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EY Regulatory Alert

Government relaxed norms for FDI from land bordering countries

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Executive summary

The Government of India, by Notification (bearing reference no. S.O. 2174(E)) dated 01 May 2026, has amended the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 ('NDI Rules') to revise the Foreign Direct Investment ('FDI') Policy governing investments originating from countries sharing land borders with India, by introducing the framework for determination of Beneficial Ownership ('BO') and providing a fast track approval process in certain key sectors with Indian majority shareholding.

This Alert summarizes the implications of the amendment.

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Background

- With a view to avoiding opportunistic acquisitions and takeovers during the COVID-19 pandemic, the Department for Promotion of Industry and Internal Trade ('DPIIT'), Ministry of Commerce & Industry, Government of India, issued Press Note 3 (2020) dated 17 April 2020 ('PN-3'). PN-3 mandated prior Government approval for FDI by an entity or a citizen of a Land Bordering Country ('LBC'), or where the BO of such investment was situated in such countries.
- Pursuant to representations from the stakeholders and experience gained while processing the proposals, the Government issued Press Note 02 of 2026 on 15 March 2026 ('PN-2') which introduced the framework for determination of BO and distinguishing between controlling and non-controlling interests and keeping certain sectors under fast-track approvals.
- The same has been notified in the NDI Rules with effect from 01 May 2026.
- On 04 May 2026, DPIIT also issued the revised Standard Operating Procedure ('SOP') for processing FDI proposals.

Key takeaways

Direct investment from LBC

- Direct investment from LBC shall continue to trigger prior Government approval irrespective of the percentage of investment.

Criteria for determination of BO

- In the case of investments originating from countries other than LBCs, the approval requirement will trigger based on the BO.
- The BO of such investment shall be deemed to be vested in an LBC if any one of the prescribed conditions is satisfied:
  - Threshold ownership:

    A citizen or entity of an LBC holds, directly or indirectly, rights or entitlements in excess of the applicable thresholds prescribed under the Prevention of Money Laundering Act, 2002 read with Prevention of Money Laundering (Maintenance of Records) Rules, 2005 ('PMLA framework').

    The PMLA framework broadly prescribes 10% threshold (15% in case of unincorporated associations and body of individuals) for determining BO. However, in case of listed entities in India or notified jurisdictions and subsidiaries thereof, BO determination may not be warranted in terms of the PMLA framework.
  - **Control over the investor entity:**

    The ability to exercise control, directly or indirectly, over the foreign investor entity.
  - **Ultimate effective control over the investee entity in any manner:**

    The ability to exercise ultimate effective control over the investee entity in any manner.

Application for BO test

- The BO test is required to be applied at the investor entity level for the purpose of determining the applicability.

Expedited processing for investments in specified sectors

- The SOP provides that investment proposals, involving LBCs, in certain identified priority sectors shall be processed within a period of 60 days, subject to the continuing condition that majority shareholding and control of the investee entity remains, at all times, with resident Indian citizens and/or Indian entities owned and controlled by resident Indian citizens.
- The identified priority sectors include:
  - Capital goods manufacturing
  - Electronic capital goods manufacturing
  - Electronic components manufacturing
  - Polysilicon and Ingot-wafer manufacturing
  - Advanced Battery Components manufacturing
  - Rare Earth Permanent Magnets
  - Rare Earth Processing

Additional reporting requirement for all cases involving LBC

- In case of indirect investment from LBC, where the BO holds an interest less than the prescribed thresholds and does not exercise control over either the investor or investee entity, such investment shall be permitted as per sectoral conditions. However, an intimation is required to be filed with DPIIT as per the SOP, prior to consummation of the transaction, if the sector is under automatic route.
- Such reporting obligations are in addition to existing reporting requirements under the Foreign Exchange Management Act, 1999 ('FEMA') and applicable rules and regulations.

Comments

a. India's FDI regime is primarily sector-driven, with the applicable entry route and conditions varying based on the sensitivity of the sector in which the Indian company operates. In contrast, PN-3 introduced an investor-specific restriction, requiring prior government approval for investments from LBC. In response to challenges faced by financial investors, and with a view to supporting investment in identified priority sectors, the government has now recalibrated certain aspects of the policy framework.

b. The revised framework represents a measured refinement of the earlier regime, bringing greater clarity to the determination of BO. By aligning BO assessment with PMLA framework, the policy draws upon an established statutory regime familiar to market participants, while the distinction between controlling and non-controlling interests addresses practical considerations in passive and diversified investment structures, without diluting regulatory oversight for LBC linked investments.

c. The introduction of a 60-day processing timeline for proposals in certain priority sectors reflects an intent to enable more time-bound consideration of investments aligned with industrial policy priorities. At the same time, the framework continues to follow a risk-sensitive approach by retaining approval requirements for controlling investments and prescribing DPIIT-level reporting even for non-controlling holdings, thereby balancing facilitation with oversight and security considerations.

d. Overall, the revised framework seeks to provide greater structure and predictability to ownership and control assessments for FDI from LBC.

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