

FEMA & FDI Handbook

*The complete guide to foreign exchange compliance for
companies operating in India*

30 days

FC-GPR DEADLINE
AFTER SHARE
ALLOTMENT

15 Jul

FLA RETURN
ANNUAL
DEADLINE

225+

FOREIGN
ENTITIES
WE FILE FOR
ANNUALLY

15+ yrs

FEMA
COMPLIANCE
PRACTICE

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What is FEMA — *and why it matters.*

FEMA stands for the Foreign Exchange Management Act, 1999. It is the primary law governing all movement of foreign currency into and out of India. Every foreign-owned Indian company operates under it — whether they know it or not.

The simple explanation

Think of FEMA as India's traffic rulebook for money crossing its borders. Every time your parent company sends money to India — as capital, as payment for services, as a loan — FEMA governs how that transaction must be documented, reported, and structured. Get it right and operations run smoothly. Get it wrong and you face penalties that compound daily.

FEMA is administered by the **Reserve Bank of India (RBI)** and enforced by the **Enforcement Directorate (ED)**. The RBI handles routine compliance and reporting. The ED handles violations — and ED investigations are serious.

FEMA replaced FERA in 1999. The Foreign Exchange Regulation Act (FERA) was India's previous exchange control law, notable for treating violations as criminal offences with the presumption of guilt. FEMA is more liberal — most violations are civil offences with compounding provisions. But "more liberal than FERA" still means significant financial penalties for non-compliance.

Who FEMA applies to

FEMA applies to every "person resident in India" who deals in foreign exchange, and to every transaction that involves foreign currency crossing India's borders. For foreign-owned Indian subsidiaries, this means:

INBOUND TRANSACTIONS COVERED BY FEMA

- Sending share capital from parent to Indian subsidiary
- Intercompany loans from parent to subsidiary (ECB)

OUTBOUND TRANSACTIONS COVERED BY FEMA

- Repatriation of profits and dividends to parent
- Repayment of intercompany loans

- Payment of dividends from India to parent

- Royalty payments from Indian subsidiary to parent

- Service fee payments to the parent company

- Payment of service fees to group entities abroad

- Salary recharges for seconded employees

- Reimbursement of costs from parent to subsidiary

Important: FEMA distinguishes between "current account transactions" (payments for goods and services — generally permitted) and "capital account transactions" (investments, loans — regulated). This distinction determines what documentation and approvals are required for each type of payment.

What is FDI — *automatic vs. approval route.*

FDI — Foreign Direct Investment — is the mechanism by which a foreign company or person holds equity shares in an Indian company. Understanding which route applies to your sector is the starting point for all FEMA compliance.

The two FDI routes

AUTOMATIC ROUTE

No prior approval from the RBI or Government of India is required. The foreign investor can proceed with the investment and file the required reports *after* the fact.

Applies to: Technology, software, engineering, CRO, back-office, SaaS, consulting, manufacturing (most sectors), and most service industries.

GOVERNMENT / APPROVAL ROUTE

Prior approval from the relevant government ministry or the Foreign Investment Facilitation Portal (FIFP) is required before investment can be made.

Applies to: Defence, media, telecom, retail (single brand vs. multi-brand), financial services, pharma (brownfield), and a small number of other regulated sectors.

Sector-specific FDI limits — the ones foreign founders most often encounter

SECTOR	FDI CAP	ROUTE	NOTES
Technology / Software / SaaS	100%	Automatic	No restrictions. Most common for foreign founders.
Engineering & manufacturing	100%	Automatic	Some defence-adjacent manufacturing requires approval

SECTOR	FDI CAP	ROUTE	NOTES
CRO / Clinical research	100%	Automatic	Greenfield pharmaceutical also 100% automatic
Professional services (CA, legal)	100%	Automatic	Subject to applicable professional regulations
Telecom	100%	Up to 49%: automatic; above: approval	Security approvals may also be required
Retail — single brand	100%	Up to 49%: automatic; above: approval	30% local sourcing requirement applies above 51%
Media (print / digital)	26–49%	Approval	Varies by type — print news is 26%; digital news is 26%
Pharma — brownfield	100%	Up to 74%: automatic; above: approval	Greenfield is 100% automatic

When in doubt about your sector, the FDI Policy consolidated circular published by DPIIT is the authoritative reference. The policy is updated periodically. We will confirm your applicable route before any investment is made — getting this wrong at the beginning creates problems that are expensive to unwind.

Downstream investment — the rule most companies miss

If your Indian subsidiary makes investments in another Indian company, this is treated as "downstream investment" and has its own FEMA compliance requirements. The Indian subsidiary is treated as a foreign-owned entity, so any investment it makes in other Indian companies must comply with the FDI policy applicable to the sector of that downstream company. This is an area where many groups inadvertently create compliance exposure.

FDI reporting requirements — *step by step.*

From the moment money crosses the border for share capital, a sequence of mandatory reporting events is triggered. Here is exactly what must be filed, in what order, and by when.

01 FIRS — Foreign Inward Remittance Statement

When the parent company wires share capital to the Indian subsidiary's bank account, the Indian bank automatically uploads a FIRS to the RBI's FIRMS portal. This is done by the bank — not by you. However, you must ensure the wire instructions include the correct purpose code, otherwise the FIRS will be filed incorrectly and need to be amended.

Filed by: Your Indian bank

Timeline: Within 5 days of receipt

Portal: RBI FIRMS

02 FIRC — Foreign Inward Remittance Certificate

The FIRC is the bank's official certificate confirming receipt of foreign funds. It contains the amount, currency, purpose code, and remitter details. You must obtain this from your bank and retain it permanently — it is your primary evidence of compliant FDI receipt and will be required by auditors, during due diligence, and in any RBI inquiry.

Obtained from: Your Indian bank

When: After funds are credited

Retain: Permanently

03

FC-GPR — the most time-critical filing

Form FC-GPR (Foreign Currency — Gross Provisional Return) must be filed on the RBI's FIRMS portal within **30 days of the date of share allotment**. This is the most important and most frequently missed FEMA deadline. The filing reports the FDI received and the shares allotted to the foreign investor.

To file FC-GPR you need: the FIRC, a Valuation Certificate from a Registered Valuer or SEBI-registered Merchant Banker certifying the fair value of the shares, the Board resolution for share allotment, and the company's RBI registration (Entity Master).

Deadline: 30 days from allotment

Portal: FIRMS (firms.rbi.org.in)

Requires: Valuation certificate

Filed by: Indian company

04

FLA Return — annual FEMA reporting

Every Indian company that has received FDI (or made foreign direct investment abroad) must file a Foreign Liabilities and Assets (FLA) Return with the RBI each year. The filing deadline is July 15. It reports all outstanding FDI positions, loans from foreign entities, and any foreign assets.

Unlike FC-GPR (which is event-triggered), the FLA Return is an annual obligation regardless of whether any new FDI was received that year. As long as the company has any outstanding foreign equity or loans on its books, the FLA return must be filed.

Deadline: July 15 each year

Portal: FLAIR (RBI)

Who must file: All companies with FDI

Additional reporting for subsequent rounds

If your parent sends additional capital (for a second or third tranche of investment), the full FC-GPR process must be repeated for each allotment. Each tranche requires a fresh valuation certificate and a new FC-GPR filing within 30 days of that allotment.

Transfer of shares between foreign investors requires a different form — Form FC-TRS (Foreign Currency — Transfer of Shares). If the parent company is restructured and shares of the Indian subsidiary are transferred from one foreign entity to another, FC-TRS

must be filed within 60 days of the receipt of consideration or transfer, whichever is earlier.

Capital vs. loan — *the FEMA difference.*

How you structure the money your parent sends to India has significant compliance and tax consequences. Equity and debt are treated very differently under FEMA.

DIMENSION	EQUITY (SHARE CAPITAL)	LOAN (EXTERNAL COMMERCIAL BORROWING — ECB)
FEMA category	Foreign Direct Investment	External Commercial Borrowing (ECB)
Reporting form	FC-GPR (within 30 days of allotment)	ECB-2 (monthly return) + Loan Registration Number (LRN)
RBI approval	Not required (automatic route)	Not required but must comply with ECB framework
Interest rate	N/A — returns are dividends	Restricted to benchmark rate + maximum spread (typically SOFR + 300–500 bps)
Minimum maturity	N/A	Minimum 3 years for most ECBs
End-use restrictions	Generally none for operational use	Cannot be used for real estate, working capital (in some cases), equity investment
Repayment	Only through dividends or buyback — regulated	Principal and interest repayable per agreed schedule
Tax treatment	Dividends taxable in India; may be exempt under tax treaty	Interest deductible for Indian subsidiary; withholding tax on payment

When is an intercompany loan the right choice?

Most foreign-owned Indian subsidiaries are capitalised purely through equity. However, in certain structures — particularly where the parent wants a deductible interest expense in India, or needs to structure the relationship as a reimbursable cost rather than permanent capital — an ECB may be appropriate.

ECB compliance is complex and ongoing. An intercompany loan from a foreign parent to an Indian subsidiary is an ECB — not a simple loan. It requires obtaining a Loan Registration Number (LRN) from the RBI before the first drawdown, filing a monthly ECB-2 return for every month the loan is outstanding, and ensuring all terms comply with the RBI ECB framework. Using an intercompany loan without ECB compliance is a serious FEMA violation. Get advice before drawing down any loan from your parent.

Intercompany payments *under FEMA*.

Once your Indian subsidiary is operational, there will be ongoing payments between it and the parent company — service fees, cost reimbursements, royalties, and more. Each type of payment has its own FEMA treatment.

Current account transactions — generally permitted

Payments for legitimate business services between the Indian subsidiary and the parent are classified as current account transactions and are generally permitted without RBI approval. However, they must be properly documented and use the correct purpose code.

PAYMENT TYPE	FEMA TREATMENT	DOCUMENTATION REQUIRED	RESTRICTIONS
Service fees (subsidiary pays parent)	Current account — permitted	Service agreement, invoices, transfer pricing documentation	Must be arm's-length. Subject to withholding tax.
Cost reimbursements	Current account — permitted	Cost-sharing agreement, invoices, supporting calculations	Must reflect actual costs. Reimbursements of profit disallowed.
Royalties (parent's IP used by subsidiary)	Current account — permitted	IP licence agreement, royalty calculation workings	No specific cap but subject to transfer pricing scrutiny
Salary recharges (seconded employees)	Current account — permitted	Secondment agreement, payroll records, recharge invoice	Must reflect actual salary + applicable costs. PE risk if not structured correctly.
Management fees	Current account — permitted	Management services agreement, service evidence	Tax authorities scrutinise heavily — robust evidence of service delivery required
Dividends (subsidiary pays parent)	Capital account — regulated	Board resolution, AGM approval, compliance certificate	Subject to dividend distribution tax and withholding tax rules

The golden rules for intercompany payments

- **Written agreement first, payment second.** Never make an intercompany payment without a signed agreement in place. The agreement defines the commercial relationship that justifies the payment under both FEMA and transfer pricing rules.
- **Correct purpose code on every remittance.** The bank will ask for a purpose code when processing the payment. Using the wrong code — even accidentally — creates a FEMA compliance issue that requires amendment and can trigger scrutiny.
- **Invoices must precede payment.** The Indian subsidiary must issue a tax-compliant invoice before making any payment abroad. Payments without invoices are not deductible and may be treated as undocumented capital outflows.
- **Transfer pricing applies to every transaction.** Every intercompany payment is subject to India's transfer pricing rules. The amount must be what independent parties would agree to — backed by annual documentation.
- **Withholding tax on outbound payments.** Service fees, royalties, interest, and dividends paid from India to a foreign parent are subject to Indian withholding tax (TDS). The applicable rate depends on the India–parent country tax treaty.

Paying Indian employees from abroad is a FEMA violation. If the parent company pays the salary of an employee working in India directly — without routing it through the Indian subsidiary's payroll — this is a FEMA violation. It also creates PE risk, payroll tax exposure, and labour law issues. All employees working in India must be on the Indian subsidiary's payroll.

Purpose codes — *what they are and why they matter.*

Purpose codes are the RBI's classification system for every foreign exchange transaction. They determine how the transaction is reported to the RBI, how it is taxed, and whether it triggers additional compliance obligations. Getting the purpose code wrong is one of the most common — and most easily avoided — FEMA mistakes.

What a purpose code actually is

Every inward and outward foreign exchange transaction processed through an Indian bank must be assigned an RBI-defined purpose code. The bank uses this code to report the transaction to the RBI. The purpose code tells the RBI what the payment is for — share capital, service fee, royalty, dividend, and so on.

Purpose codes are not optional. Your bank will ask you for a purpose code when processing any foreign exchange transaction. If you don't provide one, they will either reject the transaction or assign one themselves — which may be wrong. The responsibility for providing the correct purpose code lies with the remitter and the Indian beneficiary company.

Commonly used purpose codes for foreign-owned Indian subsidiaries

TRANSACTION	PURPOSE CODE	CATEGORY
Share capital / FDI inflow	S0001 (Equity — inward)	Capital account
Technical / professional service fees received	P0802 / P0803	Current account — services
Software development services received	P0805	Current account — software exports
Royalties and licence fees received	P1004	Current account — IP income

TRANSACTION	PURPOSE CODE	CATEGORY
Business services / BPO income received	P0806	Current account — services
Service fees paid abroad	S1005 / S1006	Current account — service imports
ECB loan receipt	S0102	Capital account — borrowing
ECB repayment	S0203	Capital account — repayment
Dividend payment to foreign shareholder	S0001 / S0004	Current account — investment income

Wrong purpose code consequences: Using the wrong purpose code causes the RBI to receive incorrect information about India's balance of payments. When the error is discovered — often during audit or due diligence — the company must file a Revised FIRS with the bank and may need to report the discrepancy to the RBI. In serious cases, this can be treated as a FEMA violation.

FEMA penalties — *what non-compliance actually costs.*

This is the section that should motivate every foreign founder to take FEMA compliance seriously. The penalties are significant, compound over time, and can affect the company's ability to raise funds or exit cleanly.

Civil penalties under FEMA

Under Section 13 of FEMA, the penalty for a contravention can be up to three times the sum involved in the contravention — or up to ₹2 lakh (approximately USD 2,400) if the amount cannot be quantified. Where the contravention involves a continuing one (like a delayed FC-GPR), an additional penalty of up to ₹5,000 per day applies for each day the contravention continues.

INDICATIVE PENALTY RANGES — COMMON VIOLATIONS

FC-GPR not filed within 30 days of share allotment	₹5,000/day + up to 3× amount
FLA Return not filed by July 15	₹5,000–50,000 + compounding
ECB drawn without LRN / ECB-2 not filed	₹5,000/day + up to 3× loan amount
Paying India employees from abroad	Up to 3× total salary payments
Intercompany payments without documentation	Up to 3× payment amount
Shares issued at below-fair-value price	Up to 3× difference in value

Compounding — the path out of a violation

If you have already committed a FEMA violation, the best course of action is usually "compounding" — a process by which the RBI or the Adjudicating Authority allows you to

settle the violation by paying a compounding fee, without the matter proceeding to formal adjudication or prosecution.

Compounding is available for most FEMA violations except those involving national security, money laundering, and serious fraud. The compounding fee is typically lower than the maximum penalty and the process resolves the matter with finality. However, compounding applications must be filed voluntarily and disclose all relevant facts — and the process can take 6–12 months.

During fundraising and M&A, FEMA violations are discovered. When a foreign company acquires or invests in an Indian company, or when an Indian company raises institutional funding, FEMA compliance is thoroughly examined during due diligence. An unresolved violation — even an old, small one — can significantly delay or derail a transaction. The cost of fixing historical FEMA issues during a time-pressured deal is always higher than the cost of getting it right from the beginning.

Common FEMA mistakes — *and how to avoid them.*

After 15 years of managing FEMA compliance for 200+ foreign-owned subsidiaries, these are the eight errors we see most often — and the ones that create the most damage.

01 Missing the FC-GPR 30-day deadline

The most common FEMA violation. Companies receive the share capital, then get busy with operations and forget to file the FC-GPR. The 30-day clock starts from the date of share allotment — not from the date funds are received. By the time the mistake is discovered, the penalty is often substantial.

Fix: Set a calendar reminder for day 25 after every share allotment. Never let the FC-GPR go into the next month unfiled.

02 Using the wrong purpose code on the wire transfer

The parent company's treasury team sends a wire with a generic or incorrect purpose code. The bank files the FIRS with the wrong code. This creates a mismatch between the FIRS and the FC-GPR that must be corrected — and may require a formal RBI communication.

Fix: Provide the bank with the specific purpose code (S0001 for FDI equity inflows) in the wire instructions. Confirm the code with your compliance team before sending.

03

Issuing shares below fair value

FEMA requires that shares issued to a foreign investor must be at or above the fair market value determined by a Registered Valuer or SEBI Merchant Banker. Issuing shares below this value is a FEMA violation — the "discount" is treated as an underpayment by the foreign investor.

Fix: Always obtain a Registered Valuer report before each allotment. For early-stage companies, this is a simple exercise but it must be done.

04

Not filing the FLA Return annually

The FLA Return is due every year by July 15 — regardless of whether any new FDI was received. Companies often file it in the year of initial investment and then stop, not realising it is an annual obligation as long as any FDI is on the company's books.

Fix: Add the FLA Return to the annual compliance calendar. It is a simple filing but the deadline is absolute.

05

Paying India-based employees directly from the parent

Some early-stage companies — to simplify payroll — pay India-based staff directly from the parent company's bank account, intending to "sort it out later." This is a FEMA violation from the first payment. It also creates PE risk for the parent and payroll tax exposure.

Fix: All India-based employees must be on the Indian subsidiary's payroll. If the subsidiary is not yet incorporated, use an Employer of Record (EOR) service — do not pay from the parent account.

06

Making intercompany payments without agreements

The parent pays for something on behalf of the subsidiary, or the subsidiary pays a management fee to the parent, without any written agreement. The payment is made, the cost is booked, and everyone moves on — until a tax authority or auditor asks for the agreement and there isn't one.

Fix: Every recurring intercompany transaction must be governed by a written agreement signed before payments begin. Retroactive agreements do not cure historical violations.

07

Treating intercompany loans as equity

When the parent sends money to the subsidiary as a "loan" (rather than as share capital), many companies fail to recognise that this triggers ECB compliance — including the requirement to obtain an LRN before drawdown and file monthly ECB-2 returns. The loan is often repaid without any of this being done.

Fix: Never draw down an intercompany loan before confirming the ECB compliance requirements with your FEMA advisor. If in doubt, convert to equity — it is simpler to manage.

08

Ignoring FEMA when transferring shares between group entities

When the parent company restructures and its shares in the Indian subsidiary are transferred from one foreign entity to another — even within the same group — FC-TRS must be filed within 60 days. This is almost universally missed in group restructurings.

Fix: Include FEMA compliance review as a mandatory step in any group restructuring or internal reorganisation involving the Indian subsidiary.

FEMA compliance calendar — *every deadline that matters.*

Use this calendar alongside your general India compliance calendar. FEMA deadlines are independent of — and additional to — your GST, TDS, and ROC obligations.

Event-triggered filings

These are triggered by specific transactions — not by calendar dates. They must be tracked for every relevant transaction.

FC-GPR — after share allotment to foreign investor **30 days**
From date of allotment. No extensions.

FIRS — after foreign funds received in bank **Within 5 days**
Filed by bank automatically — but you must provide correct purpose code

FC-TRS — after transfer of shares between foreign investors **60 days**
From date of receipt of consideration or transfer (whichever is earlier)

ECB-2 — monthly return for outstanding ECB loans **Monthly**
By last business day of following month. Every month until loan is repaid.

LRN — before ECB drawdown **Before first drawdown**
Must be obtained from RBI before any ECB funds are received

Annual compliance calendar

FLA Return — all companies with outstanding FDI

15 July

Every year. No extensions normally granted.

Annual Performance Report (APR) — for Indian companies that have made overseas direct investment

31 December

Only for companies with overseas investments

Transfer pricing documentation

Before ITR filing

Required if international transactions exceed ₹1 crore in a year

Full FEMA compliance checklist

BEFORE REMITTANCE

- FDI route confirmed (automatic or approval)
- Sector FDI cap verified
- Valuation certificate obtained
- Board resolution for share allotment passed
- Correct purpose code identified
- Bank wire instructions include purpose code
- Share allotment date confirmed for FC-GPR deadline

AFTER REMITTANCE

- FIRC obtained from bank
- FIRS confirmed as filed with correct purpose code
- Shares allotted within agreed timeline
- FC-GPR filed within 30 days of allotment
- Entity Master on FIRMS portal up to date
- FC-GPR acknowledgement retained

ONGOING / ANNUAL

- FLA Return filed by July 15 each year
- ECB-2 filed monthly (if any loan outstanding)
- Intercompany agreements in place for all payments
- TP documentation updated annually
- Purpose codes reviewed for all recurring payments
- All FIRC / FIRS records retained permanently

Need FEMA or FDI guidance for your India subsidiary?

Our dedicated FEMA desk files FC-GPR and FLA Returns for 225+ foreign-owned subsidiaries annually. Schedule a confidential consultation with a senior partner.

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