

AMENDMENTS IN INVESTMENTS ABROAD BY RESIDENTS – CHANGES IN FOREIGN EXCHANGE MANUAL

February 2021

INTRODUCTION

Foreword

Amendments in the foreign exchange rules and regulations are issued through FE Circulars, Circular Letters and Notifications to Authorized Dealers, importers, exporters, general public etc. which are placed at the State Bank's website (<http://www.sbp.org.pk/epd/index.htm>). These regulations are compiled in the form of **Foreign Exchange Manual** which is updated periodically and placed at the State Bank's website.

State Bank of Pakistan (SBP) vide [F. E. Circular No. 01 dated February 10, 2021](#) has notified critical revisions in chapter 20 of the Foreign Exchange Manual to facilitate Start-ups, FinTech and Exports.

SBP, after approval of the Federal Government, has introduced three new categories of investment abroad under its revised policy governing equity investment abroad and banks have been authorized to allow remittances under newly introduced categories. As per SBP regulations scheduled banks are allowed to deal in foreign currency and are termed as Authorized Dealers.

This document summarizes such amendments.

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TYPES OF INVESTMENTS ABROAD

Applicable Law: Foreign Exchange Manual

A. Entrepreneurs (through holding companies and sweat equity)

B. Investment abroad by resident companies/ firms for expansion of Business

C. Exporters (through subsidiaries or branch offices)

D. Investment abroad by Resident Individuals

E. Post Investment Requirements

ENTREPRENEURS (THROUGH HOLDING COMPANIES AND SWEAT EQUITY)

The following changes are primarily targeted to facilitate some foreign investors who prefer to invest indirectly through holding company established abroad specially in the Fintech and Startup firms.

Conditions on Operating Company (OpCo):

- *Shall be incorporated under the Companies' Act, 2017 for **not more than 07 years** provided that such entity is not formed by splitting up, or reconstruction of a business already in existence.*
- *The company has **annual revenue below PKR 2 billion** since its incorporation.*
- *The company has **equity (including retained earnings) below PKR 300 million** as per latest audited financials.*

Permission not required from SBP for the following:

- ***Initial incorporation expenses**, on actual basis but **not exceeding USD 10,000** to incorporate a holding company abroad to raise capital.*
- *The shareholders of resident company can **swap shares to mirror the shareholding** of local company in the holding company. No remittance in this regard shall be allowed from Pakistan.*

ENTREPRENEURS (THROUGH HOLDING COMPANIES AND SWEAT EQUITY)

Conditions on Holding Company (HoldCo):

- *Repatriation of **at least 80% of the funds raised from abroad on annual basis until USD 1 million** (net of dividend remitted by OpCo) is remitted to Pakistan.*
- *Subsequently, **at least 50% of funds raised from abroad on annual basis until USD 10 million** (net of dividend remitted by OpCo) is remitted to Pakistan on cumulative basis.*

Other Conditions:

- *The OpCo can issue shares in favor of HoldCo, against the amount received from abroad, on repatriation basis in terms of provisions of para 6 and 7 of Chapter 20 of Foreign Exchange Manual. The OpCo shall report to SBP within 30 days of issuance of shares.*
- *HoldCo shall remit the dividends to Pakistan against shares acquired by resident companies/firms and founders.*

ENTREPRENEURS (THROUGH HOLDING COMPANIES AND SWEAT EQUITY)

SIMPLE ILLUSTRATION:

ABC Private Limited is a company incorporated in Pakistan owned 100% by Mr. X (*Pakistani resident*). A foreign venture capital firm DEF Ventures wants to invest (*either via loan or equity*) USD 50 million in the Company for a 50% stake subject to the investment being in an offshore holding company.

Accordingly, Mr. X will form an entity in a foreign jurisdiction namely ABC HOLDING CO BV. As such, in ABC HOLDING CO BV, shares equal to the value of shares held by Mr. X will be issued as consideration against the shares Mr. X holds in ABC Private Limited. There will be no movement of the funds involved in this case.

DEF Ventures will now invest the USD 50 million in the ABC HOLDING CO BV. The shareholding of ABC HOLDING CO. BV will be equally held by Mr. X and DEF Ventures. At least, 80% of this investment shall flow to ABC Private Limited as repatriable investment. The only asset of ABC HOLDING CO. BV will be the shares of ABC Private Limited.

INVESTMENT ABROAD BY RESIDENT COMPANIES/ FIRMS FOR EXPANSION OF BUSINESS

No change and as such residents would need to approach SBP for approval through their banks as per existing policy. The conditions for the same were prescribed in Circular 12 of 2001. Such conditions are produced in this document as Annexure A.

EXPORTERS (THROUGH SUBSIDIARIES OR BRANCH OFFICES)

Export oriented companies will be allowed to establish their subsidiaries or branch offices for promoting their exports without the need of obtaining any approval from the SBP. One entity per jurisdiction shall be allowed for establishment/acquisition of subsidiary/marketing/liaison/ representative office abroad.

Remittance Allowed:

- ***Not exceeding the 10% of average annual export earnings of last three calendar years of the applicant, or USD 100,000 whichever is higher.*** Authorized dealer can also open standby letter of credit to facilitate the offshore entity of the applicant for raising funds from offshore jurisdiction, within this limit.
- ***Remittance of USD 30,000 allowed from 2nd year onward (from date of investment) to meet the annual budgeted expenses of representative office/subsidiary/liaison office abroad with an annual increase of 10% in expenses, subject to a valid justification.***
- ***At any point of time, investment abroad of the applicant should not exceed 80% of its equity (after adjusting for investments in subsidiaries/ associates, goodwill, Deferred Tax Assets, receivables from related entities etc.).***
- ***The export overdue of intending investor shall not be more than 1% of the previous year's exports.***

EXPORTERS (THROUGH SUBSIDIARIES OR BRANCH OFFICES)

Major Requirements/Assessment to be performed by designated bank:

- *In case applicant's export earnings during last three calendar years is **less than USD 300,000** details of products to be exported by the applicant and an undertaking that proposed investment has the potential to increase the exports of Pakistan shall be obtained.*
- *The business activity of the company, firm in which investment is desired to be made should ordinarily be of the same nature as that in which the applicant is already engaged in Pakistan. Proposal for investment abroad in the extended line of business or vertical business integration shall also be considered as similar line of business.*
- *Financial soundness evidenced by applicant's audited accounts for the last three years. In the case of a company in the I.T. business, the condition of three years may be reduced to one year.*
- *In case of acquisition of subsidiary abroad, the valuation of the company being acquired shall be justified. In case the **target company is unlisted**, and the amount of investment is **above USD 1 million**, the designated bank may allow the transaction after satisfying itself through a valuation report from an accredited business valuation firm of the country in which investment is to be made.*
- *While assessing any request for establishment/acquisition of subsidiary or marketing/ liaison/ representative office abroad, due weightage shall be given to the performance of previous investments abroad, if any, in terms of profit repatriation, increase in exports etc.*
- *In case of additional capital injection in subsidiary, due weightage shall be given to its previous performance as well as future outlook*

INVESTMENT ABROAD BY RESIDENT INDIVIDUALS

Resident Individuals of Pakistan will be allowed to acquire equity stake in international companies through share option plans or investment in listed securities or against efforts and services (sweat equity).

Investments in Listed Securities abroad:

- *Banks have been allowed to remit a **maximum amount of USD 25,000, during a calendar year**, on behalf of resident individuals to acquire shares of listed companies abroad subject to condition that their shareholding **shall not exceed 1% of shares of the investee company** at any time.*

Employee Stock Option Plans (ESOP):

- *Banks have been allowed to remit **USD 50,000, during a calendar year**, on behalf of resident employees of subsidiaries of foreign companies in Pakistan for participating in the share option plans of parent companies subject to condition that stake of an individual employee in parent company **shall not exceed 3% shareholding of investee company***

INVESTMENT ABROAD BY RESIDENT INDIVIDUALS

Sweat Equity:

- Resident individuals can **acquire the shares** of companies abroad against their efforts and services (sweat equity), **without any monetary consideration** subject to condition that their **maximum shareholding shall not exceed 20% of shares** of the investee company at any time.
- The investor shall submit the agreement, confirming this arrangement, to SBP through its designated Authorized Dealer while reporting this investment, along with its detailed profile showing his/her filed field of expertise with documentary evidences.

POST INVESTMENT REQUIREMENTS

- *Submit the documentary evidences related to establishment/acquisition of subsidiary/branch office/shares abroad, **within one month of making the investment**, through designated authorized dealer.*
- *Make a return to State Bank on the prescribed form V-100 through their banker **within one month of making the investment**.*
- *Each entity who invested abroad under this policy shall submit audited financials of the investee company to the Authorized Dealer on annual basis.*
- *Repatriate the dividend/disinvestments proceeds (including capital gains) to Pakistan through normal banking channels. The amounts so received would be **converted to local currency** by the bank concerned and a Proceeds Realization Certificate in original evidencing the same shall be filed by the owner with the State Bank through its Authorized Dealer. Such amounts shall not be allowed for credit to a Foreign Currency Account or for purchase of Pakistani securities on Repatriable basis.*

ANNEXURE A

- *Only companies incorporated in Pakistan including foreign controlled companies and firms owned by Pakistani Nationals resident in Pakistan are allowed investment under this category.*
- *The business activity of the company, firm, joint venture in which investment is desired to be made should ordinarily be of the same nature as that in which the investor is already engaged in Pakistan, or in which the investor has the potential to acquire sufficient expertise from the market for running the business. Proposal for investment abroad in the extended line of business or vertical business integration shall also be considered as similar line of business.*
- *The investor should be financially sound as shown by its audited accounts for the last three years. In the case of a company in the I.T. business, however, the condition of three years may be reduced to one year.*
- *The proposal should be economically viable as evidenced from a feasibility report. It should have the potential for future earnings of foreign exchange coupled with other advantages to the country such as employment opportunities for Pakistani nationals and improvement in national human resources.*
- *Funding for the proposed investment abroad shall be allowed from the foreign currency funds available to the credit of special foreign currency accounts maintained by the applicant in terms of applicable Foreign Exchange Regulations. However, in case the applicant does not have any such account or the balance available in its special foreign currency accounts is not sufficient, remittance can be allowed from interbank market.*
- *The State Bank under the aforesaid guideline would also deal with the proposals emanating from the Public Sector Organizations providing financial services whereas the concerned ministry would deal with the investment proposals from all other public sector organizations.*



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