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MUMBAI: The Reserve Bank of India (RBI) has ruled that foreign venture capital funds will have to provide their financial statements for regulatory approval to invest in India. The central bank has sent nearly a dozen applications of such funds back to market regulator the Securities and Exchange Board of India (Sebi), as these were not backed by financial statements.

Securities lawyers say the move is part of the Indian regulators' aim to ensure that only the credible players get approval to start operations here. Some months ago, Sebi had made it mandatory for foreign venture capital investors to obtain a firm commitment of at least \$1 million from their investors.

The rule on minimum commitment was a modification to an earlier rule that foreign venture capital funds should have a minimum capitalisation of \$100,000.

"The financial statements rule could be to ensure the ability of the FVCI to invest at least the committed amount," says Vikram Shroff of Nishith Desai Associates, who are advisors to several foreign funds.

However, he feels that newly-formed FVCIs may face difficulties in providing financial statements that meet the regulators' expectations.

The apex bank, which has the final word on all foreign investments, is keen to ensure that due diligence is carried out on these foreign entities to check whether they are eligible to invest in the Indian market.

"It is not as though RBI is barring newly-established entities from receiving the FVCI status. But for all new entrants, RBI is likely to accept the background details of the promoters or the parent to establish the credentials of the FVCI," said Suhail Nathani, Partner, Economic Laws Practice.

Often, a foreign venture capital fund looking to invest in India usually formed an investment holding firm in Mauritius with basic capital, often not more than a few dollars. The investment company then filed for registration with Indian regulators, and once it got the approval, overseas investors were gradually roped in.

Such a practice was followed because several foreign investors were uncomfortable in making commitments, unless the offshore fund had obtained necessary approvals from the regulator. But RBI was not in favour of such a structure. In the past, RBI had sent back applications of foreign venture capital funds to Sebi unapproved, citing 'under-capitalisation' as the reason.

India has attracted Rs 26,827 crore of investments through foreign venture capital funds, compared to domestic venture capital funds' Rs 24,893 crore as on December 31, 2009, according to Sebi data. At present, there are 144 foreign venture capital funds registered with the market regulator.

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