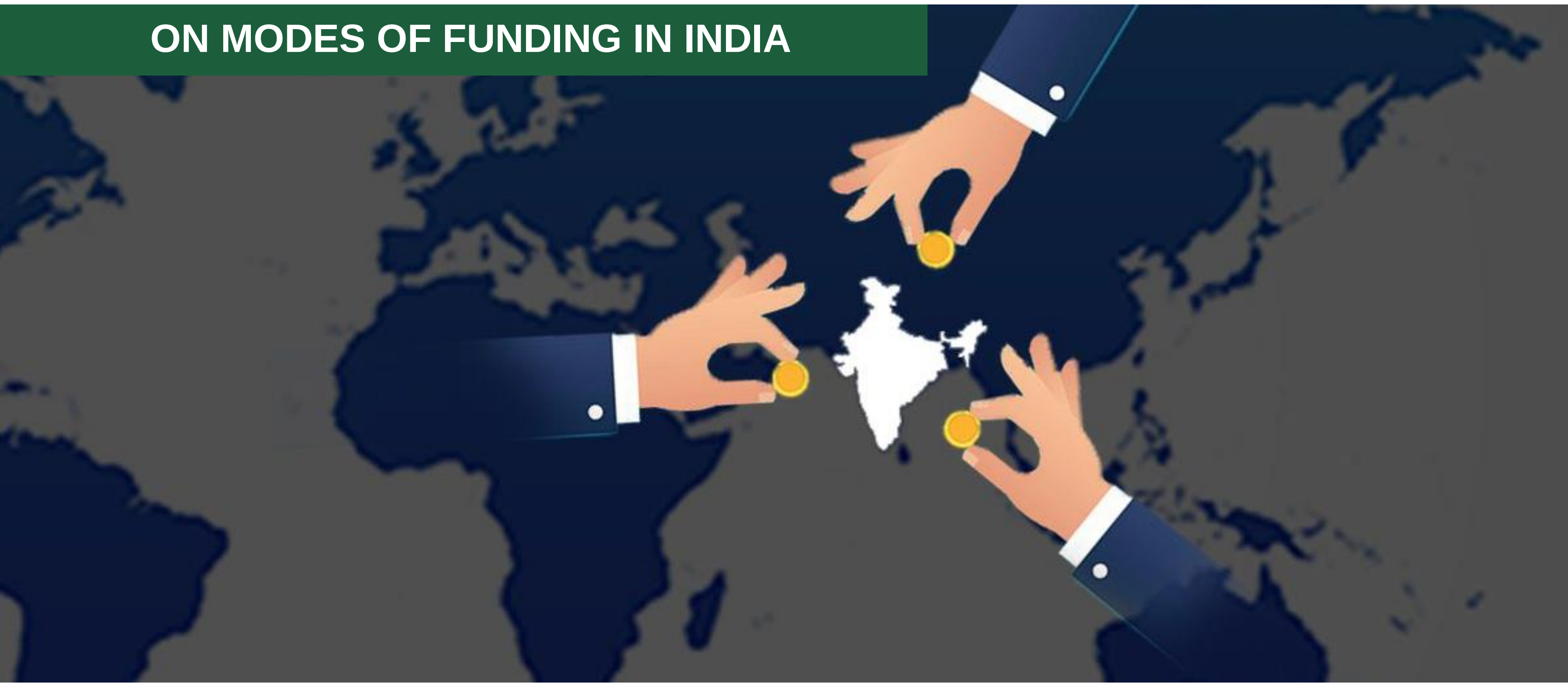
FREQUENTLY ASKED QUESTIONS

ON MODES OF FUNDING IN INDIA



Indian Entities may raise fund through different modes permissible under the Indian laws. Some of the common queries in relation to raising funds under various modes under Indian laws are answered below:

1. Which Indian laws of funds by Indian companies?

Indian company may raise funds in accordance with provisions of the Indian Companies Act, 2013 ("C**ompanies Act**"). Additionally, listed companies will have to comply with rules and regulations framed by Securities and Exchange Board of India (**SEBI**) in particular SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2018 and SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2018.

If the funding is proposed to be raised from foreign investors, that is non-residents, then such funding should also be in compliance with Indian foreign exchange laws in particular Foreign Exchange (Non-debt Instrument) Rules, 2019 (**Non-debt Rules**) and Master Direction on External Commercial Borrowings, Trade Credits and Structured Obligations.

2. What are different modes of funding a company under India laws?

A company may be funded by capital infusion through subscription to share capital of the company or through debt. Capital infusion may be undertaken through equity shares, preference shares, quasi-equity instruments or share warrants. Debt funding may be undertaking through loans, borrowings and debt instruments such as bonds and debentures.

3. What are the modes though which a Limited Liability Partnership can be funded?

A limited liability partnership ("**LLP**") is a partnership incorporated under the Limited Liability Act, 2008. The partners of an LLP can fund the LLP through infusion of capital contribution in the LLP. The different ways in which a partner of the LLP can contribute in an LLP are:

(i) Monetary contribution
(ii) Tangible movable or tangible immovable property
(iii) Agreements to contribute property or cash
(iv) Intangible property
(v) Contracts for services performed or to be performed
(vi) Promissory notes

4. What are equity shares and rights attached to such shares?

An equity share, normally known as ordinary share and denotes part ownership of the company. The key features of an equity shares are:

(i) Right to vote in shareholders meeting. Unless the equity shares have differential voting rights, one equity share is equivalent to one vote.
(ii) Right to receive dividend declared by the board of directors.
(iii) Limitation of liability to the extent of their investment.
(iv) In case of liquidation of the company, the equity shareholders have a right to participate in the liquidation proceeds.

5. Can a company issue equity shares with differential rights?

Under the Companies Act read with relevant rules, both private and public companies are eligible to issue equity share with differential rights subject to certain conditions as prescribed under the Companies Act, 2013 and relevant rules. Further, listed companies issuing equity share with differential rights would also need to comply with regulations framed by SEBI.

Some of the key conditions which a company needs to comply with for issuance of shares with differential rights are:

(i) Articles of association of the company must authorizes the issue of equity shares with differential rights.
(ii) Issue of shares with differential rights is authorized by an ordinary resolution passed at a general meeting of the shareholders. If equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot.
(iii) Voting power in respect of shares with differential rights of the company shall not exceed seventy-four per cent of total voting power including voting power in respect of equity shares with differential rights issued at any point of time.

6. hat are preference shares?

Preference shares are those shares whose holders are entitled to a preferential right of payment of dividend and repayment of share capital in the event of winding up of the company.

Key features of preference shares are as follows:

(i) Preference shareholders do not enjoy any voting rights other than on matters which directly impact the rights of preference shareholders, resolutions for the winding up of the company or for the repayment or reduction of the equity or preference share capital. Preference shareholders will have the right to vote on all resolutions if the dividend in respect of their shares has not been paid for a continuous period of two years or more.

(ii) A company cannot issue irredeemable preference shares. Company may redeem its preference shares only on the terms on which they were issued.

7. What are different types of preference shares?

Preference shares can be categorised as below:

(i) Redeemable Preference Shares - Redeemable preference shares are those shares which are redeemed or repaid after the expiry of a stipulated period

(ii) Cumulative and Non-cumulative Preference Shares - Cumulative preference shares carry additional features which allow the preference shareholders to claim unpaid dividends of the years in which dividend could not be paid due to insufficient profit. The holders of non-cumulative preference shares will get preference dividend if the company earns sufficient profit, but they do not have the right to claim unpaid dividend which could not be paid due to insufficient profit.

(iii) Participating and Non-participating Preference Shares - Participating preference shareholders are entitled to share the surplus profit of the company in addition to preference dividend. Non-participating preference shareholders are not entitled to share surplus profit and surplus assets like participating preference shareholders.

(iv) Convertible Preference Shares - The holders of convertible preference shares are given an option to convert whole or part of their holding into equity shares after a specific period of time. Convertible preference shares may be compulsorily convertible or optionally convertible preference shares.

8. Is there any valuation required to be undertaken for issuance of convertible preference shares?

Issuance of convertible preference shares required a valuation report by a registered valuer either:

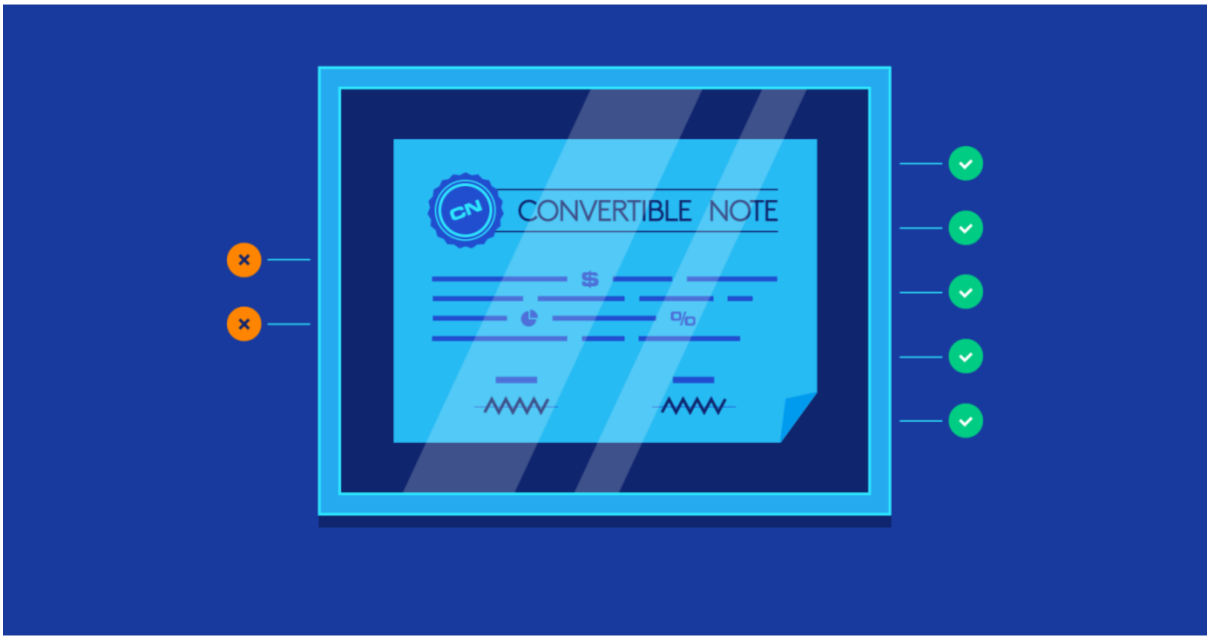
(i) Upfront at the time when the offer of convertible preference shares is made; or
(ii) At the time, which shall not be earlier than thirty days to the date when the holder of convertible preference shares becomes entitled to apply for equity shares.

9. What is a share warrant?

Share warrant is an option issued by the company that gives the warrant holder a right to subscribe equity shares at a pre-determined price on or after a pre-determined time period. The warrant holder partly pays the premium for the option which he purchased and partially pays the price for the share that ultimately will get allotted to him if he exercises the option.

10. What is a convertible note?

Convertible note is an instrument issued by a start-up company acknowledging receipt of money initially as debt, repayable at the option of the holder, or which is convertible into such number of equity shares of that company, within a period not exceeding five years from the date of issue of the convertible note, upon occurrence of specified events as per other terms and conditions agreed and indicated in the instrument.



11. What is a debenture?

Debenture is an instrument acknowledging a debt to the company. It contains a contract for repayment of principal after a specified period or at intervals or at the option of the company and for payment of coupons at specified interest rates. This amounts to borrowing of monies from the holders of debentures on such terms and conditions subject to which the debentures have been issued. Debenture includes debenture stock, bonds or any other instrument of the company evidencing a debt, whether constituting a charge on the assets of the company or not.

12. What are different types of debentures?

Debentures can be categorized as below:

(i) Convertible Debentures **-** These debentures come with an option of converting the whole or part of the amount of the debentures into equity shares, after a specified period. Convertible debentures may be fully convertible into equity shares or partially convertible into equity shares.
(ii) Non-Convertible Debentures - These debentures are not convertible into equity shares
(iii) Secured Debentures - Debentures which are secured by either a fixed charge or a floating charge on the assets of the company are called secured or mortgage debentures
(iv) Unsecured Debentures - Debentures which are not secured by a fixed charge or floating charge on assets

13. What are conditions for issuance of secured debentures?

Issuance of secured debentures under Companies Act is subject to certain conditions under rules framed under the Companies Act. For a debenture to constitute a secured debenture under Companies Act, the following conditions are required to be satisfied:

(i) The date of redemption of secured debentures should not exceed ten years from the date of issue.
(ii) The security for such debentures will be charge on the properties or assets of the company or its subsidiaries or its holding company or its associates companies and the security cover should have a value which is sufficient for the due repayment of the amount of debentures and interest.
(iii) The company will be required to appoint a debenture trustee to protect the interest of the debenture holders.
(iv) The company will be required to create a debenture redemption reserve.

In a company proposed to list its debentures on Indian stock exchanges then the security created to secure such debentures should be adequate to ensure a 100% security cover.

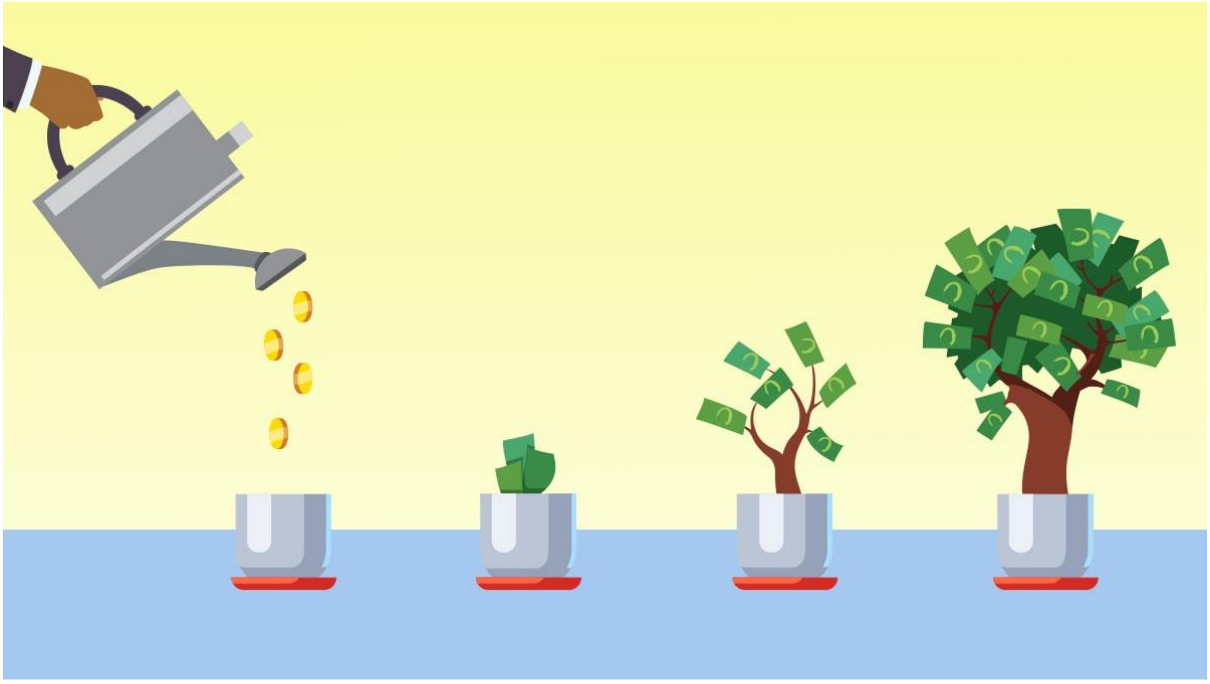
14. What are types of instruments can be issued to non-residents under the foreign direct investment policy of India?

The following equity instruments are recognized under Non-debt Rules which can be issued by an Indian company (private, public, listed and unlisted):

(i) Equity shares
(ii) Fully and compulsorily convertible debentures
(iii) Fully and compulsorily convertible preference shares
(iv) Partly paid equity shares. These shares should be fully called up within 12 months or as specified by the Reserve Bank of India. Further, at least twenty- five per cent of the total consideration amount (including share premium, if any) should be paid up-front.
(v) Share warrants. Share warrants can be issued by a company in accordance with regulations framed by the Securities and Exchange Board of India. Further, at least twenty-five per cent of the consideration shall be received upfront and the balance amount within eighteen months of the issuance of share warrants.
(vi) Convertible notes can be issued by an Indian start-up company for an amount of INR 2,500,000 or more in a single tranche.

15. Does investment by non-residents in a company through equity instruments require government approval? Are there any restrictions on the types of companies a non-resident can investment in?

Investment by non-resident is allowed under the automatic route without prior approval of the Government in all activities/ sectors as specified in the Non-debt Rules. Some of sectors in which investment is allowed up to 100% of the shares capital of the company under automatic route are airports, greenfield pharmaceuticals, online social media platforms, wholesale trading etc. Further, investment by non-resident in activities not covered under the automatic route requires prior approval of the Government.



Foreign direct investment in the following sectors is not permitted:

(i) Lottery business and gambling and betting activities.
(ii) Chit funds
(iii) Nidhi company
(iv) Trading in transferable development rights
(v) Real estate business or construction of farmhouses excluding development of townships, construction of residential or commercial premises, road or bridges and Real Estate Investment Trusts (REITs)
(vi) manufacturing of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes.
(vii) Activities or sectors not open to private sector investment
(viii) Foreign technology collaborations in lottery business and gambling and betting activities.

Foreign Exchange (Non-debt Instrument) Rules, 2019 prescribes certain limits and conditions for foreign direct investment in certain sectors.

16. Is there any restriction on price at which equity instruments can be issued by companies to non-residents?

Investment by non-residents in a company are subject to pricing guidelines. The price of the equity instruments of a company issued to a non-resident shall not be less than:

(i) The valuation of equity instruments done as per any internationally accepted pricing methodology for valuation on an arm's length basis duly certified by a chartered accountant or a merchant banker registered with the SEBI or a practising cost accountant, in case of an unlisted company; or

(ii) The price worked out in accordance with the SEBI guidelines in case of a listed company or in case of a company going through a delisting process as per the Securities

17. Can equity instruments issued to non-residents have optionality clauses and fixed returns at the time of exit?

Equity instruments issued to non-resident can contain optionality clauses such as put option for exit subject to a minimum lock-in period of 1 (one) or more, if prescribed for a particular sector.

Non-residents cannot be issued equity instruments which provided a fixed return on exit.

18. Is subscription to equity instruments by non-residents in companies required to be reported to governmental authorities?

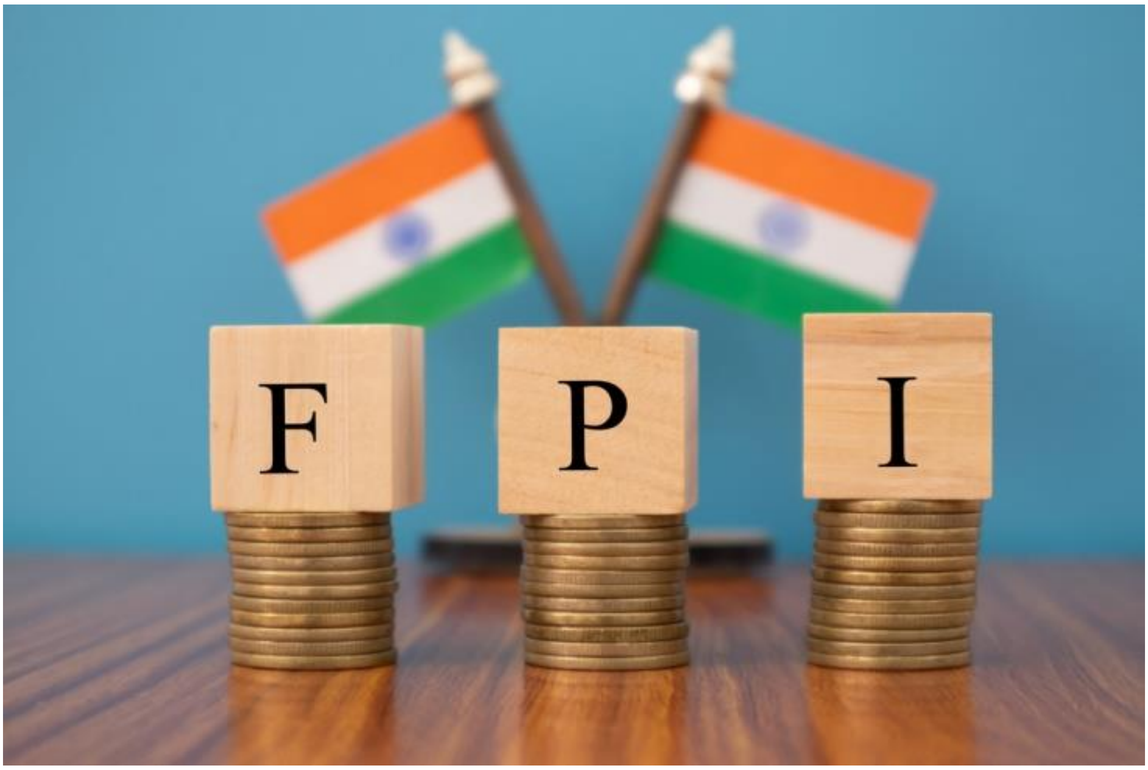
Form Foreign Currency-Gross Provisional Return (FC-GPR) has to be filed with the Reserve Bank of India within thirty days from the date of issue of equity instruments of a company to a person resident outside India.

19. Who are Foreign Portfolio Investors (FPI)? What types of instruments can PFI's invest in?

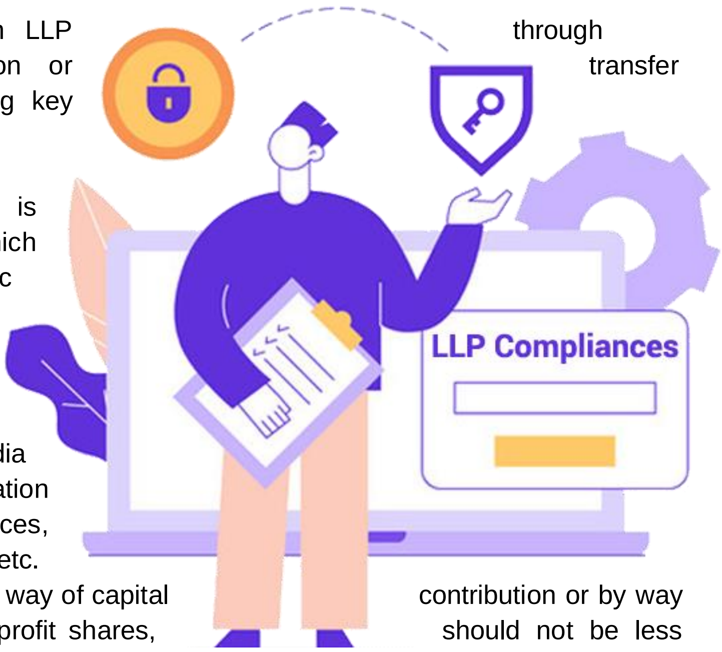
FPIs are non-resident investors who are registered in accordance with the provisions of the SEBI (Foreign Portfolio Investors) Regulations, 2014.

FPIs may purchase or sell equity instruments of an Indian company which is listed or to be listed on a recognised stock exchange in India.

The total holding by each FPI or an investor group, shall be less than 10 percent of the total paid-up equity capital on a fully diluted basis or less than 10 percent of the paid-up value of each series of debentures or preference shares or share warrants issued by an Indian company and the total holdings of all FPIs put together, including any other direct and indirect foreign investments in the Indian company permitted under these rules, shall not exceed 24 per cent of paid-up equity capital on a fully diluted basis or paid up value of each series of debentures or preference shares or share warrants.



20. Can a non-resident resident invest in an LLP? Are there any conditions required to be satisfied for investment by a non-resident in an LLP?



A non-resident can invest in an LLP through capital contribution or acquisition or transfer of profit share subject to following key conditions:

(i) Investment in an LLP is permitted only in sectors which are under 100 % automatic route and where there is no foreign direct investment linked performance conditions. Some of these sectors are online social media applications, information technology enabled services, investment advisory services etc.

(ii) Investment in a LLP either by way of capital contribution or by way of acquisition or transfer of profit shares, should not be less than the fair price worked out as per any valuation norm which is internationally accepted or adopted as per market practice and a valuation certificate to that effect shall be issued by the Chartered Accountant or by a practising Cost Accountant or by an approved valuer from the panel maintained by the Central Government.

21. Is capital contribution in LLPs by non-residents required to be reported to governmental authorities?

The LLP receiving foreign investments is required to file Form LLP (I) with the Reserve Bank of India within 30 days from the date of receipt of consideration for capital contribution and acquisition of profit shares.

22. What are the conditions required to be satisfied by a company for raising loans and borrowings from outside India?

Under Indian foreign exchange laws, a company can raise loans and borrowings from person resident outside India in the form of external commercial borrowings ("**ECBs**") as per the Master Direction - External Commercial Borrowings, Trade Credits and Structured Obligations.

ECBs can be raised as plain vanilla loans, Foreign Currency Convertible Bonds (FCCBs), non-convertible, optionally convertible, or partially convertible preference shares or debentures. ECBs can be raised either in foreign currency or Indian Rupees.

23. Is governmental approval required for availing loans under ECBs framework?

Under the automatic route, Indian companies which are eligible to raise ECBs, can raise up to USD 750 million or equivalent per financial year. Further, Indian companies raising monies above USD 750 million or equivalent would prior approval of Reserve Bank of India is required before loan can be availed.

24. What is the Minimum Average Maturity Period (MAMP) for ECBs?

MAMP for ECB will be 3 years. However, for the specific categories mentioned below, the MAMP will be:

S. No.	Category	MAMP
(i)	ECB raised by manufacturing companies up to USD 50 million or its equivalent per financial year	1 year
(ii)	ECB raised from foreign equity holder for working capital purposes, general corporate purposes or for repayment of Rupee loans	5 year
(iii)	ECB raised for: (a) working capital purposes or general corporate purposes (b) on-lending by NBFCs for working capital purposes or general corporate purposes	10 years
(iv)	ECB raised for: (a) repayment of Rupee loans availed domestically for capital	7 years

	expenditure (b) on-lending by NBFCs for the same purpose	
(v)	ECB raised for (a) repayment of Rupee loans availed domestically for purposes other than capital expenditure (b) on-lending by NBFCs for the same purpose	10 years
for the categories mentioned at (ii) to (v): (a) ECB cannot be raised from foreign branches / subsidiaries of Indian banks (b) the prescribed MAMP will have to be strictly complied with under all circumstances.		