



Report of the Committee

on

**'Rationalisation of Investment Routes and Monitoring of
Foreign Portfolio Investments'**

Chairman

Shri. K.M. Chandrasekhar

June 12, 2013

K. M. Chandrasekhar
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Sub: Committee on Rationalization of investment Routes and Monitoring of Foreign Portfolio Investments.

Dear Mr. Sinha.

I am delighted to submit the final report of the Committee set up by SEBI on December 6, 2012, inter-alia, to prepare a draft guideline and regulatory framework for an integrated policy on foreign investments, keeping as a starting point, the recommendations of the Working Group on Foreign Investment in India (WGFI), for consideration of the Government. The details of the committee members are placed below in the report.

It was indeed a great privilege for me to chair this distinguished Committee, and I am thankful to you for giving me this opportunity. In carrying out the task assigned to it, the Committee met several times to deliberate the issues and it benefited enormously from such deliberations. Further, two separate Sub Committees, which were constituted during the course of the first meeting of the Committee, also discussed various issues and provided valuable recommendations to the Committee.

I am thankful to all the members of the Committee, who actively participated in the discussions and provided valuable inputs.

The Committee also wishes to convey its sincere gratitude to Mr. S Raman, Whole Time Member, SEBI for his key role played in fruitful deliberations and also the support given by Mr. SVMR Rao, Executive Director. Further, the Committee would like to convey its deep appreciation for the professional, logistical and organizational help by the officials of SEBI including Mr. S Madhusudanan, DGM, Ms. Priyanka Mahapatra, AGM, Mr. Afanu Pan, AGM, Mr. Sandeep Kriplani, AGM, Mr. Rohit Dubey, AGM, Mr. Praveen Kamat, AGM, Mr. Rahul Pawar, Assistant Manager and Ms. Nilima Karandikar, Secretary.

I hope that this report and subsequent discussions will enable the Government to take the policy actions as recommended in this report. It is felt that recommendations would help India to become a preferred investment destination by foreign investors.

Yours sincerely,



K. M. Chandrasekhar

Shri U. K. Sinha,
Chairman, Securities and Exchange Board of India,
Mumbai

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1. Executive Summary

SEBI Board in its meeting held on October 06, 2012 decided that SEBI will prepare a draft guideline based on the guidance of the WGFI, for consideration of the Government of India (GoI). It was also decided that SEBI/RBI will create necessary regulatory framework based on the guidelines, which will be laid down by the GoI.

To implement the above, SEBI formed a “Committee on Rationalization of Investment Routes and Monitoring of Foreign Portfolio Investments” (hereinafter referred to as “Committee”) under the Chairmanship of Shri K. M. Chandrasekhar, comprising of representatives from GoI, RBI and various market participants.

This report of the committee describes the various portfolio investment routes which are currently available to foreign investors and suggests a draft guideline and regulatory framework for rationalization of foreign portfolio investments, keeping as a starting point, the recommendations of the Working Group on Foreign Investment in India (WGFI), for consideration of the Government.

This report also provides recommendations for a harmonized model of investment routes designed to overcome the shortcomings of multiple routes that exist today.

1.1. Features of the Harmonized Model

The Committee has recommended creation of a single route for various Foreign Portfolio Investors (FPI) by merging the present day FII, Sub Account and QFI regimes where there will be common market entry, limit monitoring and reporting norms. However, there will be segregations for applying risk based Know Your Customer (KYC) norms, Investment guidelines and restrictions.

The Committee felt that NRIs/PIOs presently have a liberal route for accessing securities market. NRIs/PIOs should continue to be viewed as a distinct market participant enjoying certain privileges in terms of investment permissions not available to foreign investors. Accordingly, the Committee recommended to retain NRIs as a separate investor class with the same limits as currently applicable (i.e. 10% of the paid up capital of the investee company).

The Committee felt that FVCI route has certain benefits such as non applicability of pricing norms and relaxation from post IPO lock in requirement. These benefits have been given to FVCI route to promote Venture Capital Investments. Accordingly, the Committee recommended that the FVCI as an investor class would continue. Additionally, the Committee recommended that the current FVCI regime should be expanded to include more sectors under its ambit as against the currently prescribed 9 sectors.

The features of the Harmonized Model are described below:

1.1.1. Foreign Portfolio Investor (FPI)

The Committee recommended for merging of FII, Sub Account and QFI into a new investor class to be termed as “Foreign Portfolio Investor” (FPI).

1.1.2. Simplification of entry norms for FIIs, Sub Accounts, and QFIs

The committee recommended that FPIs would not be required to obtain direct registration with SEBI. Instead, DDPs authorized by SEBI would register FPIs on behalf of SEBI subject to compliance with KYC requirements. The FPI that meet the prescribed eligibility criteria shall directly approach Designated Depository Participants (DDPs), authorised by SEBI. The DDPs shall perform due diligence and KYC, before registering FPI, on behalf of SEBI, and allowing such entities to make investment in permitted securities.

1.1.3. Uniform entry norms for Foreign Portfolio Investor

It is recommended that all the categories of portfolio investors be termed as FPIs. The FPI shall be a resident in a country, whose securities market regulator is a signatory to IOSCO’s MMOU (Appendix A Signatories) or a signatory of a bilateral MOU with SEBI. In case of a Bank, it should be resident of a country whose central bank is a member of BIS.

Provided that the person is not resident in a country listed in the public statements issued by FATF (high risk and non-compliant countries) from time to time.

1.1.4. Categorization of Foreign Direct Investment (FDI) and Portfolio investment

The Committee recommended the following with respect to categorization of foreign investment:

- i. Portfolio investments to be defined as investments by any single investor or investor group, which shall not exceed 10 percent of the equity securities including the future conversion of existing convertible securities such as Compulsorily Convertible Debentures (CCD) Compulsorily Convertible Preference Shares (CCPS) of an Indian company.

- ii. Portfolio investment shall be permitted only in listed equity securities. For this purpose, listed equity securities would also include participation by FPIs in issues such as Initial Public Offer, Qualified Institutional Placement, Institutional Placement Programme etc. of Indian companies as well as tendering shares in an open offer or buyback announced in relation to shares of listed Indian companies.
- iii. The prevailing practice where private placement may be through either FPI (for example a QIP issue) or FDI route depending on the nature of the transaction may be continued.
- iv. In case of unlisted company, the private placement shall be under FDI route.
- v. In circumstances, where the listing does not take place within the stipulated timeframe, such foreign investments shall be re-categorized as FDI.
- vi. Investments in unlisted securities, regardless of the level of ownership that they represent, shall be regarded as FDI.
- vii. Where there is an FDI investor, all equity holdings of such an investor in the concerned company, regardless of the manner in which such equity holdings have been acquired, should be classified as FDI.
- viii. Where an investor initially acquires less than 10 percent of the voting equity of an Indian company and thereafter acquires additional equity which takes the investor's aggregate holding to over 10 percent, in such a scenario, all of the investor's holdings should be classified as FDI.
- ix. Where an investor has FDI holdings in excess of 10 percent of the voting equity of a company it will retain its FDI classification even if the investor were to dilute his holding to a level below 10 percent of the voting equity of the company.
- x. Investment classification and tracking could be accomplished through the DDPs.

1.1.5. Risk Based Approach towards KYC

From the point of view of KYC, the committee recommended for following categorization of FPIs based on their perceived risk profile:

Category	Eligible Foreign Investors	Perceived Risk Profile
I	Government and Government related foreign investors such as Foreign Central Banks, Governmental Agencies, Sovereign Wealth Funds, International/ Multilateral Organizations/ Agencies	Low Risk As these entities are either owned/ controlled by respective government they are perceived to be low risk entities.
II	<p>a) *Appropriately regulated broad based funds such as Mutual Funds, Investment Trusts, Insurance/Reinsurance Companies, Other Broad Based Funds etc.</p> <p>b) *Appropriately regulated entities such as Banks, Asset Management Companies, Investment Managers/ Advisors, Portfolio Managers etc.</p> <p>c) Broad based funds whose investment manager is appropriately regulated</p> <p>d) University Funds and Pension Funds</p> <p>e) University related Endowments already registered with SEBI as FII/Sub Account</p>	Moderate Risk Generally, these entities are either pooled investment vehicles or institutions that manage portfolios of pooled vehicles. Since these entities are appropriately regulated in their respective home jurisdictions or corpus of the fund is for post retirement benefits of the employees/ academic research etc., these are perceived to be moderate risk entities
III	All other FPIs not eligible under Category I and II such as Endowments, Charitable Societies/ Trust, Foundations, Corporate Bodies, Trusts, Individuals, Family Offices, etc.	High Risk Generally, these entities are not regulated in their respective home jurisdictions, these entities are perceived as high risk entities.

**Appropriately Regulated is meant to include relevance of activity i.e. securities market regulations in case of an entity related to investment segment, capital market activities; and the Banking Regulations in case of a banking entity.*

1.1.6. Other recommendations related to KYC

- i. The requirement of submitting personal identification documents such as copy of passport, photograph etc. of the designated officials of FPIs belonging to Category I and Category II shall be done away with.
- ii. Specific Provision of PML Rules especially Rule 9 may be amended to adopt risk based approach for KYC.
- iii. To permit DDPs for placing reliance on Global Custodian/Banks for KYC while on boarding the investor. .
- iv. For updation of KYC documents, it is recommended to follow a 2 year/ 5 year rule based on the risk classification of the investor as per above i.e. 2 years for non low risk investors and 5 years for low risk investors.

1.2. Roadmap for Integration

1.2.1. Eligibility of DDP

It will be mandatory for FPI to appoint a DDP. The DDP would perform due diligence and KYC of FPIs as per the stipulated norms.

It is suggested that the DDP shall meet all of the following eligibility criteria in order to service FPIs.

- i. DDP to be a Custodian registered with SEBI.
- ii. DDP to be an Authorised Dealer Category 1 bank as per RBI.
- iii. DDP to be a Depository Participant registered with SEBI.
- iv. DDP to have multinational presence either through its branches or through agency relationships with intermediaries regulated in their respected home jurisdictions.
- v. DDP to demonstrate that it has systems and procedures to comply with the FATF Standards, Prevention of Money Laundering (PML) Act, Rules and SEBI circulars issued from time to time; and
- vi. DDP to obtain prior approval of SEBI before commencing the activities relating to opening of accounts of FPIs.

Based on the experience gathered, the eligibility criteria for registration of DDP may be later reviewed by SEBI.

1.2.2. Grandfathering Arrangements

- i. To avoid business discontinuity, it is recommended to grandfather all entities which are presently registered with SEBI as custodian of securities, as DDPs. The existing QDPs authorised by SEBI currently not meeting the proposed eligibility criteria may be allowed further time period of one year to comply with the proposed eligibility requirement of a DDP. Subsequently, if such QDPs fail to comply with the same, then they may be required to surrender the authorization.
- ii. It is recommended that all existing investments held by the FPIs acquired through either FDI route and/or PIS route shall be grandfathered.
- iii. It is recommended that all existing entities registered with SEBI as FII, sub-account, and QFIs as on the effective date, shall be deemed to be FPIs.

1.2.3. Operational Guidelines

The Committee recommended the following broad operational guidelines. However, committee was also of the view that operational guidelines/ framework may be prescribed by SEBI from time to time.

- i. The committee recommended that FPIs would not be required to obtain direct registration with SEBI. Instead, DDPs authorized by SEBI would register FPIs on behalf of SEBI subject to compliance with KYC requirements.
- ii. Orders shall be placed directly by the FPI with SEBI registered Stock Brokers on the same lines as the present framework applicable to FIIs.
- iii. Appointment of DDP shall be mandatory for all categories of FPIs. All settlement of transactions by FPIs must be done through DDP acting as a Custodian.
- iv. FPIs shall be permitted to transact in all the securities where FIIs are presently permitted and any other instruments as permitted from time to time.
- v. Margins and risk management framework as applicable in the capital market will apply.
- vi. The Committee recommended that under the proposed FPI regime, category III FPIs will not be allowed to issue PNs/ODIs. The committee also recommended that those broad based funds, belonging to Category II, which are not directly regulated by the appropriate regulator in their home jurisdiction, should not be allowed to issue ODIs/PNs. The ODIs/PNs issuer FPIs will continue to report

directly to SEBI, the details of ODIs/PNs on a regular basis, as prescribed by SEBI.

1.2.4. Investment Limits

- i. The Investor and DDP shall ensure that the total shareholding held by the FPI shall not exceed 10% of paid up equity capital of the company at any point of time. This investment limit shall be applicable to each class of equity shares having separate and distinct ISIN. Where more than one FPI have same common beneficial owner, all such FPIs shall be together treated as one FPI for the purpose of this investment limit.
- ii. Aggregate shareholding of all FPIs shall not exceed the lower of (i) 24% of the paid up equity capital of the company at any point of time or (ii) the sectoral cap, in respect of each equity share class having separate and distinct ISIN.
- iii. In case the company raises their foreign ownership limit to the sectoral cap as per the FDI policy, then the foreign ownership will be monitored at that level.
- iv. The monitoring of investment limits at the individual level may be monitored by the respective DDPs.
- v. Dissemination of FPI investment data shall be carried out by the depositories.
- vi. Prohibitions imposed on foreign investments by FEMA, shall apply to FPIs.

1.2.5. Legal Requirements

The process for evolving an integrated policy on foreign investments would entail the following amendments/modifications in the legal framework:

- i. FII regulations prescribed by SEBI and QFI framework prescribed by SEBI and the RBI would be required to be repealed and replaced by a new framework for FPIs.
- ii. FEMA (Transfer or Issue of Security by a Person Resident Outside India) Regulations, notably Regulations 5 (2), 5(6), 7A, 8 and Schedule 2, 5, 8 and other related provisions would have to be amended and replaced to prescribe the permissible caps and investment levels applicable to foreign portfolio investor;

- iii. Necessary amendments in FEMA to replace references to FIIIs with FPIs;
- iv. Necessary amendments to PML Rules;
- v. Necessary amendments in Income Tax Act, 1961;
- vi. General permission granted by RBI to FIIIs dated December 17, 2003;
- vii. GoI Guidelines dated September 14, 1992;
- viii. RBI's Foreign Exchange Management framework
- ix. Necessary amendment to the following regulations are needed to replace references to FIIIs and QFIIs and recognize the FPIIs-
 - a. Consolidated FDI Policy dated April 5, 2013 (more particularly paragraphs 2.1.14, 2.1.32, 3.1.4, 3.1.5, 3.1.7, 3.2.5(f), 3.6.2 (vi), 4.1.2, 6.2.7.5, 6.2.8.1, 6.2.8.2, 6.2.15.1.1., 6.2.17.1, 6.2.17.2, 6.2.17.4.2, 6.2.17.4.3, 6.2.17.5, 6.2.17.6., 6.2.19, paragraphs 3 and 5 of the Format of Form FC-GPR, paragraphs 2.2, 2.3, 4, 5.1(iii) and (vii), 6.5 of Annex -2, Format of Annual Return on Foreign Liabilities and Assets, Form FC-TRS, Form DR;
 - b. RBI Master Circular on Foreign Investment In India dated July 2, 2012 (Section II, Section IV (3), (5), (6), Section V(6) to make changes corresponding to the changes in the Consolidated FDI Policy in relation to references to FIIIs while calculating the sectoral cap);
 - c. SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (Regulations 2(za), 2(zb), 2(zd)(ii));
 - d. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (Regulation 2(q)(2)(ix)) ;
 - e. The SEBI Act, 1992 (Section 12(1A))

To avoid too many individual legislative amendments, it is also suggested that a clause may be introduced in the respective legislations stating that the term "FII" in the legislations shall mean "FPI registered with DDP authorised by SEBI".

2. Background

2.1. Working Group on Foreign Investment in India

During November 2009, the Ministry of Finance (MoF) set up a working group called Working Group on Foreign Investment in India (WGFI), headed by the then UTI Mutual Fund Chief Shri U. K. Sinha, with a view to rationalize the present arrangements relating to foreign portfolio investments by Foreign Institutional Investors (FII)/ Non Resident Indians (NRI) and other foreign investors like Foreign Venture Capital Investor (FVCI) and Private Equity entity etc.

A summary of major recommendations made by WGFI in its report submitted during July 2010 is listed in the table below:

Sr. No.	Summarised WGFI Recommendations
1	Single window for registration and clearance of portfolio investment regulations that does not distinguish between investor classes
2	Qualified DP with global presence through branch network and agency relationship would be legally responsible for enforcing OECD standard KYC requirement
3	Such Global DPs would have higher capital requirements and would need to pass a detailed "fitness test" administered by SEBI.
4	FII, FVCIs and NRIs would be abolished as an investor class
5	Promulgate broader KYC requirements that meet OECD standard practiced and also adhere to PMLA rules and regulations
6	Consistent with Lahiri Committee recommendations, in areas where there are no separate ceilings by an Act of Parliament, QFI investment ceilings should be reckoned over and above prescribed FDI sectoral caps
7	SEBI to have final right to demand details about end investor with regard to PNs
8	FII Regulations would be replaced by a new QFI regulations
9	Schedules specifying permitted investments by FIIs, FVCIs, and NRIs would ostensible be replaced by a new schedule for QFIs
10	All entities structuring and offering securities market related products in overseas markets, who offer these products to residents on Indian soil should be registered with SEBI
11	Remove the caps on rupee denominated corporate debt. Any desired restrictions on debt related capital flows could be expressed in percentage instead of absolute terms.
12	Grandfather existing FVCI investments to avoid business discontinuity for existing firms

13	Consider amending the consolidated FDI policy to exempt SEBI registered QFI s from seeking approval of the government prior to investing in a DVF incorporated as a Trust
14	(i) SEBI FVCI and FII Regulations would be replaced by new QFI Regulation (ii) FEMA (Transfer or issue of security by a person resident outside India) Regulations would have to restate permissible caps and investment levels, now unified, across asset classes (iii) Schedules specifying permitted investment by FIIs, FVCIs and NRIs would ostensible replaced by a new schedule for QFIs.
15	Closely review how and whether regulation tailored to fit specific classes of investors like FVCIs and NBFCs will be included, excluded or modified under the QFI framework
16	All entities structuring and offering securities market related products in the overseas market, who offer these products to residents on Indian soil, should register with SEBI and fully disclose all promotional materials, including product literature, advertisements and brochures
17	(i) Capital flows management regulations should focus on spot instruments and not derivatives (ii) Harmonize the regulation of futures, forwards, and options. There should be a general policy preference to encourage greater trade in exchange-traded, as opposed to over-the-counter derivatives; (iii) Streamline registration processes by implementing QFI model, as suggested above, to reduce the incentives to participate in offshore markets such as those for participatory notes.
18	Qualified DPs with global presence would be made responsible for enforcing KYC requirements with respect to foreign investors
19	Shifting taxation of capital gains earned by foreign investors from the existing source based system to residence based one.

2.2. Formation of Committee on Rationalization of Investment Routes and Monitoring of Foreign Portfolio Investments

SEBI Board in its meeting held on October 06, 2012 decided that SEBI will prepare a draft guideline based on the guidance of the WGFI, for consideration of the Government of India (GoI). It was also decided that SEBI/RBI will create necessary regulatory framework based on the guidelines, which will be laid down by the GoI.

Accordingly, in order to implement the Board's above decision, SEBI, formed a "Committee on Rationalization of Investment Routes and Monitoring of Foreign Portfolio Investments" (hereinafter referred to as "the Committee"), under the Chairmanship of Shri K. M. Chandrasekhar, comprising of representatives from GoI, RBI and various market participants to review and make recommendations on the following issues:

1. To prepare a draft guideline and regulatory framework for an integrated policy on foreign investments, keeping as a starting point, the recommendations of the Working Group on Foreign Investment in India (WGFI), for consideration of the Government.
2. To devise a framework for according preferential treatment to long term investors such as Sovereign Wealth Funds and pension funds for allocation of debt limits.
3. To examine the feasibility of the proposal forwarded by RBI with respect to the monitoring of foreign investment by FIIs/NRIs under the portfolio investment scheme in Indian companies.
4. To determine the feasibility of allowing FIIs to invest in Pass Through Certificates (PTC).

The committee decided to review and provide recommendations primarily with respect to issue mentioned above at Sr. No. 01. The committee further decided that SEBI and RBI would address the issues mentioned above at Sr. Nos. 2, 3 and 4 separately.

2.2.1. Sub Committee on KYC

The Sub Committee on KYC was constituted to assess whether a uniform approach or a risk based approach should be followed towards KYC for FPIs. The broad terms of reference of the sub-committee were as follows:

- i. Simplification of entry norms for different categories of foreign portfolio investors such as FII, sub-accounts, QFI, FVCI and NRIs;
- ii. Uniform entry norms for FPIs;
- iii. Eligibility criteria for designated Depository Participant;
- iv. Approach towards KYC;
- v. To suggest minimum documentation requirements for KYC in respect of all the proposed categories of foreign portfolio investors;
- vi. To review the existing KYC norms applicable to NRIs such as the document attestation options for NRIs based on the inputs to be provided by Ministry of Overseas Indian Affairs etc;
- vii. To suggest suitable modifications in Rule 9 of PML Rules on the basis of inputs to be provided by Department of Revenue, Ministry of Finance.

2.2.2. Sub Committee on Treatment of Foreign Investments

The Sub Committee on Treatment of Foreign Investments was formed to examine in detail the difficulties in implementation of the proposal of categorization of foreign investment as FDI and portfolio investment based on a threshold of 10 percent.

It was decided to refer the following terms of reference to the aforesaid sub-committee:

- i. To provide recommendations with respect to NRI and FII investments in Indian companies as against permissible investment limits and to assess the impact of possible volatility in the market due to proposed increase in aggregate foreign portfolio investment limits consequent to merging of FII, QFI and NRI investments limits.
- ii. To identify requisite amendments needed in the Income Tax Act, 1961 consequent to proposed integration of the various routes for foreign portfolio investors.
- iii. To provide recommendations to a separate committee constituted by the Government of India namely "Committee for Rationalizing the Definition of FDI and FII", which would examine and work out the details of the application of the principle internationally for defining FDI and FII.

2.3. Union Budget Proposals

The Hon'ble Finance Minister while presenting the Union Budget for the year 2013-14, inter-alia made the following budget proposals:

1. *"There are many categories of foreign portfolio investors such as FIIs, Sub-Accounts, QFIs etc. and there are also different avenues and procedures for them. Designated depository participants, authorised by SEBI, will now be free to register different classes of portfolio investors, subject to compliance with KYC guidelines."*
2. *"SEBI will simplify the procedures and prescribe uniform registration and other norms for entry of foreign portfolio investors. SEBI will converge the different KYC norms and adopt a risk-based approach to KYC to make it easier for foreign investors such as central banks, sovereign wealth funds, university funds, pension funds etc. to invest in India."*
3. *"In order to remove the ambiguity that prevails on what is Foreign Direct Investment (FDI) and what is Foreign Institutional Investment (FII), I propose to follow the international practice and lay down a broad principle that, where an investor has a stake of 10 percent or less in a company, it will be treated as FII and, where an*

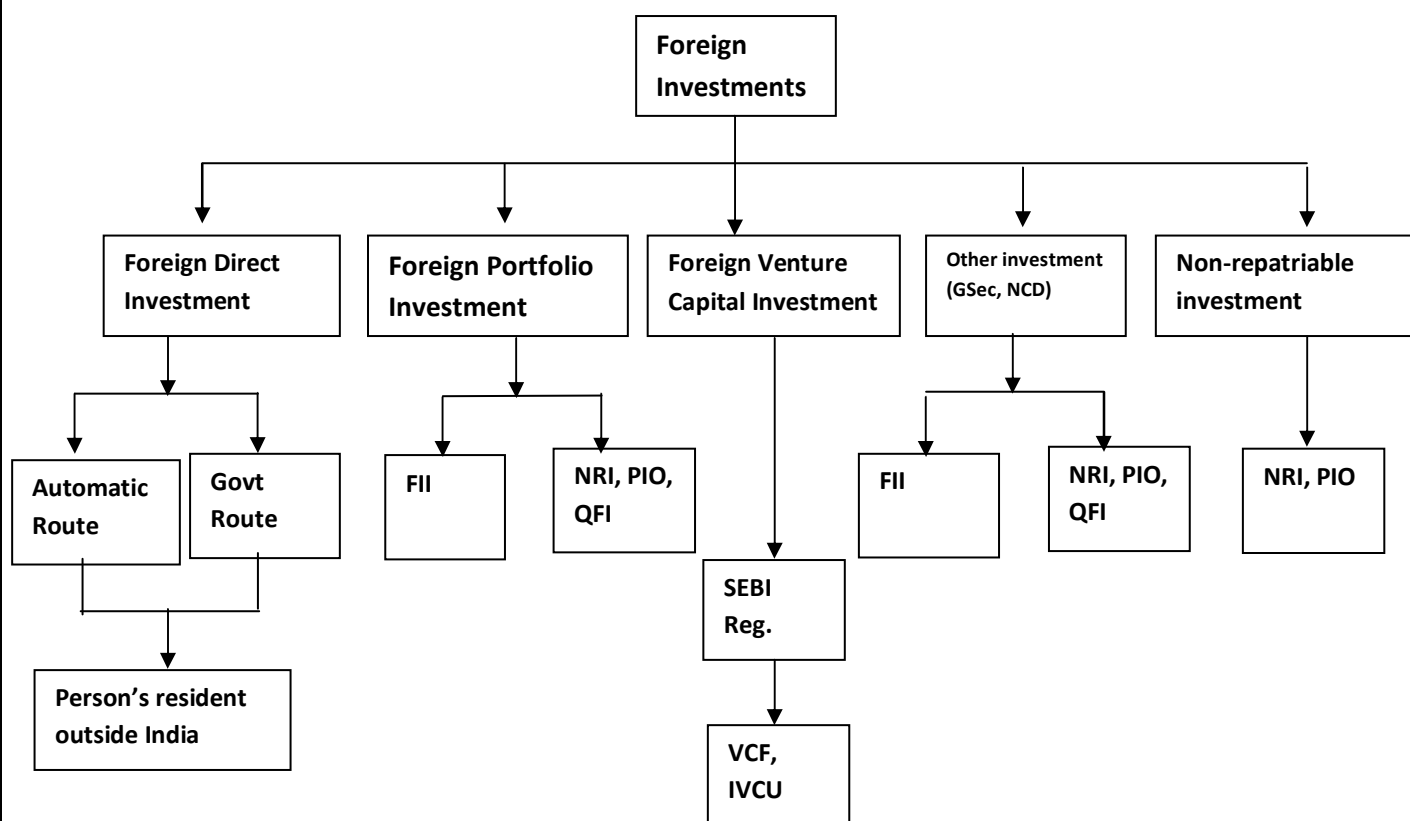
investor has a stake of more than 10 percent, it will be treated as FDI. A committee will be constituted to examine the application of the principle and to work out the details expeditiously.”

Regarding the proposal mentioned above at Sr. No. 3, the Committee decided to provide recommendations to a separate committee constituted by the Government of India namely “Committee for Rationalizing the Definition of FDI and FII”, which would examine and work out the details of the application of the international principle for defining FDI and FII.

3. Present Regulatory Framework for Foreign Investment in India

At present foreign investment in India is channelized through the following routes as depicted in the figure:

FOREIGN INVESTMENT ROUTES IN INDIA



Source: Master Circular dated July 02, 2012 issued by the Reserve Bank of India (RBI)

Foreign investment in India is primarily channelized in three forms:

1. Foreign Direct Investment
2. Portfolio Investment Scheme
3. Foreign Venture Capital Investment

3.1. Foreign Direct Investment (FDI)

Under the Consolidated FDI Policy issued by the Department of Industrial Policy and Promotion (DIPP), Ministry of Commerce and Industry, GoI, a non-resident entity can invest in India, subject to the FDI Policy except in those sectors/ activities which are prohibited.

However, a citizen of Bangladesh or an entity incorporated in Bangladesh can invest only under the Government route. Further, a citizen of Pakistan or an entity incorporated in Pakistan can invest, only under the Government route, in sectors/activities other than defence, space and atomic energy and sectors/ activities prohibited for foreign investment.

These investments are subject to the extant Foreign Exchange Management Act (FEMA) Regulations and extant FDI policy including sectoral caps.

An Indian company may receive FDI under the two routes as given under:

- i. Automatic Route
- ii. Government Route

FDI is allowed under the automatic route without prior approval either of GoI or RBI in all activities/sectors as specified in the consolidated FDI Policy, issued by the Government of India from time to time.

FDI in activities not covered under the automatic route requires prior approval of GoI which are considered by the Foreign Investment Promotion Board (FIPB), Department of Economic Affairs, Ministry of Finance.

The Indian company having received FDI either under the Automatic route or the Government route is required to comply with provisions of the FDI policy including reporting the FDI to RBI.

3.2. Portfolio Investment Scheme (PIS)

Portfolio Investment Scheme (PIS) allows eligible investors such as Foreign Institutional Investors Non Resident Indians (NRIs), Persons of Indian Origin (PIOs) and Qualified Foreign Investors to invest in shares and convertible debentures of Indian companies, and units of domestic mutual funds at any of the Indian stock exchanges.

This investment can be done under repatriation or non-repatriation basis in respect of shares or convertible debentures sold or purchased through a registered stock broker on a recognized stock exchange.

Under the Foreign Portfolio Investment route, the following entities are allowed to invest:

- i. Foreign Institutional Investors (FIIs) and Sub Accounts,
- ii. Non Resident Indian (NRIs)/ Person of Indian Origin (PIOs),and
- iii. Qualified Foreign Investors (QFIs)

3.2.1. FIIs and Sub Accounts

In terms of SEBI (Foreign Institutional Investor) Regulations, 1995, "Foreign Institutional Investor" means an institution established or incorporated outside India which proposes to make investment in India in securities. "Sub Account" means any person resident outside India, on whose behalf investments are proposed to be made in India by a foreign institutional investor and who is registered as a sub-account under these regulations.

The Reserve Bank of India (RBI), has granted general permission to SEBI Registered FIIs to invest in India under the PIS route. The registration given by SEBI also operates as approval under Foreign Exchange Management Act, 1999 (FEMA) to invest in India.

3.2.1.1. Registration Requirements

- i. As per the present regulations, the following categories are eligible for grant of FII registration:
 - a. Fund Category: Pension Fund, University fund, Endowment, Foundation, Charitable Trust, Mutual Fund, Investment Trust, Charitable society, Foreign Central Bank, Sovereign Wealth Fund (SWF), Foreign Governmental Agency, International/Multilateral agency, Insurance/Reinsurance Company, Broad Based Fund
 - b. Non Fund Category: Investment Manager/Advisor, Trustee of trust, Bank, Asset Management Company, Institutional Portfolio manager
- ii. An FII applicant should be regulated in its home jurisdiction. Following categories are granted FII registration even though they may not be regulated in home jurisdiction:

- a. University funds;
 - b. Endowments;
 - c. Foundations;
 - d. Charitable trusts; and
 - e. Charitable societies
- iii. Track record, professional competence, financial soundness, experience, general reputation of fairness and integrity of the FII applicant are considered for granting registration.
- iv. Sub-accounts can be registered under one of the following categories:
 - a. Broad based fund,
 - b. broad based portfolio,
 - c. university fund,
 - d. endowment,
 - e. foundation,
 - f. charitable trust,
 - g. charitable society,
 - h. foreign corporate,
 - i. foreign individual,
 - j. sovereign wealth fund and
 - k. Proprietary fund of the FII.
- v. The broad based criteria have been defined as 20 investors with no single investor having stake of more than 49%. A foreign corporate seeking registration as sub-account must have asset base of not less than two billion US dollars, average net profit of not less than fifty million US dollars during the three financial year preceding the date of application. A foreign individual must have network of not less than fifty million US dollars.
- vi. The FII is required to enter into an agreement with domestic custodian to act as custodian of securities and also appoint a branch of a bank approved by Reserve Bank of India for opening of foreign currency denominated account and a special non-resident rupee account.
- vii. The registration fee for an FII is USD 5,000 for every block of three years. The validity of registration of FII is permanent, subject to payment of fees every block of three years. The registration fees for Sub account is USD 1,000. The validity of registration of sub account is co-terminus with that of its FII.

3.2.1.2. Investment Opportunities

Presently, an FII can make investment in the following types of securities:

- i. Securities in primary and secondary markets including shares, debentures and warrants of companies, unlisted, listed or to be listed on a recognized stock exchange in India;
- ii. Units of mutual funds/ schemes floated by a Collective Investment Scheme;
- iii. Dated Government Securities, other debt instruments;
- iv. Derivatives traded on a recognized stock exchange;
- v. Commercial papers;
- vi. Security Receipts (sub-accounts cannot invest in SRs)
- vii. Indian Depository Receipts (IDR)

3.2.1.3. Account Opening

Before an FII starts to make investment, it needs to put in place the following, apart from SEBI registration:

- i. Appoint a Custodian of securities – The custodian of securities acts as an agent of FII and is the Power of Attorney (POA) holder.
- ii. Obtain PAN from Income Tax Department.
- iii. Open a demat account with a SEBI registered depository participant;
- iv. Open a Special Non-resident Rupee Account (SNRA) with any AD-1 bank;
- v. Open a trading account with a SEBI registered stock broker/ trading member, and obtain a Unique Client Code (UCC) with stock exchange(s);
- vi. Appoint a Tax Consultant/ Chartered Accountant for computation of taxes and certification that the relevant taxes have been paid.

FII can repatriate back any amount from his bank account, provided all taxes have been paid on such amount.

- vii. The custodian of securities generally assists the FII in opening all the requisite accounts. The custodian of securities also acts as clearing member of the FII and performs clearing and settlement functions for its FII clients.

3.2.2. Non Resident Indian (NRI)/ Person of Indian Origin (PIO)

As per RBI, Non Resident Indian (NRI) is defined as a person resident outside India who is citizen of India. In terms of Regulation 2 of FEMA Notification No.13 dated May 3, 2000, NRI means a person resident outside India who is a citizen of India. PIO means a citizen of any country other than Bangladesh or Pakistan who had:

- i. At any time held Indian passport or
- ii. He or either of his parents or any of his grandparents was a citizen of India by virtue of the Constitution of India or the Citizenship Act, 1955 or
- iii. The person is a spouse of an Indian citizen or a person referred to in (a) or (b).

Investment by PIOs in Indian Securities is treated same as the investment by NRIs and requires same approvals and enjoys the same exemptions.

3.2.2.1. Market Entry

NRIs/PIOs are eligible to purchase and sell shares / convertible debentures of Indian Companies, through a registered broker on a recognized stock exchange in India, if they have been permitted by the designated branch of any AD Category - I bank (which has been authorized by RBI to administer the PIS). RBI issues permission to specific bank branches for starting PIS activities which are then termed as Designated Bank Branches (DBBs).

NRIs/PIOs are required to approach the DBBs to register under PIS. On behalf of RBI, DBB issues PIS approval letter to the NRI/PIOs. The Non Designated Bank Branches (NDBBs) are not permitted to open PIS accounts. Hence, if the customer approaches any of the NDBBs, the said Bank Branch can accept the application from the NRI customers and forward the same to the DBB to complete the formalities for PIS account opening.

3.2.2.2.Account Structure

To invest through recognized Stock Exchange in India, the NRIs/PIOs are permitted to open the following types of bank/demat accounts:

i. **Non Resident External (NRE) PIS Savings Bank or Non-Resident Ordinary (NRO) PIS savings bank account**

The NRE PIS account is opened exclusively for making payments/receiving amount of sale proceeds for the investments made in shares/convertible debentures on repatriation basis in secondary market. Similarly, the NRO PIS account is opened exclusively for making payments/ receiving amount of sale proceeds for the investments made in shares /convertible debentures on non-repatriation basis in secondary market. For opening NRE PIS / NRO PIS account, an NRI/PIO has to submit a RPI / NRI application form respectively and give sufficient details of investments held by him along with other legal and procedural documents required by the concerned Designated Bank Branch.

ii. **NRE Saving Bank account or NRO Saving Bank account**

The NRE / NRO savings bank account is required to be opened for recovering bank charges and to route non PIS transactions.

iii. **NRE or NRO Demat Account**

The demat account is to be opened with any DP for the purpose of trading in Shares. NRI/PIO can open a demat account with any Depository Participant (DP). The NRI/PIO needs to mention the type 'NRI' as compared to 'Resident' and the sub-type 'Repatriable' or 'Non-Repatriable' in the account opening form collected from the DP. An NRI/PIO must open separate demat accounts for holding 'repatriable' and 'non-repatriable' securities. No permission is required from RBI to open a demat account. However, credits and debits from demat account may require general or specific permissions as the case may be, from designated authorised dealers.

3.2.2.3.Funding and Repatriation

Payment for purchase of shares and/or debentures on repatriation basis has to be made by way of inward remittance of foreign exchange through normal banking channels or out of funds held in NRE/FCNR (B) account maintained in India. If the

shares are purchased on non-repatriation basis, the NRIs/PIOs can also utilise their funds in NRO account in addition to the above.

An NRI/PIO can purchase shares in foreign exchange by funding it through NRE Saving Bank Account. On sale of such shares the sale proceeds amount can be freely repatriated, net of application taxes. He can also purchase shares in rupees through NRO Saving Bank Account. However, sale proceeds amount of these shares cannot be freely repatriated out of India, subject to FEMA, 1999.

3.2.2.4.Nature of Transactions Allowed

NRIs are eligible to purchase and sell shares / convertible debentures of Indian Companies, through a registered broker on a recognized stock exchange in India. NRIs are eligible to purchase and sell Units of Mutual Funds.

3.2.2.5.Nature of Transactions not covered under PIS

Purchase and sale of shares otherwise than on recognized stock exchange in India come under this category:

- i. Shares acquired during Residential tenure,
- ii. Initial Public Offer (IPO) shares,
- iii. Shares received by way of Gift,
- iv. Shares received by way of Inheritance,
- v. Acquisition and Sale of Bonus shares,
- vi. Right Shares
- vii. Shares acquire under FDI.

As per Schedule 3 (Regulation 5) of FEMA Act, 1999, NRIs have to take delivery of the shares / convertible debentures purchased and give delivery of the shares / convertible debentures sold under the PIS scheme within prescribed time frame. Therefore, an NRI investor can execute only delivery based transactions and cannot indulge in short selling, speculative, no delivery and other such transactions where delivery of shares is not undertaken.

3.2.2.6.Other Investment Guidelines

- i. Any NRI can have only one PIS account in India at a time.
- ii. It is mandatory to comply with all the rules and regulations prescribed by RBI and other regulatory authorities for all the NRI investors.

- iii. Securities received by NRI against investments under 'Foreign Direct Investment scheme (FDI)', 'Portfolio Investment scheme (PIS)' and 'Scheme for Investment' on non – repatriation basis have to be credited into separate demat accounts.
- iv. Investment under PIS can be on repatriation or non – repatriation basis. However, investment under FDI scheme can only be on repatriation basis.

3.2.2.7. Specified Limits of NRI Investments

NRI investment on repatriation/non- repatriation basis is subject to ceilings as mentioned below-

- i. NRIs can invest through designated ADs, on repatriation and non-repatriation basis under PIS route up to 5 per cent of the paid- up capital / paid-up value of each series of debentures of listed Indian companies.
- ii. The aggregate paid up value of shares / convertible debentures purchased by all NRIs cannot exceed 10 per cent of the total paid up capital of the company / paid up value of each series of debentures of the company.
- iii. The aggregate ceiling of 10 per cent can be raised to 24 per cent by passing a resolution of its Board of Directors followed by a special resolution to that effect by its General Body and should necessarily intimate the same to the Reserve Bank of India immediately as hitherto, along with a Certificate from the Company Secretary stating that all the relevant provisions of the extant Foreign Exchange Management Act, 1999 regulations and the Foreign Direct Policy, as amended from time to time, have been complied with.
- iv. The Designated Bank Branches are required to keep track of NRI individual investment limits and restrict its NRI customers from acquiring securities beyond the prescribed limits.
- v. The shares of those companies listed in Banned list (i.e. where NRI shareholding have crossed the prescribed limits) should not be further purchased by the NRIs at that point of time. However, the shares of those companies listed in Caution list (i.e. whose NRI shareholding limits has reached 2% below the ceiling limit) can further be purchased only by obtaining prior approval from RBI.

3.2.2.8. Reporting of NRI investments under PIS scheme

The link office of the designated branch of an AD Category – I bank furnishes to the Reserve Bank, a report on a daily basis on PIS transactions undertaken by it, on behalf of NRIs. It is the bank's responsibility to ensure that the data submitted to RBI is reconciled by periodically taking a NRI holding report for their bank.

3.2.3. Qualified Foreign Investors (QFIs)

QFI scheme was introduced by Government of India (GoI) during the year 2011, in consultation with SEBI and RBI, to permit foreign investors to invest in Indian equity shares, equity and debt schemes of Indian mutual fund and corporate debt in order to widen the class of investors, attract more foreign funds, reduce market volatility and to deepen the Indian capital markets.

3.2.3.1. Eligibility

QFIs include individuals, groups or associations, resident in a country that is a member of Financial Action Task Force (FATF) or a country that is a member of a group which is a member of FATF and resident in a country that is a signatory to International Organization of Securities Commission's (IOSCO) Multilateral Memorandum of Understanding (MMOU) (Appendix A Signatories) or a signatory of a bilateral MOU with SEBI. QFIs do not include FIIs/Sub accounts/ Foreign Venture Capital Investor.

3.2.3.2. Account Opening

- i. QFIs are required to open a demat account with any one of the SEBI approved qualified Depository Participant (QDP). QDP are also required to carry necessary due diligence and obtain appropriate declarations and undertakings from QFI in terms of extant framework.
- ii. QFIs are required to open a single non-interest bearing Rupee Account with an AD Category- I bank in India, for routing the receipt and payment for transactions relating to purchase and sale of eligible securities subject to the conditions as may be prescribed by RBI from time to time.
- iii. A QFI can open trading accounts with one or more SEBI registered stock brokers.

3.2.3.3. Eligibility of QDP

The eligibility criteria to act as qualified Depository Participants are as follows:

- i. DP shall have net worth of Rs. 50 crore or more;
- ii. DP shall be either a clearing bank or clearing member of any of the clearing corporations;
- iii. DP shall have appropriate arrangements for receipt and remittance of money with a designated Authorised Dealer (AD) Category - I bank;
- iv. DP shall demonstrate that it has systems and procedures to comply with the FATF Standards, Prevention of Money Laundering (PML) Act, Rules and SEBI circulars issued from time to time; and
- v. DP shall obtain prior approval of SEBI before commencing the activities relating to opening of accounts of QFI.

3.2.3.4. Permitted Investments

A QFI can make investments in the following:

- i. Equity and debt schemes of Indian mutual funds,
- ii. Equity shares listed on recognized stock exchanges,
- iii. Equity shares offered through public offers and
- iv. Corporate bonds listed/to be listed on recognized stock exchanges.
- v. G-Sec and T-Bills
- vi. Commercial Paper

3.2.3.5. Investment Limits

- i. The aggregate investments by QFIs in units of mutual fund schemes shall be subject to a total overall ceiling of US \$10 billion for equity schemes.
- ii. Total shareholding held by a QFI shall not exceed five percent of paid up equity capital of the company at any point of time. This investment limit shall be applicable to each class of equity shares having separate and distinct ISIN.

- iii. that aggregate shareholding of all QFIs shall not exceed ten percent of the paid up equity capital of the company at any point of time, in respect of each equity share class having separate and distinct ISIN.

3.2.4. Foreign Venture Capital Investors (FVCI)

Another route in which foreign investment is channelized into India is through investment by foreign venture capital investors. In terms of SEBI (Foreign Venture Capital Investors) Regulation, 2000 "foreign venture capital investor" means an investor incorporated and established outside India, registered under these Regulations and proposes to make investment in accordance with these Regulations.

3.2.4.1.Registration

- i. To seek registration under these regulations, FVCI entity shall make an application to SEBI in requisite Form along with the application fees of USD 2,500 and registration fees of USD 10,000.
- ii. SEBI on verification of documents, considering eligibility conditions and seeking clarification / information from the Applicant as it may deem fit, is satisfied that applicant is eligible, it may grant certificate of registration.

3.2.4.2.Eligibility criteria

For the purpose of grant of certificate to an applicant as a FVCI, SEBI broadly considers the following eligibility criteria:

- i. The applicant record, professional competence, financial soundness, experience, general reputation of fairness and integrity etc.
- ii. Whether the applicant has been granted necessary approval by the Reserve Bank of India for making investments in India.
- iii. Status of the applicant i.e. whether the applicant is an investment company, investment trust, investment partnership, pension fund, mutual fund, endowment fund, university fund, charitable institution, investment management company, asset management company or an investment vehicle / any other entity incorporated outside India.
- iv. Whether the applicant is authorized to invest in venture capital fund or carry on activity as a foreign venture capital investor
- v. Whether the applicant is regulated by an appropriate foreign regulatory authority or is an income-tax payer.
- vi. Whether applicant earlier has been refused registration as FVCI by SEBI and whether applicant is a fit and proper person.

3.2.4.3. Investment Conditions and Restrictions

- i. FVCI shall disclose to SEBI its investment strategy
- ii. FVCI can invest its total funds committed in one VCF. There is no limit prescribed with respect to investment in a single VCU in the FVCI regulations.
- iii. At least 66.67 per cent of the investible funds shall be invested in unlisted equity shares or equity linked instruments of VCU.
- iv. Not more than 33.33 per cent of the investible funds may be invested in :
 - a. Subscription to initial public offer of a VCU whose shares are proposed to be listed.
 - b. Debt or debt instrument of a VCU in which FVCI has already made an investment by way of equity.
 - c. Preferential allotment of equity shares of a listed company subject to lock-in period of one year.
 - d. Equity shares or equity linked instruments of a financially weak company or a sick industrial company whose shares are listed.
 - e. Special purpose vehicles which are created for the purpose of facilitating or promoting investment in accordance with these Regulations.
- v. FVCI shall disclose the duration of life cycle of the fund.

3.2.4.4. Other Conditions

- i. FVCI shall appoint a domestic custodian for the purpose of custody of securities.
- ii. FVCI shall enter in to an arrangement with a designated bank for the purpose of operating a special non-resident rupee or foreign currency account.
- iii. FVCI shall forthwith inform the SEBI in writing if any information or particular previously submitted to the SEBI are found to be false or misleading in any material particular or if there is any change in the information already submitted.

- iv. FVCI shall maintain for a period of eight years books of account, records and documents which shall give a true and fair picture of the state of affairs of the FVCI.
- v. FVCI shall submit reports on periodic basis or whenever the information is called by the SEBI.

3.2.4.5. Advantages of FVCI registration

i. No Pricing guidelines

RBI pricing norms for acquisition and disposition of investment are not applicable to an FVCI, thereby giving the flexibility to undertake transaction at a price mutually agreed between buyer and seller. This could be beneficial for undertaking mezzanine transactions which intend to provide an agreed return.

ii. No Post IPO lock-in

As per the SEBI (ICDR) Regulations, 2009; the entire pre-issue capital (except promoters shareholding where different lock-in requirements are applicable) gets locked in for a period of one year from the date of allotment. However, the aforesaid lock-in restrictions do not apply to pre-issue shares held by an FVCI or a VCF, provided the shares are held atleast for a period of one year as on the date of filing the draft red herring prospectus with SEBI.

iii. QIB status

Under the SEBI (ICDR) Regulations, 2009, FVCI are considered as a Qualified Institutional Buyer (QIB) and therefore, they are eligible to participate in Qualified Institutional Placement (QIP) process.

iv. No Takeover Code implications on transfer to promoters

As per the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations 2011, acquisition of 25% or more of the shares or voting rights of company listed on any stock exchange, would trigger the obligation to make an open offer and accordingly the acquirer has to make a public announcement to acquire minimum 26% of the voting capital of the company. However, the provisions of the SEBI Takeover Code, does not apply to transfer of shares from FVCI registered with SEBI to promoters of VCU's pursuant to an agreement.

3.2.4.6. Investment only in specified sectors

In the recent past, SEBI/RBI has been granting sector specific approvals (refer below for sectors) at the time of FVCI registration. In case of investments in sectors other than sectors specified in the approval, investment would need to be made through FDI route. Following sectors have been specified in the approval:

- i. Nanotechnology;
- ii. Information technology relating to hardware and software development;
- iii. Seed research and development;
- iv. Bio-technology;
- v. Research and development of new chemical entities in the pharmaceutical sector;
- vi. Production of bio-fuels;
- vii. Building and operating composite hotel-cum-convention centre with seating capacity of more than three thousand;
- viii. Infrastructure sector – includes activities included within the scope of the definition of infrastructure under ECB guidelines;

Infrastructure sector under ECB guidelines is defined as (i) power, (ii) telecommunication, (iii) railways, (iv) road including bridges, (v) sea port and airport, (vi) industrial parks, (vii) urban infrastructure (water supply, sanitation and sewage projects) (viii) mining, refining and exploration and (ix) cold storage or cold room facility, including for farm level pre-cooling, for preservation or storage of agricultural and allied produce, marine products and meat
- ix. Engaged in the dairy industry or poultry industry

A summary of the regulatory requirements and investment guidelines of the existing foreign investment routes as described in this chapter is annexed as Annexure I.

4. Rationale for Integrated Policy on Foreign Investments

Foreign investment in India is characterized by multiple routes and various regulators overseeing these routes, overlapping policies, complicated tax structures, and high cost of transactions leading to inconsistencies, reduced transparency and higher capital costs. These impediments translate into higher cost of capital for Indian companies who are accessing foreign equity capital.

An integrated policy on foreign investments would reduce the overall complexity and number of regulations governing inbound investments. By integrating the existing portfolio routes available for foreign investors, an attempt can be made to remove some impediments. This will also facilitate India being comparable to countries like Brazil, South Korea, etc.

However, it is suggested that a level of segregation across foreign portfolio investors, in the areas such as investment restrictions and application of KYC norms is necessary for ensuring adequate regulatory control on various forms of foreign investment and regulating end use of capital in line with economic and regulatory objectives.

It is suggested to put in place a harmonized model, designed to provide an unified market entry process for all foreign portfolio investors. While the harmonized / common foreign investor approach has merits, the ability of regulatory authorities to control investments from various kinds on investors must be maintained. Accordingly, it is suggested to maintain a single foreign portfolio investor category with common market entry, limit monitoring and reporting norms.

The harmonized model would achieve the following twin objectives –

- i. Provide a unified market entry for foreign portfolio investors, and
- ii. Retain the ability of government/regulatory authorities to incentivize or restrict end use of foreign capital.

5. A Harmonized Foreign Investment Model

5.1. Features of the Harmonized Model

The existing foreign investor routes under portfolio investment scheme have been created for specific purposes as follows:

- i. FII route, which includes FIIs and Sub accounts, enables foreign portfolio investments into Indian capital markets.
- ii. QFI is a foreign investor category where investors can directly open an account with a Qualified Depository Participant (QDP) in India.
- iii. NRI is a dedicated route for a person resident outside India who is a citizen of India (includes PIO).
- iv. FVCI allows foreign investors to make venture capital investments in India. FVCI investments are allowed in unlisted/to be listed companies.

Each of the above routes has a different set of regulations governing such investments giving government/regulatory authorities the ability to monitor and direct flow of foreign investment from different categories of investors to specific sectors / areas in the economy.

While the proposal to have harmonized/common route for foreign investors has merits, the ability of government/regulatory authorities to monitor foreign investments from various kinds of investors must be maintained. Accordingly, it is suggested to have a single foreign investor category where there would be common norms for market entry, limit monitoring, and reporting. However, it may be considered to have segregations of investor classes along the lines of portfolio and direct, to enable government/regulatory authorities to make investment guidelines and impose restrictions for different investor classes.

The Committee recommended to merge FII, Sub Account and QFI into the proposed Foreign Portfolio Investor (FPI) regime.

The Committee felt that NRIs/PIOs presently have a liberal route for accessing securities market. NRIs/PIOs should continue to be viewed as a distinct market participant enjoying certain privileges in terms of investment permissions not available to other foreign investors. Accordingly, the Committee recommended to retain NRIs as a separate investor class with the same limits as currently applicable.

The Committee felt that FVCI route has certain benefits such as non applicability of pricing norms and relaxation from post IPO lock in requirement. These benefits have been given to FVCI route to promote Venture Capital Investments. Accordingly, the Committee recommended that the FVCI as an investor class would continue. Additionally, the

Committee recommended that the current FVCI regime should be expanded to include more sectors under its ambit as against the currently prescribed 9 sectors. Alternately a negative list may be announced by Gol so that rest of the sectors are opened for VCF activity.

Further, currently FVCIs can invest in VCFs under the erstwhile VCF Regulations as per FEMA Regulations and FDI policy. Further, FDI is allowed in VCFs set up as trusts on approval of FIPB. Pursuant to repeal of VCF Regulations and notification of Alternate Investment Funds (AIF) Regulations, necessary changes are required to be made to the FDI policy and FEMA Regulations to enable foreign investment through FVCI and FDI routes into AIFs under the AIF Regulations. The Committee recommends that FDI policy and FEMA Regulations be suitable amended to enable foreign investment through FVCI and FDI route in SEBI registered AIFs.

The table at Annexure II depicts the existing foreign investment structure against various parameters, and the proposed harmonized route for the same parameters.

5.1.1. Foreign Portfolio Investor (FPI)

The Committee agreed with the recommendation to merge FII, Sub Account and QFI into a new investor class to be termed as “Foreign Portfolio Investor” (FPI). It was felt by committee members that the term “Qualified Foreign Investor” (QFI) may cause confusion as there is already an investment route under PIS termed as QFI, the framework for which was initially put in place in August 2011.

5.1.2. Simplification of entry norms for FIIs, Sub Accounts, and QFIs

The committee recommended that there would not be direct registration with SEBI. Instead, DDPs authorized by SEBI would register FPIs on behalf of SEBI subject to compliance with KYC requirements. The FPI that meet the prescribed eligibility criteria shall directly approach Designated Depository Participants (DDPs), authorised by SEBI. The DDPs shall perform due diligence and KYC, before registering FPI, on behalf of SEBI and allowing such entities to make investment in permitted securities.

5.1.3. Uniform entry norms for FPI

The FPI shall be defined as:

(i) Resident in a country whose securities market regulator is a signatory to IOSCO’s MMOU (Appendix A Signatories) or a signatory of a bilateral MOU with SEBI

OR

(ii) In case of Bank, resident of a country whose central bank is a member of BIS

Provided that the person is not resident in a country listed in the public statements issued by FATF from time to time on-(a) jurisdictions having a strategic Anti-Money Laundering/ Combating the Financing of Terrorism (AML/CFT) deficiencies to which counter measures apply, (b) jurisdictions that have not made sufficient progress in addressing the deficiencies or have not committed to an action plan developed with the FATF to address the deficiencies:

Provided further such person is not resident in India:

Explanation.-For the purposes of this clause:

The term “person” shall carry same meaning under Section 2 (31) of the Income Tax Act, 1961;

The phrase “resident in India” shall carry the same meaning as in the Income Tax Act, 1961;

“Bilateral MoU with SEBI” shall mean a bilateral MoU between SEBI and the overseas regulator that inter alia provides for information sharing arrangements.

All entities registered with SEBI as FIIs, Sub-accounts, and QFIs as on the effective date, shall be deemed to be FPIs.

A list of eligible jurisdictions for FPIs and a list of countries which are declared “High-risk and non-cooperative jurisdictions” by FATF are annexed at Annexures IV and V respectively.

5.1.4. Categorization of FDI and Portfolio investment

The Hon’ble Finance Minister while presenting the Union Budget for the year 2013-14, inter-alia proposed to follow the international practice of categorizing FDI and FII, where an investor has a stake of 10 percent or less in a company, it will be treated as FII and, where an investor has a stake of more than 10 percent, it will be treated as FDI.

To examine the feasibility of adopting above principle Govt, has constituted constitute a separate committee namely “Committee for Rationalizing the Definition of FDI and FII”, which would examine and work out the details of the application of the principle internationally for defining FDI and FII.

The Committee recommended the following with respect to categorization of foreign investment:

- i. Portfolio investments to be defined as investments by any single investor or investor group, which shall not exceed 10 percent of the equity securities including the future conversion of existing convertible securities such as Compulsorily Convertible Debentures (CCD) Compulsorily Convertible Preference Shares (CCPS) of Indian company.
- ii. Portfolio investment shall be permitted only in listed equity securities. For this purpose, listed equity securities would also include participation by FPIs in issues such as Initial Public Offer, Qualified Institutional Placement, Institutional Placement Programme etc. of Indian companies as well as tendering shares in an open offer or buyback announced in relation to shares of listed Indian companies.
- iii. The prevailing practice where private placement may be through either FPI or FDI route depending on the nature of the transaction may be continued, even when such private placement results in a foreign investor holding less than 10 per cent.
- iv. In case of unlisted company, the private placement shall be under FDI route.

- v. In circumstances, where the listing does not take place within the stipulated timeframe, such foreign investments shall be re-categorized as FDI.
- vi. Investments in unlisted securities, regardless of the level of ownership that they represent, shall be regarded as FDI.
- vii. Where there is an FDI investor, all equity holdings of such an investor in the concerned company, regardless of the manner in which such equity holdings have been acquired, should be classified as FDI.
- viii. Where an investor initially acquires less than 10 percent of the voting equity of an Indian company and thereafter acquires additional equity which takes the investor's aggregate holding to over 10 percent, in such a scenario, all of the investor's holdings should be classified as FDI.
- ix. Where an investor has FDI holdings in excess of 10 percent of the voting equity of a company should retain its FDI classification even if the investor were to dilute his holding to a level below 10 percent of the voting equity of the company.
- x. Investment classification and tracking could be accomplished through the DDPs.

The above recommendations of the Committee will be provided to a separate committee constituted by the Gol namely "Committee for Rationalizing the Definition of FDI and FII".

5.1.5. Risk Based Approach towards KYC

Keeping in view the global practice mainly prevailing in FATF countries, the budget announcement and the feedback received from market participants, the committee recommended for adoption of risk based approach towards KYC where government related FPIs would be subject to less stringent KYC norms and unregulated investors would have to undergo stringent KYC norms. SEBI would separately prescribe the documentation needed for the three categories.

From the point of view of KYC, the committee recommended for following categorization of FPIs based on their perceived risk profile:

Category	Eligible Foreign Investors	Perceived Risk Profile
I	Government and Government related foreign investors such as Foreign Central Banks, Governmental Agencies, Sovereign Wealth Funds, International/ Multilateral Organizations/ Agencies	<p>Low Risk</p> <p>As these entities are either owned/ controlled by respective government they are perceived to be low risk entities.</p>
II	<p>a) *Appropriately regulated broad based funds such as Mutual Funds, Investment Trusts, Insurance/Reinsurance Companies, Other Broad Based Funds etc.</p> <p>b) *Appropriately regulated entities such as Banks, Asset Management Companies, Investment Managers/ Advisors, Portfolio Managers etc.</p> <p>c) Broad based funds whose investment manager is appropriately regulated</p> <p>d) University Funds and Pension Funds</p> <p>e) University related Endowments already registered with SEBI as FII/Sub Account</p>	<p>Moderate Risk</p> <p>Generally, these entities are either pooled investment vehicles or institutions that manage portfolios of pooled vehicles. Since these entities are appropriately regulated in their respective home jurisdictions or corpus of the fund is for post retirement benefits of the employees/ academic research etc., these are perceived to be moderate risk entities</p>
III	All other FPIs not eligible under Category I and II such as Endowments, Charitable Societies/ Trust, Foundations, Corporate Bodies, Trusts, Individuals, Family Offices, etc.	<p>High Risk</p> <p>Generally, these entities are not regulated in their respective home jurisdictions, these entities are perceived as high risk entities.</p>

**Appropriately Regulated is meant to include relevance of activity i.e. securities market regulations in case of an entity related to investment segment, capital market activities; and the Banking Regulations in case of a banking entity.*

The detailed recommendations as regards to KYC documentary requirements are described in the Annexure III.

5.1.5.1. Categorization of Un-regulated Broad Based Funds

Presently a large proportion of FII investments come through Broad based funds, which are unincorporated entities. These funds are floated in foreign jurisdiction as per the terms of placement memorandum (PM) issued for each fund by the fund manager. The PM is normally filed with the regulator in the home jurisdiction of the fund / fund manager. In most such cases, the fund manager chooses to get registered with SEBI as FII while the funds are registered as SA of the FII. In a few instances, the funds are themselves registered with SEBI as FII.

The committee recommended that if the Investment Manager of the investment fund falls under Category-II, broad based funds managed by such Investment Managers should also be categorized in the same category of its Investment Manager for the following reasons:

- i. Presently, a large proportion of the foreign portfolio investment comes through broad based funds which are registered by SEBI as sub accounts. Such sub-accounts may not necessarily be regulated in its home jurisdiction. Therefore, in the proposed FPI regime, such broad based funds would fall under Category-III and thus would be put in a worse off position than of present. This may not be a desirable scenario.
- ii. Presently, these sub accounts are under FIIs, which are appropriately regulated in their home jurisdictions.

This approach, of classifying the underlying unregulated fund vehicle as Category-II (under an Investment Manager who is Category-II), will be subject to the following two conditions –

- a. Submission of undertaking by the Investment Manager regarding full responsibility for the actions of the underlying fund vehicle (on same lines as the extant FII undertaking for its sub-accounts), and
- b. Fulfillment of the broad-based criteria, as prescribed in existing SEBI (FII) Regulations, 1995, for the underlying fund vehicle.

Those funds which do not meet the broad based criteria, as prescribed by SEBI (FII) Regulations, 1995, would fall in Category-III.

5.1.6. Other KYC Recommendations

5.1.6.1. Amendments to PML Rules

It is recognized by the Committee that provisions of the PMLA, especially Rule 9 will need to be amended in order to give full legal effect to the changes being suggested to the KYC norms. The suggested approach is to allow intermediaries to adopt risk based documentation rules, as the PMLA permits risk based treatment.

The sub-committee on KYC also met officials of Department of Revenue (DoR), MoF to suggest necessary amendments to PML Rules including the issue of placing reliance on Global Custodian/Banks. The suggestions made by the Sub Committee on proposed amendments to PML (Maintenance of Records) Rules, 2005 is annexed at Annexure VI.

5.1.6.2. Amendments to PAN cum KYC Form No. 49AA issued by Central Board of Direct Taxes.

The committee recommended that Central Board of Direct Taxes (CBDT) may consider carrying out necessary amendments to PAN cum KYC Form 49AA so as to make the list of authorities, who can attest the documents, to be consistent with SEBI circular no. MIRSD/SE/Cir-21/2011 dated October 5, 2011.

5.1.6.3. Reliance on Global Custodian/Banks

- i. It is a well established fact that a significant majority of foreign investors in India come via Global custodians (GCs)/Banks. A large number of foreign investments in India, especially through the Portfolio Investment Scheme, operate through authorized agent institutions such as GCs. Foreign Institutional Investors (FIIs) and Sub-accounts (End clients) appoint such GCs and typically execute a Power Of Attorney authorizing the GC to act on their behalf for operating their accounts in India. The GCs in turn appoint local custodians in India for such End Clients and operate all the accounts on behalf of the End Clients (FII/sub-account/ QFI), based on instructions received from them. The GCs/Banks are typically large international banks, subject to laws and regulations in their home jurisdictions as well as the laws and regulations in the countries where they conduct business. A contractual relationship exists between the GC and the local custodian.
- ii. The GCs/Banks are generally incorporated in countries that adopt FATF standards and are signatories to IOSCO MMoU. The GCs/Banks are

therefore generally subject to KYC and AML related regulations of a reasonably high standard, typically requiring a customer identification program and appropriate due diligence practices.

- iii. Where feasible, a risk based approach is considered for lower risk customers as an acceptable practice in these countries, subject to local regulatory norms permitting the same. Further, the End Clients that form the GCs/Banks customer base are primarily institutional investors who are themselves regulated and may therefore generally be considered as low risk.
- iv. The Indian intermediary may be permitted to rely on GCs/Banks which may furnish a declaration/comfort letter stating necessary FATF standard due diligence procedures (AML & KYC related) have been followed at their end while on boarding the investor and are updated as per the country requirements.

5.1.6.4. Risk Assessment

It is also recommended to issue guiding principles on risk profiling – low, medium or high risk categorization – so that from a market perspective all intermediaries are able to use objective market-standard criteria for risk classification.

5.1.6.5. Updation of KYC documents

For updation, it is recommended to follow a 2 year/ 5 year rule based on the risk classification of the investor as per above i.e. 2 years for non low risk investors and 5 years for low risk investors. For the purpose of achieving updation, risk category of the investor will be re-evaluated and the necessary documents will be refreshed depending upon investor's risk category. In case the FPIs under consideration are sourced through Global Custodian/Banks, necessary declarations from the Global Custodian/Banks will be refreshed. Risk categorization of the investors will also need to be re-affirmed at this stage.

5.1.6.6. Continuous assessment of risk profile of FPIs

- i. The committee was of the view that the FPIs would be subject to KYC review as and when there is any change in material information/disclosure. In a circumstance where change in information results in change of category, the FPI would have to undergo KYC compliance as prescribed for the category to which it now belongs.

- ii. In addition to the above, it was also recommended that all FPIs would also be subject to KYC review every two years.

5.1.6.7. Requirement of Personal Identification documents for KYC

The requirement of submitting personal identification documents such as copy of passport, photograph etc. of the designated officials of FPIs belonging to Category I and Category II shall be done away with.

5.1.7. Account Structure

- i. Each FPI will be allowed to open one demat account for FPI investments.
- ii. Each FPI will be permitted to open bank account (s) as per RBI norms (non-interest bearing rupee account and foreign currency bank account). The bank accounts must be maintained with a DDP which is an Authorized Dealer Category 1 bank.

6. Roadmap for Integration

6.1. Operational Requirements

6.1.1. Role of Designated Depository Participant (DDP)

It will be mandatory for FPI to appoint a DDP. The DDP would perform due diligence and KYC of FPIs as per the stipulated norms.

It is suggested that the DDP shall meet the following eligibility criteria in order to service FPIs.

- i. DDP to be a Custodian registered with SEBI.
- ii. DDP to be an Authorised Dealer category 1 bank as per RBI.
- iii. DDP to be a Depository Participant registered with SEBI.
- iv. DDP to have multinational presence either through its branches or through agency relationships with intermediaries regulated in their respected home jurisdictions.
- v. DDP to demonstrate that it has systems and procedures to comply with the FATF Standards, Prevention of Money Laundering (PML) Act, Rules and SEBI circulars issued from time to time; and
- vi. DDP to obtain prior approval of SEBI before commencing the activities relating to opening of accounts of FPIs.

Based on the experience gathered, the eligibility criteria for registration of DDP may be later reviewed by SEBI.

6.1.2. Grandfathering Arrangements

- i. Presently, the volume of assets held under the custody of custodians is much greater than the volume of assets held by QFI through QDPs.
- ii. The present entry norms for QDPs are not stringent.

- iii. Out of the 59 QDPs approved by SEBI, only six QDPs have QFI investments. Out of these six QDPs, three are also custodians.
- iv. To avoid business discontinuity, it is recommended to grandfather all the entities which are presently registered with SEBI as custodian of securities, as DDPs. The existing QDPs authorised by SEBI currently not meeting the proposed eligibility criteria may be allowed further time period of one year to comply with the proposed eligibility requirement of a DDP. Subsequently, if such QDPs fail to comply with the same, then they may be required to surrender the authorization.
- v. It is recommended that all existing investments held by the foreign investors acquired through either FDI route and/or PIS route shall be grandfathered.
- vi. It is recommended that all existing entities registered with SEBI as FII, sub-account, and QFIs as on the effective date, shall be deemed to be FPIs.

6.1.3. Obligations of DDPs

- i. The entities having opaque structure(s) such that the details of ultimate/ end beneficiary owners are not accessible or where the beneficial owners are ring fenced from each other or where the beneficial owners are ring fenced with regard to enforcement shall not be allowed.
- ii. In case, the same set of ultimate/ end beneficial owner(s) invest through multiple entities, such entities shall be treated as a part of same group and the investment limits of all such entities shall be clubbed at the investment limit as applicable to single investor. For this purpose, the FPIs should consider all such entities having direct or indirect common shareholding/ beneficial ownership/ beneficial interest of more than 50%, as a part of their group. The DDP shall ensure at the time of on boarding the foreign portfolio investor whether such investor forms a part of any group.
- iii. In case of any direct/ indirect change in structure or beneficial ownership of the FPIs, it shall bring the same to the notice of its DDP forthwith.
- iv. The investor shall, as and when required by the Government, SEBI or any other regulatory agency in India, submit any information, record or documents in relation to his activities as a FPIs. An express undertaking to this effect shall be obtained by DDP from the FPIs.

- v. The DDP shall ensure that equity shares held by FPIs are free from all encumbrances including pledge or lien etc. at all times.
- vi. The DDP shall require FPI to submit necessary information for the purpose of obtaining PAN.
- vii. The DDP shall ensure that all the investor related documents/ records are available it.
- viii. In case of any penalty, pending litigations or proceedings, findings of inspections or investigations for which action may have been taken or is in the process of being taken by an overseas regulator against FPIs/ DDP, the DDP shall bring such information forthwith, to the attention of SEBI, depositories and stock exchanges. The DDP shall mandate the FPI to furnish to it the details of any such penalty, pending litigations or proceedings on an immediate basis as and when levied/initialed.
- ix. DDPs shall collect and remit fees to SEBI, as prescribed from time to time.

6.1.4. Market Entry

FPIs would not require direct registration from SEBI and they would be henceforth subject to registration by DDP. Each investor may be permitted to open one demat account for portfolio investments and a bank account as per RBI norms. In case of jointly held demat accounts, each of the joint holders shall meet the requirements specified for the investor and each shall be deemed to be holding a demat account as an individual FPI.

6.1.5. Order processing

Orders shall be placed directly by the FPI with SEBI registered Stock Brokers on the same lines as the present framework applicable to FIIs.

6.1.6. Trade Settlement

Appointment of DDP shall be mandatory for all categories of FPIs. All settlement of transactions by FPI must be done through DDP acting as a Custodian.

6.1.7. Eligible investments

FPIs shall be permitted to transact in all the securities where FIIs are presently permitted and any other instruments as permitted from time to time.

FPIs can hold securities only in dematerialized form. All securities holdings by FPIs must be through custodian of securities registered with SEBI.

6.1.8. Other Guidelines

The Committee recommended the following broad operational guidelines. However, committee was also of the view that the detailed operational guidelines/framework may be prescribed by SEBI from time to time.

- i. The investor shall transact in Indian equity shares only on the basis of taking and giving delivery of shares purchased or sold.
- ii. Each transaction shall be cleared and settled on gross basis.
- iii. Committee recommended that under the proposed FPI regime, - the ODIs/PNs issuer FPIs will continue to report directly to SEBI, the details of ODIs/PNs on a regular basis, as prescribed by SEBI.
- iv. Committee recommended that under the proposed FPI regime, Category III FPIs will not be allowed to issue PNs/ODIs. The committee also recommended that those broad based funds, belonging to Category II, which are not directly regulated by the appropriate regulator in their home jurisdiction, should not be allowed to issue ODIs/PNs. The ODIs/PNs issuer will continue to report directly to SEBI, the details of ODIs/PNs on a regular basis, as prescribed by SEBI.
- v. Margins and risk management framework as applicable in the capital market will apply.

6.1.9. Investment Limits

- i. The Investor and DDP shall ensure that the total shareholding held by the FPI shall not exceed 10% of paid up equity capital of the company at any point of time.
- ii. This investment limit shall be applicable to each class of equity shares having separate and distinct ISIN.

- iii. Where more than one FPI have same common beneficial owner, all such FPIs shall be together treated as one FPI for the purpose of this investment limit.
- iv. Aggregate shareholding of all FPIs shall not exceed the lower of (i) 24% of the paid up equity capital of the company at any point of time or (ii) the sectoral cap, in respect of each equity share class having separate and distinct ISIN.
- v. In case the company raises their foreign ownership limit to the sectoral cap as per the FDI policy, then the foreign ownership will be monitored at that level.
- vi. The monitoring of investment limits at the individual level may be monitored by the respective DDPs.

6.1.10. Dissemination of FPI Investment Data

Dissemination of FPI investment data shall be carried out by the depositories.

6.1.11. Prohibited Sectors for Investments

Prohibitions imposed on foreign investments by FEMA, shall apply to FPIs.

6.1.12. Generation and Allotment of Registration Number for the FPI

The committee discussed the matter and recommended that:

- i. The generation and allotment of registration number be done through a common central system.
- ii. The system will remain under the control of SEBI.
- iii. DDPs will have access to the system.
- iv. The system will generate a running sequence number.
- v. SEBI fees would be collected through DDP.

6.2. Taxation Framework

The Committee discussed the present taxation framework for various portfolio investors. It is recommended that GoI may consider bringing more clarity and certainty while prescribing the taxation provisions for FPIs.

6.3. Legal Requirements

The process for evolving an integrated policy on foreign investments would entail the following amendments/modifications in the legal framework:

- i. FII regulations prescribed by SEBI and QFI framework prescribed by SEBI and the RBI would be required to be repealed and replaced by a new framework for FPIs.
- ii. FEMA (Transfer or Issue of Security by a Person Resident Outside India) Regulations, notably Regulations 5 (2), 5(6), 7A, 8 and Schedule 2, 5, 8 and other related provisions would have to be amended and replaced to prescribe the permissible caps and investment levels applicable to foreign portfolio investor;
- iii. Necessary amendments in FEMA to replace references to FIIs with FPIs;
- iv. Necessary amendments to PML Rules;
- v. Necessary amendments in Income Tax Act, 1961;
- vi. General permission granted by RBI to FIIs dated December 17, 2003;
- vii. GoI guidelines dated September 14, 1992;
- viii. RBI's Foreign Exchange Management framework;
- ix. Necessary amendment to the following regulations are needed to replaces references to FIIs and QFIs and recognize the FPIs:
 - a. Consolidated FDI Policy dated April 5, 2013 (more particularly paragraphs 2.1.14, 2.1.32, 3.1.4, 3.1.5, 3.1.7, 3.2.5(f), 3.6.2 (vi), 4.1.2, 6.2.7.5, 6.2.8.1, 6.2.8.2, 6.2.15.1.1., 6.2.17.1, 6.2.17.2, 6.2.17.4.2, 6.2.17.4.3, 6.2.17.5, 6.2.17.6., 6.2.19, paragraphs 3 and 5 of the Format of Form FC-GPR, paragraphs 2.2, 2.3, 4, 5.1(iii) and (vii), 6.5 of Annex -2, Format of Annual Return on Foreign Liabilities and Assets, Form FC-TRS, Form DR;
 - b. RBI Master Circular on Foreign Investment In India dated July 2, 2012 (Section II, Section IV (3), (5), (6), Section V(6) to make changes corresponding to the changes in the Consolidated FDI Policy in relation to references to FIIs while calculating the sectoral cap);
 - c. SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (Regulations 2(za), 2(zb), 2(zd)(ii));

- d. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (Regulation 2(q)(2)(ix));
- e. The SEBI Act, 1992 (Section 12(1A))

To avoid too many individual legislative amendments, it is also suggested that a clause may be introduced in the respective legislations stating that the term “FII” in the legislations shall mean “FPI registered with DDP”.

7. ANNEXURE

ANNEXURE I: Regulatory Requirements and Investment Guidelines of the Existing Foreign Investment Routes

Regulatory Requirements and Investment Guidelines

Particulars	Foreign Direct Investment (FDI)	Portfolio Investment Scheme (PIS)			Foreign Venture Capital Investment (FVCI)
	Automatic Route or FIPB Route	Foreign Institutional Investors (FII) & Sub Accounts (SA)	Qualified Foreign Investors	Non Resident Indians (NRI)	
Nature of Investments	Strategic Investments (typically long term)	Portfolio Investments (trading activities)	Direct Portfolio Investment	Direct Portfolio Investment	Venture Capital /Private Equity Investments (typically long term)
Registration required	No registration required. In case of investments in restricted sectors, investment specific approvals need to be obtained from the Foreign Investment Promotion Board	Yes, registration with SEBI (License valid perpetually) Registration Fees: Each FII: US\$ 5,000 (upfront and subsequently every 3 years to maintain registration) Each FII Sub-Account: US\$ 1,000 (upfront and subsequently concurrent with the FII)	No registration required. Demat Account with any of the qualified Depository Participant	No registration required. Demat Account with Depository Participant (DP) Trading account with stock broker	Yes, registration with both SEBI and RBI but channeled through SEBI Application Fees: US\$2,500 (non-refundable) Registration Fees: US\$10,000 (one time)
Financial Instruments permitted	<ul style="list-style-type: none"> Equity Compulsorily Convertible Debts 	<ul style="list-style-type: none"> Equity (Primary and Secondary Markets) Listed Corporate 	<ul style="list-style-type: none"> Equity (listed/to be listed) Corporate Debt (listed/to be listed) Units of Mutual Funds 	<ul style="list-style-type: none"> Equity Units of Mutual Funds Debentures <p>Derivatives (allowed)</p>	<ul style="list-style-type: none"> Equity Compulsorily Convertible Debts

Particulars	Foreign Direct Investment (FDI)	Portfolio Investment Scheme (PIS)			Foreign Venture Capital Investment (FVCI)
		Automatic Route or FIPB Route	Foreign Institutional Investors (FII) & Sub Accounts (SA)	Qualified Foreign Investors	
		<ul style="list-style-type: none"> Debt • Exchange Traded Equity Derivatives • Interest Rate Futures • Security Receipts • Government Securities/ STRIPS • Commercial Paper • Units of Mutual Funds • IDRs • Units of Collective Investment Schemes 	<ul style="list-style-type: none"> • G-Sec & T-Bills. • Commercial Papers 	only on non repatriable basis and	
Transactions permitted	<p>Primary Placements</p> <p>Sale on recognized securities exchanges.</p> <p>Purchases on securities exchanges not permitted</p> <p>Private Arrangements subject to RBI guidelines</p>	<p>Primary Market transactions</p> <p>Secondary Market transactions (on exchange / private arrangement subject to RBI guidelines)</p> <p>Investment in Mutual Fund schemes</p>	<p>Subscriptions/ redemptions in equity and debt schemes of Mutual Funds (MFs)</p> <p>Primary Market transactions</p> <p>Secondary Market transactions (on exchange)</p>	<p>Primary Market transactions</p> <p>Secondary Market transactions (on exchange / private arrangement subject to RBI guidelines)</p>	<p>Primary Placements</p> <p>Private Arrangement</p> <p>Permitted to sell on recognized securities exchanges</p>
Short Selling	Not Allowed	Allowed within the SLB	Not Allowed	Not Allowed	Not Allowed

Particulars	Foreign Direct Investment (FDI)	Portfolio Investment Scheme (PIS)			Foreign Venture Capital Investment (FVCI)
		Automatic Route or FIPB Route	Foreign Institutional Investors (FII) & Sub Accounts (SA)	Qualified Foreign Investors	
		framework issued by SEBI			
Pricing Guidelines	Ruling market price for sale trades on recognized securities exchanges Subject to Pricing guidelines for all off market trades / specific approvals as accorded by the concerned statutory body.	Ruling market price for trades on recognized securities exchanges Subject to Pricing guidelines for all off market trades / specific approvals	Ruling market price for trades on recognized securities exchanges NAV of the day on which funds are realized in the MF's scheme bank account in India	Ruling market price for trades on recognized securities exchanges	Mutually acceptable price between buyer and seller Ruling market price for sale trades on recognized securities exchanges
FX Forward Cover	Yes to the extent of their investments / dividend receivable in India Forward contracts once cancelled cannot be rebooked	Yes to the extent of the market value of their debt / equity portfolio Forward contracts once cancelled cannot be rebooked	Not Applicable	Not Applicable	Yes, to the extent of total inward remittance. In case of outward remittance, the amount will be reduced from the eligible cover
Registration/Approval Requirements	FIPB approval required if the investment is made in non-approved sectors.	FII: <ul style="list-style-type: none"> FII Form A (SEBI prescribed formats) Declarations & Undertakings relating to PCC/ SPC/ MCV FII Group 	No registration/approval required	No registration/approval required	<ul style="list-style-type: none"> Form A (SEBI prescribed formats) Constitutive Documents including Certification of registration in the country of incorporation

Particulars	Foreign Direct Investment (FDI)	Portfolio Investment Scheme (PIS)			Foreign Venture Capital Investment (FVCI)
		Automatic Route or FIPB Route	Foreign Institutional Investors (FII) & Sub Accounts (SA)	Qualified Foreign Investors	
		<p>Letter</p> <ul style="list-style-type: none"> • Constitutive Documents • Latest audited financials covering a period of 12 months • Regulatory registration, License or Approval <p>Sub Account (SA):</p> <ul style="list-style-type: none"> • Form AA (SEBI prescribed format) • Declarations & Undertakings relating to PCC/ SPC/ MCV • FII Group Letter 			<p>n or bankers certificate or income tax return</p> <ul style="list-style-type: none"> • Structure diagram of the applicant • Declarations and undertakings on investible funds, sectors for investment, life cycle of the fund, fit and proper persons, and so on • Investor's firm commitment letter for investing at least USD 1 Million • Financial statements and email address of the applicant and the investor
Bank Accounts in India	Not permitted	Permitted to open non-interest bearing Rupee account and foreign currency account with	Permitted to open non-interest bearing Rupee account	Permitted to open non resident rupee bank accounts (NRO/ NRE)	Permitted to open non-interest bearing Rupee account and foreign currency account with

Particulars	Foreign Direct Investment (FDI)	Portfolio Investment Scheme (PIS)			Foreign Venture Capital Investment (FVCI)
		Automatic Route or FIPB Route	Foreign Institutional Investors (FII) & Sub Accounts (SA)	Qualified Foreign Investors	
		Category AD-1 Bank			Category AD-1 Bank.
PAN Card	Required	Required	Required	Required	Required
KYC Procedure - By whom	AD-1 Bank	AD-1 Bank / Local Custodian	Qualified Depository Participant	Depository Participant / Stock Broker	AD-1 Bank/ Local Custodian
Investment Restrictions	Investment upto sectoral limits prescribed by RBI;	<ul style="list-style-type: none"> FII & Broad Based SA: Investment upto 10% of paid up equity capital of investee company; Foreign Corporate/ Individual - Investment upto 5% of paid up equity capital of investee company 	<ul style="list-style-type: none"> Investment upto 5% of paid up equity capital of investee company All QFIs cannot hold more than 10% of paid up equity capital of investee company 	<ul style="list-style-type: none"> Investment upto 5% paid up equity capital of investee company All NRIs cannot hold more than 10% paid up equity capital of investee company 	<ul style="list-style-type: none"> At least 66.67% of the investible funds shall be invested in unlisted equity shares or equity linked instruments.
Repatriation benefits	Tax computation / certificate from the appointed tax consultants of the FDI Form 15CA and Form 15 CB under the IT Act	Tax computation / certificate from the appointed tax consultants of the FII	Investment made are repatriable, subject to payment of applicable taxes	NRIs can invest through designated ADs, on repatriation and non-repatriation basis, subject to payment of applicable taxes	Tax computation / certificate from the appointed tax consultants of the FVCI Form 15CA and Form 15 CB under the IT Act

ANNEUXRE II: Comparison of existing foreign investment structure and harmonized model

Sr. No			Existing Categories				Harmonised Foreign Investor Route
			FII	QFI	FVCI	NRI	FPI
1.	Market Entry		SEBI Registration	No SEBI Registration (Account with QDP)	SEBI Registration and RBI Approval	No SEBI Registration and RBI Approval	No SEBI Registration (Account with DDP)
2.	Eligible Home Jurisdiction		IOSCO or BIS member with some exceptions	FATF + IOSCO=45 countries at present	All Jurisdictions	N.A.	IOSCO Appendix A or BIS Member – FATF Negative
3.	KYC		Uniform KYC	Uniform KYC	Uniform KYC	Uniform KYC	Risk based KYC
4.	Investment Restrictions						
	-Equity (Individual/Aggregate)		10/24	5/10	Sectoral Cap	5/10	10/24
	- Debt		Limits	Limits	Corporate Debt of issuer companies, where FVCI having equity holdings	Limits	Limits (Utilisation to be monitored by Depositories)
	- Derivatives		Position Limits	Not Allowed	Not Allowed	Position Limits	Position Limits
5.	Transaction Reporting/ Dissemination		Custodian to SEBI	QDP to Depository	Direct Reporting of Net Investment by FVCI to SEBI	AD Cat-1 Bank to RBI	DDP to Depositories
6.	Limit Monitoring	Individual Level	FII through Custodian	QDP	N. A.	NRI and Issuer Company	DDP
		Aggregate Level	RBI	Depository	RBI	RBI	Depositories to inter-alia facilitate dissemination of FPI investment data
7.	Taxation responsibility		FII through AD Cat-1 Bank	QDP	FVCI through AD Cat-1 Bank	NRI	FPI and DDP as a AD Cat-1 Bank
8.	Order Placement		Broker	Broker through QDP	Broker	Broker	Broker
9.	Order Settlement		Custodian	Broker/ Custodian	Custodian, if required	Broker/ Custodian	DDP

ANNEUXRE III: DOCUMENTARY REQUIREMENTS FOR RISK BASED KYC

Document Type		SEBI Uniform KYC Norm issued vide Circular dated September 05, 2012 (FI/ QFI)	Category - I	Category - II	Category - III	Remarks
Entity Level	Constitutive Docs	Required	Required	Required	Required	-
	Proof of Address	Required Power of Attorney is already acceptable as address proof	Required Power of Attorney, mentioning the address, is already acceptable as address proof	Required Power of Attorney, mentioning the address, is already acceptable as address proof	Required - Address proof other than Power of Attorney should be submitted.	-
	PAN Card	Required	Required	Required	Required	<i>PAN No. will be the primary identifier number of investor</i>
	Financials	Risk based	Exempt	Exempt	Risk based - Financial data sufficient. No financial documentation	<i>The exemptions / changes to seeking financial documents is in line with global best practice. Reliance on professional intermediaries for AML monitoring should be permitted.</i>
	SEBI Registration Certificate	Required	Not Applicable under new FPI regime	Not Applicable under new FPI regime	Not Applicable under new FPI regime	<i>The FII registration process at SEBI will no longer be applicable.</i>
	Board Resolution	Not Applicable	Exempt	Required	Required Not applicable to Individuals	<i>Acceptance of Board Resolution will provide the permissions / authority granted by the entity's Board of Directors. This is also required under RBI guidelines.</i>
	KYC Form	Required - Can be filled by GC	Required - required with data, no supportings necessary	Required - required with data, no supportings necessary	Required - with data and supportings	<i>Entities should submit the standard KYC form, as there should be no constraints to fill entity level data. Relaxations towards submitting personal information under the KYC form must be provided.</i>
Senior Management (WTD/ Partners/ Trustees/ etc.)	List	Required - Alternately GC provides Undertaking	Required	Required	Required	<i>This information iss already forms part of KYC form.</i>
	Proof Of Identity	Required - Alternately GC provides Undertaking	Exempt	Exempt	Entity declares on letterhead - full name, nationality and DoB OR Photo-identity proof'	<i>We recommend that the requirement of obtaining personal information and documents of Directors/ Governing board members/ Trustees should be removed.</i> <i>In case of Category III</i>
	Proof of Address	Required - Alternately GC provides Undertaking	Exempt	Exempt	Exempt	

Document Type		SEBI Uniform KYC Norm issued vide Circular dated September 05, 2012 (FII/ QFI)	Category - I	Category - II	Category - III	Remarks
	Photographs	Required - Alternately GC provides Undertaking	Exempt	Exempt	Exempt	<i>(unregulated entities) necessary details of the investing entity's Directors/ Governing members/ Trustees should be obtained on the entity's letterhead – which should include Name, Designation/Relationship with entity, Nationality and Date of Birth.</i> <i>It is pertinent to note here that sharing personal information is discouraged in most foreign jurisdictions.</i> <i>Additionally, Refer Note 1 for permitting reliance on regulated intermediary KYC.</i>
Authorized Signatories	List & Signatures	Required - List of GC signatories can be given in case of POA to GC	Required - List of GC signatories can be given in case of POA to GC	Required - List of GC signatories can be given in case of POA to GC	Required	-
	Proof Of Identity	Not required	Not required	Not required	Required	-
	Proof of Address	Not required	Not required	Not required	Not required	-
	Photographs	Not required	Not required	Not required	Required	-
Ultimate Beneficial Owner	List	Required - Alternately GC provides Undertaking	Exempt	Required - Can declare "no UBO over 25%"	Required	<i>For Cat II investors, where UBO is not identifiable & no percentage declaration is possible, then details of senior management must be provided on letterhead - full name, nationality and DoB OR Photo-identity proof</i>
	Proof Of Identity	Required - Alternately GC provides Undertaking	Exempt	Exempt	Required	<i>We recommend that the requirement of obtaining personal information and documents of UBOs should be removed for Cat I and Cat II investors.</i>
	Proof of Address	Required - Alternately GC provides Undertaking	Exempt	Exempt	Exempt	
	Photographs	Required - Alternately GC provides Undertaking	Exempt	Exempt	Exempt	<i>ID proof can be accepted for Cat III to facilitate UBO determination. However, the Indian intermediary may be permitted to rely on the professional foreign intermediaries for this requirement also.</i>

Copies of all the documents, wherever applicable, to be submitted by the applicant should be self-attested and accompanied by originals for verification. In case the original of any document is not produced for verification, then the copies should be properly attested by entities authorized for attesting the documents, as per the SEBI circular no. MIRSD/SE/Cir-21/2011 dated October 5, 2011.

ANNEUXRE IV: (This has been excised)

ANNEUXRE V: COUNTRIES CATEGORIZED AS “HIGH RISK AND NON-COOPERATIVE JURISDICTIONS BY FATF

FATF High-risk and non-cooperative jurisdictions

As per the latest FATF Public Statement 22 Feb 2013 available on FATF website following countries are considered as “High-risk and non-cooperative jurisdictions”:

1. Iran
2. Democratic People’s Republic of Korea
3. Ecuador
4. Ethiopia
5. Indonesia
6. Kenya
7. Myanmar
8. Nigeria
9. Pakistan
10. São Tomé and Príncipe
11. Syria
12. Tanzania
13. Turkey
14. Vietnam
15. Yemen

ANNEUXRE VI: (This has been excised for reasons of confidentiality)

ANNEUXRE VII: LIST OF COMMITTEE MEMBERS

Sr. No.	Committee Members	Name of the Official	Designation
1	Shri K. M. Chandrasekhar, Ex Cabinet Secretary, Government of India (Gol), Chairman of the Committee.	Shri K. M. Chandrasekhar	Former Cabinet Secretary, Gol
2	Dept. of Revenue, Ministry of Finance, Gol	Shri Madan Lal Meena	Joint Secretary (Revenue)
3	Ministry of Overseas Indian Affairs, Gol	Shri Atul Kumar Tiwari	Joint Secretary (Financial Services Division)
4	Dept. of Economic Affairs, Ministry of Finance, Gol	Shri Sanjeev Kaushik	Director (External Markets)
5	Reserve Bank of India	Shri R. N. Kar	Chief General Manager
6	AZB & Partners	Ms. Zia Mody	Senior Partner
7	BMR Advisors Pvt. Ltd.	Shri Bobby Parikh	Managing Partner
8	Luthra & Luthra Law Offices	Shri Rajeev Luthra	Founder and Managing Partner
9	PricewaterhouseCoopers Pvt. Ltd.	Shri Ketan Dalal	Joint Tax Leader
10	National Stock Exchange of India Limited	Ms. Chitra Ramkrishna	MD & CEO
11	BSE Ltd.	Mr Ashish Chauhan	MD & CEO
12	National Securities Depository Limited	Shri Gagan Rai	Managing Director
13	Central Depository Services (India) Limited	Shri P. S. Reddy	CEO
14	HDFC Bank Limited	Shri Aditya Puri	MD & CEO
15	Deutsche Bank AG	Shri Mrugank Paranjpe	MD

Sr. No.	Committee Members	Name of the Official	Designation
16	Citibank N.A.	Shri Sudeep Yadav	MD & Head, Citi Transactions Services
17	HSBC Bank (Mauritius) Limited	Shri Kapil Seth	Head, India HSBC Securities Services
18	SBI-SG Global Securities Services Ltd.	Shri C. R. Sasikumar	MD & CEO
19	Infosys Technologies Ltd.	Shri V. Balakrishnan	Board Member
20	Reliance Industries Ltd.	Shri Soumyo Dutta	Treasurer
21	BlackRock Singapore Limited	Shri S. Nagnath	President and Chief Investment Officer, DSP BlackRock
22	Amansa Capital Pte Ltd.	Shri Akash Prakash	CEO
23	Link Intime India Pvt. Ltd.	Shri M. V. Ramnarayan	Director

Members of Sub Committee on KYC

1. Shri SV Muralidhar Rao
2. Shri R N Kar
3. Ms. Chitra Ramkrishna
4. Shri Ashish Chauhan
5. Shri P.S. Reddy
6. Shri Mrugank Paranjpe
7. Shri Sudeep Yadav
8. Shri Kapil Seth
9. Shri C. R. Sasikumar,
10. Shri Akash Prakash

Members of Sub Committee on Treatment of Foreign Investments

1. Shri SV Muralidhar Rao
2. Shri R N Kar
3. Shri Sanjeev Kaushik
4. Shri Bobby Parikh
5. Ms. Zia Mody
6. Shri S. Nagnath
7. Shri Ketan Dalal

LIST OF ABBREVIATIONS

1. Anti-Money Laundering ("AML")
2. Anti-Money Laundering/ Combating the Financing of Terrorism (AML/CFT)
3. Assets Under Custody ("AUC")
4. Authorized Dealer Category 1 bank ("AD-1 bank")
5. Bank for International Settlements ("BIS")
6. Central Board of Direct Taxes ("CBDT")
7. Compulsorily Convertible Debentures ("CCD")
8. Compulsorily Convertible Preference Shares ("CCPS")
9. Department of Revenue ("DoR")
10. Depository Participants ("DPs")
11. Designated Bank Branches ("DBBs")
12. Designated Depository Participants ("DDPs")
13. Domestic Venture Capital Fund ("DVCF")
14. Financial Action Task Force ("FATF")
15. Follow On Public Offer ("FPO")
16. Foreign Direct Investment ("FDI")
17. Foreign Exchange Management Act ("FEMA")
18. Foreign Institutional Investor ("FII")
19. Foreign Investment Promotion Board ("FIPB")
20. Foreign Portfolio Investor ("FPI")
21. Foreign Venture Capital Investor ("FVCI")
22. Global Custodians ("GCs")
23. Government of India ("GoI")
24. Indian Depository Receipts ("IDR")
25. Initial Public Offer ("IPO")
26. International Organization of Securities Commissions ("IOSCO")
27. International Securities Identification Number ("ISIN")
28. Indian Venture Capital Undertaking ("IVCU")
29. Know Your Client/Customer ("KYC")
30. Ministry of Finance ("MoF")
31. Multilateral Memorandum of Understanding ("MMOU")
32. Mutual Funds ("MFs")
33. Non Designated Bank Branches ("NDBBs")
34. Non-Banking Financial Companies ("NBFC")
35. Non-resident External ("NRE")
36. Non-Resident Indian ("NRI")
37. Non-Resident Ordinary ("NRO")
38. Offshore Derivatives Instrument ("ODI")
39. Offer for Sale ("OFS")
40. Organisation for Economic Co-operation and Development ("OECD")
41. Participatory Notes ("PNs")
42. Pass Through Certificates ("PTC's")

43. Protected Cell Company/Segregated Portfolio Company/Multi Class Share Vehicle ("PCC/ SPC/ MCV")
44. Permanent Account Number ("PAN")
45. Persons of Indian Origin ("PIO")
46. Portfolio Investment Scheme ("PIS")
47. Power of Attorney ("POA")
48. Prevention of Money Laundering Act ("PMLA")
49. Institutional Placement Programme ("IPP").
50. Qualified Depository Participant ("QDP")
51. Qualified Financial Investor ("QFI")
52. Reserve Bank of India ("RBI")
53. Issue of Capital and Disclosure Requirements ("ICDR")
54. Securities and Exchange Board of India ("SEBI")
55. Security Receipts ("SRs")
56. Sovereign Wealth Fund ("SWF")
57. Special Non-resident Rupee Account ("SNRA")
58. Sub Accounts ("SAs")
59. Ultimate Beneficial Owner ("UBO")
60. Unique Client Code ("UCC")
61. Working Group on Foreign Investment in India ("WGFI")