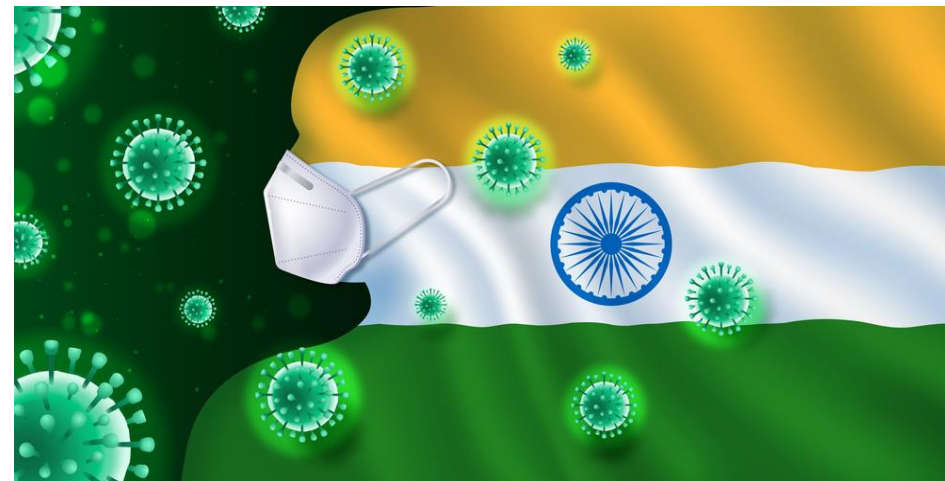


*De Jure*

*April 20, 2020*

## FDI Clampdown Amidst Covid -19 Lockdown!



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With the objective of restraining opportunistic takeovers and acquisitions of Indian companies amidst the ongoing global crisis due to the Covid 19 pandemic, the Department of Promotion of Industry and Internal Trade has issued a press note dated April 17, 2020 ("**Press Note 2020**"), proposing to impose a partial embargo on foreign direct investments ("**FDI**") from countries sharing land borders with India.

Prior to the introduction of the Press Note 2020, the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 and the relevant schedules thereunder ("**FEMA NDI Rules**") stipulated restrictions on FDI received from citizens of, and entities incorporated in, Pakistan and Bangladesh, pursuant to which, FDI in an Indian company engaged in certain sectors, by a citizen of, or entity incorporated in Bangladesh or Pakistan requires a Government approval. Further, besides the sectors and activities in India in which FDI is otherwise prohibited, a citizen of, or an entity incorporated in Pakistan is also prohibited from investing in certain sensitive sectors comprising defence, space and atomic energy.

### **Amendments Introduced by Press Note 2020**

Pursuant to the Press Note 2020 and the amended Paragraph 3.1.1(a) of the FDI Policy, FDI in Indian companies by an entity which is incorporated in a country sharing land border with India ("**Neighbouring Nations**") or an entity whose beneficial owner is situated in, or is a citizen of, the Neighbouring Nations, will require Government approval. The Press Note 2020, by way of Paragraph 3.1.1(b) further stipulates that any transfer of ownership of an existing or future FDI in an Indian company, which directly or indirectly results in its beneficial ownership to come within the purview of the Paragraph 3.1.1(a), will also require a Government approval.

### **A brief analysis of Press Note 2020**



Neighbouring Nations. It is pertinent to note that India shares land borders with seven nations comprising Pakistan, Bangladesh, China, Nepal, Myanmar, Bhutan and Afghanistan. Thus, Neighbouring Nations will comprise all of these countries and FDI by entities incorporated in, or citizens of, any of these countries would require a prior Government approval.

Concept of Beneficial Ownership. The Press Note 2020 not only mandates a Government approval for FDI in an Indian company from entities and citizens of the Neighbouring Nations but also proposes to extend a similar restriction for an indirect

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foreign investment into Indian companies from countries other than the Neighbouring Nations by introducing the concept of beneficial ownership in Paragraph 3.1.1(a). The beneficial ownership test will become applicable to FDI by an entity, though not incorporated in any of the Neighbouring Nations, but forms part of a multi-layered structure. To illustrate, a company incorporated in any country from which FDI is otherwise permitted under the automatic route but whose ultimate beneficial owner is a Chinese national or an entity incorporated in China, may require a prior Government approval if the beneficial ownership test is satisfied. It is relevant to mention here that neither the concept nor the definition of “*beneficial ownership*” has been included in the Press Note 2020.

Transfer of Ownership of Existing or Future FDI. By introducing Paragraph 3.1.1(b), the Press Note 2020, proposes to impose a restriction not only on the primary investments proposed to be made in Indian companies by entities and citizens of the Neighbouring Nations but also brings within its purview direct and indirect secondary investments in Indian companies by way of acquisition of shareholding from the existing shareholders of the Indian companies. Thus, transfer of shares or securities of Indian companies to an entity incorporated in, or a citizen of, Neighbouring Nations or to an entity whose beneficial owner is situated in, or is a citizen of, the Neighbouring Nations, will require Government approval.

### **Conclusion**

Curbs on FDI through Press Note 2020, although applicable to FDI from all Neighbouring Nations, primarily seems to be aimed at bringing FDI flow into Indian companies from China within the purview of the Government approval route. The amendments introduced by Press Note 2020 will impact FDI (*from any of these Neighbouring Nations*) not just by way of new investments but also further fund raise by Indian companies having shareholders from any of such Neighbouring Nations, including indirectly through a beneficial ownership holding. Additionally, Press Note 2020 is applicable to both primary and secondary investments in Indian companies from any of these Neighbouring Nations.

The amendments introduced by the Press Note 2020 will become effective from the date of FEMA notification and the relevant provisions of the NDI Rules will be suitably amended.

Thus, it is expected that the notification amending the NDI Rules is on the anvil and which would, not just spell out the fine print of this proposed amendment but also provide much needed clarity on concepts such as beneficial ownership and other ancillary aspects.



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## DISCLAIMER

This update only contains a summary/ limited description of the topic dealt with hereinabove for general information purposes and should not be construed as a legal opinion or be relied upon in absence of specific legal advice. For further information or legal advice please feel free to contact us.

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