



Tax alert: Cross border share swaps simplified

22 August 2024

On 16 August 2024, the Ministry of Finance, notified the Foreign Exchange Management (Non-debt Instruments) (Fourth Amendment) Rules, 2024, amending certain provisions of the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 ('FEMA NDI Rules') which govern FDI norms in India and has now relaxed cross border share swap provisions thereby allowing issue or transfer of equity instruments of Indian company in exchange for foreign company equity capital, which was earlier permitted only with the prior approval of the Reserve Bank of India (RBI).

These amendments are effective from the date of their notification.

In a nutshell



Indian companies are now permitted to issue / transfer equity instruments of an Indian Company through swap of equity instruments of an Indian Company or equity capital of Foreign Company, without any prior RBI approval. Prior government approval shall be required only in case where government approval is applicable.



Definition of "control" and "start-up company" inserted for clarity and alignment with other laws / notifications.



Allowing 100% FDI under automatic route for White Label ATM Operations (WLAO), subject to specified conditions.



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Background:

- The government had announced simplification of rules and regulation for Foreign Direct Investment (FDI) and Overseas Investment (OI) as part of the Union Budget 2024-25, as one of the initiatives.
- Accordingly, the Ministry of Finance, vide notification dated 16 August 2024, notified Foreign Exchange Management (Non-debt Instruments) (Fourth Amendment) Rules, 2024 amending the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 which govern FDI norms in India, thereby simplifying cross border swaps, allowing 100% FDI under automatic route for White Label ATM Operations (WLAO) and alignment of certain definitions for clarity/changes in other laws.

Key Highlights:

Following are key amendments to the FEMA NDI Rules:

| Sl. No. | Parameters | Key provisions of Rules |
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| 1 | Definitions | <p>Definitions of “control” and “start-up company” has been aligned / harmonised for clarity/changes in other laws, as mentioned below:</p> <ul style="list-style-type: none">• “Control” shall have the same meaning as assigned to it in the Companies Act, 2013 i.e. right to appoint majority of the directors (or) control the 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 or in any other manner. <p>Control for the purposes of Limited Liability Partnership, shall mean the right to appoint majority of the designated partners, where such designated partners, with specific exclusion to others, have control over all the policies of an LLP.</p> <ul style="list-style-type: none">• “Start-up company” means a private company incorporated under the Companies Act, 2013 and identified as “start-up” under the notification number G.S.R. 127 (E), dated 19 February 2019 issued by the Department for Promotion of Industry and Internal Trade, Ministry of Commerce and Industry, as amended from time to time. |
| 2 | Swap of equity instruments and equity capital | <p>Earlier swap of equity instruments of Indian Company with equity capital of Foreign Company required prior RBI approval.</p> <p>Swap of equity instruments and equity capital now permissible without any prior RBI approval as mentioned below:</p> <p>Transfer</p> <p>The transfer of equity instruments of an Indian company between a person resident in India and a person resident outside India is allowed by way of:</p> <ul style="list-style-type: none">• Swap of Equity Instruments of an Indian Company in |

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| | | <p>compliance with the rules prescribed by the Central Government and regulation prescribed by RBI;</p> <ul style="list-style-type: none"> • Swap of Equity Capital of a Foreign Company in compliance with the rules prescribed by the Central Government including the Foreign Exchange Management (Overseas Investment) Rules 2022, and the regulations specified by the RBI. <p>Issue</p> <p>An Indian company can issue equity instruments to a person resident outside India against swap of equity instruments of an Indian Company or equity capital of a foreign company in compliance with the rules prescribed by the Central Government including the Foreign Exchange Management (Overseas Investment) Rules 2022, and the regulations specified by RBI.</p> <p>Prior government approval shall be obtained for transfer / issue in all cases wherever Government approval is applicable.</p> <p>Note: the term “equity capital” shall have the same meaning as assigned to it in the Foreign Exchange Management, (Overseas Investment) Rules, 2022, as amended from time to time.</p> |
| 3 | Downstream investment | <p>Investment by NRI or OCI on non-repatriation basis, directly or indirectly through Indian Company not considered as foreign investment as mentioned below.</p> <p>Hitherto investments made by Indian company, which is owned and controlled by NRI on non-repatriation basis in compliance with Schedule IV of FEMA NDI Rules, was not considered for calculation of indirect foreign investment.</p> <p>Now, investments made by Indian company which is owned and controlled by NRI or an OCI including a company, a trust and a partnership firm incorporated outside India and owned and controlled by NRI or an OCI on non-repatriation basis in compliance with Schedule IV of FEMA NDI Rules, shall not be considered for calculation of indirect foreign investment.</p> |
| 4 | 100% FDI in White label ATM Operations (WLAO) allowed | <p>100% FDI allowed for WLAO under the automatic route subject to following conditions:</p> <ul style="list-style-type: none"> • Any non-bank entity intending to set-up WLAO shall have minimum net worth of INR 1 billion, as per the latest audited financial statement, at all times. • Entities engaged in ‘Other Financial Services’ intending to set-up shall also comply with prescribed capitalisation norms applicable to such financial services sector. • FDI in WLAO shall comply with specific criteria and guidelines issued by RBI under the Payment and Settlement Systems Act 2007. |

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| 5 | Permitted sectors, entry routes and sectoral caps for total foreign investment | The aggregate foreign portfolio investment by FPI up to the sectoral or statutory cap shall not require government approval or compliance of sectoral conditions as the case may be, if such investment does not result in transfer of ownership and/ or control of the resident Indian company. Earlier there was a threshold of aggregate foreign portfolio investment by FPI up to 49% of the paid-up capital on a fully diluted basis or the sectoral or statutory cap, whichever is lower. |
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Conclusion

The above amendments will simplify cross-border share swaps and shall facilitate global expansion of Indian companies through acquisitions and other strategic sales, enabling them to reach new markets and grow their presence globally. One must consider the tax implications while undertaking such transactions.

The amendments also bring clarity to the treatment of downstream investments made by Overseas Citizen of India (OCI)-owned entities, on a non-repatriation basis, not considered as foreign investment, aligning it with the treatment of Non-Resident Indian (NRI)-owned entities.

Source: Notification no. S.O. 3492(E) and Press release issued by Ministry of Finance dated 16 August 2024

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