



news flash

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Ministry of Finance amends the Foreign Exchange Management (Non-debt Instruments) Rules, 2019

Introduction

The Ministry of Finance, Government of India amended certain provisions of the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 (“**Non-debt Instruments Rules**”) vide a notification bearing number S.O. 1374(E) on 27 April 2020 (“**Amendment Rules**”), effective from 27 April 2020.

Key amendments and Analysis

1. Acquisition of equity instruments by a person resident outside India, pursuant to rights acquired by such person from a person resident in India having renounced their rights is now required to be subject as per the pricing guidelines set out in the Non-debt Instruments Rules. This now means that although equity instruments are being acquired under a rights issue, the non-resident investor may have to pay a different price for equity instruments acquired from such renounced rights as compared to (a) what other shareholders have paid under the rights issue and (b) the price paid by such investor itself, if it was then an existing shareholder of the company, for other equity instruments subscribed by it pursuant to the rights issue. This appears to be in dissonance with the provisions of the Companies Act, 2013 which only contemplates the offer and receipt of one price for all securities issued at under a rights issue. This has at least two different potential consequences. The Companies Act, 2013 does not contemplate issue of securities under a rights issue at different prices, and this may therefore be seen as a contravention of the said Act. If one takes the view that since issue of shares under rights issue at different prices is not prohibited where the subscriber pays higher than the offer price, the company would not be in violation of the Companies Act, 2013, the other issue that the company may still face is enquiries from income tax authorities and potential tax liabilities.
2. With respect to sourcing norms for single brand trading, it has been clarified that commencement of the business shall mean opening of the first store or start of online retail, whichever is earlier. This amendment was introduced by press note 4 of 2019 dated 18 September 2019 but was not included in the original Non-debt Instrument Rules. It has, fortunately, now been brought into the Non-debt Instrument Rules through these Amendment Rules.
3. A minor addition has been made to the paragraph in the Non-debt Instrument Rules dealing with ceiling breaches by Foreign Portfolio Investors (“**FPI**”) and the requirement for divestment or consequent reclassification as Foreign Direct Investment in case of failure to divest. The Amendment Rules now state that such divestment or reclassification will be subject to conditions specified by Securities and Exchange Board of India and the Reserve Bank in this regard.

4. Pursuant to the change proposed by press note 1 of 2020 dated 21 February 2020 for allowing Foreign Direct Investment (“**FDI**”) in insurance intermediaries up to 100% under automatic route, the same has been brought into effect by the Amendment Rules. Accordingly, while FDI in Insurance Company continues to be capped at 49% under the automatic route, FDI in Intermediaries or Insurance Intermediaries including insurance brokers, re-insurance brokers, insurance consultants, corporate agents, third party administrator, Surveyors and Loss Assessors and such other entities, as may be notified by the Insurance Regulatory and Development Authority of India from time to time has been increased to upto 100% under the automatic route by the Amendment Rules. While earlier FDI in insurance companies as well as the other aforementioned entities were common, the Amendment Rules now specify as follows:

- FDI in insurance companies is now subject to approval or verification of the Insurance Regulatory and Development Authority of India (“**Authority**”).
- FPI investment will be governed by specified rules and regulations of Securities and Exchange Board of India (Foreign Portfolio Investors) Regulations, 2014 and Indian Insurance Companies (Foreign Investment) Rules, 2015, as the case may be.
- All entities other than insurance companies are required to comply with conditions that are stated to be specific to insurance companies other than the condition of their ownership and control being at all times in the hands of Indian resident entities.
- FDI proposals are to be allowed under the automatic route subject to verification by the Authority and the foreign investment in intermediaries or insurance intermediaries shall be governed by the same terms as provided under rules 7 and 8 of the Indian Insurance Companies (Foreign Investment) Rules, 2015, as amended from time to time;
- Insurance intermediaries that have majority shareholding of foreign investors are required to comply with several additional conditions, most critical of which are (a) at least one from among the Chairman of the Board of Directors or the Chief Executive Officer or Principal Officer or Managing Director of the insurance intermediary shall be a resident Indian citizen, (b) the entity would need to take prior permission of the Authority for repatriating dividend, (c) the entity is required to bring in the latest technological, managerial and other skills (however, what this entails has not been clarified), (d) the entity is not entitled to make payments to the foreign group or promoter or subsidiary or interconnected or associate entities beyond what is necessary or permitted by the Authority and is required to make disclosures to the Authority in respect of all such payments.

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