

FEMA ke FUNDAE

Issue of Convertible Notes

#FamiliarwithFEMA

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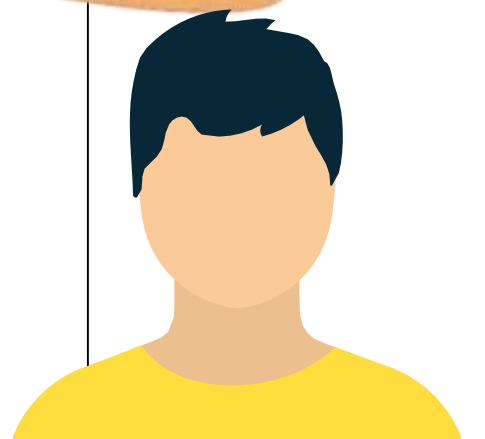


Bhaskar

Hello Mr. FEMA Gyani. I am opening a new start-up company Innovation Pvt. Ltd. I am looking for a way out to fund the start-up. One of my friend who is a non-resident wishes to provide funding. While analysing the various options regarding the same, I came through the term 'convertible notes'. I am curious whether they are a good fund-raising option? Can you enlighten me regarding the same?

Hi Bhaskar! Congrats on your new start-up. Yes, convertible Notes are indeed very convenient options to raise capital without initially diluting the ownership

A Convertible Note is an instrument **issued by a start-up company recognized by DPIIT** through which money is received **initially as debt**, which is repayable at the option of the holder, or which is **convertible into equity shares** of the start-up company, **within a period of five years from the date of issue** of the convertible note, upon occurrence of specified events as per the other terms and conditions agreed to and indicated in the instrument.



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So, can Innovation Pvt. Ltd. issue Convertible Notes to my friend as he is a non-resident?

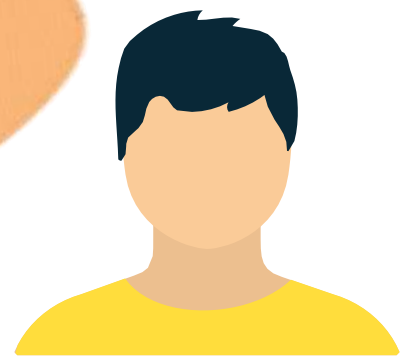
A convertible note can be issued to a **person resident outside India (other than an individual who is citizen of Pakistan or Bangladesh or an entity which is registered/ incorporated in Pakistan or Bangladesh)**. So, if your friend is not a citizen of Pakistan or Bangladesh, then it won't be a problem.



Okay. So, my friend wishes to fund me with INR 60 Lakhs that he will be remitting in three tranches of 20 lakhs each.



Well that will not work as the convertible notes should be issued minimum of **rupees twenty-five lakh or more in a single tranche**.





Oh! Okay, noted. So is there any specified way in which my friend is required to transfer the funds?

Your friend shall remit the amount **through banking channels or by debit to the NRE/ FCNR (B)/ Escrow account** maintained by him.

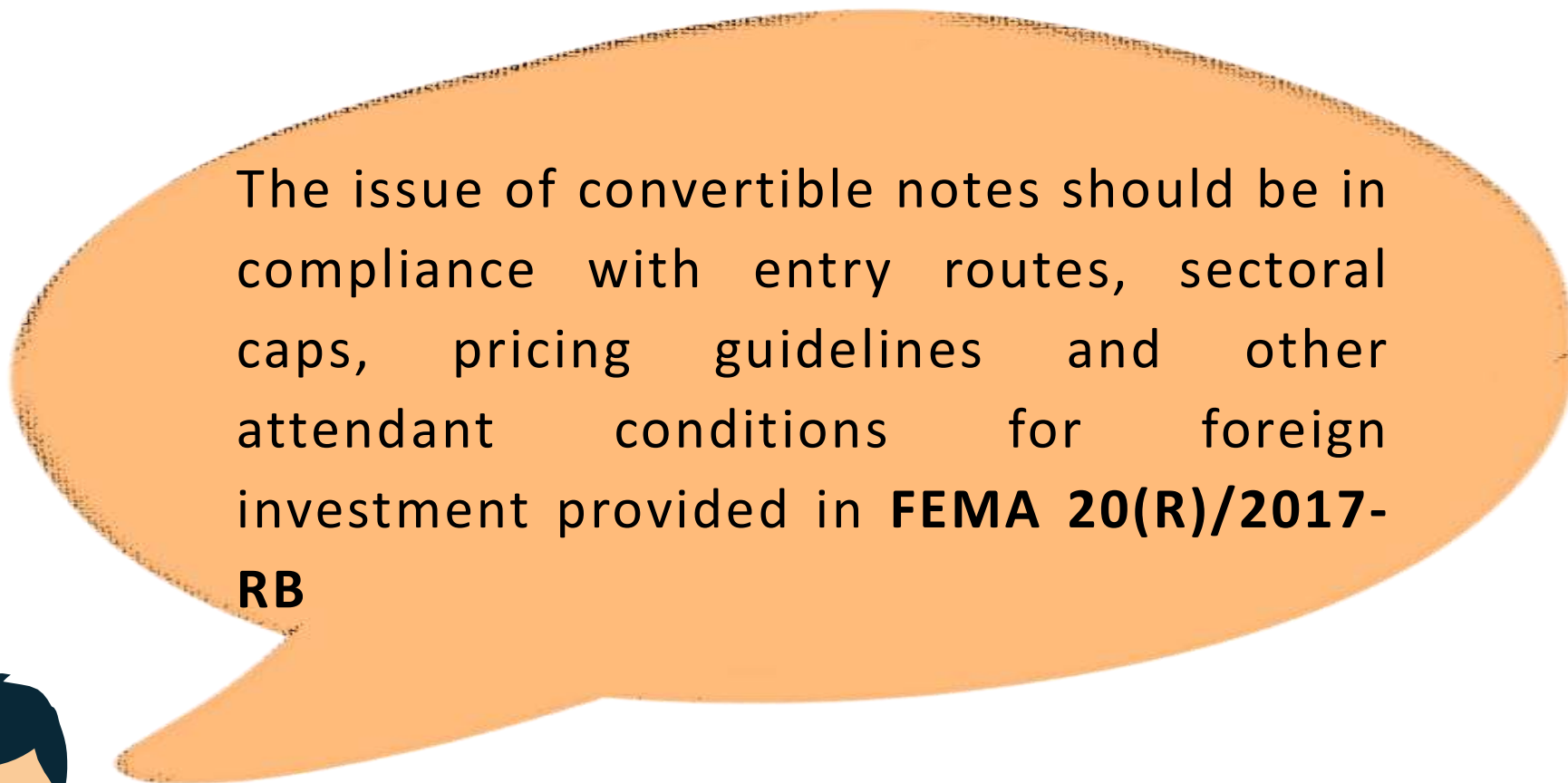


Okay. I'll inform my friend regarding the same. Is there anything else to be kept in mind while issuing convertible notes?

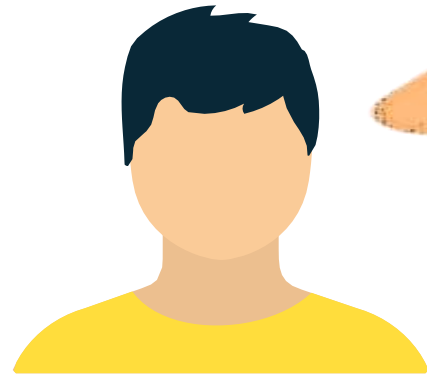


Well, there are two more things that you should be aware of:

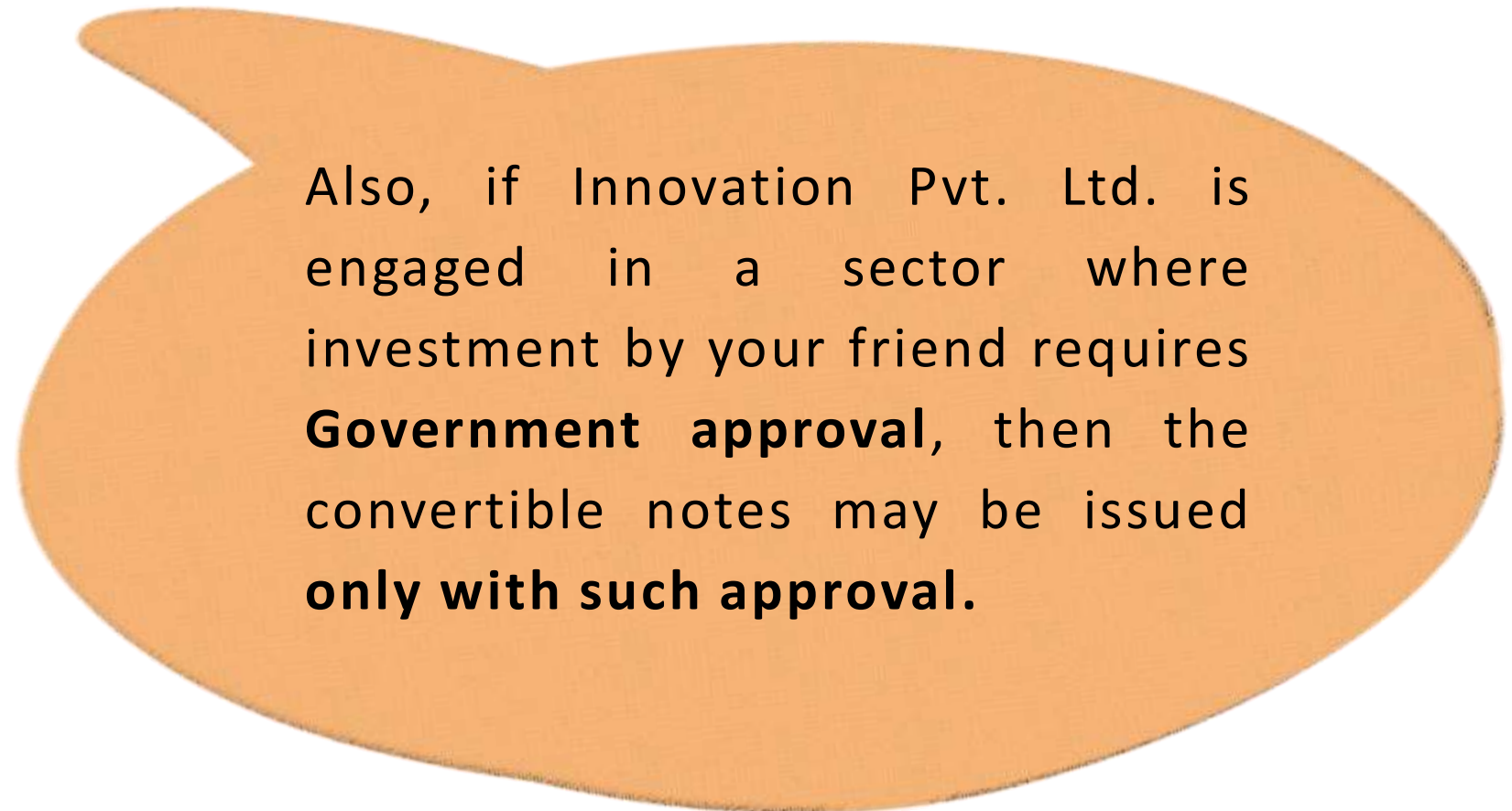




The issue of convertible notes should be in compliance with entry routes, sectoral caps, pricing guidelines and other attendant conditions for foreign investment provided in **FEMA 20(R)/2017-RB**



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Also, if Innovation Pvt. Ltd. is engaged in a sector where investment by your friend requires **Government approval**, then the convertible notes may be issued **only with such approval.**



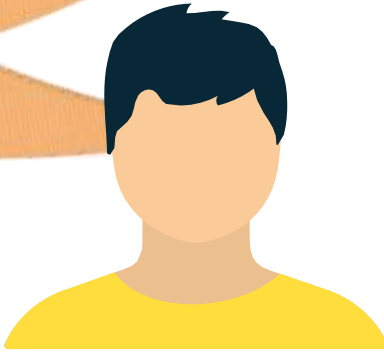
The following sectors require government approval:

- Petroleum Refining (except for private sector oil refining), Natural Gas / LNG Pipelines
- Investing companies in Infrastructure & Services Sector
- Defence and Strategic Industries
- Atomic Minerals
- Print Media
- Broadcasting
- Postal services
- Courier Services
- Establishment and Operation of satellite
- Development of Integrated Township
- Tea Sector
- Asset Reconstruction Companies



Can you tell me the reporting required to be made regarding the issue of Convertible Notes?

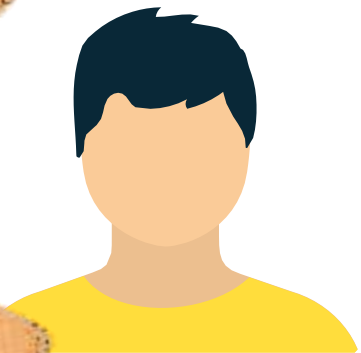
Innovation Ltd. shall report such inflows to the Authorised Dealer bank in **Form Convertible Notes (CN) within 30 days of such issue.**



Okay, In future, If my friend wishes to sell these convertible notes to his brother who is an Indian Resident. Can he do so?



- Yes, it is allowed. Your friend **may acquire or transfer by way of sale**, convertible notes, **from or to**, a person resident in or outside India. The transfer should take place in accordance with the entry routes and pricing guidelines as prescribed for capital instruments.
- Further the repayment or sale proceeds be **remitted outside India or credited to your friend's NRE/ FCNR (B) account.**





Okay. Does this transfer also need to be reported in Form CN?

Yes Bhaskar, the transfer to or from a person resident outside India shall be reported by the person resident in India, who may be a transferor or transferee of Convertible Notes issued by an Indian start-up in **Form CN to the Authorised Dealer bank within 30 days of such transfer.**



Okay! Got it. Thanks Mr. FEMA Gyani.



Most welcome Bhaskar. Good luck for the start-up! I am sure you'll do your best.



Thank You!

Let's meet every
Wednesday.

To make you more familiar with FEMA,
we are happy to listen to your

Comments

Feedbacks

Suggestions



The FEMA Gyani

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