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Foreign Exchange Management (Non-Debt Instruments) (Amendment) Rules, 2026

Key Amendments to the FDI Framework for Investments from Land-Bordering Countries

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Introduction

On 17 April 2020, the Department for Promotion of Industry and Internal Trade (DPIIT), Ministry of Commerce and Industry, Government of India, announced a significant change to India's foreign direct investment policy (FDI Policy) through Press Note No. 3 (2020 Series) (Press Note 3). Pursuant to Press Note 3, any investment by an entity incorporated in a country sharing a land border with India, or where the beneficial owner of the investment into India is situated in or is a citizen of such a country, requires prior approval of the Government of India.

This change was introduced in the backdrop of the economic disruption caused by the COVID-19 pandemic, with the stated objective of curbing opportunistic takeovers and acquisitions of stressed Indian companies. At the same time, the measure was widely viewed as a response to growing geopolitical concerns, particularly in relation to investments originating from China, given the rising tensions along the Indo-China border.

Ambiguities and Practical Challenges Under Press Note 3

Under Press Note 3, any direct or indirect investment into India from an entity incorporated in a country sharing a land border with India, or where the beneficial owner of such investment is situated in, or is a citizen of, such a country (including China, Hong Kong, Macau and other neighboring jurisdictions), requires prior approval of the Government of India. However, neither Press Note 3 nor the subsequent amendments to the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 (NDI Rules) had clarified the threshold for determining "beneficial ownership".

This lack of clarity was particularly notable given that other Indian legislations, such as the Companies Act, 2013 and the Prevention of Money Laundering (Maintenance of Records) Rules, 2005, prescribe a 10% threshold for identifying beneficial ownership. In the absence of an express threshold under the FDI framework, considerable uncertainty emerged regarding both the ambit of the beneficial ownership test and the level within the ownership chain at which such ownership was required to be assessed.

In practice, investors often operate through multi-layered global structures spanning several jurisdictions. The absence of clear guidance on whether beneficial ownership needed to be traced up to the ultimate beneficial owner, coupled with the lack of a prescribed threshold, created significant interpretational challenges. As a result, even minority or non-controlling shareholdings held by investors from land-bordering countries, or minimal exposure to such investors within global funds, were frequently viewed as potentially triggering the requirement for prior government approval.

Consequently, a conservative interpretation of Press Note 3 emerged in practice, whereby any investment involving direct or indirect beneficial ownership from China, Hong Kong, Macau or other land-bordering jurisdictions irrespective of the size of such ownership could potentially require prior approval of the Government of India. This interpretation led to significant deal uncertainty and delays, particularly in the context of venture capital and private equity investments involving globally diversified investor bases.

In addition, the approval process itself often proved time-consuming. In several cases, obtaining approval under the Press Note 3 framework took anywhere between six to eight months, and sometimes longer. This significantly affected deal timelines and execution certainty, particularly for time-sensitive venture capital and private equity transactions.

Clarification by Way of Press Note 2 (2026 Series)

Press Note 2 (2026 Series) (Press Note 2) introduced important clarifications and changes to paragraph 3.1.1 of the FDI Policy, which governs investments involving countries sharing a land border with India. While the core objective of Press Note 3 (2020 Series) continues to remain the same, that is to require prior Government approval for investments from land bordering jurisdictions or investments where the beneficial owner is linked to such jurisdictions, the latest amendments seek to provide greater clarity on the scope of the restriction and the framework for determining beneficial ownership.

A key development introduced by the amendment is the express clarification on how "beneficial ownership" is to be determined in the context of investments routed through intermediary jurisdictions. The Press Note 2 clarifies that where the investor entity is incorporated or registered in a country other than a land-bordering country, the beneficial ownership test will be applied at the level of such investor entity. Importantly, the concept of "beneficial owner" has now been aligned with the framework under the Prevention of Money Laundering Act, 2002 and the Prevention of Money Laundering (Maintenance of Records) Rules, 2005 (PML Rules), and will be determined in accordance with the criteria prescribed under Rule 9(3) of the PML Rules.

At the same time, the amendment continues to preserve the broader regulatory objective of preventing **indirect control** from restricted jurisdictions. The Press Note 2 clarified that beneficial ownership will be considered to be from a country sharing a land border with India where citizens or entities of such country have the ability, directly or indirectly and individually or collectively, to hold rights or entitlements exceeding the applicable thresholds under the PML Rules in the investor entity, or where such rights enable them to **exercise control over the investor entity or ultimate effective control over the Indian investee entity**.

Another notable addition under the amended framework is the introduction of a reporting requirement for certain investments that may not otherwise require prior Government approval. Specifically, where an investor entity making an investment into India has any direct or indirect ownership by a citizen or entity of a country sharing a land border with India, but such investment does not trigger the Government approval requirement, the investment will nonetheless be subject to a reporting obligation in the form and manner to be prescribed under the Standard Operating Procedure to be issued by DPIIT. This requirement is in addition to compliance with applicable sectoral caps, entry routes and other conditions under the FDI Policy.

It is to be noted that the aforementioned requirement is not limited to fresh investments. It also applies to transfers of existing or future foreign investment in an Indian entity, whether direct or indirect, if such transfer results in the beneficial ownership falling within the restricted category.

Notification | Foreign Exchange Management (Non-Debt Instruments) (Amendment) Rules, 2026

The aforementioned amendments introduced in Press Note 2 have now been notified by way of the Foreign Exchange Management (Non-debt Instruments) (Amendment) Rules, 2026 (the Amendment Rules) on 1 May 2026. Saliently, the Amendment Rules have retained the core substantive elements introduced under Press Note 2 in relation to the determination of beneficial ownership, including the alignment of the "beneficial owner" threshold with the regime under the Prevention of Money Laundering Act, 2002 and the PML Rules, in addition to preserving the regulatory objective of preventing indirect control from restricted jurisdictions.

However, a notable deviation in the Amendment Rules from Press Note 2 relates to the reporting framework for land-border investments that do not require prior Government approval. Under the Amendment Rules, such reporting is now required to be undertaken in the form and manner specified by the Reserve Bank of India, replacing the earlier position under Press Note 2, which prescribed reporting requirements to be undertaken as per the Standard Operating Procedure to be issued by the DPIIT.

Further, the Amendment Rules also clarify that Multilateral Banks or Funds, of which India is a member, shall not be treated as being an entity of a particular country nor shall any country be treated as the beneficial owner of the investments of such Bank or Fund in India. Additionally, aside from the amendments to the land-border investment framework, the Amendment Rules also clarify that an issue or transfer of "participating interest or rights" in oil fields by Indian companies to non-residents constitutes foreign investment, and would therefore be required to comply with the conditions specified in Schedule I of the NDI Rules.

Policy Implications of the Amendments

These Amendment Rules signal a calibrated shift in the framework governing investments from land-bordering countries. While the policy of subjecting such investments to regulatory scrutiny continues to remain in place, the Amendment Rules reflect the Government's continued focus on improving the ease of doing business in India by providing greater regulatory clarity and reducing uncertainty for cross-border investors.

The alignment of the definition of beneficial ownership with the framework under the Prevention of Money Laundering Act, 2002 and the PML Rules, is likely to provide greater clarity for global investment structures. Venture capital and private equity funds often have diversified general partner and limited partner bases across multiple jurisdictions, including passive investors from land-bordering countries. Under the earlier interpretation of Press Note 3, even minimal exposure to such investors could potentially trigger the requirement for prior government approval. By aligning the beneficial ownership test with the thresholds and criteria prescribed under the PML framework, the revised approach introduces a more objective standard for assessing such investments and is likely to reduce uncertainty for global funds deploying capital into India.

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