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**The Ministry of Finance amends the Foreign Exchange Management (Non Debt Instruments) Rules 2019**

## INTRODUCTION

In furtherance to the Finance Minister's announcement in the Union Budget 2024-24, the Ministry of Finance notified the Foreign Exchange Management (Non Debt Instruments) (Fourth Amendment) Rules, 2024 (**Amendment**) dated 16 August 2024 revising the provisions of the Foreign Exchange Management (Non Debt Instruments) Rules, 2019 (**NDI Rules**) with the intention of simplifying the regulatory landscape of foreign investments in India.

We have summarised the provisions of the Amendment below:

## DEFINITION OF CONTROL

Prior to the Amendment, the NDI Rules defined the term "control" for the purpose of evaluating downstream investments in a company to mean *the right to appoint majority of the directors or to control the management or policy decisions including by virtue of their shareholding or management rights or shareholders agreement or voting agreement.*

The Amendment has revised the definition of the term as follows:

***"control" shall have the same meaning as assigned to it in the Companies Act, 2013 and for the purposes of Limited Liability Partnership, shall mean the right to appoint majority of the designated partners, where such designated partners, with specific exclusion to others, have control over all the policies of an LLP;"***

Prior to the Amendment, a view was being taken that "control" for the purpose of Foreign Direct Investment (FDI) in an unlisted company would have the same meaning as assigned to it in the Companies Act 2013; however, the revised definition under the Amendment has clarified this in fine print. It has also been clarified that this new definition will be applicable to downstream investments as well. Therefore, this change has aligned the provisions of the Companies Act 2013 and the NDI Rules.

## GOVERNMENT APPROVAL REQUIREMENT - EXPANSION OF SCOPE

A non-resident, not being a non-resident Indian (NRI), overseas citizen of India (**OCI**) or an erstwhile overseas corporate body could transfer equity instruments of an Indian company, or units held by it to any non-resident by way of sale or gift. The NDI Rules mentioned that such transfer would require a government approval in case the Indian entity was engaged in an approval sector.

However, government approvals other than sectoral approvals (such as Press Note 3 approvals) also have to be obtained for FDI, if applicable. Accordingly, the Amendment has clarified this existing position by expanding the language provided in the NDI Rules and stating that *prior government approval shall be obtained for transfer in all cases* wherever Government approval is applicable.

## CLARIFICATION ON SWAP OF SHARES

Prior to the Amendment, Schedule I of the NDI Rules allowed an Indian company to **issue** equity instruments to a non-resident against swap of equity instruments. Further, the Foreign Exchange Management (Overseas Investment) Rules, 2022 (OI Rules) allowed: (i) an Indian entity to make or hold overseas direction investment (ODI) by way of swap of securities; and (ii) a resident individual to hold overseas investment by way of swap of securities on account of a merger, demerger, amalgamation or liquidation, provided that both legs of the transaction complied with the provisions of the Foreign Exchange Management Act, 1999. While the OI Rules provided for such swaps, the NDI Rules were silent on secondary transfers of resident entity/individual shareholder swaps.

The Amendment has now introduced Rule 9A to the NDI Rules which allows transfer of equity instruments of an Indian company between a resident and a non-resident by way of: (i) swap of equity instruments; and (ii) swap of equity capital of a foreign company in compliance with the OI Rules. Such swap remains subject to prior

government approval in cases where receipt of foreign investment in the Indian investee company requires approval. Further, Schedule I of the NDI Rules has been amended to allow issuance of equity instruments of an Indian company against swap of equity capital a foreign company under the OI Rules.

Hence the Amendment has now clarified the permissibility of swap transactions. Below is a table indicating the revised position:

TRANSACTION	PREVIOUS POSITION	REVISED POSITION
Issuance of equity instruments to a non-resident by a resident company (A) against swap of equity instruments of another resident entity (B)	<i>Permitted</i>	<i>Permitted</i>
Swap of equity instruments of an Indian company (A) against equity instruments of an Indian company (B) between a resident and a non-resident	<i>Not expressly permitted under the NDI Rules</i>	<i>Permitted</i>
Swap of equity instruments of an Indian company held by a resident entity against equity capital of a non-resident entity in compliance with the OI Rules	<i>Not expressly permitted under the NDI Rules</i>	<i>Permitted</i>
Swap of equity instruments of an Indian company held by a resident individual against swap of equity capital of a non-resident entity on account of merger, demerger,	<i>Not expressly permitted under the NDI Rules</i>	<i>Permitted</i>

TRANSACTION	PREVIOUS POSITION	REVISED POSITION
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amalgamation and liquidation in compliance with the OI Rules

While evaluating such transactions, it will be relevant to note the distinction of the terms "equity capital" and "equity instruments" under the OI Rules and the NDI Rules, respectively.

### INVESTMENT MADE BY A COMPANY, A TRUST AND A PARTNERSHIP FIRM INCORPORATED OUTSIDE INDIA OWNED AND CONTROLLED BY AN NRI/ OCI

Prior to Amendment, investment made by an Indian entity which is owned and controlled by NRI(s), on a non-repatriation basis was not considered for calculation of indirect foreign investment while evaluating downstream investments. The Amendment has clarified that that any investment made by a company, a trust and a partnership firm incorporated outside India and owned and controlled by an NRI or an OCI on a non-repatriation basis will not be considered for the calculation of indirect foreign investment while evaluating downstream investment. This has provided more clarity on the treatment of NRIs at par with OCIs while evaluating downstream investments.

### FOREIGN PORTFOLIO INVESTMENTS LIBERALISED

Prior to the Amendment, government approval for an aggregate foreign portfolio investment (FPI) up to 49% of the paid-up capital or the sectoral or statutory cap for the sector, whichever is lower, was not required. However, now the requirement of the government approval is pegged to the sectoral or statutory cap and is not limited to 49%, provided that such investment does not result in transfer of ownership and/ or control of the resident Indian company from resident Indian citizens to non-residents. Therefore, the Amendment has liberalised FPI investment laws.

The definition of the term “investor group” has been expanded by the Amendment. In case two or more FPI’s (including foreign governments) or their related entities are having common ownership (directly or indirectly) of more than 50%, or common control, all such FPI’s shall be treated as forming part of the same investor group.

### WHITE LABEL ATM OPERATIONS

Post the Amendment, 100% FDI under automatic route is now permitted for white label ATM operations *inter alia* subject to specific criteria and guidelines issued by the Reserve Bank of India under the Payment and Settlement Systems Act, 2007.

### COMMENT

The Amendment brings forth several changes that are instrumental in facilitating cross-border share swaps, providing clarity on downstream investments, standardizing the

term 'control', and enabling FDI in White Label ATMs. These clarifications/liberalisations are anticipated to streamline the investment process for both Indian and overseas companies.

These amendments highlight the government's commitment to creating an investor-friendly environment and aligning with its broader objective of promoting the Ease of Doing Business in India. By simplifying the rules and regulations, the government is paving the way for increased foreign investment, which can drive economic growth, create jobs, and enhance India's global competitiveness.

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