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- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
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THE NEW CONSOLIDATED FDI POLICY 2011: WHETHER IGNORING SOMETHING IN ITS DRIVE TOWARDS BOOSTING INVESTOR CONFIDENCE?

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ABSTRACT

India in its march towards being a developed one, is in dire need of FDI to establish itself stalwartly on economic footing. Like every other issue FDI too is governed by legal framework. Foreign investments into India are subject to the industrial policy established by the Department of Industrial Policy and Promotion (DIPP) under the Ministry of Commerce and Industry which is the nodal agency and the prime legislation governing FDI is Foreign Exchange Management Act, 1999 (FEMA), and side by side there exist a whole lot of regulations made there under and the various press notes, press releases and clarifications etc. issued on the subject from time to time. The revised FDI policy of India will surely carry forward the process of liberalization which further would assist in enhancing of the FDI into the Country. However, the revised FDI policy has kept itself miles away from significantly expected changes such as permitting FDI in Limited Liability Partnership, Multi-Brand Retail Trading – which are the most top of the chart agenda in the FDI. Further several other subjects on which draft discussion papers were released earlier for public comments have not also been responded to. It is imperative that these areas are also taken up by our Government for liberalization towards making India one of the most hot spot FDI destinations on the globe.

KEYWORDS

FDI, Investment, India, Trade, Law.

INTRODUCATION

Every developing economy today is so called "*FDI hungry*". Beyond all doubts FDI bears a direct relation with sound economy. Considering case of India distinctively; India in its march towards being a developed one, is in dire need of FDI to establish itself stalwartly on economic footing. Like every other issue FDI too is governed by legal framework. Foreign investments into India are subject to the industrial policy established by the Department of Industrial Policy and Promotion (DIPP) under the Ministry of Commerce and Industry which is the nodal agency and the prime legislation governing FDI is Foreign Exchange Management Act, 1999 (FEMA), and side by side there exist a whole lot of regulations made there under and the various press notes, press releases and clarifications etc. issued on the subject from time to time.

To attract FDI factor which plays a stellar role is legal framework. There has been always a demand from the investor circles that legal framework should be so simplified and slackened that investors have an ease in investing. But the investor destinations inherently and specifically the emerging economies like India; many times have to face contradictions and paradoxes with its domestic demands i.e. protecting the interests of the domestic producers and in parallel to promote scales of FDI as well. Realizing this very potent fact, in an attempt to simplify the rules and regulations pertaining to the foreign direct investment policy, the Department of Industrial Policy and Promotion had issued a consolidated FDI policy (the "Circular") on March 31, 2010 The Circular which became effective from April 1, 2010 consolidated all prior press notes / press releases / clarifications issued and reflected in a coherent manner the current policy framework on FDI thus becoming so called "***ready reckoner***" on foreign investment-related regulations. To the surprise of many, this time it was not meant to be a onetime affair but the Government this time had bigger plans to update the FDI policy bi-annually, by issuing a new circular which would supersede all prior press notes and circulars. Keeping intact the promise, in this chain the government of India has recently released the third edition of the Consolidated FDI Policy Circular on 31 March 2011 which has become effective from April 1, 2011. It is further crucial to note that it is necessary to comply with any changes notified by the Reserve Bank of India after the issuance of this Circular. Commenting on the new policy, commerce and industry minister Anand Sharma said, *"The Circular 1 of 2011 is a part of ongoing efforts of procedure simplification and FDI rationalization which will go a long way in inspiring \investor confidence.*[1] ***Now the question which remains to be analyzed and answered is that whether this current drive of the Indian government will in actuality help in maintaining the balance between two contradictory interests existing in India and really come out to boost investor confidence or not.***

WHY SUCH A TRIGGER OVER FDI?

The government has been mulling over liberalizing the foreign direct investment (FDI) policy since a few weeks post budget. The finance minister had said during the budget that India needs overseas funds flows to support its key domestic sectors and overhaul its infrastructure. Thus this time the prime aim of the government is to make sure that policy and legal framework do not become a stumbling block. During 2009-2010 FDI in India showed a whopping increase mainly due to grave recession in other parts of the globe but recent decline from April to May really is perturbing. Thus the Indian government has made scores of changes to the FDI policy to attract more foreign direct investment amidst 25% decline in FDI during the eleven month period between April-February 2010-11. FDI in flows in the country was USD 18.3 billion during April-February 2010-11, down 25 per cent from USD 24.6 billion in the same period last fiscal.[2] *Rajiv Kumar, director-general of FICCI, said, "We certainly need a more liberal FDI policy framework to attract larger foreign investments. This is especially needed in the context of declining FDI flows in the past few months."*[3] The recent policy review on FDI has introduced a number of changes, and we will attempt to discuss all of the major ones on this article. Primarily, the changes appear to be investor friendly as they seek to remove several obstacles that have long held back foreign investment in crucial sectors. In fact, this policy review symbolizes one of the more progressive sets of changes made to FDI policy in recent times, as we shall examine.

[1] Live Mint, *Govt. Announces Flexible Norms To Tap Overseas Capital*, Available on www.livemint.com **(** Last accessed on 4 April, 2011)
[2] The Hindu, *FDI Norms Fine-Tuned To Attract More Investment*, Available on www.thehinduonnet.com (Last accessed on 4 April, 2011)
[3] The Hindu Business Line , **Industry hails easing of foreign direct investment norms, Available on** http://www.thehindubusinessline.com (Last accessed on 3 April, 2011)

THE MAIN FEATURES OF THE NEW CONSOLIDATE FDI POLICY CIRCULAR

- **REMOVAL OF THE CONDITION OF PRIOR APPROVAL IN CASE OF EXISTING JOINT VENTURES/ TECHNICAL COLLABORATIONS IN THE "SAME FIELD":**

This has been done through deletion of Clause 4.2.2 of the earlier Circular (No. 2 of 2010) which provided that FDI would be subject to the "Existing Venture/ tie-up conditions" as stated in sub-clauses of Clause 4.2.2 (basically stating that where a non-resident investor has an existing joint venture/ technology transfer/ trademark agreement, as on January 12, 2005, new proposals in the same field for investment/technology transfer/technology collaboration/trademark agreement would have to be under the Government approval route through FIPB/ Project Approval Board).[4] A discussion paper had been released by DIPP last year on the need for review of this condition. Based on stakeholder comments received by the DIPP on its discussion paper, the Government while releasing the FDI Circular 1 of 2011 has in its press release stated that it has decided to abolish this condition.[5] The press release further states that *"It is expected that this measure will promote the competitiveness of India as an investment destination and be instrumental in attracting higher levels of FDI and technology inflows into the country*".[6] Foreign investors are no longer required to obtain Government approval even if they had previous ventures in India so long as the new investment otherwise falls within the automatic route. **This truly levels the playing field. It is perhaps the most significant and likely impactful change introduced in the new policy.**

- **PRICING OF CONVERTIBLE INSTRUMENT - GREATER FLEXIBILITY INTRODUCED**

This has been done through amendment made in Clause 3.2.1 of the Circular which earlier provided that *"The pricing of the capital instruments should be decided/determined upfront at the time of issue of the instruments"* Now it has been added that "price / conversion formula" be determined upfront so in effect instead of having to specify the price of convertible instruments upfront, companies will now also have the option of prescribing a conversion formula, subject to the condition that price at the time of conversion should not in any case be lower than the fair value worked out, at the time of issuance of such instruments, in accordance with the prevailing valuation norms (viz. DCF method of valuation for the unlisted companies).[7] This would help the recipient companies in obtaining a better valuation based upon their performance.

- **LIBERALIZATION OF POLICY FOR NON-CASH CAPITAL CONTRIBUTIONS**

This amendment has been brought about through additions in Clause 3.4.6 of the Circular. The existing policy FDI provided for conversion of only ECB/lump-sum fee/Royalty into equity. The Government has now decided to permit issue of equity, with prior approval from FIPB, in the following cases, subject to stipulated conditions:

(a) Import of capital goods/ machinery/ equipment (including second-hand machinery)

(b) Pre-operative/ pre-incorporation expenses (including payments of rent etc.)

This measure, which liberalises conditions for conversion of non-cash items into equity, is expected to significantly ease the conduct of business.[8]

- **FOREIGN INSTITUTIONAL INVESTOR INVESTMENT:**

Clause 3.1.4 (i) of the earlier Circular 2 of 2010 provided as under: "An FII may invest in the capital of an Indian company either under the FDI Scheme/Policy or the Portfolio Investment Scheme. 10% individual limit and 24% aggregate limit for FII investment would still be applicable even when FIIs invest under the FDI scheme/policy."It has now been clarified in Clause 3.1.4 (i) that aggregate FII limit of 24% can be increased to sectoral cap/ statutory ceiling by Board of Directors resolution followed by special resolution in shareholders meeting.[9] While this has always been clear under the FEMA provisions, the earlier FDI Circulars did not specifically mention this and now with this amendment the provisions relating to FII investments are aligned with the FEMA provisions.

- **HUNDRED PERCENT FDI IN SOME AREA OF FARM SECTOR:**

The new FDI Policy allow 100 per cent FDI in development and production of seeds and planting material, floriculture, horticulture, and cultivation of vegetables and mushrooms under controlled conditions. Besides, animal husbandry (including of breeding of dogs), pisciculture, aquaculture under controlled conditions and services related to agro and allied sectors have been brought under the 100 per cent FDI norm. Similarly, the tea sector has also been brought under the 100 per cent FDI norm. The DIPP has imposed certain conditions for companies dealing with development of transgenic seeds and vegetables wanting to take the 100 per cent FDI route. Under the 100 per cent FDI in tea sector, it demands compulsory divestment of 26 per cent equity of the company in favour of an Indian partner/Indian public within a period of five years prior to approval of the State Government concerned in case of any future land use change.[10]

ASSESSING THE BRIGHTER SIDE

The government this time is much determined to raise the FDI levels and thus making the changes as swiftly as possible. This is surely a positive sign towards advancement of our economy. The government has in a key policy reform introduced flexibility for Indian companies to raise overseas capital but side by side even plugged the loopholes for back door FDI entry breaching sectoral caps. The business analysts across the country have welcomed the new policy as a welcome move and have regarded it as the most important move related to joint ventures as well."PE equity across the sectors will get a huge push," said Punit Shah, executive director (tax and regulatory services) at auditing consultancy firm KPMG. Besides, FDI guidelines have been simplified and rationalised to help downstream investments.[11] "It brings in more clarity, nothing more," said Shah.[12] On the whole, the change in the policy will help particularly infrastructure companies, and capital-intensive industries in general. The change relates to more flexibility in issuance of equity. Even Power companies, new telecom operators and automobile component companies that import capital goods/machinery — including the second-hand equipment — can convert it into equity in projects in India. There has been serious opposition against the move to allow seed development by foreign companies. However, some progressive voices have supported the initiative. Sain Daas, president of Indian Mazie Development Association, termed it as a "corrective measure for growth of seed variety".

EVALUATING FLIP SIDE OF THE COIN

Though the 2011 consolidated ready reckoner has liberalized rules to a greater extent yet some concerns still remain to be sorted out and pondered over seriously in order to fully reap the benefits of enhanced FDI in our much volatile economy. We cannot go on one side in promoting FDI blindly and ignoring the impact on our domestic inhabitants. As per the new FDI policy, foreign companies having an existing joint venture in India will not require permission of the local partner to set up a wholly-owned subsidiary in the same field of business. This policy is expected to increase capital flow into the economy as well as employment. However, the new policy can lead to increasing dependency on foreign companies and shut down of small domestic firms not in a position to sustain competition from established foreign players. Critics are saying that the Government seemed to have considered only the downward trend of foreign investments in the country and not much heeded to the Indian firms, especially the small scale enterprises and booming industries. Especially with allowing 100% foreign investment in agriculture sector, the Indian authorities have brought up a storm of destruction for small enterprises and local firms. Of course the Indian consumers might see better branding, packaging and glamor in the markets of agricultural sector with 100% foreign investment, but this is bound to lead to a number of blows to the common consumers including a risk of price rise and acquisition or closing down of small scale local enterprises.

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[4] Press Release on Circular 1 of 2011 Department of Industrial and Policy and Promotion, Ministry of Commerce and Industry Government of India.

[5] *Id.*

[6] *Id.*

[7] Press Release on Circular 1 of 2011 Department of Industrial and Policy and Promotion, Ministry of Commerce and Industry Government of India.

[8] *Id.*

[9] *Id.*

[10] The Hindu, *100 % FDI Allowed In Some Areas Of Farm Sector*, Available on www.thehinduonnet.com (Last accessed on 4 April, 2011)

[11] M. Rajendran, *Some Measure of Equity* , Available on www.businessworld.in (Last accessed on 6 April, 2011)

[12] *Id.*

CONCLUSION

Thus on the whole the revised FDI policy will surely carry forward the process of liberalization which further would assist in enhancing of the FDI into the Country. However, the revised FDI policy has kept itself miles away from significantly expected changes such as permitting FDI in Limited Liability Partnership, Multi-Brand Retail Trading – which are the most top of the chart agenda in the FDI. Further several other subjects on which draft discussion papers were released earlier for public comments have not also been responded to. It is imperative that these areas are also taken up by our Government for liberalization towards making India one of the most hot spot FDI destinations on the globe.

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- Live Mint, *Govt. Announces Flexible Norms To Tap Overseas Capital*, Available on www.livemint.com **(** Last accessed on 4 April, 2011)
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