

## **Additional compliances in line with Press Note 3 of 2020**

The Government of India (“GoI”), with an intent to curb opportunistic takeovers/acquisitions of Indian companies due to COVID-19 pandemic, through Press Note 3 of 2020 dated April 17, 2020 (“**PN 3 of 2020**”) had made it mandatory to obtain prior approval of GoI for any foreign direct investment (“**FDI**”) by an entity of a country, which shares land border with India or where the beneficial owner of an investment into India is situated in or is a citizen of any such country (“**Neighbouring Countries**”).

PN 3 of 2020 applies to FDI in all sectors/ services, including those sectors which otherwise fall under automatic route. To give effect to PN 3 of 2020, amendments were made to the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 (“**NDI Rules**”), effective from April 22, 2020. Therefore, the provisions of PN 3 of 2020 are in force from April 22, 2020.

In order to ensure compliance and regulate FDI in Indian companies in line with PN 3 of 2020 read with the NDI Rules, the Ministry of Corporate Affairs has recently introduced amendments to rules prescribed under the Companies Act, 2013 (“**Act**”). A summary of these amendments is given below.

1. **Declaration by subscribers and directors at the time of incorporation** – The subscribers and first directors of a company have to make certain declarations at the time of incorporating a company. The Companies (Incorporation) Second Amendment Rules, 2022, dated May 20, 2022, has revised the form for declaration by subscribers and first directors of a company in Form INC-9. With effect from June 1, 2022, a specific declaration is required to be given by first subscribers to the memorandum of association as well as first directors named in the articles of association on whether or not, they are required to obtain the prior approval of the GoI under the NDI Rules. If any such approval is required, then that needs to be obtained prior to subscription of shares. A copy of such approval has to be enclosed with Form INC-9.
2. **Restriction on private placement of securities** – The Companies (Prospectus and Allotment of Securities) Amendment Rules, 2022 dated May 4, 2022, has introduced a condition that an Indian company cannot make an offer or invitation of any securities to a body corporate incorporated in, or a citizen of any of the Neighbouring Countries, unless such body corporate or the citizen has obtained an approval from the GoI under the NDI Rules. The private placement offer letter in Form PAS-4 has also been amended to include a declaration to this effect. Consequently, for a private placement of securities of an Indian company, approval from GoI obtained pursuant to the said provisions of the NDI Rules must be attached with the private placement offer letter.
3. **Declaration on transfer of securities** - The Companies (Share Capital and Debentures) Amendment Rules, 2022 dated May 4, 2022, now require a transferee of securities to make an express declaration in the securities transfer form in Form SH-4 if such transferee is required to obtain the approval of the GoI under the NDI Rules. In case the transferee requires such approval, then that transferee has to first obtain such approval before filing Form SH-4 with the company. A copy of such approval has to be enclosed with Form SH-4. By introducing this declaration, the onus of ensuring compliance with PN 3 of 2020 is on the transferee.

4. **Declaration on compromise / arrangement** – The Companies (Compromises, Arrangements and Amalgamations) Amendment Rules, 2022 dated May 30, 2022, provide that in a compromise / arrangement / merger / demerger between an Indian company and a company or body corporate incorporated in any of the Neighbouring Countries, a declaration must be filed at the time of making an application with the National Companies Law Tribunal (“NCLT”) in Form CAA-16 declaring whether or not the company/body corporate is required to obtain the GoI approval under the NDI Rules. In case an approval is needed under the NDI Rules, such approval has to be obtained prior to the application made to NCLT. A copy of such approval has to be enclosed with Form CAA-16.
5. **Restriction on directorship** – The Companies (Appointment and Qualification of Directors) Amendment Rules, 2022 dated June 1, 2022, has introduced a condition that any person who is a national of any of the Neighbouring Countries and who seeks appointment as a director on the board of directors of an Indian company, must obtain a security clearance from the Ministry of Home Affairs as well as the GoI. Form DIR-2, which is a form for the consent of a person to act as a director, and Director Identification Number application for Form DIR-3 has been revised to include a declaration to this effect. This is a new requirement which applies over and above the requirements of the NDI Rules and PN 3 of 2020.

With these amendments, additional measures have been put in place to regulate FDI into Indian companies from entities incorporated in any of the Neighbouring Countries or where the beneficial owner of investment in Indian company is situated in or is a citizen of any such Neighbouring Countries.

On the face of it, the amendments are merely ring fencing the requirements of PN 3 of 2020 by bringing in additional checks and balances under the Act. However, on a strict reading, the scope of the amendments to the Act for fresh issue of securities is arguably narrower than the NDI Rules. In the context of PN 3 of 2020, a certain industrywide tolerance threshold has been widely accepted in determining whether nominal beneficial holding of entities or citizens from Neighbouring Countries will fall foul of the requirements of PN 3 of 2020. A similar practice is likely to develop around the amendments to the Act where the narrower drafting of the amendments could come into play.

The onus of ensuring compliance is not only on the Indian company receiving FDI, but also on subscribers/directors/transferees of securities. The GoI grants its approval pursuant to PN 3 of 2020 read with the NDI Rules on a case-to-case-basis after reviewing and examining each application. These additional compliances and restrictions are aimed to ensure strict adherence to the provisions of PN 3 of 2020 read with the NDI Rules for FDI in India companies from the Neighbouring Countries.

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