KHAITAN & CO
Advocates since 1911

UPDATE

ERGO

Analysing developments impacting business

NDI RULES AMENDED TO ALLOW 74% FOREIGN INVESTMENT IN INDIAN INSURANCE COMPANIES | LIBERALISATION PROCESS NOW COMPLETE

23 August 2021

The Foreign Exchange Management (Non-Debt Instruments) Rules 2019 (NDI Rules) have been amended to permit foreign investment up to 74% for insurance companies in India. The amendment takes effect from 19 August 2021 and marks the completion of the liberalisation process for increasing the foreign investment limit for the sector from 49% to 74%.

The journey so far

A quick snapshot of the liberalisation process so far is appropriate:

- The budget announcement in ***February*** this year, which initiated the liberalisation process, had indicated that foreign ownership and control of Indian insurance companies would be permitted but with "*safeguards*". See our Ergo of 4 February, for further details regarding the announcement.

- The next key milestone was the amendment of the Indian Insurance Companies (Foreign Investment) Rules, 2015 (Foreign Investment Rules) in ***May***. This amendment introduced: (a) new requirements for having "resident" directors and KMPs and additional independent directors; and (b) additional "solvency control" requirements, where foreign investment exceeded 49%. February's budget announcement had already indicated that these requirements should be expected. See our Ergo of 24 May, for further details regarding the amendment and the new requirements.

- In ***June***, Press note 2 of 2021 was issued, containing the Indian exchange control framework for 74% foreign investment in Indian insurance companies. Thereafter, in ***July***, the guidelines on Indian ownership and control dated 19 October 2015 (IOC Guidelines) were withdrawn. The IOC Guidelines contained a number of governance constraints for foreign investors, so their withdrawal was a critical part of the liberalisation process. For further details regarding the withdrawal of the IOC Guidelines, please see our Ergo of 3 August.

- Finally, in ***August***, the NDI Rules were amended (see changes below) bringing about effective change in law permitting 74% foreign investment in Indian insurance companies.

Changes to the NDI Rules

The amendment to the NDI Rules makes the following key changes:

- **Increase in sectoral cap from 49% to 74%**. The sectoral cap for Indian insurance companies now stands revised from 49% to 74%. All other references to sectoral cap under the NDI Rules have been accordingly updated as well.

- **General foreign investment-linked condition**. All Indian insurance companies with foreign investment need to ensure compliance with the Foreign Investment Rules and other applicable rules and regulations of the Insurance Regulatory and Development Authority of India (IRDAI). This will include the new resident directors/KMPs, additional independent directors and solvency requirements. The amendment also removes all references to "Indian ownership/control" and similar phrases from the NDI Rules.

Comment

With the liberalisation process now fully complete, foreign investors can finally hold controlling stakes in Indian insurance companies, without onerous governance constraints. Existing foreign investors can also now exercise their change-of-law call options and consolidate up to 74%. From an exchange control perspective, no prior governmental approvals are required, although the IRDAI's approval will be required for both primary and secondary deals and investors may also require competition clearance/ notification.

We expect this landmark development to precipitate significant M&A activity in the Indian insurance sector. Higher levels of capital, increased economies of scale and improvements, and increased sophistication in underwriting and other processes would also help drive further growth and increase insurance penetration and density in the Indian market.

\- *Khaitan & Co | Insurance Practice*

For any queries please contact: editors@khaitanco.com