

NON-REPATRIABLE INVESTMENT BY NRIs/OCIs UNDER FEMA: AN ANALYSIS – PART 2

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NON-REPATRIABLE INVESTMENTS: EASY ENTRY, TRICKY EXIT!

In Part I, we explored how NRIs and OCIs can invest in India under Schedule IV, enjoying the perks of domestic investment while sidestepping FDI restrictions. We saw how this route offers flexibility in entry—with no foreign investment caps, no strict pricing rules, and freedom to invest in LLPs, AIFs, and even real estate (as long as it's not a farmhouse!). But, much like a long-term relationship, once you commit, FEMA expects you to stay for the long haul.

Now, in Part II, we address the big question: Can you transfer, sell, or gift these investments? Will FEMA allow you a graceful exit? We'll dive into the rules governing transfers, repatriation limits, downstream investments, and more—so buckle up, because while the non-repatriable entry was smooth, the exit is where the real thrill begins!

TRANSFER OF SHARES/INVESTMENTS HELD ON NON-REPATRIATION BASIS

Just as important as the entry is the ability to **transfer or exit** the investment. FEMA provides certain pathways for transferring shares or other securities that were held on a non-repatriation basis:

- **Transfer to a Resident:** An NRI/OCI can **sell or gift the securities to an Indian resident** freely. Since the resident will hold them as domestic holdings, this is straightforward. **No RBI permission, pricing guideline, or reporting form is required.** For instance, if an NRI uncle wants to gift his shares (held on a non-repat basis) in an Indian company to his resident Indian nephew, it's permitted and no specific FEMA filing is triggered (aside from perhaps a local gift deed for records). Similarly, suppose an NRI non-repat investor wants to sell his stake to an Indian co-promoter. In that case, he can transact at any price mutually agreed upon (pricing restrictions don't apply as this is essentially a resident-to-resident transfer in FEMA's eyes), and no FC-TRS form is required.

- **Transfer to another NRI / OCI on Non-Repat basis:** NRIs / OCIs can also **transfer such investments amongst themselves, provided the investment remains on non-repatriation.** For example, one OCI can gift shares held under Schedule IV to another OCI or NRI (maybe a relative) who will also hold them under Schedule IV. This is allowed without RBI approval, and again, no pricing or reporting requirements apply. The only caveat is that the transferee must be eligible to hold on a non-repat basis (which generally means they are NRI / OCI or their entity). Gifting among NRIs / OCIs on the non-repat route is quite common within families. **Note:** If it's a gift, one should ensure it meets any conditions under the Companies Act or other laws (for instance, if the donor and donee are "relatives" under Section 2(77) Companies Act, as required by FEMA for certain cross-border gifts – more on that below).

- **Transfer to an NRI / OCI on a repatriation basis (i.e., converting it to FDI):** This scenario is effectively an **exit from the non-repatriable pool into the repatriable pool.** For instance, an NRI with non-repat shares might find a foreign investor or another NRI who wants those shares but *with repatriation rights*. FEMA permits the sale, but since the buyer will hold on a repatriation basis (Schedule I or III), it must conform to **FDI rules**. That means **sectoral caps and entry routes must be respected, and pricing guidelines apply** to the transaction. If it's a **gift** (without consideration) from an NRI (non-repat holder) to an NRI / OCI (who will hold as repatriable), **prior RBI approval is required** and certain conditions must be met. These conditions (laid out in NDI Rules and earlier in TISPRO) include: (a) the donee must be eligible to hold the investment under the relevant repatriable schedule (meaning the sector is open for FDI for that person); (b) the gift amount is within 5% of the company's paid-up capital (or each series of debentures / MF scheme) cumulatively; (c) sectoral cap is not breached by the donee's holdings; (d) donor and donee are relatives as defined in Companies Act, 2013; and (e) the value of securities gifted by the donor in a year does not exceed USD 50,000. These

are designed to prevent the abuse of gifting as a loophole to transfer large foreign investments without consideration. If all conditions are met, RBI may approve the gift. If it's a **sale (for consideration)** by NRI non-repat to NRI/OCI repatriable, no prior approval is needed (sale is under automatic route) but pricing must be at or higher than fair value (since NR to NR transfer with one side repatriable is treated like an FDI entry for the buyer). **Form FC-TRS must be filed** to report this transfer, and in such a case, since the **seller was holding non-repat**, the onus is on the seller (who is the one changing their holding status) to file the FC-TRS within 60 days. Our earlier table from the draft summarizes: Seller NRI-non-repat -> Buyer NRI-repat: pricing applicable, FC-TRS by seller, auto route subject to caps.

• **Transfer from a foreign investor (repatriable) to an NRI/OCI (non-repatriable):** This is the reverse scenario – a person who holds shares as foreign investment sells or gifts to an NRI / OCI who will hold as domestic. For example, a foreign venture fund wants to exit and an OCI investor is willing to buy but keep the investment in India. FEMA allows this as well. Since the new holder is non-repatriable, the sectoral caps don't matter post-transfer (the investment leaves the FDI ambit). However, up to the point of transfer, compliance should be there. In a **sale** by a foreign investor to an NRI on a non-repat basis, **pricing guidelines again apply** (the NRI shouldn't pay more than fair value, because a foreigner is exiting and taking money out – RBI ensures they don't take out more than fair value). **FC-TRS reporting** is required, and typically, the **buyer (NRI / OCI)** would report it because the buyer is the one now holding the securities (the authorized dealer often guides who should file; it has to be a person resident in India and as non-repat investment is treated as domestic investment, it has to be filed by NRI / OCI acquiring it on non-repat basis). If it's a **gift** from a foreign investor to an NRI / OCI relative, RBI approval would similarly be needed with analogous conditions (the NDI Rules conditions on gift apply to any resident outside to resident outside transfer, repatriable to non-repat likely treated similarly requiring approval unless specified otherwise). The draft table indicated: Buyer NRI-non-repat from Seller foreign (repat) – gift allowed with approval, pricing applicable, FC-TRS by buyer, and subject to FDI sectoral limits at the time of transfer.

In all the above cases of **change of mode (repatriable vs non-repatriable)**, one can see FEMA tries to ensure

that whenever money is leaving India (repatriable side), fair value is respected and RBI is informed. But when the money remains in India (purely domestic or non-repat transfers), the regulations are hands-off.

Downstream Investment Impact: A critical implication of holding investments on non-repatriation basis is how the investing company is classified. FEMA and India's FDI policy have the concept of **indirect foreign investment** – if Company A is foreign-owned or controlled, and it invests in Company B, then Company B is considered to have foreign investment to that extent. However, **Schedule IV investments are excluded from this calculation**. The rules (as clarified in DPIIT's policy) state that if an Indian company is owned and controlled by NRIs / OCIs on a non-repatriation basis, **any downstream investment by that company will not be considered foreign investment**. In other words, an Indian company that has only NRI / OCI non-repat capital is treated as an **Indian-owned company**. So if it later invests in another Indian company, that target company doesn't need to worry about foreign equity caps because the investment is coming from an Indian source (deemed). This is a major benefit – it effectively **ring-fences NRI domestic investment from contaminating downstream entities with foreign status**. This clarification was issued to remove ambiguity, especially in cases where OCIs set up investment vehicles. Now, an NRI / OCI-owned investment fund (registered as an Indian company or LLP) can invest freely in downstream companies without subjecting them to FDI compliance, provided the fund's own capital is non-repatriable.

From a practical standpoint, when structuring private equity deals, if one of the investors is an NRI / OCI willing to designate their contribution as non-repatriable, the company can be treated as fully Indian-owned, allowing it to invest into subsidiaries or other companies in restricted sectors without ceilings. This has to be balanced with the investor's interest (since that NRI loses repatriation right). Often, OCIs with a long-term commitment to India might be agreeable to this to enable, say, a group structure that avoids FDI limits.

Summary of Transfer Scenarios: For quick reference:

• **NRI / OCI (Non-repat) -> Resident:** Allowed, **gift allowed**, no pricing rule, no reporting.

• *Resident -> NRI / OCI (Non-repat)*: Allowed, gift allowed, no pricing rule, no reporting (essentially the mirror of above, turning domestic holding into NRI non-repat).

• *NRI / OCI (Non-repat) -> NRI / OCI (Non-repat)*: Allowed, gift allowed, no pricing, no reporting.

• *NRI / OCI (Non-repat) -> Foreigner / NRI (Repat)*: Allowed, the **gift needs RBI approval (with conditions)**, if sale then pricing applies; report FC-TRS.

• *Foreigner / NRI (Repat) -> NRI / OCI (Non-repat)*: Allowed, gift possibly with approval; sale at pricing; report FC-TRS.

The key is whether the **status of the investment (domestic vs foreign) changes** as a result of transfer, and ensuring the appropriate regulatory steps in those cases.

Comparative Interplay Between Schedules I, III, IV, and VI

To fully understand Schedule IV in context, one must compare it with other relevant schedules under FEMA NDI Rules:

Schedule I (FDI route) vs Schedule IV (NRI non-repat route)

• **Nature of Investment**: Schedule I covers FDI by any person resident outside India (including NRIs) on a repatriation basis. Schedule IV covers investments by NRIs / OCIs (and their entities) on a non-repatriation basis. Schedule I investments count as foreign investment; Schedule IV do not.

• **Sectoral Caps and Conditions**: Schedule I investments are subject to sectoral caps (% limits in various sectors) and sector-specific conditions (like minimum capitalization, lock-ins, etc., in sectors like retail, construction, etc.). By contrast, Schedule IV investments are generally not subject to those caps/conditions because they are treated as domestic. For example, multi-brand retail trading has a 51% cap under FDI with many conditions – an OCI could invest 100% in a retail company under Schedule IV with none of those conditions, as long as it's on a non-repatriation basis. Similarly, real estate development has minimum

area and lock-in requirements under FDI, but an NRI could invest non-repat without those (provided it's not pure trading of real estate).

• **Prohibited Sectors**: Schedule I explicitly prohibits foreign investment in sectors like lottery, gambling, chit funds, Nidhi, real estate business, and also limits in print media, etc. Schedule IV has its own (smaller) prohibited list (Nidhi, agriculture, plantation, real estate business, farmhouses, TDR) but notably does not mention lottery, gambling, etc. **Thus, some sectors closed in Schedule I are open in Schedule IV, and vice versa** (as discussed earlier).

• **Valuation / Optionality**: Under Schedule I, any equity instruments issued to foreign investors can have an optionality clause only with a minimum lock-in of 1 year and no assured return; effectively, foreign investors cannot be guaranteed an exit price. Under Schedule IV, these restrictions **do not apply** – one can issue shares or other instruments to NRIs/OCIs with an assured buyback or fixed return arrangement since it's like a domestic deal. Likewise, provisions like deferred consideration (permitted for FDI up to 25% for 18 months) need not be adhered to strictly for non-repat investments – an NRI investor and company can agree on different terms as it's a private domestic contract in FEMA's eyes.

• **Reporting**: FDI (Sch. I) transactions must be reported (FC-GPR, FC-TRS, etc.), whereas Sch. IV initial investments are not reported to RBI as noted.

• **Exit / Repatriation**: Schedule I investors can repatriate everything freely (that's the point of FDI), whereas Schedule IV investors are bound by the NRO / \$1M rule for exits.

Bottom line: Schedule IV is far more liberal on entry (no caps, any price) but restrictive on exit, whereas Schedule I is vice versa. A legal advisor will often weigh these options for an NRI client: if the priority is to eventually take money abroad or bring in a foreign partner, Schedule I might be preferable; if the priority is flexibility in investing and less regulatory hassle, Schedule IV is attractive.

Schedule III (NRI Portfolio Investment) vs Schedule IV (NRI Non-Repatriation)

Schedule III deals with the **Portfolio Investment**

Scheme (PIS) for NRIs / OCIs on a repatriation basis, primarily buying/selling shares of listed companies through stock exchanges.

- **Listed Shares via Stock Exchange:** Under Schedule III (PIS), an NRI / OCI can purchase shares of listed Indian companies **only through a recognized stock broker on the stock exchange** and is subject to the rule that **no individual NRI / OCI can hold more than 5% of the paid-up capital** of the company. All NRIs / OCIs taken together cannot exceed 10% of the capital unless the company passes a resolution to increase this aggregate limit to 24%. These limits are to ensure NRI portfolio investments remain "portfolio" in nature and do not take over the company. In contrast, under Schedule IV, **NRIs / OCIs can acquire shares of listed companies without regard to the 5% or 10% limits** because those limits apply only to repatriable holdings. An NRI could, for instance, accumulate a larger stake by buying shares off-market or via private placements under Schedule IV.

- **Other Securities:** Schedule III also allows NRIs to purchase on a repatriation basis certain government securities, treasury bills, PSU bonds, etc., up to specified limits, and units of equity mutual funds (no limit). On this front, **both Schedule III and Schedule IV allow NRIs to invest in domestic mutual fund units freely** if the fund is equity-oriented. So whether repatriable or not, an NRI can buy any number of units of, say, an index fund or equity ETF.

- **Nature of Investor:** Schedule III is meant for NRIs investing as **portfolio investors** (often through NRE PIS bank accounts), whereas Schedule IV is not limited to portfolio activity – it can be FDI-like strategic investments too.

- **Trading vs Investment:** Under PIS (Sch. III), NRIs are typically not allowed to make the stock trading their full-time business (they cannot do intraday trading or short-selling under PIS; it's for investment, not speculation). Schedule IV has no such restriction explicitly; however, if an NRI were actively trading frequently under non-repatriation, it might raise questions – usually, serious traders stick to the PIS route for liquidity.

In summary, **Schedule III is a subset route** for market investments with tight limits, whereas **Schedule IV offers NRIs a way to invest in listed companies beyond those limits** (albeit off-market and non-

repatriable). As a strategy, an NRI who sees a long-term value in a listed company and wants significant ownership may choose to buy some under PIS (repatriable) but anything beyond the threshold under the non-repat route, combining both to achieve a larger stake.

SCHEDULE VI (FDI IN LLPs) Vs SCHEDULE IV (NRI INVESTMENT IN LLPs)

Schedule VI allows **foreign investment in Limited Liability Partnerships (LLPs)** on a repatriation basis. It stipulates that FDI in LLP is allowed only in sectors where 100% FDI is permitted under automatic route and there are no FDI-linked performance conditions (like minimum capital, etc.). This effectively bars FDI in LLPs in sectors like real estate, retail trading, etc., because those sectors either have caps or conditions. For example, multi-brand retail is 51% with conditions – so a foreign investor cannot invest in an LLP doing retail. Real estate business is prohibited entirely for FDI – so no LLP can be structured. Even an LLP in construction development is problematic under FDI if conditions (like a lock-in) are considered performance conditions.

However, **Schedule IV imposes no such sectoral conditionality for LLPs (apart from the same prohibited list)**. Therefore, **NRIs / OCIs can invest in the capital of an LLP on a non-repatriation basis even if that LLP is engaged in a sector where FDI in LLP is not allowed**. For instance, an LLP engaged in the business of building residential housing (construction development) — FDI in such an LLP would not be allowed repatriably because construction development, while 100% automatic, had certain conditions under the FDI policy. Under Schedule IV, an NRI could contribute capital to this LLP freely as domestic investment. Another concrete example: LLP engaged in **single-brand or multi-brand retail** – FDI in LLP is not permitted because retail has conditions, but NRI non-repat funds could still be infused into an LLP doing retail trade. **The only caveat** is if the LLP's activity falls under the explicit prohibitions of Schedule IV (agriculture, plantation, real estate trading, farmhouses, etc., which we already know). As long as the LLP's business is not in that small prohibited list, NRI / OCI money can be invested on non-repatriable basis.

Thus, **Schedule IV significantly expands NRIs' ability to invest in LLPs vis-à-vis Schedule VI**. It

allows the Indian-origin diaspora to use LLP structures (which are popular for smaller businesses and real estate projects), which are otherwise off-limits to foreign investors. The outcome is that an LLP which cannot get FDI can still get funds from NRI partners, treated as local funds, potentially giving it a competitive edge or needed capital infusion. As noted earlier, **an LLP receiving NRI non-repat investment remains an “Indian” entity for downstream investment purposes** as well, so it could even invest in other companies without being tagged as foreign-owned.

SCHEDULE IV Vs SCHEDULE IV (FIRM/ PROPRIETARY CONCERNS)

There is also a provision (in Part B of Schedule IV) for **investment in partnership firms or sole proprietorship concerns** on a non-repatriation basis. There is **no equivalent provision under repatriation routes** – meaning NRIs cannot invest in a partnership or proprietorship on a repatriable basis at all under NDI rules. Under Schedule IV, an NRI/OCI can contribute capital to any proprietorship or partnership firm in India provided the firm is not engaged in **agriculture, plantation, real estate business, or print media**. These mirror the older provisions from prior regulations. The exclusion of print media here is interesting, as discussed: an NRI cannot invest in a newspaper partnership but could invest in a newspaper company. This is likely a policy decision to keep sensitive sectors like news media more closely regulated (partnerships are unregulated entities compared to companies which have shareholding disclosures, etc.).

For completeness, **Schedule V** under NDI Rules is for investment by other specific non-resident entities like Sovereign Wealth Funds in certain circumstances, and Schedule VII, VIII, IX cover foreign venture capital, investment vehicles, and depository receipts respectively.

PRACTICAL CHALLENGES AND LEGAL IMPLICATIONS

While the non-repatriation route offers flexibility, it also presents some **practical challenges and considerations for legal practitioners** advising clients:

1. Exit Strategy and Liquidity: Perhaps the biggest issue is planning how the NRI/OCI will **exit or monetize the investment** if needed. Since direct repatriation of capital is capped at USD 1 million per year, clients

who invest large sums must understand that they can't easily pull out their entire investment quickly. Case in point: if an OCI invests \$5 million in a startup via Schedule IV and after a few years the startup is sold for \$20 million, the OCI cannot take \$20 million out in one go. They would either have to flip the investment to a repatriable mode before exit (e.g. sell their stake to a foreign investor prior to the main sale, thereby converting to FDI at fair value and then repatriating through that foreign investor's sale) or *accept a long repatriation timeline* using the \$1M per year route, or approach RBI (which historically is reluctant to approve a big one-shot remittance). This illiquidity needs to be clearly explained to clients

2. Mixing Repatriable and Non-Repatriable Funds: Often, companies have a mix of foreign investment – say, a venture capital fund (FDI) and an NRI relative (non-repat). In such cases, **accounting properly for the two classes is key**. From a corporate law perspective, both hold equity, but from an exchange control perspective, one part of equity is foreign, and one part is domestic. The **company's compliance team must carefully track these** when reporting foreign investment percentages to any authority or while calculating downstream foreign investment. Misclassification can lead to errors – e.g., a company might erroneously count the NRI's holding as part of FDI and think it breached a cap, or conversely ignore a foreign holding, thinking it was NRI domestic. It's advisable in company records and even on share certificates to mark non-repatriable holdings distinctly. Some companies create separate folios in their register for clarity..

3. Corporate Governance and Control: Because Schedule IV allows NRIs to invest beyond usual foreign limits, we see scenarios of **foreign control via NRI routes**. For example, foreign parents could nominate OCI individuals to hold a majority in an Indian company so that it is "Indian owned" but effectively under foreign control through OCI proxies. Regulators are aware of this risk. The law currently hinges on **“owned and controlled by NRIs / OCIs”** as the test for deeming it domestic. If an OCI is truly acting at the behest of a non-OCI foreigner, that could be viewed as a circumvention. In diligence, one should ensure OCI investors are bona fide and making decisions independently, or at least within what law permits. If an Indian company with large NRI non-repat investment is making downstream investments in a sensitive sector, one must document

that control remains with OCI and not via any agreement handing powers to someone else, lest the structure be challenged as a sham.

4. Changing Residential Status: An interesting practical point – if an NRI who made a non-repat investment later moves back to India and becomes a resident, their holding simply becomes a resident holding (no issue there). But if they then move abroad again and become NRI once more, by default, that holding would become an NRI holding on a non-repat basis (since it was never designated repatriable). That person might now wish it were repatriable. There isn't a straightforward mechanism to "retroactively designate" an investment as repatriable; typically, the person would have to do a transfer (e.g., transfer to self through a structure, which is not really possible) or approach RBI. It's a corner case, but it shows that once an investment is made under a particular schedule, toggling its status is not simple unless a third-party transfer is involved.

7. Evidence of Investment Route: Down the line, when an NRI / OCI wants to remit out the sale proceeds under the \$1M facility, banks often ask for proof that the investment was made on a non-repatriation basis (because if it was repatriable, the sale proceeds would be in an NRE account and could go out without using the \$1M quota). Thus, maintaining paperwork – such as the board resolution or offer letter mentioning the shares are under Schedule IV, or a copy of the share certificate with a "non-repatriable" stamp, or the letter to AD bank at the time of issue – becomes useful to avoid confusion. If records are lost or unclear, the bank might fear to allow remittance or might treat it as

some foreign investment needing RBI permission. So, documentation is a practical must.

8. Taxation Aspect: Though not directly a FEMA issue, note that **dividends repatriated to NRIs** will be after TDS, and any gift of shares etc. might have tax implications (gift to a relative is not taxable in India, but to a non-relative, it could trigger tax for the recipient if over ₹50,000). Also, the favourable FEMA treatment doesn't automatically confer any tax residency benefit – e.g., just because OCI investment is deemed domestic doesn't make the OCI an Indian resident for tax

BEFORE WE ALL NEED A REPATRIATION ROUTE, LET'S WRAP THIS UP!

Before we exhaust ourselves—or our dear readers start considering their own non-repatriable exit strategies—let's conclude. The non-repatriation route under FEMA is like a VIP pass for NRIs and OCIs to invest in India while enjoying the perks of domestic investors. It's a fine balancing act by policymakers: welcoming diaspora investments with open arms but keeping foreign exchange reserves snugly in place.

For legal practitioners, Schedule IV is both a playground and a puzzle—offering creative structuring opportunities while demanding meticulous planning for exits and compliance. Done right, it's a win-win for investors and Indian businesses alike, seamlessly blending "foreign" and "domestic" investment. So, whether you're an NRI looking for investment options or a lawyer navigating these rules—remember, patience, planning, and a strong cup of chai go a long way! ■

*"We always overestimate the change that will occur
in the next two years and underestimate the change
that will occur in the next ten."*

- Bill Gates

*"Happiness comes from solving problems, not
avoiding them."*

- Mark Manson