NAVIGATING FEMA FOR OUTBOUND INVESTMENTS

An Essential Guide for Indian Companies, LLPs and Resident Individuals

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1. Why This Matters Now

India's economic footprint is expanding at a pace that would have seemed improbable two decades ago. Indian corporates are acquiring businesses in Africa, Europe, and Southeast Asia. Professionals are setting up service companies in Singapore and Dubai. Promoter families are establishing holding structures across multiple jurisdictions. The impulse to go global is strong, well-funded, and, in many cases, commercially sound.

But the compliance framework governing this outward movement is detailed. The consequences of getting it wrong are serious, and, as we shall see, the nature of those consequences ranges from a correctable administrative fee to an Enforcement Directorate inquiry.

This article is an essential working guide for Indian companies, limited liability partnerships, partnership firms and resident individuals who are setting up, or have already set up, entities outside India.

This article is updated up to 17 June 2026 and is based on the Foreign Exchange Management Act, 1999, the Foreign Exchange Management (Overseas Investment) Rules, 2022, the Foreign Exchange Management (Overseas Investment) Regulations, 2022, directions and circulars issued by the Reserve Bank of India from time to time, and the Income-tax Act, 2025, as applicable for the relevant tax year. It also covers transfer pricing considerations, common violations that we encounter repeatedly in practice, and the remedies available under the law.

Since overseas investment transactions are fact-sensitive and are also subject to AD Bank review, jurisdiction-specific documentation and tax evaluation, this note should be read as a practical guide and not as a substitute for transaction-specific advice.

2. The Regulatory Architecture

The law governing outbound investments was comprehensively rewritten in 2022. The old FEMA Notification No. 120 of 2004, which had governed overseas direct investments for nearly two decades, was replaced in its entirety by three interlocking instruments:

- The Foreign Exchange Management (Overseas Investment) Rules, 2022, issued by the Ministry of Finance under FEMA.
- The Foreign Exchange Management (Overseas Investment) Regulations, 2022, notified by the Reserve Bank of India.

- The RBI Master Direction on Overseas Investment, 2022, which provides the operational guidance for the above two instruments.

These three documents together constitute the current governing framework and must be read together. They introduced cleaner definitions, a restructured reporting architecture, and a formal Late Submission Fee mechanism to regularize procedural delays without requiring full compounding. Any Indian entity setting up overseas must work from these documents and not from the old FEMA 120 framework, which is now repealed.

Two Categories of Overseas Investment

The new framework draws a clear line between two types of investment by Indian residents.

Overseas Direct Investment (ODI) covers any equity stake in an unlisted foreign entity, a 10% or more equity stake in a listed foreign entity, or investment with control even where the holding in the listed foreign entity is less than 10%, and subscription to the Memorandum of Association of a foreign company. ODI represents an active, committed relationship between the Indian investor and the overseas entity. The overseas entity in which ODI is made must be an operating entity with a genuine business purpose. A shell company or a blank-check vehicle does not qualify. Once an investment is classified as ODI, it continues to be treated as ODI even if the holding subsequently falls below the threshold or control is lost.

Overseas Portfolio Investment (OPI) covers equity holdings below 10% in listed foreign entities, investments in foreign debt instruments, and units in foreign mutual funds or alternative investment funds, which are not covered under the definition of ODI. OPI is generally treated as a passive financial investment and carries lighter compliance obligations. For this article, the focus is primarily on ODI, since that is what most corporate outbound structures involve.

3. Who Can Invest Overseas, and How Much

Eligible Investors

The following Indian entities and persons can make ODI:

- A company incorporated under the Companies Act, 2013.
- An LLP registered under the Limited Liability Partnership Act, 2008.
- A partnership firm registered under the Indian Partnership Act, 1932
- Any other body corporate duly authorised under the statute under which it is constituted.
- A resident individual, subject to the Liberalised Remittance Scheme (LRS) and the specific conditions applicable to individuals.

Investment Limits

For Indian companies, LLPs and Partnership firms, the total Financial Commitment, which includes ODI made plus all non-fund-based commitments such as guarantees issued on behalf of the overseas entity, cannot exceed 400% of the net worth of the Indian entity as per its last audited balance sheet. Net worth is computed as paid-up equity capital plus free reserves less accumulated losses and intangible assets.

For resident individuals, the permissible limit is USD 250,000 per financial year under the LRS framework. This limit is aggregate across all capital account transactions under LRS, including overseas equity investments.

A Critical Pre-Condition

Before making a financial commitment or undertaking disinvestment, the Indian investor must verify whether any additional regulatory clearance is required. Where the Indian person has an account classified as a non-performing asset, is classified as a wilful defaulter, or is under investigation by a financial sector regulator or by the CBI, ED, or SFIO, a No Objection Certificate is required from the concerned lender bank, regulator, or investigative agency before proceeding. If the concerned authority does not issue the certificate within the prescribed period after receiving the application, the framework permits the transaction to proceed based on deemed no-objection, subject to proper documentation and AD Bank satisfaction. Accordingly, such cases should not be treated as automatically prohibited, but they do require a documented NOC process before the AD Bank allows the transaction.

4. Permitted Structures and Prohibited Sectors

Permitted Structures

Indian entities can establish the following structures abroad:

- A Wholly Owned Subsidiary (WOS), which is the most common structure and gives the Indian parent full control and full reporting responsibility.
- A Joint Venture (JV), where the Indian entity partners with one or more foreign promoters in an overseas entity.
- Step-down subsidiaries, meaning subsidiaries established by the overseas entity itself. These are permitted but must be reported separately to RBI.

Prohibited Sectors and Jurisdictions

Certain sectors and geographies are expressly prohibited. ODI cannot be made in a foreign entity engaged in real estate activity, gambling in any form, or dealing with financial products linked to the Indian rupee without specific RBI approval. For this purpose, real estate activity means buying and selling of real estate or trading in Transferable Development Rights. It does not include development of townships, construction of residential or commercial premises, roads or bridges for sale or lease. Entities in countries under United Nations Security Council sanctions are off limits entirely. Countries identified by the Financial Action Task Force (FATF) as having significant deficiencies in anti-money laundering or counter-terrorism financing frameworks are also restricted. The FATF list changes periodically, and the Indian investor must verify it before proceeding.

Round-Tripping – Needs closure examination

Roundtripping requires a nuanced analysis under the current OI framework. The 2022 framework does not treat every ODI-FDI structure as automatically prohibited. However, no person resident in India may make financial commitment in a foreign entity which has invested or invests into India, directly or indirectly, if the result is a structure with more than two layers of subsidiaries, except in cases specifically carved out under the applicable rules. Even where the two-layer restriction is technically satisfied, any structure involving flow of funds from India to an overseas entity and subsequent investment back into India must be tested for commercial substance, beneficial ownership, source of funds, tax purpose, valuation, and possible scrutiny by RBI, the AD Bank, the Income-tax Department and the Enforcement Directorate. Such structures should not be implemented without a documented legal and tax review.

5. The Compliance Roadmap: From Concept to Capital

An outbound investment is not a simple wire transfer. It involves a defined sequence of steps, each of which has a legal basis. Skipping any one of them can create a compoundable violation.

Step 1: Eligibility and sector check. Before any commitment is made, confirm that the proposed investment is in a permitted sector and jurisdiction, that the aggregate financial commitment will remain within 400% of net worth, and that no disqualification applies to the Indian investor.

Step 2: Engage the Authorised Dealer Bank. Every FEMA capital account transaction must be routed through a bank designated as an Authorised Dealer (AD Bank). The AD Bank is the first and most important compliance checkpoint. It has its own due diligence obligations under the OI Regulations, and it will call for KYC documents, a certified copy of the overseas entity's incorporation documents, a valuation report where applicable, and a board resolution of the Indian entity authorising the investment.

Step 3: File Form FC (ODI) and Obtain UIN. Before the investment is remitted, Form FC (ODI) must be filed with the AD Bank. The AD Bank then reports this filing to the Reserve Bank of India through the FIRMS portal. Form FC captures the details of the Indian investor, the overseas entity, the nature and amount of investment, and the business rationale. On successful filing, the overseas entity is assigned a Unique Identification Number (UIN) by RBI. This UIN is the reference point for all future reporting relating to that overseas entity.

Step 4: Remittance through banking channels. Route payment through a permitted mode. Payment for overseas investment is ordinarily made through banking channels via the designated AD Bank. The framework also recognises other permitted modes, including payment from funds held in accounts maintained in accordance with FEMA, swap of securities, and use of ADR / GDR / stock-swap proceeds or ECB proceeds in accordance with the applicable conditions. The practical rule remains simple: the payment route must be FEMA-compliant, properly documented, and acceptable to the designated AD Bank before the transaction is executed.

Step 5: Obtain and submit allotment documents. After remittance, capitalisation or acquisition of equity capital, the Indian investor must obtain share certificates, register extracts or other legally acceptable evidence of investment under the host country law. Such evidence must be submitted to the AD Bank within the prescribed period. This is an important compliance step and should not be treated as a mere post-closing formality.

Step 6: Report subsequent investments, loans, and guarantees. Each additional round of equity, any loan extended to the overseas entity, and any guarantee given on its behalf must be reported through Form FC. These transactions also count toward the 400% financial commitment limit.

Step 7: File the Annual Performance Report and FLA. For each foreign entity in which ODI is held, the Indian investor is required to submit the Annual Performance Report by 31 December every year. Where the accounting year of the foreign entity ends on 31 December, the APR is to be submitted by 31 December of the following year. The APR is generally based on audited financial statements of the foreign entity, though unaudited financials may be accepted in limited cases where the Indian investor does not have control, and the host jurisdiction does not mandate audit. The Indian entity must also ensure filing of the Annual Return on Foreign Liabilities and Assets within the time prescribed by RBI.

Step-down subsidiaries require careful annual tracking. Where the foreign entity acquires, sets up, winds up or transfers a step-down subsidiary, or where there is any change in the shareholding pattern of the foreign entity during the reporting year, the relevant details must be captured in the APR. Technology, trading and holding company structures frequently miss this requirement because overseas subsidiaries often create local operating entities without involving the Indian parent’s finance and compliance team at the planning stage.

Step 8: Report disinvestment and closure. Any disinvestment must be reported within the prescribed time after receipt of disinvestment proceeds. Restructuring must also be reported within the applicable timeline. Dues receivable from the foreign entity, disinvestment proceeds, and net realisable value on liquidation must be repatriated to India within the prescribed period, unless a specific permission or permissible treatment is available under FEMA. Exit documentation should therefore be reviewed before execution and not after funds are received.

6. RBI Reporting: What You Must File and When

All reporting under the OI framework is done through the FIRMS portal of the Reserve Bank of India. The investor does not file directly. The AD Bank files on behalf of the investor, based on the documents and information provided to it.

The key filings are:

- Form FC (ODI): Filed before or on the date of each investment round. Every overseas entity in which ODI is made gets a UIN, which is referenced in all future filings for that entity.
- Annual Performance Report (APR): Filed by December 31 every year. The APR reflects the audited or management-certified financials of the overseas entity for the year ended March 31. A CA certificate is mandatory. Where the overseas jurisdiction does not require statutory audit, management-certified accounts are accepted, but they must be accompanied by a CA's review certificate.
- Step-down subsidiary report: If the overseas entity sets up its own subsidiary, this step-down structure must be reported within 30 days of its formation or acquisition.
- Disinvestment report: Filed within 30 days of completion of exit from the overseas entity.

Late Submission Fees (LSF) apply to delayed filings. Delayed reporting under the OI framework may be regularised through the Late Submission Fee mechanism in eligible cases. LSF is available for delayed submission of evidence of investment and delayed filings prescribed under the OI Regulations, subject to the manner, rate and period specified by RBI. The facility is subject to an outer time limit, and no further financial commitment or transfer in relation to the foreign entity should be undertaken until the reporting delay is regularised. Where the delay is beyond the LSF window, or where the contravention is substantive rather than procedural, compounding or specific regulatory advice may be required.

The LSF is calculated on the amount involved and the period of delay, with a prescribed formula and a maximum cap. The LSF mechanism was introduced to provide a lighter-touch regularization route for delays, as an alternative to compounding. In our experience, most investors prefer the LSF route for procedural delays, since it does not create a formal compounding record.

Investors often ask whether an APR needs to be filed for an overseas entity that has had no activity during the year. The answer is yes. The APR obligation exists so long as the Indian investor holds an ODI stake in the overseas entity, regardless of whether the entity conducted any business.

7. Transfer Pricing: Getting the Structure Right

Most Indian entities that invest overseas also enter into transactions with their overseas subsidiaries or group entities. These may include management services, technical support, software development, licensing of intellectual property, loans, guarantees, procurement support, marketing support or cost-sharing arrangements.

Such transactions are required to be tested under the transfer pricing provisions of the Income-tax Act applicable for the relevant tax year.

The governing principle is that transactions between associated enterprises should be at arm's length. The price, margin, interest rate, royalty, guarantee fee or management fee should be capable of being supported as if the parties were independent and acting commercially. Contemporaneous agreements, invoices, benchmarking, benefit test documentation and evidence of actual service delivery are critical. A transfer pricing adjustment may result not only in tax demand but also in penalty exposure and secondary adjustment implications, depending on the facts.

Key Inter-Company Transactions and Their TP Implications

Management fees: If the Indian parent provides management services to an overseas subsidiary, the fee must be documented and benchmarked using appropriate transfer pricing methods. Setting the fee too high may create a TP adjustment in India or a tax issue in the subsidiary's jurisdiction. Charging nothing, or less than arm's length, leaves value in the overseas subsidiary untaxed in India.

Loans to overseas entities: The interest rate on any loan to an overseas subsidiary must be at arm's length as determined by the transfer pricing analysis. Separately, RBI prescribes a minimum interest rate for loans from Indian entities to overseas entities. The higher of the two rates must be used.

Intellectual property licensing: If the Indian entity licenses IP to an overseas subsidiary, the royalty rate must be benchmarked. Post-BEPS Action 8 to 10, the substance of IP development matters. An Indian entity that developed IP in India must recognise the economic ownership in India, and a royalty-bearing arrangement flowing from India to an overseas IP holding company, with no development activity, will face heightened scrutiny.

Country-by-Country Reporting (CbCR): Country-by-Country Reporting and group-level documentation obligations should be evaluated separately for multinational groups that cross the prescribed consolidated revenue thresholds. The relevant obligations under the Income-tax Act, 2025 include reporting in respect of international groups and maintenance / furnishing of prescribed transfer pricing documentation. These requirements are separate from FEMA reporting, but both sets of records should be aligned because inconsistencies between ODI filings, financial statements, transfer pricing reports and tax returns can create avoidable scrutiny.

Jurisdiction Choice and Transfer Pricing

Singapore offers a favorable treaty network, no withholding tax on dividends paid out, and a well-regarded OECD-aligned transfer pricing framework. UAE, following the introduction of its 9% corporate tax regime from June 2023, offers potential exemptions for entities that qualify as Free Zone Persons under prescribed conditions, and has been expanding its treaty network through the MLI and bilateral negotiations.

However, post-BEPS substance requirements in both jurisdictions have tightened considerably. A holding company or intermediate entity with no employees, no physical office, and no genuine decision-making capacity will not access treaty benefits. It may instead be characterised as a Permanent Establishment of the Indian entity, which would wholly defeat the structure.

Bilateral Advance Pricing Agreements (APAs), available between India and several treaty partner countries, offer the best available certainty for groups with material inter-company transaction volumes. They are administratively demanding but eliminate transfer pricing disputes for the agreed period.

8. Common Violations: Where Indian Entities Go Wrong

In our practice across corporate advisory and FEMA compliance, we see the same categories of violations recur across clients. Most do not stem from any intent to evade. They arise from ignorance of the compliance framework, from relying on overseas incorporation agents who have no understanding of Indian FEMA law, or from assuming that rules which did not exist under the old FEMA 120 regime still do not apply.

Violation 1: Treating formation-related payments casually

A common practical issue arises when an Indian promoter or Indian company pays an overseas incorporation agent, law firm or company secretary through a personal or corporate credit card. This is perhaps the most widespread violation among first-time overseas investors, and we encounter it with striking frequency.

When an Indian promoter or Indian company sets up an entity in Singapore, Dubai, or any other jurisdiction, the overseas incorporation agent or law firm presents an invoice for their professional fees. The promoter reaches for a corporate credit card or a personal card and pays it.

The FEMA treatment will depend on the nature of the payment. Pure professional fees may, depending on facts and AD Bank treatment, be a current account payment. However, where the payment is linked to share subscription, capital contribution, acquisition of membership interest, formation of a WOS / JV, or any financial commitment in the foreign entity, the transaction must be routed and reported under the OI framework.

The safest practice is to involve the AD Bank before any formation-linked payment is made. Credit card payments should be avoided where the payment has any capital account character or where the foreign entity is being incorporated with an Indian resident as subscriber, shareholder, member or beneficial owner. Small value does not remove the compliance issue if the payment results in an overseas investment or financial commitment.

> *The fact that the amount involved is small does not mitigate the violation. The existence of the overseas entity, from the date it is incorporated with the Indian entity as a subscriber or shareholder, creates an ODI that was not reported. Every year that passes without an APR filing compounds the violation further.*

Violation 2: Assuming that deferred payment means no FEMA reporting

This is a subtler violation but one that we have seen cause significant compliance difficulties for clients.

In several jurisdictions, a company may be incorporated with subscribed capital that is not required to be paid immediately. Indian investors sometimes assume that because no money has moved from India, there is no FEMA reporting obligation. This assumption can be risky.

Where the Indian resident subscribes to the memorandum, becomes a shareholder or otherwise acquires equity capital in a foreign entity, the transaction may constitute ODI even if the consideration is deferred. Deferred consideration is recognised under the OI framework, but the foreign securities corresponding to the total consideration are required to be issued or transferred upfront, and the deferred component may be treated as a non-fund-based commitment. The transaction should therefore be reported and documented through the AD Bank at the time of acquisition or subscription, rather than waiting for actual cash remittance.

We have seen clients who ran UAE or Singapore subsidiaries for four to six years without any RBI reporting, because no money had ever been sent from India. By the time they sought advice to regularize, they were looking at compounding requirements covering every year of non-compliance, and the resulting amounts were significant.

Violation 3: Not Reporting Step-Down Subsidiaries

An Indian entity sets up a WOS in Singapore. The Singapore WOS then sets up its own subsidiary in Germany or the UK for operational purposes. The Indian entity assumes its FEMA reporting obligation ends at the

Singapore entity level. It does not. Every step-down subsidiary must be reported to RBI within 30 days of its formation or acquisition.

This violation is particularly common in the technology sector, where overseas subsidiaries frequently set up local entities across multiple countries for sales or support operations without the Indian parent tracking the reporting implications.

Violation 4: Failure to realise and repatriate amounts receivable

The OI framework requires the Indian investor to realise and repatriate amounts receivable from the foreign entity in relation to the overseas investment within the prescribed period. This includes dues receivable from the foreign entity, consideration received on transfer or disinvestment of ODI, and the net realisable value of assets on liquidation. If dividends, sale proceeds, liquidation proceeds or other receivables are left overseas without permissible treatment or proper documentation, the matter may become a FEMA contravention.

Violation 5: Guarantees Without Proper Reporting

An Indian entity providing a guarantee to a bank or counterparty on behalf of its overseas subsidiary creates a non-fund based financial commitment. This commitment must be reported and included in the calculation of the aggregate financial commitment against the 400% net worth limit. Guarantees given without reporting, or that push the aggregate commitment beyond the limit, are violations.

Violation 6: Misuse of LRS or family remittances

Resident individuals may undertake overseas investment within the Liberalised Remittance Scheme limit and subject to the conditions applicable to individuals. However, LRS should not be used as a backdoor route to create or fund what is in substance a corporate overseas structure of an Indian business without complying with the ODI framework. Similarly, the use of relatives or family members merely to pool limits, obscure beneficial ownership or bypass reporting obligations can attract scrutiny under FEMA, income-tax and anti-money laundering laws. In family-owned business groups, the substance of ownership and control should be documented before remittances are made.

Violation 7: Delay in Filing the Annual Performance Report

The APR must be filed by December 31 each year. This is a firm deadline and there is no automatic extension. Non-filing is among the most common violations we see, and it is entirely avoidable. Every overseas entity in which an Indian investor holds an ODI interest requires an APR, including entities that had no activity during the year.

9. Matters to Be Aware of Before You Set Up Overseas

Beyond the compliance mechanics, there are broader matters of substance and law that every Indian entity considering an overseas investment should evaluate.

The financial health of the overseas entity. The OI Rules impose a condition on investing in a foreign entity that has accumulated losses and has a negative net worth for three or more preceding years. Such an investment is not permitted unless RBI grants prior approval. Indian entities that have already invested in such an entity, or are considering doing so, must verify this condition carefully.

Country risk and treaty access. The choice of jurisdiction directly affects the tax efficiency of the structure. A jurisdiction with no DTAA with India means that dividends and royalties paid to the Indian entity may bear full Indian tax without credit for overseas taxes paid. The treaty position must be assessed alongside FEMA eligibility.

Place of Effective Management. The absence of commercial substance in an overseas entity can create multiple tax and regulatory risks. Depending on the facts, the risks may include denial of treaty benefit, transfer pricing adjustment, POEM exposure, GAAR scrutiny, attribution of income, or permanent establishment exposure. The mere incorporation of an overseas company does not by itself establish tax substance. Board meetings, decision-making, employees, office infrastructure, risk assumption, asset ownership and actual conduct of business must be consistent with the stated commercial purpose of the structure.

The Black Money Act. Resident individuals who hold overseas assets, including shares of overseas companies, are required to disclose them in their Income Tax returns. Undisclosed overseas assets are subject to tax at 30% plus a penalty of 90% of the undisclosed value under the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015. Prosecution with imprisonment of up to 10 years is possible. This is separate from and in addition to any FEMA consequences. The Act applies to individuals, Hindu Undivided Families, companies, and firms alike.

Automatic exchange of information. India is an active participant in the Common Reporting Standard (CRS) framework. Overseas banks and financial institutions in CRS-participating jurisdictions automatically report account information of Indian tax residents to India annually. Overseas shareholdings and bank balances held by Indian residents are now routinely known to the Indian tax and enforcement authorities. This fundamentally alters the risk calculus for anyone contemplating non-disclosure of overseas assets or non-compliance with FEMA reporting.

Substance requirements in the overseas jurisdiction. Post-BEPS, most jurisdictions that were previously used as holding locations have introduced statutory substance requirements. The Cayman Islands, BVI, Bermuda, Jersey, and others all require that entities demonstrate genuine economic activity in the jurisdiction. Failure to meet substance requirements can lead to automatic exchange of information with India and denial of treaty benefits.

10. Remedies

FEMA is, at its core, a civil statute. Contraventions of FEMA provisions give rise to civil penalties under Section 13. Unlike the old Foreign Exchange Regulation Act, 1973, criminal prosecution is not the default or first-line response to FEMA violations. The law provides structured, accessible remedies for those who have violated its provisions.

Late Submission Fees

The LSF mechanism was formalized under the OI framework to provide a simpler, faster regularization route for delayed filings such as Form FC and APR. The LSF amount is computed on the basis of the amount of the ODI or financial commitment involved and the period of delay, subject to a maximum cap. Payment of the LSF through the AD Bank regularizes the delayed filing without creating a formal compounding record. For most administrative delays, this is the preferred first step.

Compounding Under Section 15 of FEMA

For substantive FEMA contraventions, the principal statutory remedy is compounding under Section 15 of FEMA, read with the Foreign Exchange (Compounding Proceedings) Rules, 2024 and the directions issued by RBI. Compounding is a voluntary process through which the contravener acknowledges the contravention, files an application before the competent authority, and pays the amount determined in the compounding order. It is generally more efficient to approach the regulator proactively than to allow the matter to be detected during an enforcement inquiry.

The application should set out the facts, chronology, nature of contravention, amount involved, period of delay, corrective steps already taken, and supporting documents. In most routine overseas investment matters, compounding jurisdiction lies with RBI, subject to the nature of contravention and the exceptions under the compounding framework. Cases involving serious concerns, non-quantifiable amounts, suspected money laundering, terror financing, national security issues or matters requiring ED investigation may not be eligible for ordinary compounding before RBI.

Once a compounding order is passed by RBI and the compounding amount is paid, the violation is extinguished. The compounding order bars any future prosecution or penalty proceeding in respect of the same violation. This makes compounding a powerful and definitive remedy, provided the application is made proactively, before any enforcement action is initiated.

> *Compounding is not available for violations that are already under investigation by the Enforcement Directorate, violations involving national security or foreign policy considerations, or contraventions connected with scheduled offences under the Prevention of Money Laundering Act, 2002.*

Adjudication Before the Enforcement Directorate

Where a violation is detected by the Enforcement Directorate rather than self-reported by the investor, the matter proceeds to adjudication under Section 16 of FEMA. The Adjudicating Authority issues a Show Cause Notice, the respondent has an opportunity to be heard, and thereafter an order is passed imposing a penalty. The penalty can go up to three times the amount involved in the contravention.

An appeal against an adjudication order under FEMA lies to the Appellate Tribunal for Foreign Exchange (ATFE) under Section 19, and thereafter to the concerned High Court. The penalty is stayed during the appeal process if the appellant deposits the amount directed by the Tribunal.

11. When Violations Become Serious: ED Inquiries, PMLA, and the Black Money Act

As noted, FEMA violations are civil violations. The penalty under Section 13(1) is a civil monetary penalty. FEMA itself does not provide for criminal prosecution in the ordinary course.

However, certain categories of violations attract qualitatively different treatment, and every Indian entity with overseas operations should be aware of the line between a civil FEMA matter and one that draws criminal exposure.

Violations That Necessarily Draw Enforcement Directorate Attention

- Non-repatriation of foreign exchange: Where an Indian entity remits funds overseas and fails to bring back the proceeds in the manner and within the time prescribed, and particularly where the overseas entity shows no genuine business activity, the ED treats this as a serious violation warranting investigation and adjudication.

- Roundtripping: Any structure where funds flow from India to an overseas entity and return to India as foreign investment is a priority area for ED investigation. The specific prohibition in the Master Direction on Overseas Investment makes the ED's jurisdiction clear.

- Wilful defaulters investing overseas: An entity or individual classified as a wilful defaulter who nonetheless continues to operate or invest in overseas entities simultaneously becomes a subject of regulatory concern across both RBI and the ED.
- Violations involving amounts above INR 1 crore: The Enforcement Directorate's adjudication hierarchy allocates matters by the value involved. Violations above INR 1 crore are heard by Additional Directors and Special Directors of Enforcement, and the investigation is correspondingly more intensive.
- Failure to comply with a compounding order: Once RBI passes a compounding order, non-payment of the compounding amount within the time allowed can result in the matter being referred for further action, including prosecution before the designated court.

Where the PMLA Enters

The Prevention of Money Laundering Act, 2002 (PMLA) is a criminal statute administered by the Enforcement Directorate through its investigation wing. PMLA applies when a FEMA violation involves, or is connected with, proceeds of a scheduled offence. Scheduled offences include tax evasion involving specific sums, offences of cheating and fraud under the Indian Penal Code, corruption, and related crimes.

If an Indian entity remits funds overseas through a transaction that simultaneously constitutes tax evasion, the funds may be treated as proceeds of crime under PMLA. The ED can investigate, arrest, attach movable and immovable property in India or overseas, and prosecute. Conviction under PMLA can result in imprisonment of three to seven years, extendable to ten years for violations involving amounts that cross the prescribed threshold.

PMLA exposure does not arise merely because there is a delayed FEMA filing or a technical OI reporting lapse. PMLA is attracted where the transaction involves proceeds of crime arising from a scheduled offence and the person is involved in a process or activity connected with such proceeds, including concealment, possession, acquisition, use, projecting or claiming them as untainted property. Therefore, the legal risk changes materially where an overseas structure is used to divert funds, conceal beneficial ownership, evade tax through criminal conduct, launder money, or route funds connected with fraud or other scheduled offences.

On conviction under PMLA, the punishment is rigorous imprisonment of not less than three years and up to seven years, along with fine. The maximum sentence may extend to ten years only where the proceeds of crime relate to specified offences under the NDPS-related part of the Schedule. The note should therefore avoid suggesting that the ten-year punishment applies merely because the value of the transaction crosses a monetary threshold.

The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015

This is a standalone criminal statute, separate from both FEMA and PMLA, and it applies to Indian residents who hold overseas assets without disclosing them in their Income Tax returns. The Act imposes a tax of 30% on undisclosed overseas income and assets, a penalty equal to 90% of the undisclosed value, and, on prosecution, imprisonment of three to ten years.

The Black Money Act is not technically a FEMA statute, but it is almost always triggered alongside FEMA violations where overseas assets are identified by Indian authorities. The Act has been invoked in several high-profile matters since its enactment and is one of the primary reasons that proactive regularization of FEMA violations is strongly advisable.

> *Practical note: The Common Reporting Standard now ensures that overseas bank accounts, shareholdings, and financial assets held by Indian residents are automatically reported to India by participating jurisdictions. As of the current date, over 100 countries are active CRS participants. The assumption that overseas assets are invisible to Indian authorities is no longer tenable.*

12. A Final Word from Practice

Building an overseas presence is not inherently complicated. The legal framework, while detailed, is navigable if approached systematically and with proper advice at the outset. The cost of getting it right from the start is always a fraction of the cost of regularizing it later, and far less than the cost of an enforcement proceeding.

From our years of advising Indian entities across the full spectrum of overseas investment matters, a few principles consistently hold.

Never use any payment route other than the banking channel. Every rupee and every dollar related to an overseas entity must flow through an Authorised Dealer Bank. Credit cards, overseas account transfers, and barter arrangements are not permitted. The paper trail through the banking system is both a FEMA requirement and your best evidence of compliance.

File your APR every year, without exception. The December 31 deadline for the APR is firm. It applies to every overseas entity in which you hold an ODI stake, regardless of whether the entity conducted business during the year. Treat the APR the same way you treat an income tax return: it is a statutory obligation with prescribed consequences for non-compliance.

Document every inter-company transaction before it begins. Transfer pricing disputes arise when commercial arrangements lack contemporaneous documentation. A management services agreement, a loan agreement, or a licensing arrangement that is documented after the fact, or not documented at all, invites an adjustment. Draft and sign the agreement before the first invoice is raised.

Regularize proactively. FEMA's compounding and LSF mechanisms exist for a reason. A voluntary application under Section 15, made before any ED inquiry is opened, is treated far more sympathetically than a contravention detected in the course of an investigation. If your overseas compliance history has gaps, seek advice immediately and regularize.

Remember that the information environment has changed. Overseas financial information is now routinely shared with India. The window for non-disclosure of overseas assets is effectively closed. FEMA compliance and income tax disclosure go hand in hand, and an entity that has maintained its FEMA reporting impeccably but failed to disclose overseas income in its tax return is still at risk.

The practical approach is straightforward: plan the structure before incorporation, involve the AD Bank before funds move or shares are subscribed, document the commercial purpose, maintain consistency between FEMA filings and tax records, and regularise past lapses before they become enforcement issues. Overseas expansion is a legitimate business step. The risk arises not from going global, but from treating incorporation, funding, inter-company dealings and annual reporting as separate administrative events rather than as one connected compliance chain.

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