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THE FOREIGN DIRECT INVESTMENT POLICY 2017 NOTIFIED BY DIPP

A. INTRODUCTION

The Department of Industrial Policy and Promotion (**DIPP**) has notified India's Consolidated Foreign Direct Investment Policy 2017 ("**FDI Policy 2017**"), effective from August 28, 2017. The FDI Policy 2017 is a consolidation of the various decisions taken by the Government of India in the past one year. The present consolidation subsumes and supersedes all Press Notes/Press Releases/Clarifications/Circulars, which were in force as on August 28, 2017 and reflects the FDI policy as on August 28, 2017.

During the last one year, the Government has radically liberalised FDI regime by easing norms for a host of important sectors such as Defence, Civil Aviation, Pharmaceuticals, Private Security, Broadcasting etc. to boost FDI investment. Most of the changes have already been notified by the DIPP and Reserve Bank of India (RBI), which are now consolidated in the present FDI Policy 2017.

B. KEY CHANGES

The key changes in the FDI regime through the FDI Policy, 2017 are set out below:

(1) **Startups**: The FDI Policy 2017 for the first time contains provisions specific to start-up companies. The start-up companies can issue equity or equity linked instruments or debt instruments to foreign venture capital investor (FVCI) against receipts of foreign remittance, as per the FEMA Regulations. In addition, start-ups can issue convertible notes to person resident outside India, subject to certain conditions mentioned therein. This was already notified by the Reserve Bank of India ("**RBI**") *vide* Notification No. FEMA.377/2016-RB dated January 10, 2017 and amendments to the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000 (FEMA 20) were made to allow startups to issue convertible notes to foreign investors. The aforesaid notification also provides for the meaning of a 'start-up company' which means a private company incorporated under the Companies Act, 2013 or the Companies Act, 1956 and recognised as such in accordance with the notification number G.S.R. 180(E) dated February 17, 2016 issued by the DIPP. The FDI Policy 2017 also provides for the definition of "Convertible Notes" which means an instrument issued by a startup company evidencing receipt of money initially as debt, which is repayable at the option of the holder, or which is convertible into such number of equity shares of such start-up company within a period not exceeding five (5) years from the date of issue of the convertible note, upon occurrence of specified events as per the other terms and conditions agreed to and indicated in the instrument. A person

resident outside India (other than citizens/entities of Pakistan and Bangladesh) will be permitted to purchase convertible notes issued by an Indian start-up company for an amount of Rs. 25 lakh or more in a single tranche.

(2) **Competent Authority:** The FIPB was abolished *vide* office memorandum dated June 5, 2107 issued by the Department of Economic Affairs (DEA), Ministry of Finance. Further, DIPP released a standard operating procedure (SOP) on June 29, 2017 for processing FDI proposals which *inter-alia* listed out the competent sectoral authorities for grant of approval for foreign investment with respect to sectors/activities requiring Government approval. The FDI Policy, 2017 replicates the aforesaid changes announced in the SOP. The FDI Policy, 2017 also has a definition of "Competent Authority" which means the concerned Administrative Ministry/Department empowered to grant Government Authorities for foreign investment under the extant of FDI Policy and FEMA Regulations. Further, Chapter 4 pertaining to Procedure for Government Approval provides for the relevant Competent Authorities for grant of approval for foreign investments for sectors/activities requiring government approvals, which is in line with the SOP. It *inter-alia* provides that the proposals for foreign investment would be examined by the relevant Competent Authorities as per the Standard Operating Procedure laid down by the DIPP (available at http://www.fifp.gov.in/Forms/SOP.pdf). In the event the proposals involves total foreign equity inflow of more than Rs. 5000.00 Crore the relevant competent authority will place the proposal for consideration of Cabinet Committee on Economic Affairs ("**CCEA**"). Further, additional FDI has been capped upto cumulative amount of INR 5,000 crore into the same entity, beyond which, fresh approval will be required to be sought.

(3) **FDI Linked Performance Conditions**: A new addition in the FDI Policy 2017, means the sector specific condition for companies receiving foreign investment.

(4) **FDI in LLPs**: The FDI Policy 2017 permits that conversion of an LLP into a company or vice-a-versa having foreign investment and operating in sectors/activities where 100% FDI is allowed through the automatic route and there are no FDI linked performance conditions is permitted under automatic route. The FDI Policy 2016 was silent on the conversion of an FDI funded LLP into a company or vice-a-versa.

(5) **Venture Capital Fund**: The FDI Policy 2017 also simplifies the definition of 'Venture Capital Fund', which is now defined as a fund registered under the SEBI (Venture Capital Funds) Regulations, 1996.

(6) **Downstream Investment**: The FDI Policy 2016 required an entity to notify its downstream investment to the Secretariat of Industrial Assistance ("**SIA**"),

DIPP and FIPB. The FDI Policy requires this intimation to be made to the RBI and the Foreign Investment Facilitation Portal. However, the FDI Policy 2017 does not provide clarity on whether the intimation has to be made to regional offices of RBI or the central office of RBI.

(7) **Cash & Carry Wholesale Trading**: The FDI Policy 2016 allowed a wholesale/cash & carry trader to undertake single brand retail trading, subject to the conditions related to FDI in single brand retail trading. The FDI Policy 2017 allows wholesale/cash & carry traders to undertake retail trading and reference to "single brand" has been done away with. Therefore, the wholesale/cash & carry traders can undertake both the activities of single brand retail trading and wholesale through a single entity, subject to prescribed conditions.

(8) **Single Brand Retailing**: Sourcing norms have been relaxed up to three (3) years from the date of commencement of the business, i.e. opening of the first store for entities undertaking single brand retail trading of products having 'state¬ of ¬art' and 'cutting edge' technology and where local sourcing is not possible, pursuant to which the provisions of Paragraph 5.2.15.3 (2)(e) will be applicable. The Government's decision to relax the local sourcing norms was notified in Press Note 5 (2016) Series dated June 24, 2016, which has now been consolidated in FDI Policy 2017. Further, a committee under the Chairmanship of Secretary, DIPP with representative of NITI Ayog, concerned Administrative Ministry and independent technical expert(s) on the subject will examine the claim of applicants on the issue of the products being in the nature of 'state-of-art' and 'cutting-edge' technology where local sourcing is not possible and give recommendations for such relaxation.

(9) **E-commerce**: The Government had earlier mandated 25% maximum sales from a single vendor but had not specified the period for computation of sales. The FDI Policy 2016 prohibited an e-commerce entity from permitting more than 25% of the sales effected through its market place from one vendor or its group companies. The New FDI Policy clarifies that the 25% of sales value must be computed per financial year.

(10) **Branch office, Liaison office or Project office**: For establishment of branch office, liaison office or project office or any other place of business in India if the principle business of the applicant is Defence, Telecom, Private Security or Information and Broadcasting, approval of the RBI is not required in cases where Government approval or license/permission by the concerned Ministry/Regulator has already been granted. This was already notified by the RBI last year.

C. LIBERALIZATION IN KEY SECTORS

Some of the key decisions taken by the Government and amendments made by the Press Notes in the past one year, which have been consolidated in the FDI Policy 2017 are provided below:

(i) **Defence Sector**: Press Note 5 (2016 Series) issued by the DIPP last year allowed 100% FDI in the defence sector where upto 49% is permitted under the automatic route and beyond 49% is permitted under the Government route wherever it is likely to result in access to the modern technology for other reasons to be recorded. This sectoral caps and conditions have also been extended to manufacturing of small arms and ammunition under the Arms Act, 1959. The FDI Policy, 2017 reflects these changes.

(ii) **Broadcasting Sector:** The sectoral cap in broadcasting carriage services such as Teleports, DTH, Cable Networks (Digital), Mobile TV, HITS has been raised from 49% to 100% automatic route.

(iii) **Civil Aviation:** With a view to aid in modernization of the airports to establish a high standard while helping in easing the pressure on the airports, 100% FDI under automatic route has been permitted in existing projects under automatic route. The earlier FDI Policy 2016 permitted upto 74% under the automatic route and beyond that upto 100% through Government approval route. Further, in terms of the Scheduled Air Transport Service/Domestic Scheduled Passenger Airlines and Regional Air Transport Service, the FDI Limit has been raised to 100%, with FDI upto 49% permitted under automatic route and FDI beyond 49% through Government approval.

(iv) **Food Products:** 100% FDI under automatic route for trading, including through e-commerce, is permitted in respect of food products manufactured and/or produced in India.

(v) **Other Financial Services**: The FDI Policy 2016 provided that an NBFC having FDI under the automatic route is permitted to engage in only 18 specified NBFC activities, subject to minimum capitalization norms prescribed under the FDI Policy, 2016. Financial activities other than those 18 specified NBFC activities required prior approval of the Government. The Press Note 6 (2016 Series) dated October 25, 2016 permits 100% FDI under the automatic route in any financial services activities, provided the activities are regulated by financial sector regulators such as RBI, Securities and Exchange Board of India, Pension Fund Regulatory and Development Authority, Insurance Regulatory Authority of India etc. Further, minimum capitalization norms as mandated under FDI Policy 2016 for foreign investment in NBFCs are no more applicable and hence the same are done away with, considering the financial regulators prescribe their own set of capitalization norms. This was much awaited change, which is likely to provide a level playing field in the concerned sector.

(vi) **Private Security Agencies**: The FDI Policy 2016 permitted FDI upto 49% under government approval route in Private Security Agencies. Press Note 5 (2016 Series) allows FDI up to 49% under automatic route and beyond 49% and upto 74% is permitted through government approval route.

(vii) **Pharmaceutical Sector**: The earlier FDI policy on pharmaceutical sector provided for 100% FDI under automatic route in greenfield pharma and FDI up to 100% under government approval in brownfield pharma. The FDI Policy 2017 permits 74% FDI under automatic route in brownfield pharmaceuticals and beyond 74% will be permitted through Government approval route.

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