

Legacy Growth Insights



Investments in Offshore Funds

June 2024

KEY TAKEAWAY

- The Reserve Bank of India (RBI), vide its recent circular¹, has introduced amendments to the Foreign Exchange Management (Overseas Investment) Directions, 2022. These amendments enhance the flexibility for making Overseas Portfolio Investments (OPI) by:
 - Resident individuals and Indian listed companies in Overseas Funds, specifically in terms of:
 - the legal form of the fund and the instrument for making the investment; and
 - the manner in which the overseas funds are regulated.
 - Resident individuals, Indian listed companies and unlisted Indian entities in units or *any other instruments* issued by an investment fund or vehicle established in the International Financial Services Centre (IFSC).
- The latest amendment now encompasses the following modes of investment for Indian investors:

Investors Category	Offshore funds	Gujarat International Finance Tech City (Gift City)	Limit on investment
Resident Individuals	Permitted in any regulated funds (including where fund manager is regulated) by way of any instrument	Investment Fund or vehicle in the International Financial Services Centre (IFSC)	Up to the Liberalised Remittance Scheme (i.e., USD 250,000 per Financial Year in aggregate)
Listed Indian company			Up to 50% of its Net-worth as on the date of its last audited balance sheet
Unlisted Indian entities	Not permitted		

¹ A.P. (DIR Series) Circular No. 09 dated 7th June 2024

BACKGROUND

- To enhance the ease of doing business and in the spirit of liberalization, the RBI amended the Overseas Investment regime in August 2022, clarifying that the investments in 'Units' of overseas regulated funds and IFSC Investment Funds or vehicles are to be considered as 'OPI'.
- Prior to the current regulatory update, OPI in offshore funds required such funds be regulated within their host jurisdiction. Additionally, investments were restricted to 'units' of these funds, leading to the following ambiguities:
 - Whether instruments other than 'Units' could qualify as 'OPI', especially since many offshore funds operate as corporate entities or partnerships issuing shares or partnership interests
 - Whether investments in Overseas Funds would qualify as 'OPI' in cases where the fund managers, rather than the funds themselves, are regulated—a common situation in many overseas jurisdictions
- RBI has removed the above ambiguities in its recent circular.

IMPACT ANALYSIS

Earlier framework under Foreign Exchange Management (OI) Directions, 2022	Amended framework under Foreign Exchange Management (OI) Directions, 2022	Impact
<p>Investment in offshore funds</p> <p>Para 1 (ix) (e) reads as under:</p> <p><i>“The investment (including sponsor contribution) in units of any investment fund overseas, duly regulated by the regulator for the financial sector in the host jurisdiction, shall be considered as OPI. Accordingly, in jurisdictions other than IFSC, listed Indian companies and resident individuals may make such investment. Whereas in IFSC an unlisted Indian entity may also make such OPI in units of an investment fund or vehicle, in terms of schedule V of the OI Rules subject to limits, as applicable.”</i></p>	<p>Investment in offshore funds</p> <p>Replaced Para 1 (ix) (e) :</p> <p><i>“The investment (including sponsor contribution) in units <u>or any other instrument (by whatever name called) issued by an investment fund overseas,</u> duly regulated by the regulator for the financial sector in the host jurisdiction, shall be treated as OPI. Accordingly, in jurisdictions other than IFSCs, listed Indian companies and resident individuals may make such investment. Whereas in IFSCs, an unlisted Indian entity also may make such OPI in units or any other instrument (by whatever name called) issued by an investment fund or vehicle, in terms of schedule V of the OI Rules subject to limits, as applicable.</i></p> <p><u>Explanation: investment fund overseas, duly regulated' for the purpose of this para shall also include funds whose activities are regulated by financial sector regulator of host country or jurisdiction through a fund manager.”</u></p>	<ul style="list-style-type: none"> The amendment broadens the coverage of instruments from 'Unit' to a broader spectrum of instruments. Many jurisdictions regulate investment funds through its Fund Manager . This clarification will broaden the choice of jurisdictions where funds can be set up to raise capital from Indian investors.

Earlier framework under Foreign Exchange Management (OI) Directions, 2022	Amended framework under Foreign Exchange Management (OI) Directions, 2022	Impact
<p>Investment in GIFT City funds</p> <p>Para 24 (1) reads as under:</p> <p><i>“A person resident in India, being an Indian entity or a resident individual, may make investment (including sponsor contribution) in the units of an investment fund or vehicle set up in an IFSC as OPI. Accordingly, in addition to listed Indian companies and resident individuals, unlisted Indian entities may also make such investment in IFSC”</i></p>	<p>Investment in GIFT City funds</p> <p>Replaced Para 24 (1) :</p> <p><i>“A person resident in India, being an Indian entity or a resident individual, may make investment (including sponsor contribution) in units <u>or any other instrument (by whatever name called)</u> issued by an investment fund or vehicle set up in an IFSC, as OPI. Accordingly, in addition to listed Indian companies and resident individuals, unlisted Indian entities also may make such investment in IFSC.”</i></p>	<ul style="list-style-type: none"> • The amendments broadens the spectrum of instruments by permitting investments in other instruments, which were earlier restricted to ‘Units’ only.

LEGACY GROWTH'S VIEWPOINT

The RBI’s recent circular has significantly enhanced the flexibility for Fund Managers/ General Partners (GPs). This development is a welcome change that allows greater ease in structuring offshore funds and designing financial instruments to attract capital from Limited Partners (LPs). Importantly, these changes have clarified previously existing ambiguities concerning the types of permissible investments and the regulatory status of fund managers versus the funds themselves, ensuring a clearer path for Indian investors, including listed companies and resident individuals.



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