant activity and accounting norms specified by its regulator may be used for the consolidation of similar transactions and events. Where banking is the dominant activity, accounting norms applicable to a bank shall be used for consolidation purposes in respect of like transactions and other events in similar circumstances.
- Reserves and Surplus are to be divided into the following –(i) Statutory Reserves, (ii) Capital Reserves, (iii) Share Premium, (iv) Revenue and other Reserves and (v) Balance

Guidelines on Compensation of Whole Time Directors/ Chief Executive Officers/ Material Risk Takers and Control Function staff - Clarification

[RBI/2021-22/95 dated 30th August 2021](#)

As per the [Circular dated 4th November 2019](#), share-linked instruments are required to be fair valued on the date of grant using Black-Scholes model. However, banks do not recognise grant of the share-linked compensation as an expense in their books of account concurrently. In order to bring clarity, the following has been added- *"The fair value thus arrived at should be recognised as expense beginning with the accounting period for which approval has been granted"*.

Banks should ensure compliance to above instructions for all share-linked instruments granted after the accounting period ending 31st March 2021.

Master Circular - Prudential norms on Income Recognition, Asset Classification and Provisioning pertaining to Advances

[RBI/2021-2022/104 dated 1st October 2021](#)

Please refer to the [Master Circular No. RBI/2015-16/101 dated 1st July 2015](#) consolidating instructions / guidelines issued to banks till 30th June 2015 on matters relating to prudential norms on income recognition, asset classification and provisioning pertaining to advances.

This Master Circular consolidates instructions on the above matters issued as on date.

KEY TAKE AWAY

- To provide clarity on ambiguous issues ,further liberalize regulatory framework and also to promote relaxation in carrying out business, it has been decided to rationalize the existing provisions governing overseas investment.
- To enable banks to have all current instructions on presentation and disclosure in financial statements at one place for reference, Master Directions on Financial Statements issued.



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CNK
& ASSOCIATES LLP

MUMBAI

3rd Floor, Mistry Bhavan, Dinshaw Vachha Road,
Churchgate, Mumbai. 400 020, India.
Tel: +91 22 6623 0600

501/502, Narain Chambers, M.G. Road,
Vile Parle (East), Mumbai 400 057, India.
Tel: +91 22 6250 7600

Bengaluru: +91 80 2535 1353

Ahmedabad: +91 79 2630 6530

Dubai: +971 4 3559533

Chennai: +91 44 4384 9695

Gandhinagar: +91 79 2630 6530

Sharjah: +971 4 3559544

Vadodara: +91 265 234 3483

Delhi: +91 11 2735 7350