



news flash

April 2017



FOREIGN INVESTMENT UPDATES

The Department of Industrial Policy and Promotion (“DIPP”) has issued Press Note No. 1 of 2017 (“Press Note”), liberalising the terms governing foreign direct investment (“FDI”) in infrastructure companies in the securities market.

The Reserve Bank of India (“RBI”) recently amended the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations 2000 (“Regulations”), to further liberalise the FDI in Limited Liability Partnerships (“LLP”).

This newsflash sets out these recent amendments brought about by the Press Note and the Regulations.

BACKGROUND

A. INFRASTRUCTURE

As per the FDI policy dated 7 June 2016, FDI in ‘*infrastructure companies in the securities market*’ was permitted upto 49% under the automatic route (without any approval). However, foreign institutional investors (“FII”) and foreign promotional investors (“FPI”) could invest only through purchases made in the secondary market. Further, a non-resident investor/ entity, including ‘*persons acting in concert*’, were not allowed to hold more than 5% of the equity in commodity exchanges. It was also clarified that foreign investment in commodity exchanges would be subject to the guidelines of the Central Government (“CG”)/ Securities and Exchange Board of India (“SEBI”). Further, certain definitions applicable to the said sector were also set out in the FDI Policy.

The Press note, while retaining the sectoral cap of 49%; has amended the conditions attached to FDI in the *infrastructure companies in the securities market*. FDI, including investment by FPIs, will be subject to the Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012 (“SECC Regulations”), and Securities and Exchange Board of India (Depositories and Participants) Regulations, 1996 (“Depositories Regulations”) and other guidelines/regulations issued by the CG, SEBI and the RBI. It is also clarified that words and expressions used in the FDI policy pertaining to this sector and not defined in the aforesaid regulations but defined in the Companies Act, 2013 or the Securities Contracts (Regulation) Act, 1956 or the Securities and Exchange Board of India Act, 1992 or the Depositories Act, 1996 or in the concerned regulations issued by SEBI shall have the same meanings respectively assigned to them in those acts/ regulations.

B. LLP

In November 2015, by the Press Note No. 12 the DIPP had liberalised FDI in LLP by permitting the foreign investors to invest in LLP under the automatic route in sectors where 100% FDI was

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permitted under the automatic route. The RBI has further liberalised FDI in LLP by withdrawing the following conditions:

- (i) LLP with FDI could admit a body corporate as a designated partner or have an individual nominated as designated partner of a body corporate, only if such body corporate was a company registered in India and not otherwise. Further for such LLPs the designated partners had to pass the test of '*resident in India*' as per the Limited Liability Act of 2008 as well as the definition of '*person resident in India*' as prescribed under Foreign Exchange Management Act, 1999 ("**FEMA**").
- (ii) Conversion of a Company with FDI, into LLP, were allowed only if certain stipulations were met and with the prior approval of foreign investment promotional board ("**FIPB**")/Government; and
- (iii) LLPs were not permitted to avail External Commercial Borrowings ("**ECBs**").

ALMT analysis

A. INFRASTRUCTURE

The Press note does not liberalise the sector cap but relaxes the conditions attached therewith. However, the Press note merely states that the conditions shall be according to the regulations stated therein. Upon perusing the SECC Regulations, it specifies that no FII shall acquire shares of a recognised stock exchange otherwise than through secondary market. In addition, it also states that no person resident outside India, directly or indirectly, either individually or together with persons acting in concert, shall acquire or hold more than 5% of the paid up equity share capital in a recognised clearing corporation. Therefore, it appears that the conditions, although not stated in the FDI policy due to this amendment, still stand as the same is covered under the SECC Regulations. The Depositories Regulations states that the combined holding of all persons resident outside India in the equity share capital of the depository shall not exceed 49% of its total equity share capital, subject to (i) the combined holdings of such persons acquired through the FDI route is not more 26% of the total equity share capital, at any time; (ii) the combined holdings of FIIs should be not more than 23% of the total equity share capital, at any time; and (iii) no FII acquires shares of the depositories otherwise than through the secondary market. The Depositories Regulations also clarify that no foreign institutional investor shall have any representation in the board of directors of the depository.

The amendment vide the Press Note appears to be due to the budget 2017, which states the intention of the government to abolish the foreign investment promotion board and direct all applications regarding approval for FDI to the respective ministry and departments.

B. LLP

By deleting the conditions in the Regulations relating to LLPs by RBI, now (i) any body corporate can become a designated partner in LLPs including foreign companies; (ii) the individual appointed as designated partner does not have to satisfy the residency test under the FEMA; (iii) No prior approval of FIPB/government is required for conversion of LLP into Company; and (iv) Though the prohibition on the LLPs from availing ECBs has been removed; the ECB regulations are yet to be amended to include LLPs as eligible borrowers.

The step of amending the Regulations in LLP is another step of government for ease of doing business in India. The Regulations have simplified the compliance and is expected to widen the borrowing powers of LLPs.

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