

The Chamber of Tax Consultants

(3-Day Residential Refresher Conference on the Foreign Exchange Management Act 1999 and its Rules / Regulations with focus on practical aspects)

Issues and challenges surrounding Resident Individuals and Non-Resident Indians / Overseas Citizens of India
(including issues of Inheritance and Trust)

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Overview of the Paper & structure

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- ▶ History & Background of FEMA
- ▶ Important provisions of FEMA
- ▶ Important definitions of FEMA
- ▶ Important concepts / schemes of FEMA
- ▶ Posers in the Paper – Conceptual understanding
- ▶ Emigrating Indian – a Non-Resident (PROI)
- ▶ Procedure – Resident to Non-Resident
- ▶ Bank Accounts of Non-Resident
- ▶ Properties in India – NDI Rules
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Overview of the Paper & structure (cont'd)

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- ▶ FDI in Construction
- ▶ Portfolio Investment – Schedule III
- ▶ Transfer of Assets by Non-Resident in India
- ▶ Returning Indians
- ▶ Overseas Remittances & Investment by Residents
- ▶ Trusts – Implications under FEMA

Abbreviations

- ▶ Authorised Dealer (AD)
- ▶ Capital Account transaction (CAP)
- ▶ Current Account Transaction (CAT)
- ▶ Foreign Currency Non Resident Account (FCNR)
- ▶ Foreign Direct Investment (FDI)
- ▶ Foreign Exchange (FE)
- ▶ Foreign Exchange Management Act (FEMA)
- ▶ Foreign Investment Facilitation Portal (FIFP)
- ▶ Government of India (GOI)
- ▶ Income-tax Act (ITA)
- ▶ Liberalized Remittance Scheme (LRS)
- ▶ Notification No.(Ntf.)

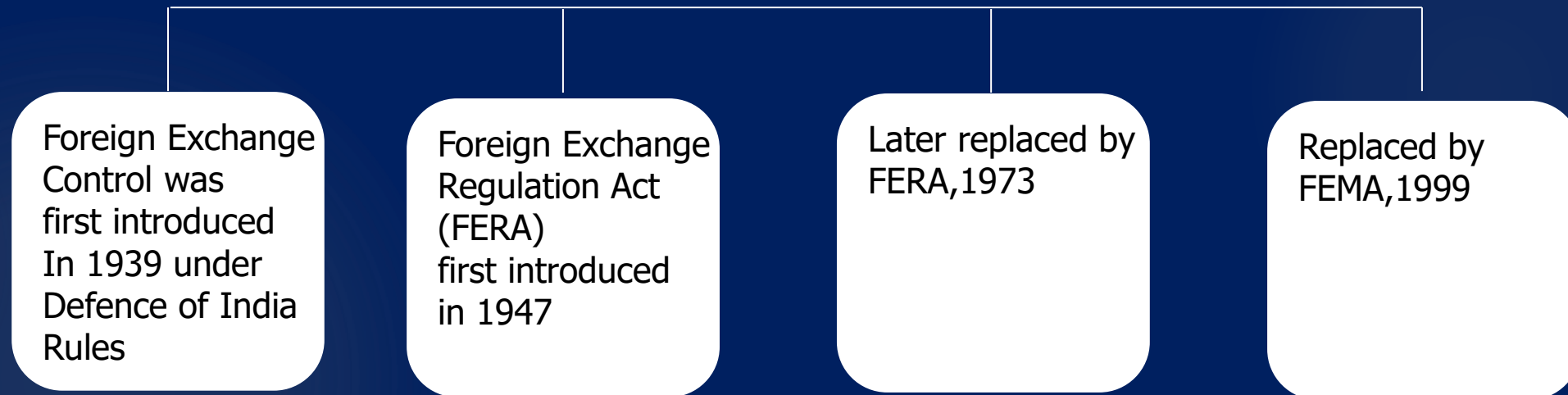
Abbreviations (cont'd)

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- ▶ Non Resident External Account (NRE)
- ▶ Non Resident Indian (NRI)
- ▶ Non Resident Ordinary Account (NRO)
- ▶ Overseas Citizen of India (OCI)
- ▶ Overseas Direct Investment (ODI)
- ▶ Overseas Portfolio Investment (OPI)
- ▶ Person Resident Outside India (PROI)
- ▶ Person Resident in India (PRII)
- ▶ Person of Indian Origin (PIO)
- ▶ Reserve Bank of India (RBI)
- ▶ Resident Foreign Currency Account (RFC)
- ▶ Joint Venture (JV)
- ▶ Wholly owned Subsidiary (WOS)

History of FEMA

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Background of FEMA

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- ▶ Foreign Exchange Management Act, 1999(FEMA) was introduced on 1st June,2000 superseding the Foreign Exchange Regulation Act,1973 (FERA)
- ▶ The replacement was a great relief as FERA was unduly stringent in its criminal provisions now reintroduced by FA 2015.
- ▶ Main objective of FEMA is to facilitate external trade and payments and To promote the orderly development and maintenance of foreign exchange market
- ▶ Applies to whole of India and all branches, offices and agencies outside India, which are owned or controlled by person resident in India – Extra territorial jurisdiction

Important Provisions of FEMA

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- ▶ FEMA has in all 49 sections of which the first 9 sections are substantive and the rest are procedural/administrative
- ▶ Section 46 of the Act grants power to Central Government to make rules and section 47 (as amended by Finance Act, 2015) of the Act grants power to RBI to make regulations to implement its provisions and the rules made there under; also provides that earlier regulations made by RBI, for which power now vests with Central Govt. remain valid until amended / rescinded by Central Govt
- ▶ Every Rule and Regulation made under this Act shall be laid before each house of parliament Section 48
- ▶ A number of Notifications are issued after the initial 25 Notifications, most of the time only to amend the existing one or more of the 25 Notifications.

Important Provisions of FEMA (cont'd)

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Section	Description
1	Application and commencement of FEMA w.e.f. 1/6/2000
2	Definitions (amended by Finance Act, 2015 to include "Authorised Officer" and "Competent Authority")
3 to 9	Substantive provisions, Dealing in FE, No drawal of FE, CAT, CAP, Export & Import, Repatriation, Possession of FE etc. (Section 6 amended by Finance Act, 2015 to provide that equity flows shall be under Central Govt.)
10 to 12	Authorized person Delegation of power by RBI ,ADs & Documents
13 to 15	Contraventions and penalties (Section 13 amended by Finance Act, 2015 for penalty for holding foreign exchange, security or property in excess of threshold specified in new S. 37A)
16 to 38	Adjudication, Appeal and Directorate of enforcement [new Section 37A vide Finance Act, 2015: Special provisions relating to assets held outside India in contravention of section 4]
39 to 49	Miscellaneous provisions, Power of RBI, Power of Government of India, Procedure for issue of Notification etc. Sunset clause for FERA upto 31 st May 2002, Repeal and Savings. [Section 46 & 47 amended for change in powers of Govt. & RBI respectively]

Important Provisions of FEMA (cont'd)

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Section	Description
3	Dealing in foreign exchange by any Person in India. Receipt by PRII without Remittance, Payment in India by PRII with a right O/I
4	Holding of foreign exchange, Security and Immovable property by PRII.
5	Current account transactions, List and Restrictions
6	Capital account transactions-Powers of RBI, Central Govt. and the list.
7	Export of goods and services- Declaration, Information, Direction to receive FE.
8	Realisation and repatriation of foreign exchange
9	Exemption from realization and repatriation in certain cases And possession of FE

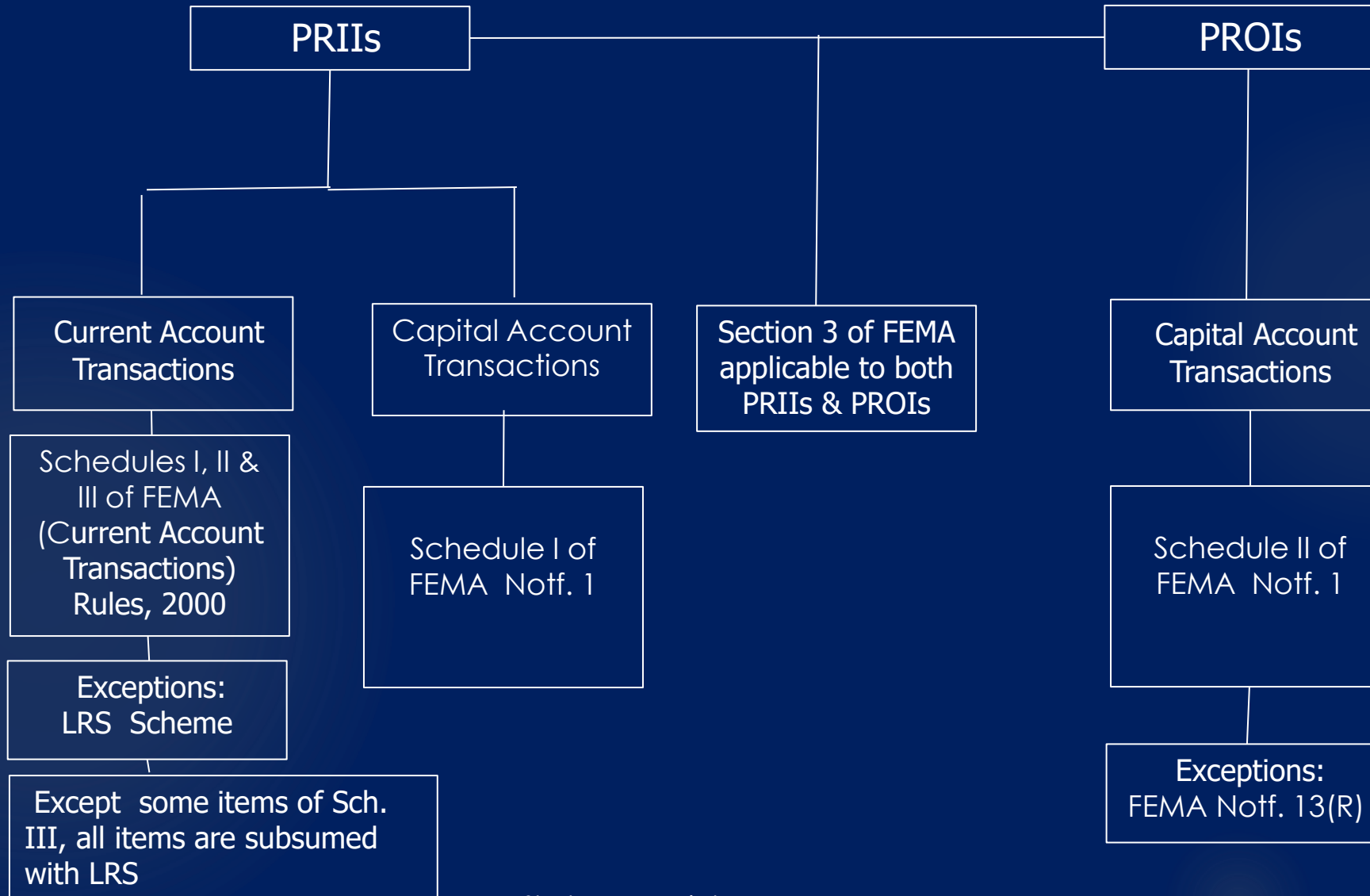
Fundamentals of FEMA

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- ▶ Foreign Exchange belongs to Govt. of India except permitted
- ▶ Dealing in Foreign Exchange and Security by PRII as well as by PROI is regulated (Section 3(a) of The FEMA)
- ▶ Dealing between PRII and PROI in Rupees is also regulated (Borrowing and Lending in Rupees, deposit in Rupees, Gifts in India by PROI except to relatives etc)
- ▶ Dealing of FE/Foreign Security and Foreign Property between PRII are regulated
- ▶ Dealing of Indian Security between PROIs is also regulated.
- ▶ Manner of Receipts from and Payments to PROI, regulated and to be reported to AD
- ▶ Permissible Capital Account or Current Account Transaction -Drawal of Foreign Exchange are specific to purposes for which they are granted.

FEMA Practice

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Important Definitions

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- The most important definitions under FEMA are the Capital Account Transactions and Current Account Transactions
- These definitions will provide an overview as to what activities and transactions can be carried out by a Resident Indian and Non Resident; as a consequence it is important to know the definitions of Person Resident in India (PRII) and Person Resident Outside India (PROI)
- In the upcoming slides let us look at the definitions of Capital Account transactions, Current Account Transactions, PRII, PROI and a few other important ones

Capital Account Transaction - Sec 6

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- According to Sec 2(e) of FEMA "capital account transaction" means a transaction which alters the assets or liabilities, including contingent liabilities, outside India of persons resident in India or assets or liabilities in India of persons resident outside India, **and includes transactions referred to in sub-section (3) of section 6;**
- Capital account transactions are generally prohibited unless permitted. They are regulated by RBI.
- Capital Account Transactions are notified through Notification FEMA 1, segregating the transactions of residents and non-residents as Schedule I & Schedule II respectively.
- About 25 Notifications have been issued by RBI to deal with the manner in which permissible Capital Account Transactions can be carried out.

Capital Account Transaction - Sec 6

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- Sec (6)(1) - Subject to the provisions of sub-section (2), any person may sell or draw foreign exchange to or from an authorised person for a capital account transaction.
- Sec 6(2) The Reserve Bank may, in consultation with the Central Government, specify—
 - (a) any class or classes of capital account transactions which are permissible;
 - (b) the limit up to which foreign exchange shall be admissible for such transactions;
 - (c) any conditions which may be placed on such transactions;

[Provided that the Reserve Bank shall not impose any restriction on the drawal of foreign exchange for payments due on account of amortization of loans or not depreciation of direct investment in the ordinary course of business.]
- Sec 6(2A) The Central Government may, in consultation with the Reserve Bank, prescribe—
 - (a) any class or classes of capital account transactions, not involving debt instruments, which are permissible;
 - (b) the limit up to which foreign exchange shall be admissible for such transactions; and
 - (c) any conditions which may be placed on such transactions.]
- Sec 6(3) [Omitted]

Capital Account Transaction - Sec 6

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- **Schedule I - Classes of capital account transactions of persons resident in India (PRII)**
 - i. Investment by a PRII in foreign securities.
 - ii. Foreign currency loans raised in India and abroad by a PRII.
 - iii. Transfer of immovable property outside India by a PRII.
 - iv. Guarantees issued by a PRII in favour of a person resident outside India.
 - v. Export, import and holding of currency/currency notes.
 - vi. Loans and overdrafts (borrowings) by a PRII from a PROI.
 - vii. Maintenance of foreign currency accounts in India and outside India by a PRII.
 - viii. Taking out of insurance policy by a PRII from an insurance company outside India.
 - ix. Loans and overdrafts by a PRII to a PROI.
 - x. Remittance outside India of capital assets of a PRII.
 - xi. Sale and purchase of foreign exchange derivatives in India and abroad and commodity derivatives abroad by a PRII.

Capital Account Transaction - Sec 6

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- **Schedule II - Classes of capital account transactions of persons resident outside India (PROI)**
 - i. Investment in India by a PROI, that is to say:
 - a) Issue of security by a body corporate or an entity in India and investment therein by a PROI; and
 - b) Investment by way of contribution by a PROI to the capital of a firm or a proprietorship concern or an association of persons in India.
 - ii. Acquisition and transfer of immovable property in India by a PROI.
 - iii. Guarantee by a PROI in favor of, or on behalf of, a person resident in India.
 - iv. Import and export of currency/currency notes into/from India by a PROI.
 - v. Deposits between a PRII and a PROI.
 - vi. Foreign currency accounts in India of a PROI.
 - vii. Remittance outside India of capital assets in India of a PROI.

- POSER: Guarantees are contingent liabilities. As per above definition, guarantee by PRII outside India is a capital account transaction but not so for guarantee by PROI. So, if guarantee by PROI is not a capital account transaction, participants are requested to discuss the implications under FEMA including under FEMA Ntf. 8.
- SOLUTION:
 - Guarantees by PROI are not capital account transactions as per FEMA, and hence it is freely permitted, unless specifically prohibited. Accordingly, Notification 8 only applies to and prohibits guarantee / surety by PRII towards debt, obligation or other liability owed by a PRII to PROI, or incurred by a PROI.
 - However, Regulation 3A was inserted w.e.f. 06.12.2012 which requires prior RBI approval for guarantee by international Banks, Fis, or JV partners towards credit enhancement of rupee denominated structured obligations of domestic companies. Despite such a transaction not being a Capital account transaction and therefore a Current account transaction, the said Regulation 3A in Notification 8 was introduced which appears ultra vires as it goes beyond the provisions of the main act FEMA.

POSER – ‘qua transaction’ or ‘qua person’

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- POSER: Whether a transaction is capital account “qua transaction” or ‘qua person’? Participants may discuss the implication in following examples
 - (a) Gift of foreign shares by one Resident to another Resident
- SOLUTION:
 - As per the definition of capital account transaction, it may appear that due to the Gift transaction, the assets outside India of the donor who is resident in India are being altered. Similarly, the assets outside India of the donee, also a resident in India, are being altered. Hence, this is a capital account transaction.
 - Normally, in cross-border transactions, there would be a party resident in India and another that is resident outside India. However, in the instant case, both the parties are resident in India. Definition of capital account transactions refers to alteration of assets and liabilities of 'persons' resident in India (two or more persons resident in India who are party to a transaction). Participants may discuss the question whether the gift alters assets outside India of 'persons' resident in India in a transaction of transfer of foreign security.
 - Can it be said that there is no alteration of assets of 'persons' resident in India? When considered individually, there may be an alteration but the definition refers to 'persons' resident in India thereby leading to a possible interpretation that the scheme of FEMA considers all residents on one side of the transaction and non-residents on the other side in the application of the various rules & regulations for a transaction.
 - Thus, “qua transaction”, it is not capital account in nature; however “qua person” it is capital account in nature.

POSER – ‘qua transaction’ or ‘qua person’ (cont’d)

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- POSER: (b) Resident beneficiary in an irrevocable offshore discretionary trust without any remittance
- SOLUTION:
 - FEMA prescribes regulations for permissible methods of acquisition of foreign assets. When a resident acquires foreign assets, it is a change in his assets outside India and hence it is a capital account transaction which is permissible only in the form and manner that is expressly allowed. However, when a resident is made a beneficiary in an offshore trust, there is no remittance from India and he acquires a right to the asset or its income only on distribution in future. In such a case, does the capital account transaction definition apply “qua transaction” or ‘qua person’?
 - A Trust is not included as a ‘Person’ as per the definition of ‘Person’ under FEMA. Hence, there is no question of examining the transaction ‘qua person’ and consequently there is no implication under FEMA and hence it is not a capital account in nature.
 - But PRII, has acquired beneficial interest in foreign assets which is a contingent asset, hence a view may be taken that it may not be treated as capital account in nature, unless distribution takes place.
 - Further, when distribution is made the beneficial owner derives a right in the asset outside India at which time it would be a capital account transaction.

Current Account Transaction – Sec 5

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- **Current Account Transaction:** According to section 2(j) Current account transaction means a transaction other than a capital account transaction. Such transaction includes:-
 - i. Payments due in connection to foreign trade, other current business, services and other short-term banking facilities in the ordinary course of business.
 - ii. Payments due as interest on loans and as net income from investments.
 - iii. Remittances for living expenses of parents, spouse and children residing Abroad.
 - iv. Expenses in connection with foreign travel, education and medical care of parents, spouse and children.
- Current Account transactions are freely permitted, unless prohibited. They are regulated by Central Government and the same is discussed in the upcoming paragraphs.
- **As per Sec 5** Any person may sell or draw foreign exchange to or from an authorised person if such sale or drawal is a current account transaction:
Provided that the Central Government may, in public interest and in consultation with the Reserve Bank, impose such reasonable restrictions for current account transactions as may be prescribed.

Current Account Transaction – Sec 5

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- As per Rule 3 of FEM (CAT) Rules, 2000, drawal of foreign exchange by any person for the following purpose is prohibited, namely:-
 - a) Transaction specified in the Schedule I; or
 - b) Travel to Nepal and/or Bhutan; or
 - c) Transaction with a person resident in Nepal or Bhutan;

Provided that the prohibition in clause (c) may be exempted by RBI subject to such terms and conditions as it may consider necessary to stipulate by special or general order.
- Current account transactions are covered by Foreign Exchange Management (Current Account Transaction) Rules,2000 (“Current Account Transaction Rules”)
- Current account transaction are divided into 3 schedules in current Account Transactions rules:
 - SCHEDULE I -Transactions which are prohibited
 - SCHEDULE II -Transactions which require prior approval of the Central Government
 - SCHEDULE III- Transactions which require prior approval of the RBI only if the limits or conditions specified therein are exceeded or not met

Schedule 1 – Current Account Transaction

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Schedule I -Transactions which are prohibited

- Remittance out of lottery winnings.
- Remittance of income from racing/riding, etc., or any other hobby.
- Remittance for purchase of lottery tickets, banned/prescribed magazines, football pools, sweepstakes etc.
- Payment of commission on exports made towards equity investment in Joint Ventures/Wholly Owned Subsidiaries abroad of Indian companies.
- Remittance of dividend by any company to which the requirement of dividend balancing is applicable.
- Payment of commission on exports under Rupee State Credit Route, except commission up to 10% of invoice value of exports of tea and tobacco.
- Payment related to “Call Back Services” of telephones.
- Remittance of interest income on funds held in Non-resident Special Rupee Scheme a/c.

Schedule 2 – Current Account Transaction

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- Schedule II -Transactions which require prior approval of the Central Government

No.	Purpose of Remittance	Ministry/Department of Govt. of India whose approval is required
1.	Cultural Tours	Ministry of Human Resources Development (Department of Education and culture)
2.	Advertisement in foreign print Media for the purposes other than promotion of tourism, foreign Investments & International bidding (exceeding USD 10,000) by a state government & its public sector undertaking	Ministry of Finance, (Department of Economic Affairs)
3.	Remittance of freight of vessel chartered by a PSU	Ministry of surface Transport, (Charter wing)
4.	Payment of import through ocean transport by a Govt. department or PSU on c.i.f basis	Ministry of Surface Transport (chartering wing)

Schedule 2 – Current Account Transaction

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No.	Purpose of Remittance	Ministry/Department of Govt. of India whose approval is required
5.	Multi Modal transport operators making remittance to their agents abroad	Registration certificate from the Director General of shipping
6.	Remittance of hiring charges of transponders by a) T.V. channels b) Internet Service Providers	a) Ministry of Information & Broadcasting b) Ministry of Communication & Information Technology
7.	Remittance of container detention charges exceeding the rate prescribed by Director General of Shipping	Ministry of Surface Transport (Director General of Shipping)
8.	Omitted	
9.	Remittance of prize money/sponsorship of sports activity Abroad by a person other than International/National/State Level sports bodies, if the amount involved exceeds US\$ 100,0000	Ministry of Human Resources Development (Department of Youth Affairs & Sports)
10.	Omitted	
11.	Remittance of Membership of P& I club	Ministry of Finance (Insurance Division)

Schedule 3 - Current Account Transaction

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SCHEDULE III (As per Rule 5)

► Facilities for individuals—

1. Individuals can avail of foreign exchange facility for the following purposes within the limit of USD 2,50,000 only. Any additional remittance in excess of the said limit for the following purposes shall require prior approval of the Reserve Bank of India.

(i)	<i>Private visits to any country (except Nepal and Bhutan).</i>
(ii)	<i>Gift or donation.</i>
(iii)	<i>Going abroad for employment.</i>
(iv)	<i>Emigration.</i>
(v)	<i>Maintenance of close relatives abroad.</i>
(vi)	<i>Travel for business, or attending a conference or specialised training or for meeting expenses for meeting medical expenses, or check-up abroad, or for accompanying as attendant to a patient going abroad for medical treatment/check-up.</i>
(vii)	<i>Expenses in connection with medical treatment abroad.</i>
(viii)	<i>Studies abroad.</i>
(ix)	<i>Any other current account transaction:</i>

Provided that for the purposes mentioned at item numbers (iv), (vii) and (viii), the individual may avail of exchange facility for an amount in excess of the limit prescribed under the Liberalised Remittance Scheme as provided in regulation 4 to FEMA Notification 1/2000-RB, dated the 3rd May, 2000 if it is so required by a country of emigration, medical institute offering treatment or the university, respectively

Schedule 3 - Current Account Transaction (cont'd)

Provided further that if an individual remits any amount under the said Liberalised Remittance Scheme in a financial year, then the applicable limit for such individual would be reduced from USD 250,000 (US Dollars Two Hundred and Fifty Thousand Only) by the amount so remitted :

Provided also that for a person who is resident but not permanently resident in India and—

- (a) is a citizen of a foreign State other than Pakistan; or
 - (b) is a citizen of India, who is on deputation to the office or branch of a foreign company or subsidiary or joint venture in India of such foreign company,
- may make remittance up to his net salary (after deduction of taxes, contribution to provident fund and other deductions).

Explanation : For the purpose of this item, a person resident in India on account of his employment or deputation of a specified duration (irrespective of length thereof) or for a specific job or assignments, the duration of which does not exceed three years, is a resident but not permanently resident :

Provided also that a person other than an individual may also avail of foreign exchange facility, mutatis mutandis, within the limit prescribed under the said Liberalised Remittance Scheme for the purposes mentioned herein above.

Schedule 3 - Current Account Transaction (cont'd)

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Facilities for persons other than individual—

2. The following remittances by persons other than individuals shall require prior approval of the Reserve Bank of India.
- (i) Donations exceeding one per cent of their foreign exchange earnings during the previous three financial years or USD 5,000,000, whichever is less, for—
 - (a) creation of Chairs in reputed educational institutes;
 - (b) contribution to funds (not being an investment fund) promoted by educational institutes;
 - (c) contribution to a technical institution or body or association in the field of activity of the donor Company.
 - (ii) Commission, per transaction, to agents abroad for sale of residential flats or commercial plots in India exceeding USD 25,000 or five per cent of the inward remittance whichever is more.
 - (iii) Remittances exceeding USD 10,000,000 per project for any consultancy services in respect of infrastructure projects and USD 1,000,000 per project, for other consultancy services procured from outside India.

Explanation :—For the purposes of this sub-paragraph, the expression "infrastructure" shall mean as defined in explanation to para 1 (iv) (A) (a) of Schedule I of FEMA Notification 3/2000- RB, dated the May 3, 2000.
 - (iv) Remittances exceeding five per cent of investment brought into India or USD 100,000 whichever is higher, by an entity in India by way of reimbursement of pre-incorporation expenses.

- POSER: Participants are requested to discuss whether activity of export, short-term advances are current account transactions. If they are current account transactions, are various stipulations and restrictions on exports under FEMA Ntf. 23(R) justified?
- Leads: The change from FERA to FEMA was operationalised by A.D. (M.A. Series) Circular No.11 dt. May 16, 2000 which states that “Remittances for all other current transactions which are not specifically prohibited under the Rules or which are not included in Schedule II or III may be permitted by authorised dealers without any monetary/percentage ceilings subject to compliance with the provisions of sub-section (5) of Section 10 of the Act.”

Thus, Current Account transactions are permitted except what is prohibited, yet various stipulations and restrictions are imposed by FEMA Ntf. 23(R). Please discuss.

- SOLUTION:
 - Export or Import of goods are in the nature of Capital Account transactions as it creates an asset in the form of receivables outside India or a liability in the form of payables outside India as the case may be. However, owing to peculiar definition of Current account transactions in FEMA, export / import of goods are considered as Current account transactions. Due to default in undertaking a transaction, character of the transaction will also undergo change which may be subject to separate set of regulations and to avoid it, though Current account transactions are freely permissible, Section 5 of FEMA regulates Current account transactions and gives power to the Central Government to impose such reasonable restrictions for current account transactions as may be prescribed in consultation with RBI. Accordingly, Notification 23(R) has been issued covering such declarations, obligations and directions to be observed by exporters.

POSER – Proprietary Export business

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- POSER: There can be a situation where a proprietary export business that was started by a person when he was resident in India is continued by him with the help of staff after emigrating to a foreign country. Participants are requested to discuss the implications of the above situation under FEMA, including declaration required under Export Declaration Form.
- SOLUTION:
 - Earlier, there was a requirement of declaring the export of Goods / Software in Form SDF which contained, inter alia, the following declaration – “I/We further declare that I/We am/are resident in India and I/We have a place of business in India”. In such a situation, the non-resident proprietor would not be able to give this declaration. However, vide Circular No. 101 dt. 14.05.2015, the said Form SDF is discontinued as the mandatory statutory requirements contained in the SDF have been subsumed in the Shipping Bill format. However, the Shipping Bill format does not contain the said declaration about resident status of the exporter. In view thereof, there exists a possibility of a resident continuing his Indian proprietorship export business after re-locating abroad and becoming non-resident.
 - Probably earlier format included the declaration of Resident status of an exporter only to avoid misuse of any of the CAT Schedules by a non-resident relating to Business purposes vs Private purposes of the proprietor. Proprietor and NRI is the same legal person, so CAT Rules available to him is for business purpose only.
 - Further, so far as holding investment in a proprietorship in India is concerned, Schedule IV of NDI rules permits an NRI to invest in a sole proprietorship on a non-repatriation basis, therefore there is no restriction on the emigrating Indian to continue with the sole proprietorship firm. Any income received by the Emigrating Indian will be deposited in the NRO Account.

POSER – Current Account Rules for Non-Resident

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- POSER: Are there any Current Account Rules for Non-residents? This situation may arise in case of transactions of a non-resident who sets up proprietary business in India.
- SOLUTION:
 - This has been discussed in earlier Poser on export proprietary business of non-resident. It may be noted that Current Account Rules apply either to 'Individual' or 'non-individual' as there is no reference in CAT Rules to resident status of the person undertaking a transaction. Further, CAT Rules are issued as per powers given under Section 5 of FEMA which refers to 'person' and not to his resident status. Hence, CAT Rules shall apply to proprietary business in India of a non-resident to the extent the transactions are current account in nature. However if they are in nature of Schedule III expenses it is advisable to pay such expenses from NRO account of the Non Resident as overall limit available for CAT is that of LRS, available only to Resident India.

- POSER: In the context of Item No. 7 (Remittance of container detention charges exceeding the rate prescribed by Director General of Shipping) in table above, participants may discuss as to what can be remitted towards container detention charges if no limit is prescribed by Director General of Shipping
- SOLUTION:
 - As the above refers to a transaction under Sch. II of CAT Rules which requires prior approval of the Central Govt., in case any container detention charges are payable, application may be made to relevant Ministry. In case no limits are prescribed, nevertheless approval will be required for remittance of the entire charges.

POSER – LRS & Current Account Rules for Emigration

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- POSER: The language employed on emigration related remittances under LRS Scheme restricts any remittance related to Immigration Visa / Residence Permit / Acceptance of citizenship of any foreign country. But Proviso 1 to Schedule III above reads that if country of immigration requires higher amount in excess of LRS limit, same is allowed. Participants are required to discuss as to whether such language employed under LRS Scheme is at variance with Schedule III.
- SOLUTION:
 - The LRS Scheme is applicable to Residents whereas CAT Rules apply to Individuals and Non-individuals. Under LRS Scheme, withdrawal of foreign exchange upto \$ 250,000 for various purposes including those listed in Sch. III of CAT Rules such as emigration is permitted. Further, remittance under LRS of any amount of foreign exchange outside India in excess of this limit may be allowed only towards meeting incidental expenses in the country of immigration and not for earning points or credits to become eligible for immigration by way of overseas investments in government bonds; land; commercial enterprise; etc. Thus, it is clear that so long as an individual is resident and is utilizing LRS, he will not be permitted for extra remittances unless for meeting incidental expenses on emigration.

POSER – LRS & Current Account Rules for Emigration (cont'd)

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- However, CAT Rules permit remittances higher than the limit of \$ 250,000 if so required by a country of emigration. CAT Rules are independent of LRS and are therefore not bound by or limited by the provisions of LRS. Confusion is probably created by the mention of 'LRS limit' in Sch. III of the CAT Rules whereas the intention of the law is to put a limit of \$ 250,000 in CAT Rules less amounts, if any, utilized for LRS purposes. Sch. III is not a part of LRS, only the limit of \$ 250,000 is applicable to the transactions, except additional requirements for emigration, medical and education.
- In case an individual has already proceeded abroad for employment and is thus not a resident but now desires to pursue 'citizenship by investment' programme in the foreign country, he may seek additional funds to be remitted for this purpose. It may be noted that in such a situation, the individual being a non-resident may seek to utilize the \$ 1 mn. scheme available under Ntf. 13(R). One can avoid the debate with AD-Bank through alternative available to PRII.

Person Resident in India (PRII) – Individual - Definition

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- ▶ Under Section 2(v)(i) of the FEMA, 'person resident in India' means- (i) a person residing in India for more than one hundred and eighty-two days during the course of the preceding financial year but does not include—
 - (A) a person who has gone out of India or who stays outside India, in either case—
 - (a) for or on taking up employment outside India, or
 - (b) for carrying on outside India a business or vocation outside India, or
 - (c) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;
 - (B) a person who has come to or stays in India, in either case, otherwise than—
 - (a) for or on taking up employment in India, or
 - (b) for carrying on in India a business or vocation in India, or
 - (c) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period;

Residential Status – Other Person

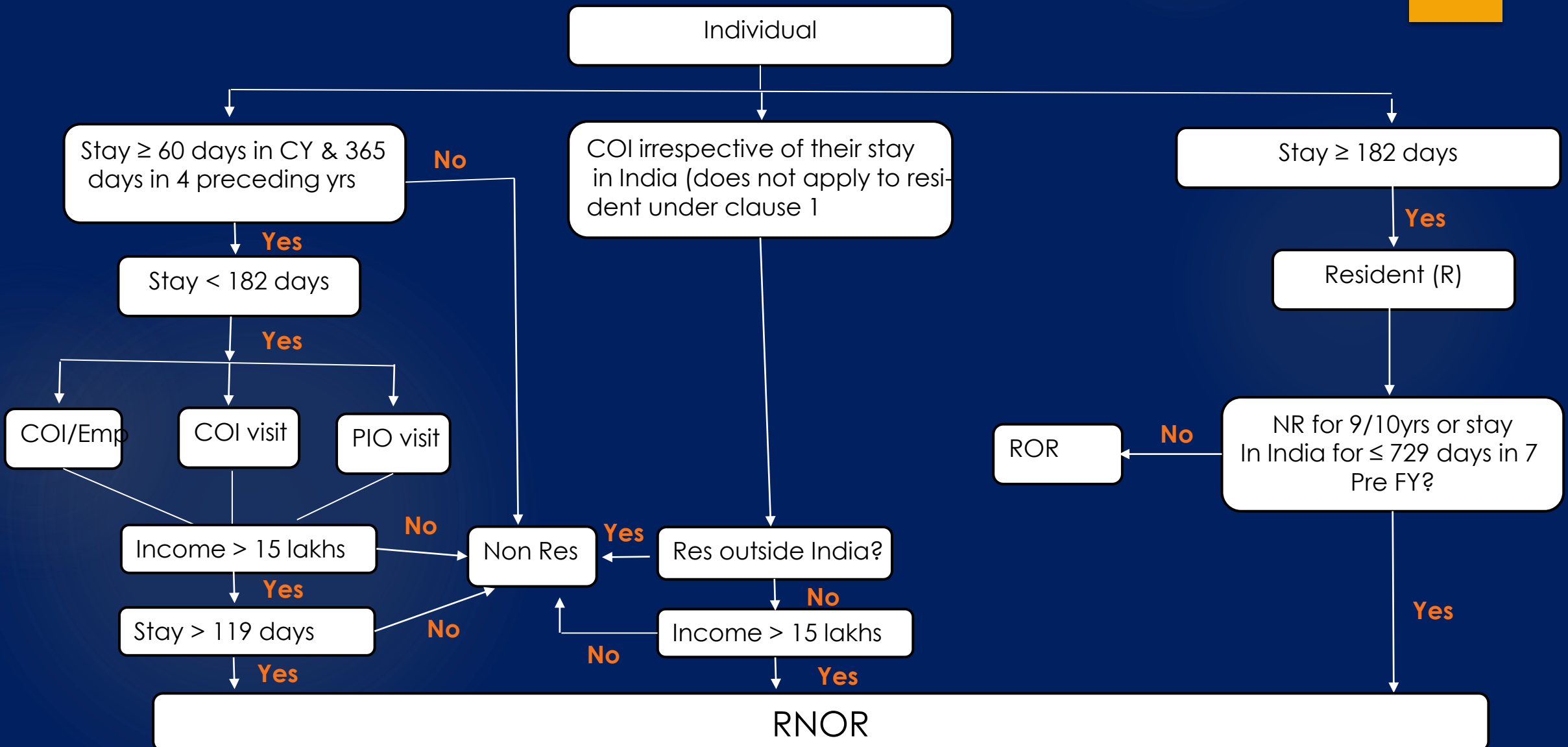
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As per Sec 2(v) person resident in India means

- ▶ 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;

Definition of Resident – Sec 6 of I. T. Act

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Residential Status under ITA - For Others

Status	Assessee	Conditions
Resident [S 6(2)]	HUF/Firm/AOP	Resident in India EXCEPT where in that year control & management of its affairs is situated wholly outside India
Resident but not Ordinary Resident [S 6(6)(b)]	HUF	Karta/Manager is present in India for less than 729 days during the preceding seven years OR who was a non resident in nine out of ten preceding previous years <i>(not a Resident v Non Resident)</i>
Resident [S 6(3)]	Company	-Indian Company - Control & Management of its affairs is situated wholly in India (upto 31.03.2016) -Place of Effective Management is in India (w.e.f 01.04.2016). C.NO. 8 of 2017 dt 23 rd Feb 2017

POSER – Branch in India of Foreign Company

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- POSER: An office, branch or agency in India of a Foreign company is a resident of India. Transactions of Residents or between residents in INR are generally not subject matter of FEMA.
Yet, for a branch / liaison office / project office in India of a foreign company, various stipulations and restrictions are specified under the Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016 issued under FEMA Ntf. 22(R). Participants are requested to discuss whether such stipulations and restrictions under FEMA Ntf. 22(R) are justified?
- SOLUTION:
 - Though transactions between Residents are not sought to be regulated under FEMA, however where ever there is possibilities of dealing in Foreign Exchange or payments are anticipated or receipts are likely, in order to facilitate trade and avoid any transactional breach, Section 6(6) of FEMA gives authority to Reserve Bank to prohibit, restrict, or regulate establishment in India of a branch, office or other place of business by a PROI, for carrying on any activity relating to such branch, office or other place of business. As a result, Notification 22(R) has been issued which prescribes the various operational aspects.

POSER – Foreign Branch of Indian Company

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- POSER: Similarly as above, foreign branch of an Indian Company is also a Resident. Accordingly, its transactions are outside the purview of Schedules I, II & III of FEM (Current Account) Rules. Participants are requested to discuss whether such stipulations and restrictions are justified?
- SOLUTION:
 - As defined in FEMA, foreign branch of an Indian company is a resident. Accordingly, it is freely permitted to undertake all current account transactions other than those specifically restricted or prohibited under the CAT Rules. Further, transactions between the H.O. in India and the foreign branch are between two residents which should not attract the provisions of FEMA. Similar to the obligations of a Resident under FEMA while undertaking cross-border transactions whether Capital account or Current account in nature, the foreign branch is also subject to the same obligations as its H.O.
 - Despite this legal fact, RBI sought to regulate the remittances to foreign branch and its business activities by amending Ntf. 10 dt. 03.05.2000 vide Ntf. 47 dt. 05.12.2001 as updated by Circular No. 18 dt. 04.12.2006. The said Notification 10 was issued as per powers conferred on RBI by Section 9(b) of FEMA which provides exemption from holding, realization & repatriation of foreign exchange to a foreign currency account held or operated by such person or class of persons and the limit up to which the Reserve Bank may specify. It appears that the amended Notification 10 goes beyond the statutory powers given under FEMA as it restricts remittances from India by setting limits and also imposes rules applicable to the business activities of the foreign branch including acquisition of office equipment etc.

POSER – PRII leaving for employment

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- POSER: LRS permits a person going abroad for the purpose of employment to draw USD 2, 50,000 per financial year. However as per the definition of person resident in India (PRII) as per Sec 2(v) of FEMA, a person who has gone out of India for the purpose of employment is not considered as a PRII. Will the person going out for employment be permitted to remit USD 2,50,000 (permitted to PRII) + USD 1 Mn (permitted to PROI from NRO A/c) in the year of going out for employment?
- SOLUTION:
 - A person would be considered non resident from the day he leaves the country for the purpose of employment and would be eligible to remit USD 1Mn from his/her NRO account. From the time he/she has got the job till he leaves for employment he would still be considered as FEMA resident and would be eligible to remit USD 250,000. Therefore in the 1st year of his employment he may be permitted to remit USD 1.25Mn

CASE STUDY - 1

Incorporation of WOS by an Indian company and deputation of Indian citizen to promote business outside India

India Ltd. is planning to incorporate a wholly owned subsidiary in U.K. and proposing deputation of one of its chief executive Mr. Patel an Indian Citizen to pursue promotion of business of Wholly Owned Subsidiary (WOS). Number of options deliberated on proposed deputation of Mr. Patel to U.K. are as under:-

- i. To relocate the employment of Mr. Patel to U.K.
- ii. To request Mr. Patel to look after operations in India & U.K., simultaneously as duties may not require aggregate travel of about 100 days to U.K. for few years
- iii. To relocate the employment of Mr. Patel to U.K. and request him to travel to India from time to time for Indian operations.

Questions for consideration

Mr. Patel informed that his other income is more than Rs. 15 lacs and requested advice on:-

- i. possibility of dual employment, both in India & U.K. under FEMA & under I.T. Act, 1961 and
- ii. his Non-Resident status under FEMA, on account of his desire to migrate his family with him & for higher studies of his children and various investment proposition outside India

India Ltd. also has WOS in Tax Heaven near U.K. Discuss the employment potential with such a Tax Heaven company.

CASE STUDY - 1

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Leads to Case study:

Mr. Patel is given with three options:

- i. To relocate the employment to U.K.
- ii. To request Mr. Patel to look after operations in India & U.K., simultaneously from India
- iii. To relocate the employment of Mr. Patel to U.K. and request him to travel to India from time to time

Under FEMA, there is no stipulation of stay in India for a Person to be PROI in a case he goes outside India for employment or for uncertain duration.

A person is regarded as Resident of U.K. if his stay in U.K. exceeds 90 days in a tax year with maintenance of dwelling house in U.K.

Overview of Legal Provisions

- ▶ Under FEMA residential status is of two types :
 - A. Person resident in India
 - B. Person resident outside India
- ▶ According to Sec 2(v) of FEMA " person resident in India" means-
 - (i) a person residing in India for more than one hundred and eighty- two days during the course of the preceding financial year but does not include-
 - (A) a person who has gone out of India or who stays outside India, in either case-
 - a) for or on taking up employment outside India, or
 - b) for carrying on outside India a business or vocation outside India, or
 - c) for any other purpose, in such circumstances as would indicate his intention to stay outside India for an uncertain period;
 - (B) a person who has come to or stays in India, in either case, otherwise than-
 - a) for or on taking up employment in India, or
 - b) for carrying on a business or vocation in India, or
 - c) for any other purpose, in such circumstances as would indicate his intention to stay in India for an uncertain period;
 - (ii) any person or body corporate registered or incorporated in India,
 - (iii) an office, branch or agency in India owned or controlled by a person resident outside India,
 - (iv) an office, branch or agency outside India owned or controlled by a person resident in India;
- ▶ As per sec 2 (w) " person resident outside India" means a person who is not resident in India;

Residential status for I.T. Act is determined u/s 6 as under :

Sec. 6(1) An individual will be treated as resident in India in any previous year if he fulfils any of the following two conditions:

- (a) he is in India in that year for a period or periods amounting in all to 182 days or more; or b.deleted
- (c) having within the four years preceding that year been in India for a period or periods amounting in all to 365 days or more and has been in India for 60 days or more in that year.

Explanation 1—In the case of an individual,—

- ▶ (a) being a citizen of India, who leaves India in any previous year as a member of the crew of an Indian ship as defined in clause (18) of section 3 of the Merchant Shipping Act, 1958 (44 of 1958), or for the purposes of employment outside India, the provisions of sub-clause (c) shall apply in relation to that year as if for the words "sixty days", occurring therein, the words "one hundred and eighty-two days" had been substituted.
- ▶ (b) being a citizen of India, or a person of Indian origin within the meaning of Explanation to clause (e) of section 115C, who, being outside India, comes on a visit to India in any previous year, the provisions of sub-clause (c) shall apply in relation to that year as if for the words "sixty days", occurring therein, the words "one hundred and eighty-two days" had been substituted 30[and in case of 31 [such person] having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the previous year, for the words "sixty days" occurring therein, the words "one hundred and twenty days" had been substituted.]
- ▶ Sec 6 (1A) Notwithstanding anything contained in clause (1), an individual, being a citizen of India, having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the previous year shall be deemed to be resident in India in that previous year, if he is not liable to tax in any other country or territory by reason of his domicile or residence or any other criteria of similar nature.]
- ▶ [Explanation.—For the removal of doubts, it is hereby declared that this clause shall not apply in case of an individual who is said to be resident in India in the previous year under clause (1).;

CASE STUDY - 1

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Overview of Legal Provisions – Not Ordinary Resident

- ▶ An Individual who fulfils any of the conditions mentioned in section 6(1) is treated as resident in India. But in order to become an “ordinarily resident”, he must satisfy either of the following four conditions as laid down under section 6(6) of the Income-tax Act, 1961 the provisions are :
 - i. He should have been resident in India in nine out of the ten previous years preceding the previous year in which he is resident within the meaning of section 6(1); or
 - ii. He should have been in India for a period or periods amounting in all to 730 days (i.e. on an average 104 days per year) or more during the seven years preceding that previous year.
 - iii. citizen of India, or a person of Indian origin, having total income, other than the income from foreign sources, exceeding fifteen lakh rupees during the previous year , who has been in India on a visit for a period or periods amounting in all to one hundred and twenty days or more but less than one hundred and eighty-two days; or
 - iv. a citizen of India who is deemed to be resident in India under clause 6(1)(A)

CASE STUDY - 1

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Applicability to Case Study

Mr. Patel is given with three options:

- i. To relocate the employment to U.K [No India duty].
- ii. To request Mr. Patel to look after operations in India & U.K., simultaneously from India [India base]
- iii. To relocate the employment of Mr. Patel to U.K. and request him to travel to India from time to time [UK base]

Analysis of the definition of person resident in India as given in sec. 2 (v) of FEMA for the purpose of given case:

If Mr. Patel goes out of India for employment , for vocation or for any other purpose for uncertain period, then even if he has resided in India for more than 182 days he will become person resident outside India from the day he goes abroad for the purpose of employment.

Analysis of the sec. 6 of Income Tax Act 1961 for the purpose of given case: From combine reading of sec. 6 and explanation to sec. 6 (1), we can conclude that if a person goes outside India for employment then he will be regarded as resident only if his stay in India is 182 days or more.

From second year (unless he visits India in the year of departure) he will become 'a person visiting India' and therefore, expln (b) will be applicable, in which case if his stay on visit is 120 days or more he would be a resident of India.

- i. Mr. Patel is advised to leave India before 28th September, and hence his stay in India during previous year of departure will be less than 182 days and visit days will be NIL. He will be regarded as Non Resident for the year of Departure under FEMA as well as ITA
- ii. To request Mr. Patel to look after operations in India & U.K., simultaneously from India
 - Mr. Patel can do so with a designation as Group MD, employed with a Company where Head office Function is located outside India say UK. Mr. Patel could be Resident or a Non Resident as per ITA depending upon his stay / visit in India. However if his base duty is in India, he will be regarded as PRII under FEMA,. Also, we are faced with a situation to demonstrate as to whether Mr. Patel went abroad for employment.

CASE STUDY - 1 - SOLUTION

- iii. To relocate the employment of Mr. Patel to U.K. and request him to travel to India from time to time

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Mr. Patel can do so he has to establish that he has gone abroad for the purposes of his employment, a fact that family is also migrated with him to UK supports his status as PROI in the year of departure. However he may be Resident under ITA 1961, while he is also tax resident of UK.

Therefore, the tie-breaker rule of the India-U.K. Tax Treaty will have to be applied to help determine which country has the right to tax him as the country of residence. He shall be deemed to be a resident of the State in which he has a permanent home available to him; if he has a permanent home available to him in both States, he shall be deemed to be a resident of the State with which his personal and economic relations are closer (Centre of vital interests).

However, it should be also be noted that even if he is deemed to be a resident of U.K., it is only for the purposes of the Treaty provisions; it does not mean that he becomes non-resident of India. Hence for purposes of application of Indian domestic tax law, he will continue to be treated as resident of India. Art 16 of India UK DTC will apply to test the taxability of Salary Income in India.

One can also explore if a Resident test of ITA can be modified by Article 4 of the tax treaty, where only due to income being INR 15 lakhs or more, status triggers to Resident from an NR.

Other Important Definitions under FEMA

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- ▶ Terms Non Resident Indian (NRI)/ Overseas Citizen of India (OCI) have not been defined under FEMA but have been specifically defined for its application under the relevant regulations
- ▶ **'Non-Resident Indian' (NRI)** means an individual resident outside India who is a citizen of India
- ▶ **OCI** is now defined separately in new FEMA Foreign Exchange Management (Non Debt Instruments) Regulations, 2019 as: 'Overseas Citizen of India (OCI)' means an individual resident outside India who is registered as an Overseas Citizen of India Cardholder under Section 7(A) of the Citizenship Act, 1955.
- ▶ **'Persons of Indian Origin'** cardholders registered as such under Notification No. 26011/4/98 F.I. dated 19.8.2002 issued by the Central Government are now deemed to be 'Overseas Citizen of India' cardholders w.e.f. 12.05.2015. PIO's were directed to accept the OCI card by extending the timeline from time to time up to September, 2018 without any additional fee.
- ▶ OCI is wider in scope than PIO which used to be up to 3 generations of foreign citizens. Now up to 4th generation of foreign citizens can be considered as OCI. Further, there are additional conditions in case of spouses that marriage should have subsisted for at least two years prior to application for OCI card.

Other Important Definitions under FEMA

- ▶ Following categories of foreign nationals are eligible for registration as Overseas Citizen of India (OCI) Cardholder:-
 - (1) Who was a citizen of India at the time of, or at any time after the commencement of the Constitution i.e. 26.01.1950; or
 - (2) who was eligible to become a citizen of India on 26.01.1950; or
 - (3) who belonged to a territory that became part of India after 15.08.1947; or
 - (4) who is a child or a grandchild or a great grandchild of such a citizen; or
 - (5) who is a minor child of such persons mentioned above; or
 - (6) who is a minor child and whose both parents are citizens of India or one of the parents is a citizen of India; or
 - (7) spouse of foreign origin of a citizen of India or spouse of foreign origin of an Overseas Citizen of India Cardholder registered under section 7A of the Citizenship Act, 1955 and whose marriage has been registered and subsisted for a continuous period of not less than two years immediately preceding the presentation of the application.
- ▶ Note : No person, who or either of whose parents or grandparents or great grandparents is or had been a citizen of Pakistan, Bangladesh or such other country as the Central Government may, by notification in the Official Gazette, specify, shall be eligible for registration as an Overseas Citizen of India Cardholder.

Other Important Definitions under FEMA

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- **Currency:** As per Sec 2(h) "currency" includes all currency notes, postal notes, postal orders, money orders, cheques, drafts, travellers cheques, letters of credit, bills of exchange and promissory notes, credit cards or such other similar instruments, as may be notified by the Reserve Bank;

It also includes ATM cards and Debit card or any other instrument by whatever name called that can be used to create a financial liability, as 'currency'. (Notf 15(R)/2015-RB dated 29th December, 2015)

- **Foreign Currency:** As per Sec 2(m) "foreign currency" means any currency other than Indian currency;
- **Foreign Security:** As per Sec 2(o) "foreign security" means any security, in the form of shares, stocks, bonds, debentures or any other instrument denominated or expressed in foreign currency and includes securities expressed in foreign currency, but where redemption or any form of return such as interest or dividends is payable in Indian currency;
- **Transfer:** As per Sec 2(ze) "transfer" includes sale, purchase, exchange, mortgage, pledge, gift, loan or any other form of transfer of right, title, possession or lien. Thus, the definition is very wide. It covers not only transfers of ownership but also simple transfer of possession or even lien.

POSER – Status of PIO without OCI Card

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- POSER: Participants are requested to discuss the case of a PIO who has not converted his status to OCI by 30.09.2018 and the implications on different kinds of transactions which have a separate dispensation for OCIs under FEMA
- SOLUTION:
 - If a PIO does not register himself as OCI and take OCI Card, he may not be eligible for any benefits extended to OCIs under FEMA even though he is PIO by birth. The reason is that from 30.09.2018, PIOs were required to compulsorily convert their status to OCI card holders or else they were required to re-apply for OCI card afresh. Some of the transactions which are available only to NRIs/OCIs include no lock-in period for FDI in Construction, opening of NRE / FCNR accounts, immovable property in India, etc. Implications for non-holding of OCI Card will also be discussed in the subsequent Case Study on KYC requirements of NRIs/OCIs under PMLA and under SEBI investment limits.
 - Holding an OCI card means parity with NRI except certain political rights, employment in India, travelling to restricted areas, etc.
 - Conversely, can an unregistered PIO claim that he is a foreign citizen and hence any restriction placed in statute / rules / regulations on PIO will not be applicable to him?

Important Concepts / Schemes under FEMA

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- Dealing in Foreign Exchange – Section 3
- Drawal of Foreign Exchange – Section 4 and 5
- Liberalised Remittance Scheme
- Investment on Repatriation and Non-repatriation basis
- Remittance of Assets by PROI

Important Concepts / Schemes

- Mechanism & Monitoring of Transactions

■ **Sec 3 – Dealing in Foreign Exchange**

Save as otherwise provided in this Act, rules or regulations made thereunder, or with the general or special permission of the Reserve Bank, no person shall—

- (a) deal in or transfer any foreign exchange or foreign security to any person not being an authorised person;
- (b) make any payment to or for the credit of any person resident outside India in any manner;
- (c) receive otherwise through an authorised person, any payment by order or on behalf of any person resident outside India in any manner;

Explanation.—

For the purpose of this clause, where any person in, or resident in, India receives any payment by order or on behalf of any person resident outside India through any other person (including an authorised person) without a corresponding inward remittance from any place outside India, then, such person shall be deemed to have received such payment otherwise than through an authorised person;

Important Concepts / Schemes

- Mechanism & Monitoring of Transactions

- **Sec 3 – Dealing in Foreign Exchange (cont'd)**

- (d) enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person.

Explanation.—

For the purpose of this clause, "financial transaction" means making any payment to, or for the credit of any person, or receiving any payment for, by order or on behalf of any person, or drawing, issuing or negotiating any bill of exchange or promissory note, or transferring any security or acknowledging any debt.

Important Concept / Schemes

- Rule for Drawal of Foreign Exchange – Sec 4 & 5

- Sec 4 - Save as otherwise provided in this Act, no person resident in India shall acquire, hold, own, possess or transfer any foreign exchange, foreign security or any immovable property situated outside India.
- Sec 5 - Any person may sell or draw foreign exchange to or from an authorised person if such sale or drawal is a current account transaction:
Provided that the Central Government may, in public interest and in consultation with the Reserve Bank, impose such reasonable restrictions for current account transactions as may be prescribed

Important Concept / Schemes

- Liberalized Remittance Scheme (LRS)

- Eligible for Individual Resident Indians
- Upto USD 2,50,000 per Financial Year
- For permissible Capital or Current Account Transactions
- Combine limits of family Members
- Reporting

POSER – Change of Purpose for remittances under LRS

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- POSER: In case funds are remitted under LRS from a PRII's account in India in to the personal account of PRII under the purpose code of maintaining relatives abroad, however the funds were not utilised for the same. Can the PRII use the funds for another permitted purpose like purchase of immovable property outside India? Participants may discuss the permissibility and implications of the same including issues with AD-Bank that may arise in case of sale of the aforesaid property during repatriation to India.
- SOLUTION:
 - As per recent amendment dt. 24.08.2022, Investor, who has remitted funds under LRS can retain, reinvest the income earned on the investments. The received / realized / unspent / unused foreign exchange, unless reinvested, shall be repatriated and surrendered to an authorised person within a period of 180 days from the date of such receipt / realization / purchase / acquisition or date of return to India, as the case may be, in accordance with Regulation 7 of FEMA Ntf. 9(R). It may be noted that prior to such amendment, the resident individual was not required to repatriate the funds or income generated out of investments made under the Scheme.
 - Regulation amending the LRS refers to uninvested income to be repatriated within 180 days as provided in Ntf. 9(R), dealing with repatriation of unused/unspent/received/realized foreign exchange within 180 days.
 - Probably purchase/acquisition or date of return appearing in the amendment is picked up from the language of Ntf. 9(R)
 - In view of the above, the amendment can be said to apply only to uninvested income as referred and does not apply to remittance under the LRS

POSER – Change of Purpose for remittances under LRS (cont'd)

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■ SOLUTION:

- Immovable property can always be purchased by a Resident Individual from the overseas banking account
- An intimation that you have done so may be sufficient as remittance can be made for any of the permissible transactions including remittance from bank A/c abroad
- However, in the instant case, the funds are remitted under LRS for maintenance of relatives. The funds are not in the nature of income from investments made out of LRS remittances. Accordingly, even though such funds are not utilized for maintenance of relatives abroad and they represent unspent / unused foreign exchange, in an extremely technical manner, a view may be taken that they need to be surrendered to AD-Bank within 180 days of acquisition.

Emigrating Indian: A Non-Resident (PROI)

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- LRS - Emigrating Indian
 - Remittance of Assets
- Holding permission: Section 4 & 6(5) of FEMA
- A citizen of India leaving India
- Person of Indian origin – An OCI Card holder

Procedure: A Resident becoming Non-Resident

- Scan various Notifications to verify implications on continuing to hold various types of assets and entities in India
- Accordingly, confirm continuing of transaction and holding
- Else, discontinue transaction and exit / re-structure
- Section 6(5) of FEMA provides that a PROI may hold, own, transfer or invest in Indian currency, security or any immovable property situated in India if such currency, security or property was acquired, held or owned by such person when he was resident in India or inherited from a person who was resident in India

Procedure: A Resident becoming Non-Resident - Steps to be taken in respect of Assets / Investments

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Investment – Assets/Activity	FEMA – Provisions – Steps to be taken
1. Bank Accounts, Fixed Deposits with Banks	The emigrating Indian should inform his bank regarding the change in his status as Non-Resident under the FEMA All the above accounts will be designated as Non-Resident Ordinary Account (NRO – A/cs) except the account of Family Trust and Discretionary Trust. Mr. Resident can continue to operate the above accounts, Legitimate dues such as Dividend, interest, sale proceeds of shares, rent etc. receivable in India in rupees, can be credited to the NRO accounts.
2. a) Shares Debentures, Convertible Debentures in Private & Public Limited Companies	Inform the companies concerned about change of status as “PROI” under FEMA PROI can hold Indian security [S.2(za) of FEMA] as provided u/s.6(5) of FEMA
b) Fixed Deposits with Companies	Fixed Deposit with companies is permitted under Reg.6(2) of the Ntf. 5(R) of the FEMA on non-repatriation basis.

Procedure: A Resident becoming Non-Resident

- Steps to be taken in respect of Assets / Investments

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Investment – Assets/Activity	FEMA – Provisions – Steps to be taken
3. Units & Govt. Securities, PPF	No permission is required as securities can be held by PROI as provided u/s. 6(5) of the FEMA. Further, he can continue with the PPF Account as now provided under PPF Act.
4. Holding of Insurance Policies	No permission is required. Allowed to pay the premium on LIC Policies as per Ntf. 12(R) of the FEMA, out of NRE/NRO account of the policy holder
5. Credit Cards	Can continue to hold Domestic Cards and International Credit Cards as well. Pay for Domestic Cards from NRO / NRE accounts. Pay for International Credit Cards from NRE account or from remittance from abroad. Local expenses in rupees can only be debited through International Credit Card.

Procedure: A Resident becoming Non-Resident - Steps to be taken in respect of Assets / Investments

Investment – Assets/Activity	FEMA – Provisions – Steps to be taken
6. Loans given or loans taken	Reg. 8 of Ntf. 3(R) permits continuation of the loans given by resident to another resident, before the lender becomes PROI. In respect of loans taken from Authorised Dealer/bank, the same can continue as provided in Reg. 8 of Ntf. 3(R). Lending by Resident to Non-Resident is generally not allowed to be continued as per the Ntf. 3(R) except allowed specifically and hence emigrating Indian requires RBI approval to continue with loan taken from another Resident.
7. Jewelry	No permission is required for continuing to hold it in India as what is sought to be regulated by FEMA is Securities, Currencies and Immovable Property.
8. Holding of Immovable Properties in India (and not dealing in them)	No permission of RBI is required [Section 6(5) of the FEMA] to continue holding the same.

Procedure: A Resident becoming Non-Resident - Steps to be taken in respect of Business Ventures

Business Venture	FEMA Provisions
1. a) Continuation of proprietary business in India b) As a partner of a firm c) As Co-venturer in Real Estate Development	These are permitted Capital Account Transactions under Schedule IV of Foreign Exchange Management (Non-debt Instruments) Rules, 2019 (“NDI Rules”), therefore Mr. Resident can continue with the Banking A/c and the business.
2. a) Continuing as a Director of a Company b) Continuing as a Member of Association of Persons c) Continuing as a trustee d) Having interest in Trust	No permission of RBI is required as same is not prohibited
3. Partner of a firm dealing in Real Estate	Should retire from the firm as RBI does not allow real estate dealings by Non-Residents including NRIs [NDI Rules]

Procedure: A Resident becoming Non-Resident - Steps to be taken in respect of Business Ventures

Business Venture	FEMA Provisions
4. Real estate development	Activity is permitted by RBI [Notification No. FEMA 1 & NDI Rules]
5. Agricultural activities and holding of Agricultural land and acquiring additional Agricultural land	Agricultural activities are not permitted; however, holding of Agricultural land is permitted including acquiring additional Agricultural land for non-agricultural purposes. Sale of Agricultural land is permitted as per NDI Rules read with Section 6(5) of FEMA.

- POSER: In case entire family is migrating, participants are requested to discuss how they can remit their Wealth from India to settle outside India.
- SOLUTION:
 - Every NRI is permitted to remit up to USD 1 Mn annually from their NRO account. Therefore before emigrating, entire family may ensure that such limit per person is fully utilized so as to remit Foreign Exchange from India as required by them abroad.
 - They can also send funds under LRS in the same year as residents before migrating

Bank Accounts of Non-Resident

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- i. Bank Accounts and Term Deposits [As per Notification 5(R) of the FEMA]
 - a) Non-Resident (External) Rupee (NRE) Accounts (Principal / Interest Repatriable) which may be in the form of Savings Accounts and Term Deposits
 - b) FCNR (B) (Principal/Interest Repatriable)
Deposits of funds in any permitted currency which would mean a foreign currency which is freely convertible as defined in terms of Regulation 2(v) of FEMA 14/2000-RB dated May 3, 2000, as amended from time to time.
 - c) NRO Accounts (Current earnings repatriable)
Repatriation from NRO balances - Authorised Dealers can allow remittance/s up to USD 1 million per financial year (April-March) for bonafide purposes, from balances in NRO accounts subject to payment of applicable taxes. The limit of USD 1 million per financial year includes sale proceeds of immovable properties held by NRIs/PIO.

Investment in India – Entry routes for Non-Resident

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- FDI & Portfolio Investment Scheme – Schedule I & III of NDI Rules
- FPI – Schedule II of NDI Rules
- LLP – Schedule VI of NDI Rules
- Investment Vehicles (MF, AIF, ReIT, InvIT) – Schedule VIII of NDI Rules
- Investment on Non-repatriation basis – Schedule IV of NDI Rules
- Depositary Receipts & Indian Depositary Receipts – Schedule IX & X of NDI Rules
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Immovable Property in India – NDI Rules

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A person resident outside India who is a citizen of India may –

- a) acquire immovable property in India other than an agricultural property, plantation, or a farm house by way of purchase, gift from a relative (PRII, NRI, OCI) or inheritance
- b) transfer any immovable property in India to a person resident in India
- c) transfer any immovable property other than agricultural or plantation property or farm house to an NRI or an OCI
- d) Citizen of selected countries (other than OCI cardholder) prohibited to acquire properties from India
- e) Repatriation of sale proceeds is permitted subject to conditions:
 - ▶ only 2 residential properties
 - ▶ original foreign exchange brought to be repatriated

Immovable Property in India – NDI Rules

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- NRI / OCI – an eligible Investor
- Other eligible Investors
- Prohibitions
- Repatriation
- Method of payment and conditions
- Loans from Bank

FDI in Construction Sector

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- Schedule I & VI of NDI Rules: Through Company and LLP in India
- Schedule IV of NDI Rules: Through Proprietary Concern, Firm, LLP or Company in India on a non-repatriation basis
- Schedule VIII of NDI Rules: Through REITs, InvITs, AIFs in India

FDI in Construction Sector – Permitted activities

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- Residential & Commercial infrastructure, Purchase of Mall & Lease but not in Real Estate sector
- Lock-in for 3 years
- No Lock-in for NRI / OCI
- Real Estate sector is defined

Facts of the Case:

Mr Ramesh a Non-resident of India and a PIO is very actively considering to return to India for good after attending the last annual NRI conference organised by GOI every year in January, 2022. He is engaged in USA, in various real estate related projects namely construction of apartments, large commercial infra-mall structure and portfolio investment funds representing property investments. He is contemplating having a similar business in India and desires to purchase two residential houses for his own use and his Iranian daughter's use, married to PIO since last one year. He has also been in touch with Indian banks for the purpose of leveraging his properties including purchase of residential houses if such houses are purchased in the company's name. Since he wants to explore India for good he is not worried about whether investment is done on repatriation or non-repatriation basis, however he has not closed any of his businesses in USA and within commercial reality if the Indian investment can be held on repatriation basis then that will be a preferred option.

Question

Mr Ramesh has approached the participants of CTC Residential Refresher Conference to resolve the following questions:

The entity structure and related procedure involved in:

- a. Carrying out the business of large commercial mall infrastructure, its acquisition and earning long term lease revenues.
- b. A small construction project involving an investment of USD 500,000 with his close friend in India to develop a residential apartment building to be completed within a period of 2 years in all its respect.
- c. Consolidating purchase of residential units in a potentially viable redevelopment project for construction
- d. Purchase of 2 residential houses as mentioned above in Company's name with leverage
- e. To participate into a large portfolio of properties to de-risk and mutualise the yield to be managed by the professional managers

FDI In Real Estate Projects

Under the NDI Rules, PROs are permitted to acquire immovable property in India under two methods (i) as FDI under the sectoral policy under Schedule I of the NDI Rules and (ii) acquisition and transfer of immovable property under Rules 24 to 33 of the NDI Rules.

While focussing on FDI for real estate projects, this Case Study also aims to bring out the nuances and differences

- (a) between acquisition of immovable property for business purposes under FDI and for personal purposes under Rules 24 to 33 of the NDI Rules,
- (b) as to how it may be viewed when investment is predominantly in immovable properties, through a company in service sector
- (c) when investment is made for Business purposes on a non-repatriation basis,
- (d) how NRI / OCI are treated favourably in Housing Construction related activities in India,
- (e) when investment is contemplated in Property bank to avoid the larger risk associated with the single property

FDI In Real Estate Projects – Overview of Legal provisions

Schedule I of NDI Rules - Sectoral Policy for Construction Development: PROIs including NRIs/OCIs are permitted to hold 100% shareholding under the Automatic route for Construction-development projects (which includes development of townships, construction of residential/ commercial premises, roads or bridges, hotels, resorts, hospitals, educational institutions, recreational facilities, city and regional level infrastructure, townships).

The PROI is subject to a lock-in period of three years calculated with reference to each tranche of foreign investment except in case of transfer to another PROI. However, condition of lock-in period shall not apply to investment by NRIs / OCIs in Hotels and Tourist Resorts, Hospitals, Special Economic Zones (SEZs), Educational Institutions, Old Age Homes.

Schedule IV of NDI Rules – Investment on non-repatriation basis: NRIs / OCIs including a company, a trust and a partnership firm incorporated outside India and owned and controlled by NRIs or OCIs, can invest in equity instruments / capital of LLP which may undertake any bonafide business in India which will be deemed to be domestic investment at par with the investment made by residents.

Rules 24 to 31 of NDI Rules: Investment by individual NRI/OCI in Residential and Commercial properties for bonafide Personal use

CASE STUDY - 2

Overview of Legal Provisions:

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1. Further as per Chapter IX of Foreign Exchange Management (Non-debt Instruments) Rules, 2019

An NRI or an OCI may –

a) acquire immovable property in India other than an agricultural property, plantation, or a farm house: Provided that in case of acquisition of immovable property, payment of purchase price, if any, shall be made out of (i) funds received in India through normal banking channels by way of inward remittance from any place outside India or (ii) funds held in any non-resident account maintained in accordance with the provisions of the Act, rules or regulations framed thereunder:

Provided further that no payment of purchase price for acquisition of immovable property shall be made either by traveller's cheque or by foreign currency notes or by other mode other than those specifically permitted by this clause'.

b) transfer any immovable property in India to a person resident in India.

c) transfer any immovable property other than agricultural or plantation property or farm house to an NRI or an OCI.

Provided that no person who is citizen of Pakistan or Bangladesh or Sri Lanka or Afghanistan or China or Iran or Hong Kong or Macau or Nepal or Bhutan or Democratic People's Republic of Korea (DPRK) shall acquire immovable property, other than on lease not exceeding five years, without prior approval of the Reserve Bank.

CASE STUDY - 2 - SOLUTION

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- i. Carrying out the business of large commercial mall infrastructure, its acquisition and earning long term lease revenues – 100% FDI is permitted. Foreign investment up to 100 percent under automatic route is permitted in completed projects for operating and managing townships, malls/ shopping complexes and business centres. The ownership of the Investee Company will be transferred from PRII to Mr. Ramesh who is NRI. Further, lock in period of 3 years which is applicable for each tranche in case of PROI will not be applicable in case of Mr. Ramesh as he is NRI.

But it should be noted that if Mr. Ramesh is not an NRI and he does not register himself as OCI and take OCI Card, he may not be eligible for any benefits extended to OCIs under FEMA even though he is PIO by birth. The reason is that from 30.09.2018, PIOs were required to compulsorily convert their status to OCI card holders or else they were required to re-apply for OCI card afresh.

- ii. A small construction project involving an investment of USD 500,000 with his close friend in India to develop a residential apartment building to be completed within a period of 2 years in all its respect – Mr. Ramesh can undertake FDI in the company in India undertaking the construction activity. Also, since he is NRI, no lock in of 3 years required
- iii. Consolidating purchase of residential units in a potentially viable redevelopment project for construction – Permitted, since the motive of the purchase of the residential home after undertaking redevelopment of the project will not fall under the definition of real estate business under NDI rules as he is not purchasing the residential units with the intention of earning profits out of sale of the units. He has not sold it after buying but shall redevelop the property in future.

- iv. Purchase of 2 residential houses as mentioned above – Mr Ramesh can purchase both the properties. Since the 2nd property is purchased only for the use by the Iranian daughter and the daughter is not the owner (assuming Ramesh is the owner), it is permitted under NDI Rules. A citizen of Iran is prohibited from acquiring immovable property in India (other than lease not exceeding 5 years) without prior RBI approval. However, this prohibition does not apply to an OCI; hence the Iranian daughter may register as OCI Card holder and acquire the property. Since the properties are purchased for bonafide use, only individual NRI/PIO can acquire and company owned by Mr. Patel cannot acquire the property with leverage
- v. To participate into a large portfolio of properties to de-risk and mutualise the yield to be managed by the professional managers – Investment in REITs is not construed as real estate business and hence 100% FDI is permitted under Schedule VIII of the NDI Rules. NRIs looking to take exposure to the real estate sector can invest in REITs as it offers part ownership of a rent-yielding quality commercial property. Being listed, there is easy liquidity, no commitment of minimum investment amount or tenure. REITs are mandated to pay 90% of their income to investors via dividends which acts as a stable income for NRIs.

POSER – NRI/OCI acquiring Property from another NRI/OCI

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- POSER: Can an NRI/OCI acquire property in India from another NRI/OCI by directly remitting funds from his foreign bank account to the seller NRI's foreign bank account? Participants may discuss if such transaction is permitted and its implications.
- Lead: As per Rule 24 of NDI Rules, An NRI/ OCI may acquire immovable property in India other than an agricultural land or farm house or plantation property: Provided that the consideration, if any, for transfer, shall be made out of :
 - (i) funds received in India through banking channels by way of inward remittance from any place outside India ; or
 - (ii) funds held in any non-resident account maintained in accordance with the provisions of the Act, rules or regulations framed thereunder:

Provided further that no payment for any transfer of immovable property shall be made either by traveler's cheque or by foreign currency notes or by any other mode other than those specifically permitted under this clause;

- SOLUTION:
 - One may err in taking the view that the above is permissible as clause (e) of Rule 24 of NDI Rules permits an NRI/OCI to transfer any immovable property other than agricultural land or farm house or plantation property to an NRI or an OCI. However, Section 3(b) of FEMA prohibits a person from making any payment to or for the credit of any person resident outside India in any manner. As the immovable property is situated in India and any dealing in such property is covered under the ambit of FEMA rules / regulations, any payment for the same would have to be effected in accordance with the rules. Hence, payment for the same will have to be made out of funds received in India or funds held in India as discussed above in the Poser.

POSER – Interplay of Section 6(5) and NDI Rules

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- POSER: Rules 24 to 33 of NDI Rules permit acquisition of immovable property in India by PROIs. Further Section 6(5) of FEMA permits PROIs to acquire, hold, etc. immovable property in India when resident in India or inherited from a person who was resident in India. Participants are requested to discuss the inter-play and nuances that arise in such situations as to what happens if inheritance is from a non-resident
- SOLUTION:
 - As discussed in an earlier Poser, Section 6(5) permits inheritance by a PROI of assets located in India from the deceased PRII. So far as inheritance of Indian immovable property from PROI is concerned, Rule 24(c)(i) of NDI Rules permits a NRI / OCI to acquire immovable property in India by way of inheritance from a PROI who has acquired such property as per the foreign exchange provisions in force at the time of such acquisition.
 - It may be noted that Section 6(5) refers to two modes of acquiring immovable property in India – (i) by purchase when resident in India, and (ii) by inheritance from a person who was resident in India. As against this, the NDI Rules primarily covers acquisition, mode of payment, etc. by way of purchase by a PROI

POSER – Section 6(5) assets in India

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- POSER: In case of inheritance by a PROI from a person who was resident in India, the apparent meaning is that the deceased should be resident at time of death. But in case the deceased is non-resident at the time of death, what happens to such inheritance of assets situated in India?
- SOLUTION:
 - This situation is the reverse of the earlier Poser. Section 6(5) permits inheritance by a PROI of assets located in India from the deceased PRII.
 - So far as inheritance of Indian immovable property from PROI is concerned, Rule 24(c)(i) of NDI Rules permits a NRI / OCI to acquire immovable property in India by way of inheritance from a PROI who has acquired such property as per the foreign exchange provisions in force at the time of such acquisition.
 - However, so far as securities in India are concerned, there is no general permission under the NDI Rules for inheritance by a PROI from another PROI even though such deceased PROI had acquired the securities in accordance with the provisions of FEMA. It may be noted that Rule 9(1) of NDI Rules permits a PROI, not being NRI / OCI to gift equity instruments / units to another PROI. Further, Rule 13(1) of NDI Rules permits NRI / OCI to gift equity instruments / units to a PROI.

Portfolio Investment – Schedule II & III of NDI Rules

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- Provisions of Schedule II & III of NDI Rules
- SEBI guidelines
- Beneficial Owner ('BO') of FPI in India
- Investor Group
- Clubbing of FPI's limit
- SEBI Circular on KYC and Khan Committee Report – Materiality Threshold
- Identification of BO only for KYC and not for Clubbing

CASE STUDY - 3 - PMLA KYC and holding of shares by NRIs/OCIs through FPIs

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Facts:

XYZ Pte. Ltd., a company incorporated under the laws of Singapore and beneficially owned by NRIs, has made certain investments in funds in Bermuda which in turn have invested in units in various Mauritius fund structures which are independently managed / controlled by different Investment Managers. These Mauritius funds are registered as FPIs in India and have accordingly invested in Indian listed shares which is individually below the maximum limit permissible for FPIs in any listed company. However, it is possible that these different funds may have invested in the shares of the same Indian listed company.

It may be noted that in terms of NDI Rules, investment in shares of an Indian company cannot exceed 10% in case of FPI (i.e. either singly by FPI or by the FPI investor group if any) and 5% in case of NRI as stipulated in Schedule II and III of the NDI Rules respectively. The total holdings of all FPIs put together, including any other direct and indirect foreign investments in the Indian company permitted under these rules, shall not exceed 24 per cent of paid-up equity capital.

SEBI issued a Circular dt. 10.04.2018 regarding changes to KYC requirements of FPIs whereby it required identification and verification of Beneficial Owners ('BOs') in accordance with Rule 9 of the Prevention of Money-laundering (Maintenance of Records) Rules, 2005 (hereinafter referred as PMLA Rules – attached as Annexure 4).

Accordingly, the materiality threshold for identification of BOs of FPIs on controlling ownership interest (or ownership/ entitlement) basis shall be same as prescribed in PMLA Rules i.e. 25% in case of company and 15% in case of partnership firm, trust & unincorporated association of persons.

Prior to the aforesaid SEBI Circular, clubbing of investment limit for FPIs was on the basis of common ownership or control of more than 50 percent, as mentioned in Operational Guidelines for Designated Depository Participants i.e. these common control or ownership were to be determined at level 1 who have contributed to the corpus of the FPI. Post SEBI Circular, this effectively meant that the current clubbing provisions will also be applicable where BOs are identified on the basis of control.

CASE STUDY -3 (cont'd)

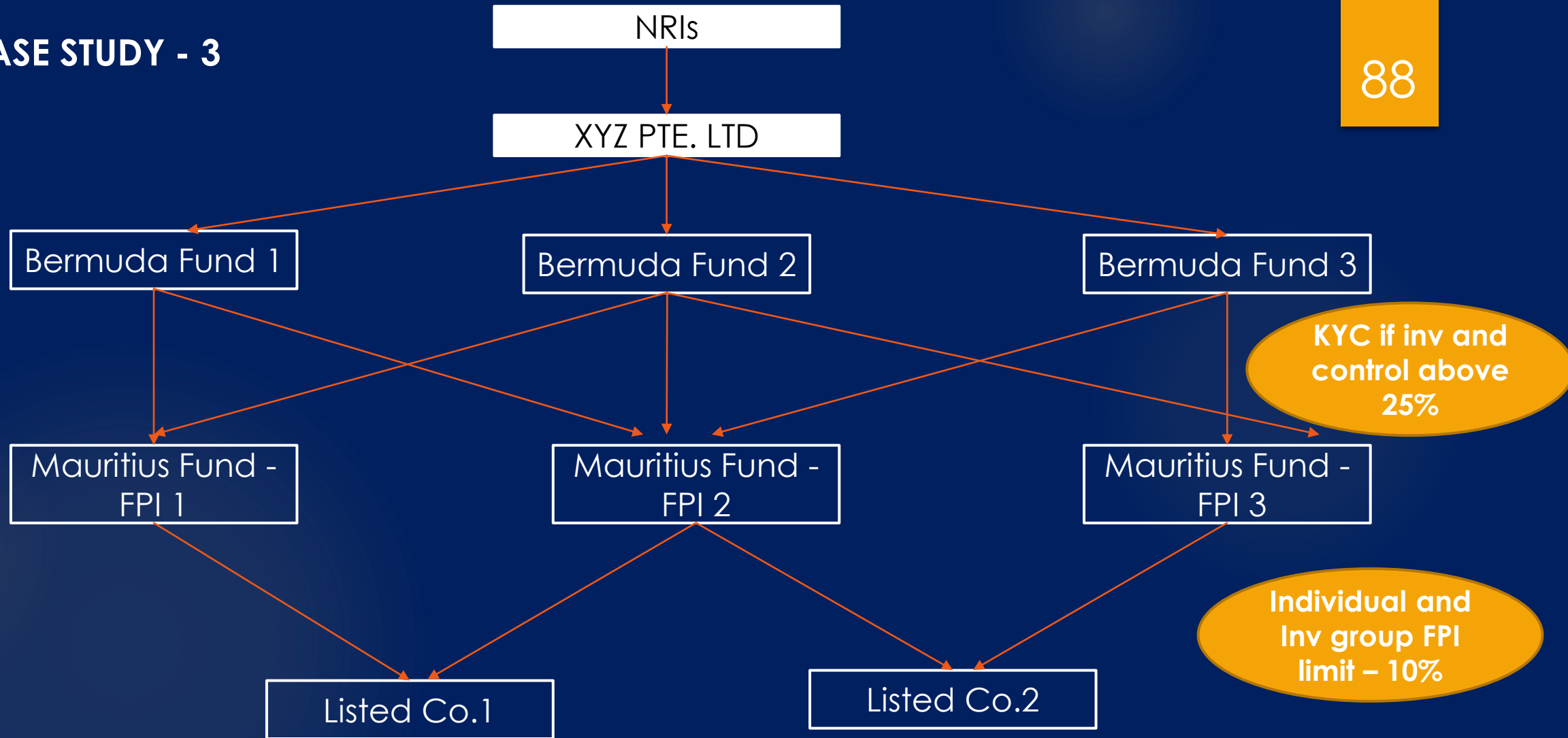
The aforesaid materiality threshold to identify the beneficial owner should be first applied at the level of FPI and next look through principle shall be applied to identify the beneficial owner of the material shareholder/ owner entity i.e. at FPI level if owner is company or trust then BO should be identified if such Company or Trust owns more than 25% or 15% respectively. Only beneficial owner with holdings equal & above the materiality thresholds in the FPI need to be identified through the aforesaid look through principle.

In view of the above changes to KYC requirements, participants are required to discuss whether the above structure of XYZ Pte. Ltd. complies with the NDI Rules read with revised SEBI KYC requirements based on PMLA Rules.

It may be noted that by a subsequent Circular dt. 13.12.2018, SEBI decided that BO criteria in PMLA Rules, 2005 should be made applicable for the purpose of KYC only and not for clubbing of investments of FPIs. Accordingly, so far as clubbing of investment limits for FPIs is concerned, it will be on the basis of common ownership of more than 50% of the corpus or based on common control.

CASE STUDY - 3

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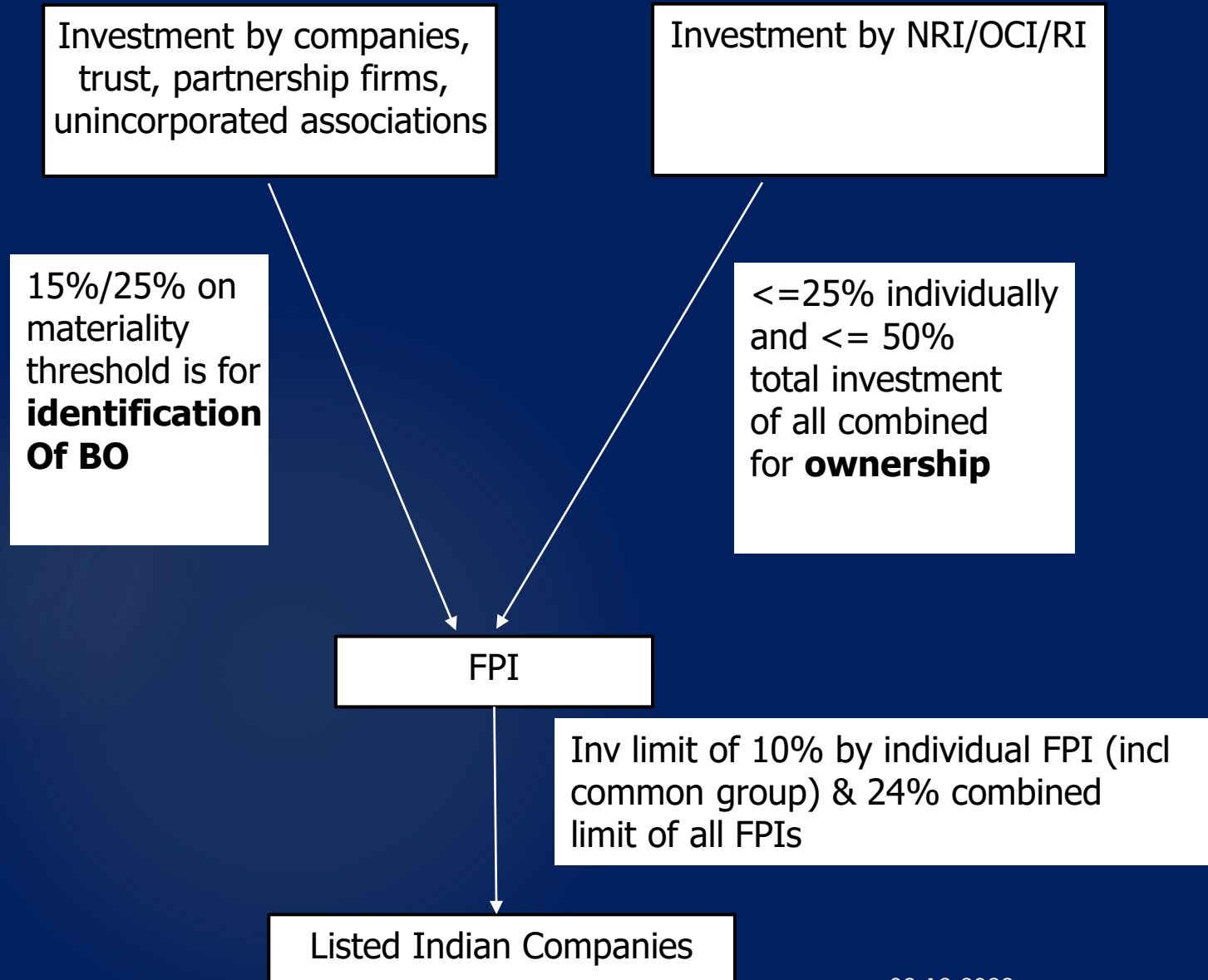


FPIs managed by different independent IMs

- FPIs with Group investment $\leq 10\%$
- All Independent FPI combined $\leq 24\%$

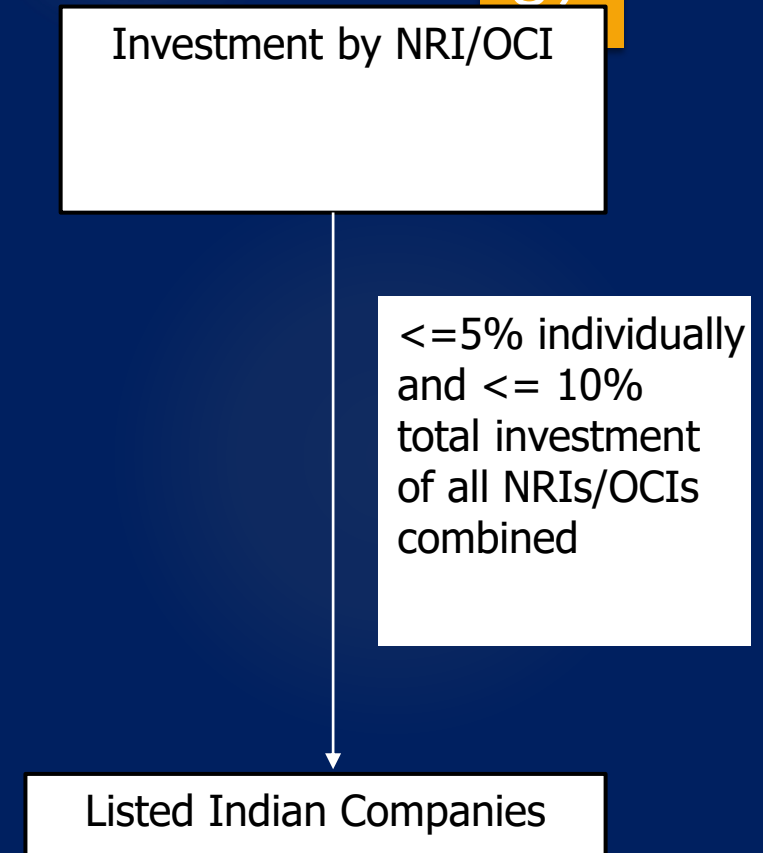
- Individual NRI $\leq 5\%$
- All NRIs combined $\leq 10\%$

Ceilings - FPI and NRI



02-12-2022

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The issues that need careful consideration are the following:

- i. Limits specified in NDI Rules relating to maximum shareholding by FPIs and by NRIs/OCIs in Indian listed co.
- ii. KYC requirements of PMLA Rules relating to identification of UBOs keeping in view the materiality tests of 25% in case of corporate shareholder and 15% in case of others such as Partnership Firm, Trust & unincorporated Association of Persons
- iii. FPI Regulations of SEBI relating to clubbing of investment limit of FPIs having common ownership of more than 50% of corpus of the FPI or based on common control of the FPI where more than one FPI is controlled by a common Investment Manager
- iv. Effect and implication of SEBI Circular dt. 10.04.2018 for implementing KYC norms as modified by its subsequent Circular dt. 13.12.2018
- v. In the instant case, whether, on a co-joint reading of all of the above applicable provisions, there is an actual breach of the maximum shareholding that can be held by FPI and NRIs/OCIs in the listed Indian company, by way of an opaque multi-level structure (i) which does not fall within the 25% / 15% materiality limits (thereby not necessitating disclosure of the UBO being NRI/OCI) (ii) which does not violate the 25% / 50% SEBI norms for contribution by NRIs/OCIs in an FPI, and (iii) yet be appointed as Investment Manager by way of non-investing FPI which is permitted to have control of FPI?

i. Historical Background of SEBI provisions

SEBI (Foreign Portfolio Investors) Regulations, 2014 (“FPI Regulations”) were notified in the year 2014 vide notification dated 07.01.2014. In order to review the same and the issues arising out of the SEBI Circular dated 10.04.2018 on KYC requirements for FPIs which had generated widespread discussions and debate, a SEBI Working Group (“Group”) on Re-drafting of FPI Regulations under the chairmanship of Shri H R Khan was formed by SEBI in March 2018.

The Group gave interim recommendations with regard to the April 10 Circular under four sections relating to:

- A. Non-Resident Indians (NRIs)/ Overseas Citizens of India (OCIs)/ Resident Indians (RIs)
- B. Clubbing of Investment limit of FPIs
- C. Identification and verification of Beneficial Owners
- D. Other aspects

A. NRIs/OCIs/RIs

Regime prior to the April 10 Circular: Entities owned by NRIs/ RIs could be registered as non-investing FPIs for the purpose of acting as an investment manager for other FPIs (i.e. investing FPIs).

Condition imposed by the April 10 circular: The April 10 circular clarifies that NRIs, OCIs and RIs cannot be beneficial owners (BOs) of investing FPIs. Since NRIs and RIs are prohibited from becoming FPIs in accordance with Regulations 4(a) and 4(e) of the SEBI FPI Regulations, the same should also not be permitted indirectly by becoming BOs of FPIs.

Recommendation of the Group: The Govt. had communicated to SEBI that the principle laid down in Rule 9(3) of the PMLA Rules 2005 is for the purpose of customer due diligence and need not apply mutatis mutandis to determine the eligibility for of foreign investors as FPIs.

The Group therefore recommended that the BO criteria under PMLA may be made applicable only for the purpose of KYC and not as eligibility criteria for FPIs, including those having NRIs/OCIs/ RIs as their constituents. Accordingly, the Group considered separate set of norms for determining the eligibility conditions where NRIs/OCIs/RIs are constituents of FPIs as under:

- i. Single NRI/ OCI/ RI holding is below 25% of the Assets Under Management (AUM) in the FPI
- ii. Aggregate NRI/ OCI/ RI holdings is below 50% of AUM in the FPI
- iii. NRI/ OCI/ RI should not be in Control of an FPI.
- iv. However, there should be no restriction on NRIs / OCIs / RIs investment managers to be in control of the FPI provided any of the following conditions is satisfied:
 - a) The investment manager entity of the FPI is appropriately regulated in its home jurisdiction and registers itself with SEBI as a non-investing FPI, or
 - b) The investment manager is incorporated or setup under Indian laws and appropriately registered with SEBI, or
 - c) Where such FPIs are 'offshore funds' as approved by SEBI

B. Clubbing of investment limit of FPIs having common ownership or control

Regime prior to the April 10 Circular: Clubbing of investment limit for FPIs was on the basis of common ownership or control of more than 50 percent, as mentioned in Operational Guidelines for Designated Depository Participants.

Condition imposed by the April 10 circular: As per April 10 circular, clubbing of investment limit for FPIs is on the basis of Beneficial Ownership (as per PMLA Rules) of FPIs. This effectively means that the current clubbing provisions will also be applicable where BOs are identified on the basis of Control.

Recommendation of the Group: As mentioned above, the BO criteria under PMLA may be made applicable only for the purpose of KYC and not for clubbing of investment limits.

Accordingly, Clubbing of investment limit for FPIs may be on the basis of common ownership i.e. all entities having direct or indirect common shareholding / beneficial interest, of more than 50% OR based on common control.

However, Clubbing of investment limit of FPIs having common control may not be applicable in any of the following cases where:

- (i) FPIs are appropriately regulated public retail funds or
- (ii) FPIs are appropriately regulated public retail funds majority owned by public retail fund on look through basis or
- (iii) FPIs are public retail funds and investment managers (IMs) of such FPIs are appropriately regulated.

In case the investment by the Individual Bermuda funds is less than 25%/15% in Mauritius Fund

i. KYC requirements under PMLA

- The materiality threshold is 1st required to be applied at the FPI level i.e. Mauritius Fund level.
- If investment by the individual Bermuda fund structure in a single FPI is less than the threshold limit of 25% /15% then there is no need for further KYC of the investors in the FPI.

ii. Investment limit compliance as per NDI rules

- The FPIs are controlled by different independent managers, therefore there is no common control. If there is common ownership of more than 50% of the corpus of the FPI, then clubbing of the investment limit for FPIs will be applicable for determining the investment limit of 10% in listed companies by FPIs.

In case the investment by the Individual Bermuda funds is more than 25/15% in Mauritius Fund

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i. KYC requirements under PMLA

- The materiality threshold is 1st required to be applied at the FPI level. If investment by the individual Bermuda Fund structures in a single FPI is more than the threshold limit, KYC requirement of BO of Bermuda Fund will be required.
- Since XYZ Pte Ltd. holds 100% of Bermuda Funds, it will be identified as the BO of the Bermuda Funds as it holding in Bermuda Funds exceeds the materiality threshold of 25%
- The final level BO's shall be the natural persons who are NRIs holding more than 25% shares of XYZ Pte Ltd.
- Thus, on doing the KYC if it is realised that the NRIs due to the indirect route have invested more than the permissible limit of 5% in listed companies and have exceeded the NRI investment limit in the FPI of 25% of the AUM by a single NRI, the structure will be non-compliant under PMLA Rules as well as SEBI regulations for investment by FPIs & NRIs in Indian listed shares, unless the PIO is not an OCI card holder
- Although the FPIs are controlled by different independent managers (i.e. there is no common control and / or ownership >50% not triggering clubbing of the investment limit for FPIs), the structure would not be SEBI compliant if clubbing provisions are applied to the BOs identified as per PMLA Rules as sought by SEBI's earlier Circular of 10.04.2018 before it issued subsequent Circular dt. 13.12.2018.
- As per Circular dt. 13.12.2018, SEBI decided that BO criteria in PMLA Rules, 2005 should be made applicable for the purpose of KYC only and not for clubbing of investments of FPIs. Accordingly, so far as clubbing of investment limits for FPIs is concerned, it will be on the basis of common ownership of more than 50% or based on common control of the FPI and not of the intermediate BOs and / or ultimate BOs who are natural persons.

Returning Indian

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- Holding approval for Assets outside India
- Repatriation of Foreign Exchange & Currency
- RFC Bank Accounts
- Declaration on Import of Currencies
- Surrender of Currencies to AD-Bank

Returning Indian

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- General Rule
- Exception under Section 6(4)
- Repatriation, Realisation & Surrender of Foreign Currency – Section 8 & Ntf. 9(R)
- Exemption from Repatriation, Realisation & Surrender of Foreign Currency – Section 9 & Ntf. 11(R)

Returning Indian

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- Section 6(4) – An Exception to Realisation, Repatriation and Surrender
 - Section 6(4) of FEMA: A person resident in India may hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India
- A.P. (DIR Series) Circular No. 90 dated 9-1-2014 clarifies that Section 6(4) covers the following transactions:
 - i. Foreign currency accounts opened and maintained by such a person when he was resident outside India;
 - ii. Income earned through employment or business or vocation outside India taken up or commenced while such person was resident outside India, or from investments made while such person was resident outside India, or from gift or inheritance received while such a person was resident outside India;
 - iii. Foreign exchange including any income arising therefrom, and conversion or replacement or accrual to the same, held outside India by a person resident in India acquired by way of inheritance from a person resident outside India.
 - iv. A person resident in India may freely utilise all their eligible assets abroad as well as income on such assets or sale proceeds thereof received after their return to India for making any payments or to make any fresh investments abroad without approval of Reserve Bank, provided the cost of such investments and/ or any subsequent payments received therefor are met exclusively out of funds forming part of eligible assets held by them and the transaction is not in contravention to extant FEMA provisions.

POSER – Section 6(4) assets outside India

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- POSER: Section 6(4) permits PRII to hold assets outside India which were acquired by him when he was PROI. It further provides that in case of inheritance from a person who was resident outside India, the deceased donor should have been non-resident at the time of death. But in a case where deceased donor is resident at the time of death, what happens to inheritance of such assets acquired outside India during the period the deceased was non-resident?
- SOLUTION:
 - Generally, Gift / Inheritance of an asset outside India from a PROI to PRII is freely permitted under Section 6(4).
 - So far as inheritance of foreign immovable property from PRII is concerned, Rule 21 (2)(i) of ODI Rules permits a PRII to acquire immovable property outside India by way of inheritance or gift or purchase from a PRII who has acquired such property as per the foreign exchange provisions in force at the time of such acquisition.
 - Similarly, Para 2(1) of Sch. III of ODI Rules permits PRII, without any limit, to acquire foreign securities by way of inheritance from a PRII who is holding such securities in accordance with the provisions of the Act or from a PROI.
 - In the aforesaid situations, if the deceased PRII had acquired the foreign securities / immovable property when he was PROI (or by way of inheritance in accordance with FEMA), then on his demise while resident, the inheritance to his PRII-heirs will be in order.

Repatriation of Section 6(4) assets to India

- Mr. 'A' and Mr. 'B' who are brothers were born in Kenya, Africa. Their grand-father, father and uncle (all now deceased) had migrated to Africa since 1920s and had set up various businesses in various parts of Africa including Uganda, Kenya, Tanzania and Nigeria and had also expanded the businesses in South East Asia, Middle East, Afghanistan, Kazakhstan, etc. These businesses comprised of diverse areas including trading in natural resources, manufacturing of various hardware products, chemicals, resins and polymers, etc. In 1975, the family set up a company in India and ventured into India in manufacture of plastic products which was listed in late 80s.
- Since completion of their education in 1970s and 1980s, both the brothers have been engaged in managing the various businesses and assets of the family.
- Due to political turmoil in Africa, both brothers sought citizenship of UK and obtained British passport in 1980. Most of the Indian business community in Africa followed a practice of keeping the asset base to as low as possible in Africa, while continuing to carry on the business there keeping low value-added job function in Africa. The profits in Africa were generally kept to a level of not more than required and most of the profits were attributed to entities outside Africa through effective transfer pricing acceptable in Africa. Further, all investments were held through the trusts set up and investment companies incorporated outside Africa.
- From FY 2002-2003 onwards, both the brothers started spending more time in India as the business in India demanded more attention primarily due to the expansion. Accordingly, they became residents under FEMA and under the Income-Tax Act, 1961.

Repatriation of Section 6(4) assets to India

- During the period that they were resident in India, they continued to hold personal joint bank accounts that were opened outside India prior to their becoming resident in India in which both of them held 1/2 ownership rights & interests. Income generated from their aforesaid African territories was deposited in such joint bank accounts held abroad which are permissible to be held under section 6(4) of FEMA even after becoming residents in India under FEMA;
- Further, the proceeds of whatever disinvestments of their foreign assets that were made were deposited in the said joint foreign bank accounts abroad. None of these foreign investments were made from India but were made only from foreign resources available to them prior to their returning to India.
- As they are Residents in India, they have disclosed the joint foreign bank accounts and other assets in their Indian tax return. Moreover, the deposits into their personal joint bank accounts have been accepted by the tax authority in India as income earned outside India and taxes have been paid on such deposits as applicable Indian taxes. Further, the said deposits are retained abroad as permissible under FEMA.

Issues for discussion under FEMA:

As the deposits were received in their personal joint bank accounts, can it be said that such deposits are in the nature of personal income from business conducted from India while they are resident? If yes, what are the implications under FEMA especially considering provisions of Section 8 and FEMA Ntf. 23(R) - Exports of goods and Services

Would it have made a difference if the foreign sources of income were in corporate form instead of being received in personal bank accounts?

Overview of Legal Provisions

- i. Section 8 Realisation and repatriation of foreign exchange.—Save as otherwise provided in this Act, where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realise and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank
- ii. Notification 23(R) – Timeline for realization of export proceeds is 9 months from the date of providing the service or export of goods.
- iii. Circular 90
 - As per the circular A.P. (DIR Series) Circular No. 90 issued by RBI, it is clarified that Section 6(4) includes the following transaction:
 - Income earned through employment or business or vocation outside India taken up or commenced while such person was resident outside India, or from investments made while such person was resident outside India, or from gift or inheritance received while such a person was resident outside India
 - The income earned by A and B was income generated via business which was commenced before they become residents in India

Section 6(4) states that a PRTI can only hold, own, transfer or invest in foreign currency, foreign security or any immovable property situated outside India if such currency, security or property was acquired, held or owned by such person when he was resident outside India or inherited from a person who was resident outside India.

By plain reading of the above provision, one may conclude that it refers only to foreign assets in the nature of (i) currency, (ii) security, and (iii) immovable property. However, RBI clarified vide Cir. No. 90 that Section 6(4) includes income earned through employment or business or vocation outside India taken up or commenced while such person was resident outside India.

The income earned by A and B was income generated via business which was commenced before they become residents in India. One may therefore take a valid stand that since the income generated by A and B is from a business already commenced when non-resident, the income is not required to get repatriated as it falls under provisions of section 6(4) r.w. Circular 90.

But in case A and B are unable to substantiate the above facts by way of adequate documentation about the business having been commenced by them while non-resident as well as the nature of current income being received from the conduct of such old business, they may find it difficult to make a case with the regulators in India. In such a situation, as the income has been received by them in their personal bank accounts, the income may be determined as one from export of services rendered from India keeping in view that they are now resident in India. Accordingly, A and B are required to repatriate the income received in their foreign personal bank account as required by Section 8 of FEMA and Sec 7 read with Notification 23(R).

If the said foreign business was instead in a corporate form, then such income would have been received in the bank account of the company which was set up by A and B when they were non-resident. As permitted under Section 6(4) r.w. Circular 90, repatriation of such income to India is not required and there may not have been any doubts or debate on the issue.

Similarly, if the said foreign business was in a corporate form and A & B receive remuneration and / or dividend from the foreign company, there would have been no debate over repatriation of the same as it is not mandatory due to operation of Section 6(4) r.w. Circular 90

Foreign Exchange – Realisation, Repatriation, Surrender & Exemption

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FEMA Ntf. (9R) [Ref. Sec. 8]

Realisation, repatriation and surrender of foreign exchange

Regn. 5: In case of Person not being Resident Individual -

- (1) Sell to AD realized foreign exchange due or accrued as remuneration for services rendered, whether in or outside India, or in settlement of any lawful obligation, or an income on assets held outside India, or as inheritance, settlement or gift, within 7 days from the date of its receipt;
- (2) in all other cases within a 90 days from the date of its receipt.

FEMA Ntf. 11(R) [Ref. Sec. 9]

Possession and Retention of Foreign Currency

Regn. 3: For the purpose of Section 9 clause (a) and clause (e), the following limits are specified for possession or retention of foreign currency or foreign coins:-

- i) Possession without limit of foreign currency and coins by an authorised person within the scope of his authority;
- ii) Possession without limit of foreign coins by any person;
- iii) Retention by a PRIL of foreign currency notes, bank notes and travellers' cheques upto US\$ 2000 or its equivalent in aggregate, provided that such FE -
(a) was acquired by him while on a visit to any place outside India by way of payment for services not arising from any business in or anything done in India; or

Foreign Exchange – Realisation, Repatriation, Surrender & Exemption (cont'd)

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FEMA Ntf. (9R)

Realisation, repatriation and surrender of foreign exchange

Regn. 6: In case of Person not being Resident Individual –
(1) Unspent or unused FE purchased / acquired for any purpose as per declaration to be surrendered within 60 days of purchase / acquisition by him.

(2) However, if above FE is for foreign travel, unspent FE to be surrendered within 90 days of return to India if in form of notes & coins and within 180 days if in form of Travellers cheques.

Regn. 7: In case of Person being Resident Individual -

Surrender the received/realised/unspent/unused foreign exchange whether in the form of currency notes, coins and travellers cheques, etc. to an authorised person within 180 days from the date of such receipt / realization / purchase / acquisition or date of his return to India, as the case may be

FEMA Ntf. 11(R) [Ref. Sec. 9]

Possession and Retention of Foreign Currency

(b) was acquired by him, from any person not resident in India and who is on a visit to India, as honorarium or gift

or for services rendered or in settlement of any lawful obligation; or

(c) was acquired by him by way of honorarium or gift while on a visit to any place outside India; or

(d) represents unspent amount of foreign exchange acquired by him from an authorised person for travel abroad.

POSER – Repatriation of Income, Salary, etc.

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- POSER: Participants are requested to discuss the implications under Sections 4, 6(4), 8 and 9 of FEMA with respect to:
 - i. Repatriation of Income of Business commenced outside India in the form of (a) Private limited company, (b) Partnership Firm, and (c) Proprietary concern
 - ii. Repatriation of Salary from foreign business, honorarium, Gift, etc
 - iii. Retention of maximum assets abroad by availing of benefits of Section 6(4)

- SOLUTION:

- i. Since the business was commenced before the person became a resident in India, the income generated will be considered as income from a Section 6(4) asset and repatriation of such income is not required as provided by Circular 90 dt. 09.01.2014. The form of the business does not matter
- ii. If the employment was commenced before he became a PRII, no repatriation is required as permitted under said Circular 90 r.w. Section 6(4). Further, even though the person is now rendering services from India, so long as the employment was commenced before becoming PRII, no repatriation is required. Money received in the form of currency notes as Gift or Honorarium is required to be surrendered with the Authorised person within 180 days except that the person can only retain USD 2,000 as stipulated in Notification 11(R) r.w. Section 9(e)

However it may be noted that Gift and Honorarium can be deposited in RFC Domestic Account in Foreign Currency.

Repatriation and deposit of Foreign Currency

Mr. Returning Indian, a PRII has a proprietary business in India. He has the following transactions involving foreign exchange for which he has approached participants of CTC RRC to understand the implications under FEMA:

- a. Exports from India with outstanding export proceeds
- b. Remuneration earned by him from Company outside India from continuous employment taken up while he was PROI
- c. Honorarium / Gift received in the form of valuable mementos by him from Charitable organisation abroad while on visit
- d. Foreign currency purchased from India for visits abroad
- e. Unspent foreign currency on hand from earlier purchases as well as withdrawn from RFC A/c.

CASE STUDY - 5

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Leads to be considered

Leads relating to the 5 sub-questions (a) to (e) to the Case Study as under:

- a) deals with export proceeds which is dealt in FEMA **Nff. 23(R)**
- b) remuneration is covered under **Section 6(4)** of the Act
- c) honorarium, etc is included at Section 9 read with FEMA **Nff. 11(R)**
- d) foreign currency purchased from India and its repatriation is covered under **Section 8** read with FEMA **Nff. 9(R)**
- e) unspent currency not exceeding US\$ 2,000 is provided in FEMA **Nff. 11(R)** and withdrawal from RFC A/c. is provided in FEMA **Nff. 10(R)**
- f) Permitted credits in **RFC (Domestic) Account**

1. **Section 8 of FEMA** - Realisation and repatriation of foreign exchange.—Save as otherwise provided in this Act, where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realise and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank.
2. **Section 9 of FEMA** - Exemption from realisation and repatriation in certain cases.—The provisions of sections 4 and 8 shall not apply to the following, namely:—
 - (a) possession of foreign currency or foreign coins by any person up to such limit as the Reserve Bank may specify;
 - (b) foreign currency account held or operated by such person or class of persons and the limit up to which the Reserve Bank may specify;
 - (c) foreign exchange acquired or received before the 8th day of July, 1947 or any income arising or accruing thereon which is held outside India by any person in pursuance of a general or special permission granted by the Reserve Bank;
 - (d) foreign exchange held by a person resident in India up to such limit as the Reserve Bank may specify, if such foreign exchange was acquired by way of gift or inheritance from a person referred to in clause (c), including any income arising therefrom;
 - (e) foreign exchange acquired from employment, business, trade, vocation, services, honorarium, gifts, inheritance or any other legitimate means up to such limit as the Reserve Bank may specify; and
 - (f) such other receipts in foreign exchange as the Reserve Bank may specify.

Overview of Legal Provisions

3. Notf 9(R) - Period for surrender of received/ realised/ unspent/ unused foreign exchange by Resident individuals

A person being an individual resident in India shall surrender the received/realised/unspent/unused foreign exchange whether in the form of currency notes, coins and travellers cheques, etc. to an authorised person within a period of 180 days from the date of such receipt/realisation/purchase/acquisition or date of his return to India, as the case may be

4. Nff. 11(R) – Retention by a person resident in India of foreign currency notes, bank notes and foreign currency travellers' cheques not exceeding US\$ 2000 or its equivalent in aggregate, provided that such foreign exchange in the form of currency notes, bank notes and travellers cheques; -
Regulation 3(iii)

- a. was acquired by him while on a visit to any place outside India by way of payment for services not arising from any business in or anything done in India; or
- b. was acquired by him, from any person not resident in India and who is on a visit to India, as honorarium or gift or for services rendered or in settlement of any lawful obligation; or
- c. was acquired by him by way of honorarium or gift while on a visit to any place outside India; or
- d. represents unspent amount of foreign exchange acquired by him from an authorised person for travel abroad.

Overview of Legal Provisions

5. Resident Foreign Currency (Domestic) Account

(1) A resident Individual may open, hold and maintain with an Authorised Dealer in India a foreign currency account, to be known as Resident Foreign Currency (Domestic) Account, out of foreign exchange acquired in the form of currency notes, bank notes and travellers' cheques as under:

- a. by way of payment for services not arising from any business in or anything done in India while on a visit to any place outside India; or
- b. from any person not resident in India and who is on a visit to India, as honorarium or gift or for services rendered or in settlement of any lawful obligation; or
- c. by way of honorarium or gift while on a visit to any place outside India; or
- d. in the form of unspent amount of foreign exchange acquired by him from an authorised person for travel abroad; or
- e. as gift from a relative;
- f. by way of earning through export of goods/ services, or as royalty, honorarium or by any other lawful means;
- g. representing the disinvestment proceeds received by the resident account holder on conversion of shares held by him to ADRs/ GDRs under the DR Scheme, 2014 approved by the Government of India.
- h. by way of earnings received as the proceeds of life insurance policy claims/ maturity/ surrender values settled in foreign currency from an insurance company in India permitted to undertake life insurance business by the Insurance Regulatory and Development Authority

Analysis of the Legal provisions – Remuneration & Honorarium

- Provision of services by PRII:
 - (a) from India to any PROI
 - (b) while a PRII is on a visit outside India
 - (c) to a business which has commenced or a continual employment with a company, taken up while PRII was PROI
 - (d) when PROI is on a visit to India
- Gift or Honorarium received from PROI while on a visit outside India or while PROI is on a visit to India

- i. Exports from India with outstanding export proceeds – Export proceeds shall be realised and repatriated within nine months from the date of export. Mr. returning Indian can make an application to AD bank for extension of time for realization of export proceeds up to a period of six months, at a time for maximum 3 years.
- ii. Remuneration earned by him from Company outside India from continuous employment taken up while he was PROI – He can keep the remuneration outside India as provided in Section 6(4) r.w. Circular 90 and reinvest the same; alternatively he can bring it to India and deposit the same in RFC account.

It may be noted that Section 9(e) of FEMA permits retention of foreign exchange acquired from employment up to such limit as the Reserve Bank may specify; however FEMA Ntf. 11(R) which deals with the matter only permits retention by a PRII of foreign currency notes, bank notes and foreign currency travellers' cheques not exceeding US\$ 2,000 which was acquired by him while on a visit to any place outside India by way of payment for services not arising from any business in or anything done in India. This provision does not cover our instant case where the PRII is continuing to receive remuneration was acquired by him while on a visit to any place outside India by way of payment for services not arising from any business in or anything done in India by way of bank transfer (not currency / coins / TCs) for employment taken up while he was PROI for services being rendered from India. As a result, benefit of Section 6(4) r.w. Circular 90 may be availed.

It should be kept in mind that Cheques received in foreign bank a/c are not covered under FEMA Ntf. 11(R). Only currency / bank notes and travelers' cheques are covered. Also, Remuneration arising from services other than those rendered while on a visit outside India is not covered in Ntf. 11(R).

- iii. Honorarium / Gift received in the form of valuable mementos by him from Charitable organisation abroad while on visit – Section 9(e) of FEMA permits retention of foreign exchange acquired from honorarium / gift up to such limit as the Reserve Bank may specify. FEMA Ntf. 11(R) which deals with the matter only permits retention by a PRII of foreign currency notes, bank notes and foreign currency travellers' cheques not exceeding US\$ 2,000 was acquired by him by way of honorarium or gift while on a visit to any place outside India. It may be observed that instead of currency, he has received honorarium / gift in the form of valuable mementos which are not covered in Ntf. 11(R). However, if RBI does not permit you to hold gifts of currency in excess of US\$ 2,000, can one hold valuable gift items in excess of the said limit? If yes, it can be misused to violate the law. Probably it is not intended to regulate such a transaction which are not in the form of Foreign Exchange, Security or the Immovable Property.
- iv. Foreign currency purchased from India for visits abroad –Every member of his family is permitted to retain USD 2,000 in the form of currency notes, bank notes and foreign currency travellers' cheques as provided in Notification 11(R); the balance unspent foreign exchange shall be surrendered to an authorised person within a period of 180 days from the date of his return to India as provided in Notification 9(R).
- v. Unspent foreign currency on hand from earlier purchases as well as withdrawn from RFC A/c.- FEMA provisions will not apply to exchange withdrawn from RFC account. Unspent foreign currency on hand in excess of US\$ 2,000 from earlier purchases shall be surrendered to an authorised person within 180 days from date of return to India.

Facilities for Resident Indians for overseas remittances / investment

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- Foreign Exchange drawal for foreign travel – Master Direction FED No. 8 / 2015-16
- Retention of foreign currency notes, coins and travellers cheques - FEMA Ntf. 11(R)
- Unspent / Unutilised Foreign Exchange drawn for travel abroad or for other purposes – FEMA Ntf. 9(R)
- Foreign Currency Bank Accounts abroad by Residents – FEMA Ntf. 10(R)
- LRS remittances and prohibited Current Account Transactions – LRS & CAT Rules
- Overseas Investments by Resident Individuals – OI Rules
 - ODI means investment by way of: (a) acquisition of unlisted equity capital of a foreign entity, or subscription as a part of the memorandum of association of a foreign entity, or (b) investment in 10% or more of the paid-up equity capital of a listed foreign entity, or (c) investment with control where investment is less than 10% of the paid-up equity capital of a listed foreign entity (Rule 2(q) of OI Rules).
 - OPI means any investment, other than ODI, in foreign securities, but not in any unlisted debt instruments or any security issued by a person resident in India who is not in an IFSC (Rule 2(s) of OI Rules).

Facilities for Resident Indians for overseas remittances / investment (cont'd)

- Overseas Investments by Resident Individuals – Other modes of acquisition
 - Capitalisation of dues
 - Swap on account of merger, amalgamation, etc.
 - Rights Issue / Bonus shares
 - Gift
 - Inheritance
 - Sweat Equity
 - Qualification Shares
 - ESOP / EBS

POSER – Interplay of Section 6(4) and ODI Rules

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- POSER: Rule 21 of ODI Rules permits acquisition of immovable property outside India by PRIs subject to conditions. Further Section 6(4) of FEMA permits PRIs to acquire, hold, etc. immovable property outside India when resident outside India or inherited from a person who was resident outside India. Participants are requested to discuss the inter-play and nuances that arise in such situations.
- SOLUTION:
 - Discussed earlier in Poser on Section 6(4) assets / inheritance.

POSER – Gift / Inheritance by PRII

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- POSER: Is the PRII who has received the property as a gift/inheritance from another resident required to repatriate the sale proceeds from the property sold or can the PRII reinvest the sale proceeds in any other permitted asset outside India?
- SOLUTION:
 - Holding approval and subsequent conversion in to new assets i.e. transfer or reinvest provided u/s. 6(4) is with respect to both the types of assets - one, which is acquired by and another being inherited by PRII but this facility is not available to all the PRII under this provision.
 - A PRII, however, is allowed to Purchase immovable property from PROI out of the income or the sale proceeds of the Non-ODI assets acquired overseas – Regn. 21 (2)(ii)(e) of ODI Rules.

POSER – PRII acquiring Foreign Property from PRII

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- POSER: Can PRII pay in INR in India to another PRII for the property outside India as per the exchange rate prevailing on the date of sale? If yes is the payment required to be made within the permitted LRS limit?
- SOLUTION:
 - Section 3 (d) forbids any person to enter into any financial transaction in India as consideration for or in association with acquisition or creation or transfer of a right to acquire, any asset outside India by any person.
 - Explanation.—For the purpose of this clause, “financial transaction” means making any payment to, or for the credit of any person, or receiving any payment for, by order or on behalf of any person, or drawing, issuing or negotiating any bill of exchange or promissory note, or transferring any security or acknowledging any debt

POSER – Gift of Immovable Property from PROI to PRII

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- POSER: Gifting of immovable property is not permitted from PROI to PRII, what solution would you give in case a son (PROI) wishes to gift his father (PRII) an immovable property located outside India?
- SOLUTION:
 1. Approval route
 2. Sale transaction of the property

POSER – Gift of Foreign Securities from PROI to PRII

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- POSER: What are the implications if the proposed Gift is of Foreign securities from a PROI to PRII?
- SOLUTION:
 - As far as foreign securities are concerned, it may be noted that the new OI Guidelines now state that any gift of foreign securities from a person resident outside India to an individual resident in India may be made only in accordance with the Foreign Contribution (Regulation) Act, 2010 (“FCRA”). This is a key restriction imposed upon investments by resident individuals, especially since there is no clarity on the compliances required to be fulfilled under the FCRA. The FCRA norms are applicable only where such shares may be considered as ‘foreign contribution’ under the FCRA. The FCRA allows a resident to receive foreign contribution from a relative. Thus, it appears that a gift from a non-resident may be acceptable as long as such non-resident is a relative of the resident individual. A ‘relative’ in such case shall be as defined under the Companies Act, 2013.

A Returning Indian, Mr. R. Patel holds Shares in various Limited Liability entities abroad, some of them in Joint Venture with Non-Residents as well as with Non-Resident relatives in few companies. He also held various Options and Cashless Shares while he was Non-Resident. Participants are requested to discuss the implications and compliances under OI Rules & Regulations of the following proposed transactions being contemplated by Mr. R. Patel.

- i. Receipt of Shares aggregating 9% in a Private Ltd. Company in Kenya by way of transfer from Executor of Will of his deceased friend.
- ii. Investing in a new step-down subsidiary in Kenya of the aforesaid Kenyan company holding 51% and balance shares being held by Mr. R. Patel with participation in management and control of the step-down subsidiary.
- iii. Acquiring 15% shareholding in a company in USA by way of Sweat equity for services rendered but not resulting in participation in management and control of the US company.
- iv. In case the above-mentioned company in USA has a step-down subsidiary, what would be the implication on the offer of Sweat equity received from the said holding company?
- v. Investment of 5% in unlisted entity in USA as portfolio investment without control. Would your answer be different if Mr. R. Patel was to utilize his foreign bank balance which is retained abroad i.e. Section 6(4) asset?
- vi. Remittance from India under LRS for investment in interest-bearing bonds issued by US company which are not listed

Overview of the Legal Provisions - Definitions

- i. “Overseas Direct Investment” or “ODI” means investment by way of acquisition of unlisted equity capital of a foreign entity, or subscription as a part of the memorandum of association of a foreign entity, or investment in ten per cent, or more of the paid-up equity capital of a listed foreign entity or investment with control where investment is less than ten per cent. of the paid-up equity capital of a listed foreign entity
- ii. “Overseas Portfolio Investment” or “OPI” means investment, other than ODI, in foreign securities, but not in any unlisted debt instruments or any security issued by a person resident in India who is not in an IFSC
- iii. “Control” means the right to appoint majority of the directors or to control management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by virtue of their shareholding or management rights or shareholders’ agreements or voting agreements that entitle them to ten per cent. or more of voting rights or in any other manner in the entity;

CASE STUDY - 6

Overview of the Legal Provisions – Schedule III, OI Rules, 2022

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- Regulation 1 (1) - Any resident individual may make ODI by way of investment in equity capital or OPI in the manner provided in this Schedule and unless otherwise provided hereunder, shall be subject to the overall ceiling under the Liberalised Remittance Scheme of the Reserve Bank

- Regulation 1 (2) - A resident individual may make or hold Overseas Investment by way of,–
 - (i) ODI in an operating foreign entity not engaged in financial services activity and which does not have subsidiary or step down subsidiary where the resident individual has control in the foreign entity;
 - (ii) OPI, including by way of reinvestment;
 - (iii) ODI or OPI, as the case may be, by way of–
 - (a) capitalisation, within the time period, if any, specified for realisation under the Act, of any amount due from the foreign entity the remittance of which is permitted under the Act or does not require prior permission of the Central Government or the Reserve Bank;
 - (b) swap of securities on account of a merger, demerger, amalgamation or liquidation;
 - (c) acquisition of equity capital through rights issue or allotment of bonus shares;
 - (d) gift as per the conditions laid down under this Schedule;
 - (e) inheritance;
 - (f) acquisition of sweat equity shares;
 - (g) acquisition of minimum qualification shares issued for holding a management post in a
 - a. foreign entity;
 - (h) acquisition of shares or interest under Employee Stock Ownership Plan or Employee Benefits Scheme;

CASE STUDY - 6

Overview of the Legal Provisions – Schedule III, OI Rules, 2022

- Provided that ODI in respect of clauses (e), (f), (g) and (h) may be made in a foreign entity whether or not such foreign entity is engaged in financial services activity or has subsidiary or step down subsidiary where the resident individual has control:
- Provided further that the acquisition of less than ten per cent. of the equity capital, whether listed or unlisted, of a foreign entity without control under clauses (f), (g) and (h), shall be treated as OPI.
- Explanation.— For the purposes of this Schedule, a foreign entity will be considered to be engaged in the business of financial services activity if it undertakes an activity, which if carried out by an entity in India, requires registration with or is regulated by a financial sector regulator in India

Overview of the Legal Provisions - Schedule III, OI Rules, 2022

2. Acquisition by way of gift or inheritance.—

(1) A resident individual may, without any limit, acquire foreign securities by way of inheritance from a person resident in India who is holding such securities in accordance with the provisions of the Act or from a person resident outside India.

(2) A resident individual, without any limit, may acquire foreign securities by way of gift from a person resident in India who is a relative and holding such securities in accordance with the provisions of the Act.

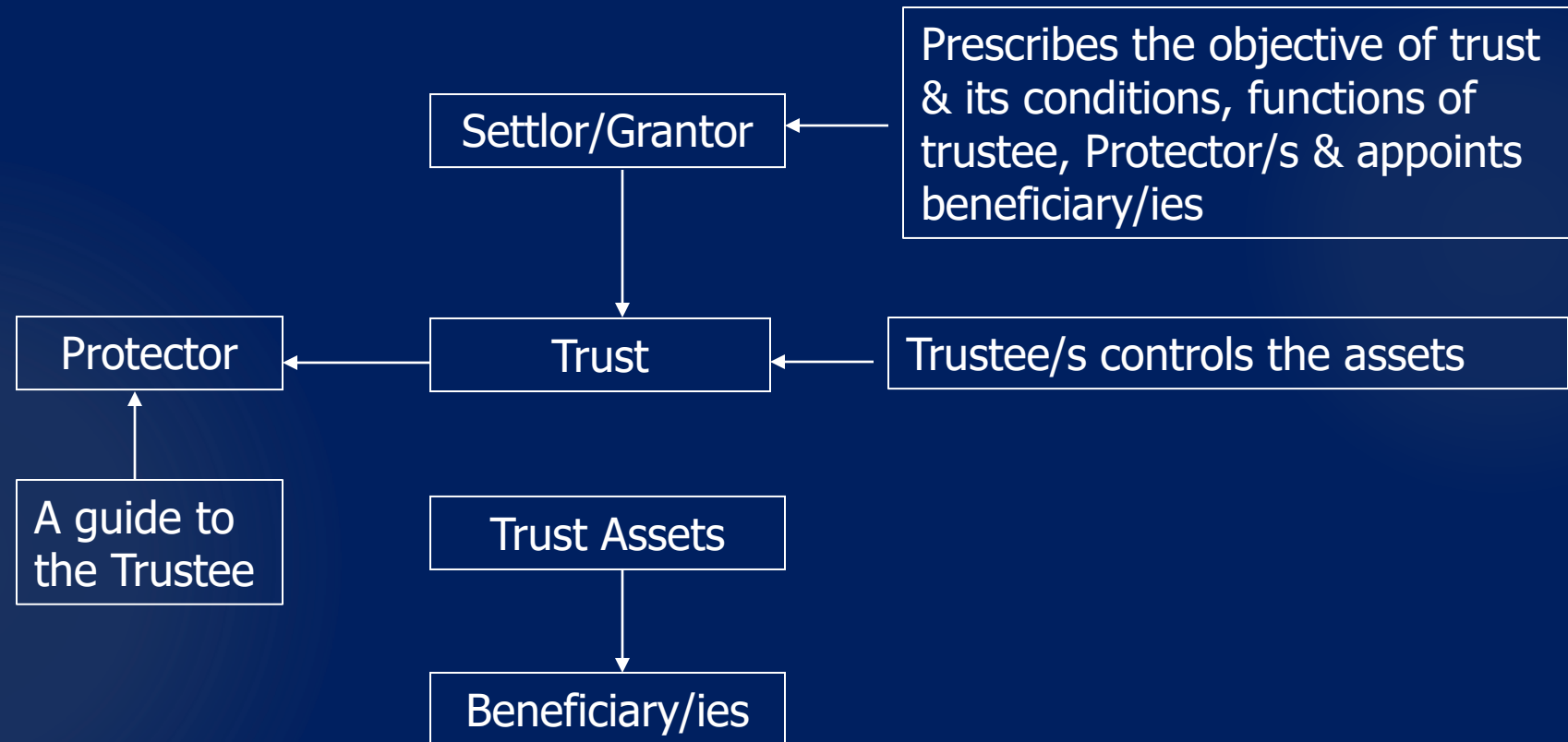
(3) A resident individual may acquire foreign securities by way of gift from a person resident outside India in accordance with the provisions of the Foreign Contribution (Regulation) Act, 2010 (42 of 2010) and the rules and regulations made thereunder.

- i. Receipt of Shares aggregating 9% in a Private Ltd. Company in Kenya by way of transfer from Executor of Will of his deceased friend
 - Mr. R. Patel can acquire foreign shares by way of inheritance from PROI without any limit (Para 2 and 3(e) of Sch. III of OI Rules). Such shares shall be categorized as ODI in the hands of Mr. Patel even though he may not be having control of the Kenyan company (Proviso 1 to Para 1 of Sch. III of OI Rules) the reason being that all investment in unlisted shares is categorized as ODI as per definition of ODI in Section 2(q). However, if the shares were listed, the inheritance would be classified as OPI as the shareholding is less than 10%
- ii. Investing in a new step-down subsidiary (SDS) in Kenya of the aforesaid Kenyan company holding 51% and balance shares being held by Mr. R. Patel with participation in management and control of the step-down subsidiary
 - Though Mr. R. Patel has no control in the Kenyan entity, his shareholding by way of inheritance as also u/s 2(q) is categorized as ODI. Therefore, the Kenyan company cannot form a SDS, unless Mr. R. Patel divests his 9% shareholding in the Kenyan company. Thereafter, a SDS can be formed with Mr. R. Patel directly holding 49% of the SDS with management control
- iii. Acquiring 15% shareholding in a company in USA by way of Sweat equity for services rendered but not resulting in participation in management and control of the US company.
 - Permitted as ODI as shareholding in more than 10% even though he does not have control. File Form FC. If acquiring less than 10% with no management control then it would be treated as OPI and the reporting would have to be done by the company issuing the sweat equity shares

- iv. In case the above-mentioned company in USA has a step-down subsidiary, what would be the implication on the offer of Sweat equity received from the said holding company?
 - As Mr. R. Patel's equity holding of 15% is in nature of ODI, the company cannot have a SDS. If Mr. Patel's equity holding was restricted to 10%, it would have qualified as OPI and in such a case the US company could form a SDS.
- v. Investment of 5% in unlisted entity in USA as portfolio investment without control. Would your answer be different if Mr. R. Patel was to utilize his foreign bank balance which is retained abroad i.e. Section 6(4) asset?
 - The above investment in an unlisted company will be treated as an ODI and not OPI as only investment below 10% in a listed company qualifies as OPI. However, if his foreign bank balance retained abroad in terms of Section 6(4) is utilized, OI Rules would not be applicable and hence there would be no issue relating to nature of investment being ODI or OPI.
- vi. Remittance from India under LRS for investment in interest-bearing bonds issued by UK company which are not listed
 - Not permitted. Only listed debt instruments are permitted under OPI.

Trust – A Typical Structure

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Trust vs Will for Estate Planning

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	Revocable Living Trusts	Wills
Name beneficiaries for property	✓	✓
Leave property to young children	✓	✓
Revise your document	✓	✓
Avoid probate	✓	
Keep privacy after death	✓	
Requires a notary public	✓	
Requires transfer of property	✓	
Protection from court challenges	✓	
Avoid a conservatorship	✓	
Name guardians for children		✓
Name property managers for children's property		✓
Name an executor		✓
Instruct how taxes and debts should be paid		✓
Simple to make		✓
Requires witnesses		✓
Reduce estate taxes	-	-

- Estate Planning for PRIs having overseas assets and PROs having Indian assets:
 - i. General Permission has been given to a PRI to inherit assets outside India from a PRO as per Section 6(4) of FEMA and Rule 21 of OI Rules and to PRO to bequeath assets in India to PRI as per Section 6(5) of FEMA and Rule 24 of NDI Rules
 - ii. Assets can be bequeathed by way of Will or a Trust
- A trust is not included within the definition of Person, as provided under FEMA. Under the Indian trust law, a trust is a contract / arrangement. Accordingly, it becomes difficult to accord any residential status to the trust since it does not fall within the definition of Person
- For Indian tax purposes, a trust is not considered as an entity. Under the tax law, a trustee is taxed as representative assessee of the Beneficiary/ies. Once the trustees are taxed no tax is levied on the beneficiary/ies

- iv. Under FEMA there are no clear rules for a trust, There are three views:
 - a. FEMA provisions applicable to Non-Residents are applicable to Trust having non-resident beneficiaries, since a Trust is mere pass-through entity
 - b. If there are mixed beneficiaries, FEMA as applicable to each one of them, either as Resident or Non-resident, will apply
 - c. Cannot determine Residential Status in a straight manner because Trust is not a person and it is an arrangement/contract

Inheritance, Will, Trust (cont'd)

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- Gift vs Settlement – A distinction, Section 47(iii) and Section 48 of I.T. Act
 - It is not an AOP [(1960) 39 ITR 546 (Supreme Court) CIT vs Indira Balkrishna]
- If a Trust is regarded as Person, then settlement would be regarded as Transfer and various FEMA provisions based on asset-class will be triggered.
- If Transfer provisions of Gift are on Automatic basis, then settlement in favour of such a transferee who is a beneficiary will not trigger any requirement of approval
- When Transfer of an asset to a Trust is on an Automatic basis, there may not be any issue on distribution
- If Transfer was not on Automatic basis, an approval at the time of distribution may suffice
- The provisions of Transfer by a Non-resident of an Indian asset to an Indian Trust and by a Resident to a Foreign Trust of an Indian or Foreign asset are discussed in subsequent slides

Transfer of Equity Instruments

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Sub Reg	Transferor	Transferee	Form	Automatic/App roval Route	Conditions
1	PROI (other than NRI, OCI)	PROI	Sale/Gift	Automatic	One Non Resident to another Non Resident (Rule 9(1) of NDI Rules)
	FPI	PRII	sale	Automatic	(only when FPI breaches investment limit)
2	NRI/OCI holding on Repatriable basis	PROI	Sale/Gift	Automatic	Prior Govt approval if Sector requires Govt Approval, generally so when transferee is other than OCI (Rule 13 of NDI Rules)
3	PROI	PRII/Stock exch	sale/gift	Automatic	subject to the adherence to pricing guidelines, documentation and reporting requirements for such transfers. If non-repatriable, then no conditions (Rule 9(2) of NDI Rules)
4	PRII/NRI/OCI holding on Non Repatriable basis	PROI	sale	Automatic	subject to the adherence to entry routes, sectoral caps/ investment limits, pricing guidelines and documentation and reporting requirements as may be specified by Reserve Bank (Rule 13 of NDI Rules)
5	PRII/OCI/NRI holding on Non Repatriable basis	PROI on Repatriable basis	Gift	Approval	Gift ≤ 5% of paid up cap of Indian co, deb, mf. Donor & Donee relatives. Value of all gifts of donor to be less than 50,000\$ (Rule 9(4) of NDI Rules)
6	NRI/OCI holding on Non Repatriable basis	NRI/OCI on Non Repatriable basis	Gift	Automatic	

- Prior Government Approval is required for any transfer in case the company is engaged in sector which requires government approval
- NRI holding on Non Repatriation basis or under 6(5) and transferring to Resident is under automatic route and does not require any compliance

Transfer of Immovable Property in India

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Immovable Property in India	PRII			NRI/OCI		
	Sale	Gift	Inheritance	Sale	Gift	Inheritance
Acquisition by NRI/OCI from	✓	✓ (relative)	✓	✓	✓ (relative)	✓
Transfer by NRI/OCI to	✓	✓ (relative)	✓	✓	✓ (relative)	✓

NRI Settlor with Resident and Non – Resident beneficiaries – Trust in India

Particulars	Gift to NR	Gift to R
1. Settlement of Assets - from NRO - from NRE	- Ntf. 13(R) - \$1Mn repatriation from NRO - Freely permitted from NRE	Permitted
2. Settlement of Currency (FCY) by way of remittance from abroad	FEMA not applicable as there is no change of assets in India for NR	FEMA not applicable as there is no change of assets in India for NR
3. Settlement of shares in Indian companies	FEM NDI Rules, 2019 - permitted	FEM NDI Rules, 2019 - permitted
4. Settlement of Immovable Property in India	FEM NDI Rules, 2019 - permitted	FEM NDI Rules, 2019 - permitted

Resident Settlor with Resident and Non – Resident beneficiaries – Trust in India

Particulars	Gift to NR	Gift to R
1. Settlement of Currency (INR)	LRS Scheme – permitted to NRI relatives	FEMA not applicable
2. Settlement of shares in Indian companies	FEM NDI Rules, 2019 – Approval Route, subject to conditions	FEMA not applicable
3. Settlement of Immovable Property in India	FEM NDI Rules, 2019 – Permitted to relatives	FEMA not applicable

NRI Settlor with Resident and Non – Resident beneficiaries – Trust outside India

Particulars	Gift to NR	Gift to R
1. Settlement of Foreign Currency	FEMA not applicable	Permitted
2. Settlement of shares in Foreign companies	FEMA not applicable	FEM OI Rules, 2022 - Permitted
3. Settlement of Immovable Property outside India	FEMA not applicable	FEM OI Rules, 2022 - Permitted

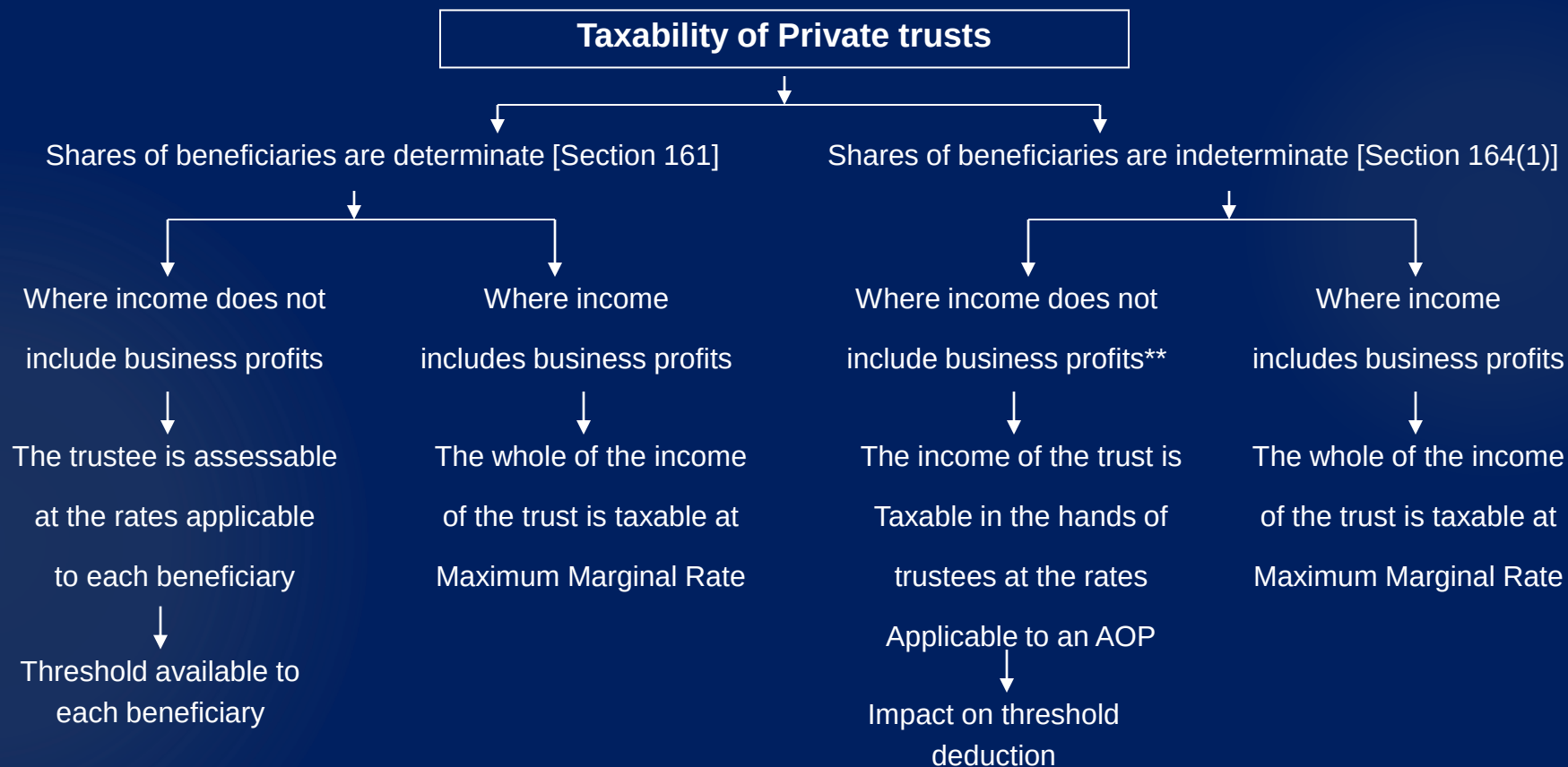
Resident Settlor with Resident and Non – Resident beneficiaries – Trust outside India

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Particulars	Gift to NR	Gift to R
1. Settlement of Currency (INR) under LRS scheme	LRS Scheme – permitted to any NRI	LRS Scheme –not permitted
2. Settlement of shares in Foreign companies	FEM OI Rules, 2022 Not permitted	FEM OI Rules, 2022 - Permitted
3. Settlement of Immovable Property outside India	FEM OI Rules, 2022 – not permitted	FEM OI Rules, 2022 - Permitted
4. Settlement of assets held outside India u/s. 6(4) of FEMA	FEMA not applicable	General permission under OI Rules

Taxability of Private Trust – I.T.Act

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** Note: Subject to conditions as specified in the following slides

	I	II	III	IV	V	VI
SETTLOR	NRI	NRI	NRI	R	R	R
TRUSTEE	R	R	NRI	R	NRI	R
BENEFICIARY	R	NRI	R	NRI	NRI	R
LOCATION OF ASSETS	India	India	Outside India	India	Outside India	India
Application of FEMA:						
Creation of Corpus	- NRO –Applicable - Remittance from abroad - NA	- NRO – Applicable - Remittance from abroad - NA	NA	NA	- If 6(4) asset – NA - Other assets - Applicable	NA
Income generation	NA	NA	NA	NA	NA	NA
Distribution / Remittance of Income to Beneficiary	NA (Res. To Res.)	Applicable (Res. To NR)	Applicable (NR to Res.)	Applicable (Res. To NR)	NA	NA
Remittance of Corpus to Beneficiary	NA	Applicable	Applicable	Applicable	NA	NA
Taxation in the hands of Trustee (Note 1)	- AOP Rate - If there is Business Income then MMR	- AOP Rate - If there is Business Income then MMR	Taxable in India (Note 2)	- AOP Rate - If there is Business Income then MMR	Not taxable in India	- AOP Rate - If there is Business Income then MMR

- Note 1 - Taxation: if it is a non-discretionary trust, then tax will be determined with respect to each beneficiary as if Income is earned by the beneficiary irrespective of distribution; No tax at the time of distribution
- Note 2 – If only Resident is beneficiary, then he himself will be taxed. Trustee may not be taxed as he is non-resident. If there are mixed beneficiaries, computation mechanism fails

- POSER: Although this paper is not an attempt to discuss tax issues, participants are requested to discuss the implications of settlement on a trust in context of Section 93 of the Income Tax Act, 1961.
- SOLUTION:
 - Section 93 is a deeming provision which aims to curb the practice of tax avoidance by the resident taxpayers through transfer of assets (by a resident or non resident) to non-residents but enjoying the fruits of the assets even after such transfer. However, it is not applicable if the purpose is not for avoiding tax or if it is a case of bona fide commercial transactions. Can the transaction of settlement to a Trust by a returning Indian who will be resident beneficiary on his return to India be regarded as bona fide?

Thank You