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ABOUT US

WHITE BLACK LEGAL is an open access, peer-reviewed and refereed journal provided dedicated to express views on topical legal issues, thereby generating a cross current of ideas on emerging matters. This platform shall also ignite the initiative and desire of young law students to contribute in the field of law. The erudite response of legal luminaries shall be solicited to enable readers to explore challenges that lie before law makers, lawyers and the society at large, in the event of the ever changing social, economic and technological scenario.

With this thought, we hereby present to you

REGULATORY LANDSCAPE OF CROSS-BORDER INVESTMENT IN INDIA

AUTHORED BY - ADV. VAISHNAVI PARATE

ABSTRACT

The large pool of highly qualified workers is one element that guarantees international investors a strong return on their investments. Should foreign Businesses consider the short-term advantages? The worldwide financial environment has made cross-border banking transactions essential for smooth international commerce and investment. Given the rapidly developing economic linkages between India and the rest of the globe, it is critical to resolve legal difficulties about cross-border banking rules. This article explores the present state of cross-border banking rules in India, focusing on jurisdictional concerns, legal difficulties, and continuing initiatives to promote effective international financial operations. Making the correct entity structure choice aids in the company's financial success and helps it become a major force in the Indian market. Three Foreign investment methods are available in India are as follows: FVCI, FPI, and FDI. FDI In India, FDI is the most common and favoured kind of investment, and it is the subject of this chapter. The following section discusses the FDI mode's accompanying conditionalities, regulations, and limits on investments. "Investment through equity instruments by a person resident outside India in an unlisted Indian company; or 10% or more of the post-issue paid-up equity capital on a fully diluted basis of a listed company" is how the FEMA Regime defines foreign direct investment (FDI).

INTRODUCTION

India has made major structural economic reforms in recent years to improve the business climate. These measures include eliminating retroactive taxation, modernising bankruptcy and labour laws, easing limits on international investment, and substituting a federal Goods and Services Tax for state border taxes. However, ongoing trade barriers prevent bilateral trade from growing and provide difficulties for Indian manufacturers looking to join international supply networks. These policies include enacting norms and laws unique to India that essentially bar the importation of products and services, encouraging the localization of production to promote "self-reliance," and levying some of the highest tariffs among the major

countries. Is it a Cross-Border Investment, though? “The term "cross-border investment" describes net inflows of capital used to purchase a long-term management stake (10 per cent or more of voting shares) in a business that operates in a different country than the investor. Stated differently, Investing in a foreign-incorporated firm in your capacity through the purchase of shares and/or debentures, or in your company capacity through mergers and acquisitions, the formation of a new company, the acquisition of an existing company, etc. It is believed that using foreign money will close the gap between local savings and investment.”¹

REQUIREMENTS OF ENTRY & ESTABLISHMENT

For international investors wishing to establish their firms in India, there are several entity alternatives accessible. These include liaison offices, project offices, branch offices, limited liability partnerships (LLP), and completely owned subsidiaries. Every entity type has benefits and drawbacks. It is important to select an appropriate entity type based on the sort of work and the industry the firm plans to invest in. Therefore, before investing, we advise businesses to thoroughly research several entry approaches. Through unincorporated corporations, which let foreign entities conduct business in India using any of the following methods:

Branch Office: The Reserve Bank of India ("RBI") must give its prior approval before a foreign firm can open a branch office in India. While examining the application, RBI takes into account the applicant company's history, current commercial connections with India, the company's proposed establishment of an office in India, and its financial standing. “A branch office may serve as the international parent company's representative for purchases or sales in India.” Subject to the payment of relevant taxes, the branch office's profits are freely remittable from India. “A branch office's ability to do some operations is limited, e.g., it cannot conduct any form of retail trade or engage in manufacturing or processing activities in India, either directly or indirectly. For international businesses looking to do research and development in India, it is an alternative.”²

Liaison Office: The RBI must give its prior approval before opening a liaison office. A liaison

¹ NEXGENO, *Foreign Investment in India: Regulatory Framework* | Ahlawat & Associates, [HTTPS://WWW.AHLAWATASSOCIATES.COM](https://www.ahlawatassociates.com), <https://www.ahlawatassociates.com/blog/foreign-investment-in-india-and-its-regulatory-framework> (last visited Apr 1, 2024).

² India: Overview of the Legal Framework and Treatment of FDI, <https://globalcompetitionreview.com/guide/foreign-direct-investment-regulation-guide/third-edition/article/india-overview-of-the-legal-framework-and-treatment-of-fdi> (last visited Apr 1, 2024).

office, often called a representative office, is limited to liaison tasks, such as serving as a communication link between parties in India and the head office outside. It is not permitted to conduct business in India and is not able to generate revenue there. These offices' entire operating budget must come from foreign exchange remittances sent in from the main office located outside of India. Therefore, the only duties assigned to these offices are gathering data on potential market prospects and educating potential Indian clients about the business and its offerings. Initial approval to establish a liaison office is good for three years, with potential extensions. In India, a LO is not permitted to engage in any economic activity that generates income. They are unable to do business, trade, or manufacture, thus their foreign parent company's inward remittances are required to cover its operational expenses.

Project Office: If certain requirements are met, a foreign corporation may establish a project office in India automatically. The operations of a project office have to be associated with or ancillary to carrying out the pertinent project. It is legal for a project office to keep an account with an Indian bank and to send any extra money from the project to the overseas parent business. Businesses working on installation or one-time turnkey projects typically choose project offices. It has a time restriction on it. "For instance, suppose a foreign business gets awarded a contract to carry out an installation or infrastructure project in India through project offices that are properly registered with the Registrar of Companies (ROC) and the RBI. A WOS may operate in a completely different industry from that of its parent firm, or it may operate in the same sector."³

ACCESS TO THE SECTORS AND MARKETS

Who is qualified to invest across borders?

Any of the following individuals can make an overseas investment in India. A single person or a collection of connected people An Open Firm, An Independent Business, An Organization inside Government Social institutions or a trust. The following individuals are eligible to make inward investments in India.

"A non-resident alien or an overseas citizen Subject to the FDI policy, a non-resident that is, someone who is not a citizen of Bangladesh or Pakistan or a business incorporated in either country may invest in India, except certain industries and activities. Under the unique

³ NEXGENO, *supra* note 1.

permission granted to NRIs under the FDI Policy, a business, trust, or partnership firm formed outside of India and owned and managed by NRIs may make investments in India.”⁴

In terms of nominal Gross Domestic Product, India ranks seventh globally and has the second-highest population. As such, the state of the global economy is highly dependent on the advancement of the country. The expansion of the Indian economy and enhancing the business climate seem to be top priorities for the government. “It has made several efforts to improve attitudes among both local and foreign investors, turn the Indian economy into a worldwide centre for manufacturing, and draw in financial and technical investment. Both the automatic route and the government (approved) route are considered for foreign direct investment into India under the FEMA Regime.” The industry that the Indian investee firm operates in and the amount of the investment will determine the possible investment avenue. Under the automatic method, up to 100% of FDI or any other maximum that may be specified for a sector is allowed without any permission from the government or RBI. Manufacturing, telephony, and other financial services are among the industries covered by the 100% automated route. “Furthermore, the 100% automatic route applies to industries and activities that are not subject to any sectoral cap and are neither expressly mentioned under the FEMA Regime nor given within the forbidden sectors as indicated below. However, FDI in certain industries is still governed by the laws and policies in force. Any investment made through this route is subject to the criteria that may be specified by the government, RBI, or both in its approval. Investments in sectors falling under the government route require prior permission from the government, RBI, or both.”⁵

AUTOMATIC

The automatic route permits foreign investment in the majority of industries without the Indian government's previous consent. “The automatic route to foreign investment allows investment in certain areas, subject to certain restrictions and constraints, as outlined in the Foreign Direct Investment (FDI) policy. For example, the automatic route permits foreign investment in the following industries: manufacturing, e-commerce, railway infrastructure, asset construction companies, credit information companies, pharmaceuticals, plantations, mining, petroleum and natural gas, airports, construction, manufacturing, industrial parks, and agriculture and animal

⁴ *Id.*

⁵ *Id.*

husbandry.”⁶

GOVERNMENTAL

“The government route, sometimes referred to as the approval route in FDI, is the process by which foreign direct investments need to have the Reserve Bank of India ("RBI") or the government's prior clearance.” This guarantees appropriate regulation of the industries where the participation of foreign entities is essential. The Indian government must give its prior consent before the government may direct foreign investment into certain areas. The Foreign Direct Investment (FDI) policy delineates the industries and prerequisites for allowing foreign investment through the government method.

CORPORATE TAXATION

“The tax that resident firms must pay is based on their total worldwide income minus the permissible deductions that they can claim, such as materials costs, labour, salaries, bonuses, commissions, rent, insurance, interest, lease payments, and depreciation.” If a business is entirely controlled and managed from India or is incorporated there, it is considered a resident firm. A resident firm is eligible for various incentives and refunds in addition to lower taxes. Any firm that does not fit the above definition of a resident company is considered a foreign company. For revenue that is either directly or indirectly received from Indian sources, foreign corporations are liable to Indian income tax. “A foreign company's branch is subject to corporation tax on the earnings that are attributable to it at the foreign company's rate. The computation of taxable income for firms involves the consideration of company earnings or gains, capital gains, and income derived from other sources.”⁷

“One is to codify into law the economic and moral rights of artists over their works as well as the public's right of access to them. Second, as a purposeful act of policy, the government should support fair trade, which will advance social and economic development, as well as innovation and the distribution and implementation of its findings.” Since the information technology age began, intellectual capital has become increasingly significant. As a result, intellectual property and the rights associated with it, or "IPRs," have gained significant value

⁶ *Id.*

⁷ What is Cross Border Investment and its regulations in India?, DILZER CONSULTANTS PRIVATE SEBI REGISTERED INVESTMENT ADVISOR, <https://www.dilzer.net/public/financial-health/what-is-cross-border-investment-and-its-regulations-in-india> (last visited Apr 1, 2024).

and are subject to ardent protection.

Important terms from deal structures and elements contributing to deal success

To execute transactions successfully, a transaction must be properly structured. “While acquiring an Indian business can benefit from local management and geographic strength, joint ventures and strategic alliances can accomplish business objectives without requiring integration, new reporting procedures, compliance with foreign government laws, or other post-deal issues.” Consequently, conducting enough due diligence and properly structuring a deal is crucial. “The transaction paperwork should also contain other significant articles including indemnity, damages, non-compete, confidentiality, and a dispute resolution clause, in addition to the parties' relevant representations and warranties.”⁸

TRADE IN INDIA

Many manufacturers and service providers are interested in doing business with India, even if other people may only want to conduct business in India. India is a profitable export location with a market. Customs duty is the main levy that applies to products imported into India.

Customs Tax

Duty-free imports and exports are subject to customs charges if there is any trafficking of commodities across an Indian customs barrier. Imports into or exports out of India are taxable events. Excise duty levied on a similar product made or produced in India is equivalent to the additional customs charge, often known as the countervailing duty (or "CVD"). The purpose of the CVD is to equalise the price of imported products with locally produced items that have already paid an excise duty due to their manufacturing in India. “The CVD is levied at the same rate as the excise duty levied on indigenous goods. Apart from the aforementioned additional duties in place of state and local taxes, or "ACD," are levied as a countervailing duty against state-imposed value-added tax and sales tax.” Currently, 4% of sales are subject to the ACD. Furthermore, the Central Government may establish a Safeguard Duty if it is convinced that there are circumstances that call for prompt action to safeguard the interests of any industry against an unexpected spike in the import of products of a certain class or classes. The purpose of the temporary safeguard duty on certain commodities is to shield a specific industry against an unexpected increase in imports. The Central Government may levy an anti-dumping duty

⁸ *Id.*

on imported goods under Section 9A of the Tariff Act if the exporting country's normal value is less than the amount being shipped to India.

SECURITIES TYPES

“A non-resident may invest in any of the following equity instruments of an Indian firm under the FEMA Regime's FDI mode: Partially paid shares, fully paid and legally convertible preference shares, fully paid and legally convertible debentures, and share warrants are examples of equity shares. The FEMA Regime also allows for optionality provisions in equity instruments, provided that they are subject to the conditionalities for the particular sector or a minimum lock-in duration of one year. The non-resident may leave when the lock-in time ends, but there is no guarantee that they will return.”⁹

FVCI

“A foreign venture capital investor (FVCI) is incorporated and formed outside of India and has to be registered with SEBI. An FVCI may invest in unlisted securities of Indian businesses operating in the following industries: biotechnology; IT-related fields such as hardware and software development; nanotechnology; seed and pharmaceutical industry research and development; creation of new chemical entities; dairy and poultry industries; biofuel production; lodging establishments and convention centres that can accommodate more than 3,000 people; and the infrastructure sector.”¹⁰

If FVCIs abide by the relevant SEBI requirements, they may also invest in securities of listed Indian firms. “Choosing to invest through an FVCI offers investors the following advantages: (1) FVCIs are not subject to pricing restrictions that apply to foreign direct investment (FDI) investments; and (2) shares held by an FVCI are not subject to the one-year statutory lock-in period after the initial public offering, as long as the FVCI has held the shares in question for at least six months after the date of acquisition.”¹¹

RESTRICTED SECTORS

The following industries in India are off-limits to foreign investment:

Press Note 3 of 2020 limits foreign direct investment (FDI) from nations like China, Pakistan,

⁹ Indian Legal Landscape in the Context of Cross Border Business, <https://samistilegal.in/indian-legal-landscape-in-the-context-of-cross-border-business/> (last visited Apr 1, 2024).

¹⁰ *Id.*

¹¹ NEXGENO, *supra* note 1.

Bangladesh, Afghanistan, and others that border India on land. In India, several industries are off-limits to foreign direct investment (FDI): gaming and betting, lottery, chit funds, and transferable development rights trade. Nonetheless, under the automatic method, India's military industry currently accepts consolidated FDI of up to 49%.

Prohibited Sectors

The following industries restrict foreign direct investment (FDI) in entities:

The lottery industry; gaming and betting, such as casinos; Nidhi firms; chit funds; trading in transferable development rights; real estate or building farm homes; producing tobacco or tobacco substitutes for use in cigars, cheroots, cigarillos, and cigarettes; Nuclear energy, railroad operations (apart from those expressly allowed by the FEMA Regime), and foreign technology collaborations in any form including franchise, trademark, brand name, and management contract licensing are among the industries or activities that are closed to private sector investment. Lottery, gambling, and betting operations are also prohibited.

DISPUTE RESOLUTION

International businesses should choose offshore arbitration with Indian rivals since it might take over ten years to resolve disputes in Indian courts. The recent Supreme Court decision of *PASL Wind Solutions v. GE Power* established that Indian parties have the option to choose an arbitration seat outside of India, even though contracts are frequently made through Indian companies. Given the parallels between the legal systems of these jurisdictions and India, Singapore and London were determined to be the most popular arbitration centres in a 2021 poll conducted in collaboration with White & Case and Queen Mary University of London. As such, both locations may be appealing for arbitration involving conflicts involving India. In the past ten years, international investors have also filed lawsuits against India for their investments made by several bilateral investment treaties.¹²

OWNERSHIP RESTRICTIONS

The following ownership limits apply to foreign investment in India: the implementation of ownership limitations by India on foreign investment from nations bordering it on land. "Only with government approval may a company from a nation sharing a land border with India, or where the beneficial owner of an investment into India is located, invest in India." Most

¹² (1918) 1 KB 247 (CA).

industries allow 100% foreign ownership of businesses and entities, although others may have limits or need government clearance. Non-resident entities are permitted to invest in India under the terms of the Foreign Direct Investment (FDI) Policy, except for some industries and activities that are restricted. India allows non-resident entities from nations other than Bangladesh and Pakistan to make investments.

CONCLUSION

India's economy continues to thrive mostly due to foreign investment. The limits on foreign investment in several areas are outlined in these rules. They fit into the following categories: Industries classified as Prohibited Sectors, meaning they are off-limits to foreign direct investment; Industries classified as Automatic Route, meaning they allow foreign investment into an Indian company without the need for previous government clearance. Once more, these fall into two categories: sectors where automated routes allow FDI up to 100%. Industries where foreign direct investment (FDI) is automatically allowed but is subject to set threshold restrictions; that is, FDI in certain industries cannot exceed the set limits. Sectors covered by the Approval Route, or places where FDI is only permitted with the Central Government's prior consent. sectors with a partial government route and a partly automated route, meaning that foreign investment is permitted under the automatic route up to a particular proportion and requires government permission for investment over that amount. The sentiment of a nation's residents toward foreign businesses, goods, and people is another crucial component. Citizens of nations that have previously been under the sway of foreign powers are naturally suspicious of strangers and may be reluctant to welcome foreign investment, preferring to promote their native goods. Furthermore, the legal component may differ from nation to nation; that is, if one nation does not impose an excessive amount of formalities on foreign investment, it may not be required, and other nations would follow suit. "One way to determine whether a market is attractive is to look at its potential revenue generation, accessibility to the market based on the host nation's willingness to accept investments from foreign corporations, potential competition, and industry dynamics."¹³ A large market that is expanding quickly can be highly alluring, and in such a market, a significant upfront investment can make sense. The market is more appealing when there are fewer well-established competitors and consistency in the kind and quantity of competitors. The company's capacity to make investments in this kind of market

¹³ Recent regulatory and industry trends in India involving cross-border financings, FINANCIER WORLDWIDE, <https://www.financierworldwide.com/recent-regulatory-and-industry-trends-in-india-involving-cross-border-financings> (last visited Apr 1, 2024).

is the final and most crucial consideration. “A corporation should assess its skills and resources before deciding to expand internationally. The company needs to have distinct competitive advantages in terms of technology, product portfolio, dependable partners, and other pertinent factors.”¹⁴ If not, it risks suffering significant losses in international markets or incurring losses so severe that it could negatively impact its reputation in the home market.



¹⁴ *Id.*