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Mergers & Acquisitions

**An Indian Legal, Regulatory and
Tax Perspective**

June 2025

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List of Abbreviations

Abbreviation	Description
2019 Amendment Regulations	Amendment to Competition Commission of India (Procedure in regard to the Transaction of Business relating to Combinations) Regulations, 2019
2021 Act	Taxation Laws (Amendment) Act, 2021
2024 Combination Regulations	Competition Commission of India (Combination) Regulations, 2024
AAEC	Appreciable Adverse Effect on Competition
AD Bank	Authorized Dealer Bank
ADR	American Depository Receipt
AI	Artificial Intelligence
AIFs	Alternative Investment Funds
Amendments to Non-Debt Instruments Rules	Amendment Rules 2024 and Fourth Amendment Rules (as amended on January 24, 2024 and August 16, 2024 respectively)
Block	Block of assets
CA, 2013	Companies Act, 2013
Cairn Arbitration	Cairn Energy Plc and CUHL v. the Republic of India
Cat-I AIF	Category I AIF
CBDT	Central Board of Direct Taxes
CCI	Competition Commission of India
CCS	Compulsory Convertible Securities
Combination Regulations	CCI (Procedure in regard to the Transaction of Business relating to Combinations) Regulations, 2011
Competition Act	Competition Act, 2002
CSI	Commercially Sensitive Information
DIPP	Department of Industrial Policy and Promotion
DPIIT	Department for Promotion of Industry and Internal Trade
DRHP	Draft Red Herring Prospectus
DR Scheme	Depository Receipts Scheme, 2014
DVT	Deal Value Threshold
ECB	External Commercial Borrowings
EEFC	Exchange Earner's Foreign Currency
ESOP	Employees Stock Option
Exemption Rules	CCI (Criteria for Exemption of Combinations) Rules, 2024
FDI	Foreign Direct Investment
FDI Scheme	Foreign Direct Investment Scheme
FEMA Act, 1999/ FEMA	Foreign Exchange Management Act, 1999
FIPB	Foreign Investment Promotion Board
FMV	Fair Market Value
FPI	Foreign Portfolio Investments

List of Abbreviations

FVCI	Foreign Venture Capital Investors
FY 21	Financial Year of 2021
GDR	Global Depository Receipt
Green Channel Rules/ Green Channel Rules, 2024	CCI (Criteria for Combination) Rules, 2024
GST	Goods and Services Tax
ICDR Regulations	Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018
IDRs	Indian Depository Receipts
IFSC	International Financial Services Centre
Indirect Transfer	Explanation 5 to clause (i) of sub-section (1) of section 9 of Income-tax Act, 1961
Indirect Transfer Test	Explanation 6 to section 9(1)(i) of the Income Tax Act, 1961
INR	Indian Rupees
InvITs	Infrastructure Investment Funds
IRDAI	Insurance and Regulatory Development Authority of India
ITA	Income Tax Act, 1961
Listing Regulations	Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements), 2015
LLP	Limited Liability Partnership
LRS	Liberalised Remittance Scheme
LTCG	Long Term Capital Gains
M&A	Mergers and Acquisitions
MCA	Ministry of Corporate Affairs
Merger Provisions	Sections 230-234 of CA 2013
Merger Regulations	Foreign Exchange Management (Cross Border Merger) Regulations, 2018
MPC	Minimum Promoter Contribution
MVAT	Minimum Value of Assets and Turnover
MVAT Rules	Competition (Minimum Value of Assets and Turnover) Rules, 2024
NCLT	National Company Law Tribunal
NRI	Non-Resident Indian
Non-Debt Instruments Rules	Foreign Exchange Management (Non-Debt Instruments) Rules, 2019
OCB	Ordinary Course of Business
OCI	Overseas Citizen of India
ODI	Overseas Direct Investment
OI Directions	Foreign Exchange Management (Overseas Investment) Directions, 2022
OI Laws	Foreign Exchange Management (Overseas Investment) Directions, 2022, Foreign Exchange Management (Overseas Investment) Regulations, 2022 and Foreign Exchange Management (Overseas Investment) Rules, 2022
OI Regulations	Foreign Exchange Management (Overseas Investment) Regulations, 2022
OI Rules	Foreign Exchange Management (Overseas Investment) Rules, 2022
OPI	Overseas Portfolio Investment

List of Abbreviations

PAC	Persons acting in concert
PIT Regulations	Securities and Exchange Board of India (Prohibition of Insider Trading) Regulations, 2015
PPT	Principal Purpose Test
Preferential Issue Regulations	Provisions of Chapter V, ICDR Regulations
RBI	Reserve Bank of India
REITs	Real Estate Investment Trusts
SAT	Securities Appellate Tribunal
SC	Supreme Court
SCRR	Securities Contracts (Regulations) Rules, 1957
SEBI	Securities and Exchange Board of India
SEBI Act, 1992	Securities and Exchange Board of India Act, 1992
SEBI Delisting Regulations	SEBI (Delisting of Equity Shares) Regulations, 2021
STCG	Short Term Capital Gain
STT	Securities Transaction Tax
SWFs	Sovereign Wealth Funds
Takeover Code	SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011
UPSI	Unpublished price sensitive information
USD	United States Dollar
Vodafone Arbitration	Vodafone International Holdings v. The Republic of India
VCF	Venture Capital Funds
WDV	Written Down Value

Introduction

I. Overview of the M&A Market

In 2025, the M&A market in India is expected to maintain its upward trajectory, driven by strong investor confidence and a favorable economic outlook. While the momentum in deal activity in traditional sectors is expected to continue (such as healthcare, financial services and consumer goods), it is likely that M&A activity in sectors such as industry and manufacturing (driven by the automotive sector and e-mobility), renewable energy (driven by the government initiatives to propel green energy) and technology (driven by rapid innovation in AI and digital transformations) may dominate this year.

II. Conceptual Overview

In this section, we have briefly explained the different types of M&As that may be undertaken and an overview of certain laws that would be of significance to M&A in India.

A. Mergers and Amalgamations

The term ‘merger’ is not defined under the Companies Act, 2013 (“CA 2013”) or under the Income Tax Act, 1961 (“ITA”). As a concept, a ‘merger’ is a combination of two or more entities into one; the desired effect being not just the accumulation of assets and liabilities of the distinct entities, but the organization of such entities into one business. The possible objectives of mergers are manifold - economies of scale, acquisition of technologies, access to varied sectors/ markets etc. Generally, in a merger, the merging entities would cease to exist and would merge into a single surviving entity.

The ITA does, however, define the analogous term ‘amalgamation’¹ as the merger of one or more companies with another company, or the merger of two or more companies to form one company. The ITA goes on to specify certain other conditions that must be satisfied for an ‘amalgamation’ to be eligible for benefits accruing from beneficial tax treatment (discussed in Part VI of this Paper).

Sections 230-234 of CA 2013 (the “Merger Provisions”) deal with the schemes of arrangement or compromise between a company, its shareholders and/or its creditors. These provisions are discussed in greater detail in Part II of this Paper. Commercially, mergers and amalgamations may be of several types, depending on the requirements of the merging entities. Although corporate laws may be indifferent to the different commercial forms of merger/amalgamation, the Competition Act, 2002 does pay special attention to the forms.

¹ Section 2 (1B), Income Tax Act, 1961.

i. Horizontal Mergers

Also referred to as a 'horizontal integration', this kind of merger takes place between entities engaged in competing businesses which are at the same stage of the industrial process. A horizontal merger takes a company a step closer towards a monopoly by eliminating a competitor and establishing a stronger presence in the market. The other benefits of this form of merger are the advantages of economies of scale and economies of scope. These forms of merger are heavily scrutinized by the Competition Commission of India ("CCI").

ii. Vertical Mergers

Vertical mergers refer to the combination of two entities at different stages of the industrial or production process. For example, the merger of a company engaged in construction business with a company engaged in production of brick or steel would lead to vertical integration. Companies stand to gain on account of lower transaction costs and synchronization of demand and supply. Moreover, vertical integration helps a company move towards greater independence and self-sufficiency.

iii. Congeneric Mergers

A congeneric merger is a type of merger where two companies are in the same or related industries or markets but do not offer the same products. In a congeneric merger, the companies may share similar distribution channels, providing synergies for the merger. The acquiring company and the target company may have overlapping technology or production systems, making for easy integration of the two entities. This type of merger is often resorted to by entities who intend to increase their market shares or expand their product lines.

iv. Conglomerate Mergers

A conglomerate merger is a merger between two entities in unrelated industries. The principal reason for a conglomerate merger is utilization of financial resources, enlargement of debt capacity, and increase in the value of outstanding shares by increased leverage and earnings per share, and by lowering the average cost of capital. A merger with an unrelated business also helps the company to foray into diverse businesses without having to incur large start-up costs normally associated with a new business.

v. Cash Merger

In a 'cash merger', also known as a 'cash-out merger', the shareholders of one entity receives cash instead of shares in the merged entity. This is effectively an exit for the cashed-out shareholders.

vi. Triangular Merger

A triangular merger is often resorted to, for regulatory and tax reasons. As the name suggests, it is a tripartite arrangement in which the target merges with a subsidiary of the acquirer. Based on which entity is the survivor after such merger, a triangular merger may be forward (when the target merges into the subsidiary and the subsidiary survives), or reverse (when the subsidiary merges into the target and the target survives).

B. Takeovers and Acquisitions

A 'takeover' is the purchase by one person, of controlling interest in the share capital or of all or substantially all of the assets and/or liabilities, of the target. A takeover may be friendly or hostile and may be structured either by way of agreement between the offeror and the majority shareholders or purchase of shares from the open market or by making an offer for acquisition of the target's shares to the entire body of shareholders.

An 'acquisition' is the purchase of shares of the target or acquisition of assets and liabilities of the target. In the latter case, entire business of the target may be acquired on a going concern basis or certain assets and liabilities may be cherry picked and purchased by the acquirer. The transfer when a business is acquired on a going concern basis is referred to as a 'slump sale'² under the ITA. Section 2(42C) of the ITA defines slump sale as a "transfer of one or more undertakings as a result of the sale for a lump sum consideration without values being assigned to the individual assets and liabilities in such transfers". The legal and tax considerations of slump sale vis-a-vis an asset sale is discussed in greater detail in Part VI of this Paper.

Another form of acquisition may be by way of a demerger. A demerger is the opposite of a merger, involving the splitting up of one entity into two or more entities. An entity which has more than one business, may decide to 'hive off' or 'spin off' one of its businesses into a new entity. The shareholders of the original entity would generally receive shares of the new entity.

In some cases, if one of the business units of a company is financially sick and the other business unit(s) is financially sound, the sick business units may be demerged from the company, thereby facilitating the restructuring or sale of the sick business, without affecting the assets of the healthy business unit(s). Conversely, a demerger may also be undertaken for moving a lucrative business into a separate entity. A demerger may be completed through a court process under the Merger Provisions or contractually by way of a business transfer agreement.

C. Joint Ventures

A joint venture is the coming together of two or more businesses for a specific purpose, which may or may not be for a limited duration. The purpose of the joint venture may be an entry into a new business, or an entry into a new market (which requires specific skills, expertise or the investment by each of the joint venture parties). Parties can either set up a new company or use an existing entity, through which the proposed business will be conducted.

The parties typically enter into an agreement to set out the rights and obligations of each joint venture party and the broad framework for the management of the company, and such terms are then incorporated in the by-laws of the company for strengthening the enforceability.

² Section 2(42C), Income Tax Act, 1961.

Mergers and Amalgamations: Overview

I. Company Law

The Merger Provisions govern schemes of arrangements between a company, its shareholders and creditors. The Merger Provisions are in fact worded so broadly that they provide for and regulate all kinds of corporate restructuring that a company can possibly undertake, such as mergers, amalgamations, demergers, spin-off / hive off, and every other compromise, settlement, agreement or arrangement between a company and its members and/or its creditors.

A. Procedure Under the Merger Provisions

Since a merger essentially involves an arrangement between two or more companies, those companies which intend to merge must make an application to the National Company Law Tribunal (“NCLT”) having jurisdiction over such company for (i) convening meetings of its respective shareholders and/or creditors; (ii) or seeking dispensation of such meetings basis the consents received in writing from the shareholders and creditors. Basis the NCLT order, either a meeting is convened or dispensed with. If the majority in number, representing 3/4th in value of the creditors or shareholders present and voting at such meeting (if the meeting is held) agree to the merger, then the merger, if sanctioned by the NCLT, is binding on all creditors and shareholders of the company. The Merger Provisions constitute a comprehensive code in themselves, and under these provisions, the NCLT has full power to sanction any alterations in the corporate structure of a company.

B. Fast Track Merger

The Fast Track merger covered under Section 233 of CA 2013 requires approval from shareholders, creditors, the Registrar of Companies, the Official Liquidator and the Regional Director. Under the fast track merger, scheme of merger shall be entered into between the following companies:¹

- i. two or more small companies (private companies having paid-up capital of equal to or below INR 40 million (USD 461.3 thousand approx.)² or such a higher amount specified not exceeding more than INR 100 million (USD 1.2 million approx.), and turnover of equal to or below INR 400 million (USD 4.6 million approx.) or such a higher amount specified not exceeding more than INR 1 billion (USD 11.5 million approx.) (as per last audited financial statements³); or
- ii. a holding company with its wholly owned subsidiary; or
- iii. such other class of companies as may be prescribed.

The scheme, after incorporating any suggestions made by the Registrar of Companies and the Official Liquidator, must be approved by shareholders holding at least 90% of the total number of shares, and creditors

¹ Section 233, Companies Act, 2013.

² The exchange rate used for the purposes of conversion was 1 USD = 86.72 INR.

³ Section 2(85), Companies Act, 2013.

representing 9/10th in value, before it is presented to the Regional Director and the Official Liquidator for approval. Thereafter, if the Regional Director/ Official Liquidator has any objections, they should convey the same to the Central Government. The Central Government upon receipt of comments can either direct NCLT to take up the scheme under Section 232 (general process) or pass the final order confirming the scheme under the Fast Track process.

C. Cross Border Mergers

Section 234 of the CA 2013 permits mergers between Indian and foreign companies with prior approval of the Reserve Bank of India (“RBI”). A foreign company means any company or body corporate incorporated outside India, whether having a place of business in India or not.⁴ The following conditions must be fulfilled for a cross border merger:

- i. The foreign company should be incorporated in a permitted jurisdiction which meets certain conditions.
- ii. The transferee company is to ensure that the valuation is done by a recognized professional body in its jurisdiction and is in accordance with internationally accepted principles of accounting and valuation.
- iii. The procedure prescribed under CA 2013 for undertaking mergers must be followed.

The RBI also issued the Foreign Exchange Management (Cross Border Merger) Regulations, 2018 (“**Merger Regulations**”) on March 20, 2018 which provide that any transaction undertaken in relation to a cross-border merger in accordance with the Merger Regulations shall be deemed to have been approved by the RBI.⁵ These Merger Regulations distinguish between inbound mergers (foreign company merging into an Indian company) and outbound mergers (Indian company merging into a foreign company) and lay down specific compliance requirements for each.

In the case of inbound mergers, the resultant Indian company must comply with the applicable provisions under the FEMA Act, 1999 including issuance of shares to non-resident shareholders in accordance with the respective pricing guidelines and applicable sectoral caps.

For outbound mergers, the Indian company’s shareholders and creditors receiving consideration in the form of securities or other assets of the foreign transferee company must ensure that such remittances or holdings are in compliance with the Liberalised Remittance Scheme (“LRS”), the Foreign Exchange Management (Overseas Investment) Regulations, 2022, and other applicable FEMA provisions. Additionally, the resultant foreign entity must not be engaged in any sector prohibited for foreign investment under Indian laws.

Further, post-merger compliances such as reporting to the RBI, repatriation or disposal of Indian assets/liabilities not permitted to be held by the foreign entity, and timelines for such disposal (typically within two years from the date of sanction of the merger) must be duly adhered to. The approval process also involves close scrutiny by the NCLT and requires certification from professionals confirming compliance with the applicable accounting and regulatory standards.

⁴ Section 2(42), Companies Act, 2013.

⁵ Section 9, Foreign Exchange Management (Cross Border Merger) Regulations, 2018.

II. Securities Laws

A. Takeover Code

The Securities and Exchange Board of India (the “SEBI”) is the nodal authority regulating entities that are listed or to be listed on stock exchanges in India. The SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (the “Takeover Code”) restricts and regulates the acquisition of shares, voting rights and control in listed companies. Acquisition of shares or voting rights of a listed company, entitling the acquirer to exercise 25% or more of the voting rights in the target company or acquisition of control, obligates the acquirer to make an offer to the shareholders of the target company. The offer must be to further acquire at least 26% of the voting capital of the company.⁶ Further, if the acquirer already holds 25% or more but less than 75% of the target company and acquires more than 5% shares or voting rights in the target company within a financial year, it shall be obligated to make an open offer.⁷ However, this obligation is subject to the exemptions provided under the Takeover Code. Exemptions from open offer requirement under the Takeover Code include inter alia acquisition pursuant to a scheme of arrangement approved by the NCLT.⁸ Further, SEBI has the power to grant exemption or relaxation from the requirements of the open offer under the Takeover Code in the interest of investors and the securities market. Such relaxations or exemptions can be sought by the acquirer by making an application to SEBI.

B. Listing Regulations

The SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“Listing Regulations”) provides for a comprehensive framework governing various types of listed securities. Under the Listing Regulations, SEBI has laid down conditions to be followed by a listed company while making an application before the NCLT, for approval of a scheme of merger / amalgamation / reconstruction. Certain key provisions under the Listing Regulations applicable in case of a scheme involving a listed company are as follows:

- i. **Applicability of Listing Regulations:** Based on the market capitalization of listed entities/entities to be listed, recognized stock exchanges prepare a ranking of entities fulfilling the average market capitalization criteria before December 31 of the calendar year, calculated on a six-month basis in a calendar year. In the event that an entity falls below the threshold and remains below the threshold for three consecutive years, unless its ranking by the stock exchange is affected, the regulations shall continue to apply.⁹
- ii. **Filing of scheme with stock exchanges:** Any listed company undertaking or involved in a scheme of arrangement, must file the draft scheme with the relevant stock exchanges, prior to filing them with the NCLT (as per the process laid down under CA 2013), to seek a no-objection letter from the relevant stock exchanges.¹⁰ In order to file the scheme of arrangement with the relevant stock exchanges, all listed entities would be required to submit valuation report, auditor’s certificate, no-objection certificates from lending scheduled commercial banks/financial institutions.¹¹

6 Regulation 3 read with Regulation 7, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

7 Regulation 3(2), SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

8 Regulation 10, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

9 Regulation 3 of Listing Regulations; as amended by SEBI (Listing Obligations and Disclosure Requirements) (Amendment) Regulations, 2024.

10 Regulation 37(1), SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

11 SEBI Master Circular No. SEBI/HO/CFD/DIL1/CIR/P/2020/249 dated December 22, 2020; as amended by Circular No. SEBI/HO/CFD/DIL2/CIR/P/2021/0000000657 dated November 16, 2021, Circular No. SEBI/HO/CFD/DIL2/CIR/P/2021/0000000659 dated November 18, 2021; and Circular No. SEBI/HO/CFD/DIL2/CIR/P/2022/11 dated February 01, 2022.

Mergers and Amalgamations: Overview

- iii. **Compliance with securities law:** The listed companies shall ensure that the scheme does not violate, limit or override any of the provisions of the applicable securities law or requirements of the stock exchanges.¹²
- iv. **Change in shareholding pattern:** The listed companies are required to file the pre and post arrangement shareholding pattern and the capital structure with the stock exchanges as per requirements of the listing authority or stock exchanges of the home country in which the securities are listed.¹³
- v. **Corporate actions pursuant to merger:** The listed company needs to disclose to the stock exchanges all information having a bearing on the performance/ operation of the listed entity and/or price sensitive information.¹⁴

12 Regulation 11, SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

13 Regulation 69(2), SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015; Part I, Para A, 2(e) of the SEBI Master Circular No. SEBI/HO/CFD/DIL1/CIR/P/2020/249 dated December 22, 2020.

14 Regulation 51(1), SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

Key Corporate and Securities Laws Considerations

I. Company Law

A. Transferability of Shares

Broadly speaking, an Indian company can be set up as a private company or as a public company. A restriction on transferability of shares is inherent to a private company, such restrictions are contained in its articles of association (the byelaws of the company) and are usually in the form of a pre-emptive right in favor of the other shareholders. With the introduction of CA 2013, although shares of a public company are freely transferable, share transfer restrictions for even public companies' shares have been granted statutory sanction.¹ The articles of association may prescribe certain procedures for transfer of shares that must be adhered to in order to effect a transfer of shares. It is therefore advisable for the acquirer of shares of a private company to ensure that the non-selling shareholders (if any) waive their rights of pre-emption and any other preferential rights that they may have under the articles of association. Any transfer of shares, whether of a private company or a public company, must comply with the procedure for transfer specified under its articles of association.

B. Squeeze-Out Provisions

Section 236 of CA 2013, provides that, if a person or group of persons acquire 90% or more of the shares of a company by virtue of an amalgamation, share exchange, conversion of securities or for any other reason, then such person(s) shall besides notifying the company of their intention to buy the remaining equity shares of the company, have a right to make an offer to buy out the minority shareholders at a price determined by a registered valuer, which shall be determined based on the fair value of shares of the company after taking into account valuation parameters including return on net worth, book value of shares, earning per share, price earning multiple vis-a-vis the industry average, and such other parameters as are customary for valuation of shares of such companies.²

C. Scheme of Arrangements

Section 230 read with Rule 3 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 made effective from February 7, 2020, permits the shareholders of unlisted companies holding at least 75% of the securities (including depository receipts) with voting rights to make an offer for acquisition of any part of the remaining shares in such company, pursuant to an application of compromise or arrangement to be filed before the NCLT.³

¹ Public company can refuse registration of share transfers pursuant to section 58(4) of the CA 2013 for a 'sufficient cause'.

² Rule 27 of the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

³ Rule 3, Companies (Compromises, Arrangements and Amalgamations) Rules, 2016.

Once NCLT approves such offer for acquisition, the minority shareholders would mandatorily be required to sell their shares to the acquiring shareholder. This method of squeeze-out is only available to unlisted companies and listed companies will be subject to the regulations prescribed by SEBI in this regard.

D. Scheme of Capital Reduction

Section 66 of the CA 2013 permits a company to reduce its share capital and prescribes the procedure to be followed for the same. The scheme of capital reduction under Section 66 of the CA 2013 must be approved by, (i) the shareholders of the company vide a special resolution; and (ii) by the NCLT by an order approving the reduction. When the company applies to the NCLT for its approval, the creditors of the company would be entitled to object to the scheme of capital reduction. The NCLT will approve the reduction only if the debt owed to the objecting creditors is safeguarded/provided for. In addition, the NCLT is also required to give notice of application of reduction of capital to the Central Government, Registrar of Companies, the creditors and SEBI (in case of a listed company) who will have a period of 3 (three) months to file any objections.⁴ Companies will have to mandatorily publish the NCLT order sanctioning the scheme of capital reduction. The framework for reduction of capital under Section 66 (and the erstwhile Section 100 under CA 1956) has been used by companies to provide exit to select shareholders, as opposed to all shareholders on a proportionate basis. The courts have held that reduction of share capital need not necessarily be amongst all the shareholders of the company.⁵

E. Buy-back of Shares

As per section 68 of the CA 2013, a company can buy-back its own shares subject to certain statutory restrictions (mainly, that the limit for a permissible buy-back is set to 25% of the total paid up share capital and free reserves of the company, and the buy-back can only be made out of the free reserves or the securities premium account of the company, or the proceeds of the issue of any shares or specified securities, provided that this is not an issue of the same kind of shares being bought back). Additionally, the buyback cannot be made through borrowed funds and the company must adhere to the restriction that the post buyback ratio of the aggregate debts owed by the company does not exceed twice the paid-up capital and its free reserves. The company is also restricted from buying back its shares if it has defaulted on the repayment of deposits, interest payments, or any other financial obligations. Further, the buyback cannot be conducted if the company has made any previous buyback within the last 12 months and, following the buyback, the company is barred from issuing the same class of securities for a period of twenty-four months, though it may issue other securities during this 6 month restriction on doing private placement after having done a buy-back period. Further, pursuant to Section 68(8) of the CA 2013, a company shall not make a further issue of the same kind of shares or other securities including allotment of new shares pursuant to Section 62(1)(a), i.e., Private Placement of Shares, within a period of at least six months, except by way of bonus issuance, discharge of subsisting obligations, conversion of warrants, stock option schemes, sweat equity or conversion of preference shares / debentures into equity shares.

⁴ Section 66(2), Companies Act.

⁵ Sandvik Asia Limited vs. Bharat Kumar Padamsi and Ors [2009]92SCL272(Bom); Elpro International Limited (2009 4 Comp LJ 406 (Bom)).

The buyback has to be authorized by the articles of the company. Authorizations of the company's board of directors and a special resolution of the shareholders authorizing the buyback (if the buy back is greater than 10% of the total paid up equity capital and free reserves of the company) will also be required, to initiate the process. Prior to this, a declaration of solvency also has to be filed by the Company with the Registrar and SEBI (if listed). Every buyback must be completed within one year from the date of passing the special resolution or the board resolution. The buyback can be conducted in one of three ways: (a) from the existing shareholders or security holders on a proportionate basis, (b) from the open market, or (c) by purchasing securities issued to employees under a scheme of stock option or sweat equity. After the buyback, the company is required to extinguish the purchased shares within seven days to reduce its share capital accordingly and file with the Registrar and the SEBI (if listed) a return containing such particulars relating to the buy-back within thirty days of such completion.

F. Private Placement / Preferential Offer

Sections 42 and 62 of CA 2013 read with Rule 13 of the Companies (Share Capital and Debenture) Rules 2014 and Rule 14 of Companies (Prospectus and Allotment of Securities) Rules, 2014 prescribe the requirements for any new issuance of shares on a preferential basis (i.e. any issuance that is not a rights or bonus issue to existing shareholders) by an unlisted company.⁶ Some of the important requirements under these provisions are described below:

- i. The company must engage a registered valuer to arrive at a fair market value of the shares proposed to be issued.⁷
- ii. The issuance must be authorized by the articles of association of the company⁸ and approved by a special resolution passed by shareholders in a general meeting,⁹ authorizing the board of directors of the company to issue the shares.¹⁰ A special resolution is one that is passed by at least 3/4th of the shareholders present and voting at a meeting of the shareholders. If shares are not issued within 12 months from date of passing of such special resolution, the resolution will lapse and a fresh resolution will be required for the issuance.¹¹
- iii. The explanatory statement to the notice for the general meeting should contain key disclosures pertaining to the object of the issue, pricing of shares including the relevant date for calculation of the price, shareholding pattern, change of control, if any, pre-issue and post-issue shareholding pattern of the company, whether the promoters/directors/key management persons propose to acquire shares as part of such issuance, etc.¹²
- iv. All newly issued shares must only be issued in the dematerialized form by all private companies.¹³ All private companies (not falling under the umbrella of small companies¹⁴) are required to comply with the requirements of dematerialization on or before June 30, 2025.

6 Sections 42 and 62, Companies Act, 2013; Rule 13, Companies (Share Capital and Debenture) Rules 2014; Rule 14, Companies (Prospectus and Allotment of Securities) Rules, 2014.

7 Section 62(1) (c) of CA 2013.

8 Rule 13(2)(a) of the Companies (Share Capital and Debenture) Rules 2014.

9 Rule 13(2)(b) of the Companies (Share Capital and Debenture) Rules 2014.

10 Rule 13(1) of the Companies (Share Capital and Debenture) Rules 2014.

11 Rule 13(2)(f) of the Companies (Share Capital and Debenture) Rules 2014.

12 Rule 13(2)(d) of the Companies (Share Capital and Debenture) Rules 2014.

13 Rule 9B, Companies (Prospectus and Allotment of Securities) Amendment Rules, 2023.

14 As defined in Section 2 (85) of CA 2013 read with the Companies (Specification of Definitions Details) Rules, 2014.

Key Corporate and Securities Laws Considerations

- v. Shares must be allotted within a period of 60 days of receipt of application money, failing which the money must be returned within a period of 15 days thereafter. Interest is payable @ 12% p.a. from the 60th day.¹⁵

These requirements apply to equity shares, fully convertible debentures, partly convertible debentures or any other securities, which would be convertible into or exchanged with equity shares at a later date.¹⁶

Differential Voting Rights

The CA 2013¹⁷ also allows for issuance of equity shares with differential voting rights as to dividend, voting or otherwise, provided that the company complies with the rules prescribed in this regard,¹⁸ which require that:

- i. The articles of association of the company authorizes issue of shares with differential voting rights;
- ii. The issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders;
- iii. The voting power in respect of the shares with differential rights shall not exceed 74% of the total voting power including voting power in respect of equity shares with differential rights issued at any point in time;
- iv. The company shall not have defaulted in filing financial statements and annual returns for 3 financial years immediately preceding the financial year in which it has decided to issue shares with differential voting rights. Private companies may be exempt from these requirements if their memorandum and articles of association so provide.
- v. The company cannot convert its existing equity share capital with voting rights into equity share capital carrying differential voting rights and vice-versa.

G. Asset / Business Purchase

Besides share acquisition, the acquirer may also decide to acquire the business of the target which could typically entail acquisitions of all or specific assets and liabilities of the business for a pre-determined consideration. Therefore, depending upon the commercial objective and considerations, an acquirer may opt for (i) an asset purchase, whereby one company purchases all or part of the assets of the other company; or (ii) a slump sale, whereby one company acquires the 'business undertaking' of the other company on a going concern basis i.e., acquiring all assets and liabilities of such business.

Under CA 2013, the sale, lease or other disposition of the whole or substantially the whole of any undertaking of a company (other than a private company¹⁹) requires the approval of the shareholders through a special resolution.²⁰ The term "undertaking" means an undertaking in which the investment of the company exceeds 20% of its net worth as per the audited balance sheet of the preceding financial year, or an undertaking

¹⁵ Section 42(6) of CA 2013.

¹⁶ Rule 13(1) of the Companies (Share Capital and Debenture) Rules.

¹⁷ Section 43 of CA 2013.

¹⁸ Rule 4 of the Companies (Share Capital and Debenture) Rules, 2014.

¹⁹ Private companies are exempted from this provision with effect from June 2015.

²⁰ Section 180 of CA 2013.

which generated 20% of the total income of the company during the previous financial year. Further this requirement applies if 20% or more of the undertaking referred to above is sought to be sold, leased or disposed of.

An important consideration for these options is the statutory costs involved i.e., stamp duty, tax implications etc. We have delved into this in brief in our chapter on ‘Taxes and Duties’.

II. Other Securities Laws

A. Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 (“ICDR Regulations”)

If the acquisition of an Indian listed company involves the issue of new equity shares or securities convertible into equity shares (“Specified Securities”) by the target (issuer) to the acquirer, the provisions of Chapter V (“Preferential Issue Regulations”) contained in ICDR Regulations will apply (in addition to company law requirements mentioned above). We have highlighted below some of the important provisions of the Preferential Issue Regulations.

i. Pricing of the Issue

The Preferential Issue Regulations set a floor price for an issuance. If the equity shares of the issuer have been listed on a recognized stock exchange for a period of 90 trading days or more as on the relevant date,²¹ the floor price of the equity shares to be allotted pursuant to preferential issue shall not be less than the higher of the volume weighted average prices, quoted on a recognized stock exchange of the stock of the company either (a) 90 trading days; or, (b) 10 trading days preceding the relevant date.²²

However, if the issuer’s Articles of Association specify a method for calculating the floor price that results in a higher value than what is prescribed under the regulations, then that higher price will be treated as the floor price for issuing equity shares through the preferential issue.²³

If the equity shares of the issuer have been listed on a recognized stock exchange for a period of less than 90 trading days as on the relevant date, the floor price of the shares shall not be less than the higher of (a) the price at which the equity shares were issued via initial public offer, or value of price per share arrived under the scheme pursuant to which the equity shares of the issuer were listed; or (b) the average of the volume weighted average prices of the stock of the company during the period the stock has been listed prior to the relevant date; or (c) the average of 10 trading days volume weighted average prices of the related equity shares quoted on a recognized stock exchange during the two weeks preceding the relevant date.²⁴

21 ‘relevant date’ in case of (a) preferential issue of equity shares shall be 30 (thirty) days prior to the date on which the shareholders meeting is held to consider the proposed preferential issue (in case of a preferential issue pursuant to a resolution plan under Insolvency and Bankruptcy Code, 2016 or any resolution of stressed assets framework specified by RBI, the relevant date shall be the date of approval of the resolution plan or the corporate debt restructuring package); and, (b) in case of a preferential issue of convertible securities, either the relevant date referred in (a) or a date 30 (thirty) days prior to the date on which the holders of convertible securities become entitled to apply for equity shares.

22 Regulation 164(1) of ICDR Regulations.

23 Proviso to Regulation 164(1) of ICDR Regulations.

24 Regulation 164(2) of ICDR Regulations.

ii. Minimum Promoter Contribution

Minimum promoter contribution is the percentage of the fully paid-up equity share capital of a company that is required to be held by the promoter(s) of a company planning to list its shares on a recognized stock exchange, pursuant to the ICDR Regulations. At the pre-IPO stage, the promoter(s) are required to hold at least 20% of the post-issue share capital of the concerned company. In the event that the post-issue shareholding falls below 20%, such gaps can be contributed to by Alternative Investment Funds (AIFs), Foreign Venture Capital Investors (FVCIs), insurance companies registered with the Insurance Regulatory and Development Authority of India (IRDAI), public financial institutions or scheduled commercial banks forming part of the promoter group but not promoters. Further, pursuant to an amendment to the ICDR Regulations, any shortfalls in the minimum promoter contribution can also be contributed to by any non-individual public shareholders (forming part of the promoter group but not promoters) holding at least 5% of the post-issue capital.²⁵ Additionally, these contributions made by the aforementioned entities cannot be more than 10% and they shall not have the right to assume the title of a promoter.

Equity shares arising from the conversion of Compulsorily Convertible Securities (CCS), including depository receipts held by promoters, FVCIs, AIFs, scheduled commercial banks, public financial institutions, insurance companies registered with the IRDAI, non-individual public shareholders holding at least 5% of the post-issue share capital, or any entity (individual or non-individual), forming part of the promoter group other than promoters, are ordinarily excluded from the minimum promoter contribution (among various other categories), when they are held for a period of at least one year prior to the filing of the draft offer document and are converted into equity shares prior to the filing of the offer document.²⁶

iii. Lock-in

Securities issued to the acquirer (who is not a promoter of the target) are locked-in for a period of 6 months²⁷ from the date of trading approval.

The date of trading approval is the latest date when approval for trading is granted by all stock exchanges on which the equity shares of the issuer are listed. Further, if the acquirer holds any equity shares of the target prior to such preferential allotment, then such prior holding will be locked-in for a period of 90 trading days from the date of the trading approval.²⁸ If securities are allotted on a preferential basis to promoters/ promoter group,²⁹ they are locked-in for a period of 18 months from the date of trading approval, subject to a limit of 20% of the total capital of the company.³⁰

The locked-in securities may be transferred amongst promoter/ promoter group or any person in control of the company, subject to the transferee being subject to the remaining period of the lock-in.³¹

²⁵ Regulation 14 of ICDR Regulations; Amendment to ICDR Regulations on May 17, 2024.

²⁶ Regulation 15(b)(iv) of ICDR Regulations; Amendment to ICDR Regulations on May 17, 2024.

²⁷ Regulation 167 of the ICDR Regulation.

²⁸ Regulation 167(6) of the ICDR Regulation.

²⁹ The terms 'promoter' and 'promoter group' are defined in great detail by the ICDR Regulations. Generally speaking, promoters would be the persons in over-all control of the company or who are named as promoters in the prospectus of the company. The term promoter group has an even wider connotation and would include immediate relatives of the promoter. If the promoter is a company, it would include, a subsidiary or holding company of that company, any company in which the promoter holds 10% or more of the equity capital or which holds 10% or more of the equity capital of the promoter, etc.

³⁰ Regulation 167 of the ICDR Regulation.

³¹ Regulation 168 of the ICDR Regulation.

iv. Exemption to court approved merger

The Preferential Issue Regulations shall not apply in case a preferential allotment of shares is made pursuant to a scheme of arrangement approved by the NCLT under the Merger Provisions discussed above.³²

B. Securities and Exchange Board of India (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 (the “Takeover Code”)

If an acquisition is contemplated by way of issue of new shares, or the acquisition of existing shares or voting rights, of a listed company, to or by an acquirer, the provisions of the Takeover Code are applicable. The Takeover Code regulates both direct and indirect acquisitions of shares³³ or voting rights in, and control³⁴ over a target company.³⁵ The key objectives of the Takeover Code are to provide the shareholders of a listed company with adequate information about an impending change in control of the company or substantial acquisition by an acquirer and provide them with an exit option (albeit a limited one) in case they do not wish to retain their shareholding in the company.

i. Mandatory Offer

Under the Takeover Code, an acquirer is mandatorily required to make an offer to acquire shares from the other shareholders in order to provide an exit opportunity to them prior to consummating the acquisition, if the acquisition fulfils the conditions as set out in Regulations 3, 4 and 5 of the Takeover Code. Under the Takeover Code, the obligation to make a mandatory open offer by the acquirer³⁶ is triggered in the following events:

a. Initial trigger

If the acquisition of shares or voting rights in a target company entitles the acquirer along with the persons acting in concert (“PAC”) to exercise 25% or more of the voting rights in the target company.³⁷

b. Creeping Acquisition

If the acquirer already holds 25% or more and less than 75% of the shares or voting rights in the target, then any acquisition of additional shares or voting rights that entitles the acquirer along with PAC to exercise more than 5% of the voting rights in the target in any financial year.³⁸

32 Regulation 158 of the ICDR Regulation.

33 The term ‘shares’ means shares in the equity share capital of a target company carrying voting rights and includes any security which would entitles the holder thereof to exercise voting rights. The term also includes all depository receipts carrying an entitlement to exercise voting rights in the target company. Therefore, acquisition of depository receipts entitling the acquirer to exercise voting rights in the target company may trigger the open offer obligation.

34 The term ‘control’ includes the right to appoint the majority of the directors or to control the management or policy decisions exercisable by a person or persons acting individually or in concert, directly or indirectly, including by the virtue of their shareholding or management rights or shareholders agreements or voting agreements or in any other manner.

35 A ‘Target Company’ has been defined as a company and includes a body corporate or corporation established by a Central Legislation, State Legislation or Provincial Legislation for the time being in force, whose shares are listed on a stock exchange.

36 See Annexure 2 for the meaning of persons acting in concert.

37 Regulation 3(1), SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

38 Regulation 3(2), SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

It is important to note that the 5% limit is calculated on a gross basis i.e., aggregating all purchases and without factoring in any reduction in shareholding or voting rights during that year or dilutions of holding on account of fresh issuances by the target company.³⁹ If an acquirer acquires shares along with other subscribers in a new issuance by the company, then the acquisition by the acquirer will be the difference between its shareholding pre and post such new issuance.

It should be noted that an acquirer (along with PAC) is not permitted to make a creeping acquisition beyond the statutory limit of nonpublic shareholding in a listed company i.e., 75%.⁴⁰

c. Acquisition of 'Control'

If the acquirer acquires control over the target

Regardless of the level of shareholding, acquisition of 'control' of a target company is not permitted, without complying with the mandatory offer obligation under the Takeover Code.⁴¹ What constitutes 'control' is most often a subjective test and is determined on a case-to-case basis. For the purpose of the Takeover Code, 'control' has been defined to include:

- Right to appoint majority of the directors;
- Right to control the management or policy decisions exercisable by a person or PAC, directly or indirectly, including by virtue of their shareholding or management rights or shareholder's agreements or voting agreements or in any other manner.

Over time, the definition of 'control' has been subject to different assessments and has turned out to be, quite evidently, a grey area under the Takeover Code. The Supreme Court order in case of SEBI vs. Subhkam Ventures Private Limited⁴² - which accepted an out-of-court settlement between the parties - left open the legal question as to whether negative control would amount to 'control' under the Takeover Code. In fact, the Supreme Court had ruled that SAT ruling in this case (against which SEBI had appealed before the Supreme Court) which ruled that 'negative control' would not amount to 'control' for the purpose of Takeover Code, should not be treated as precedent. With no clear jurisprudence on the subject-matter, each veto right would typically be reviewed from the commercial parameters underlying such right and its impact on the general management and policy decisions of the target company. SEBI, in light of Jet-Etiad transaction,⁴³ had indicated its plans to introduce new guidelines to define 'bright lines' to provide more clarity as regards 'change in control' in cases of mergers and acquisitions by issuing a discussion paper.⁴⁴ However, SEBI finally decided not to go ahead with the bright line test for determination of acquisition of 'control' and concluded that it needs to be determined on case-to-case basis.⁴⁵

39 Explanation (i), Regulation 3, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

40 Maximum permissible non-public shareholding is derived based on the minimum public shareholding requirement under the Securities Contracts (Regulations) Rules 1957 ("SCRR"). Rule 19A of SCRR requires all listed companies (other than public sector companies) to maintain public shareholding of at least 25% of share capital of the company. Thus, by deduction, the maximum number of shares which can be held by promoters i.e. Maximum permissible nonpublic shareholding) in a listed companies (other than public sector companies) is 75% of the share capital.

41 Regulation 4, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

42 SAT Appeal No. 8 of 2009, Date of decision: January 15, 2010.

43 <https://www.nishithdesai.com/SectionCategory/33/M&A-Hotline/12/59/MAHotline/5613/4.html>.

44 Discussion Paper on "Brightline Tests for Acquisition of 'Control' under SEBI Takeover Regulations" available at: https://www.sebi.gov.in/sebi_data/attachdocs/1457945258522.pdf.

45 https://www.business-standard.com/article/economy-policy/sebi-scarps-bright-line-control-test-proposal117090801010_1.html.

ii. Indirect Acquisition of Shares or Voting Rights

For an indirect acquisition obligation to be triggered under the Takeover Code, the acquirer must, pursuant to such indirect acquisition be able to direct the exercise of such percentage of voting rights or control over the target company, as would otherwise attract the mandatory open offer obligations under the Takeover Code.⁴⁶ This provision was included to prevent situations where transactions could be structured in a manner that would side-step the obligations under Takeover Code. Further, if:⁴⁷

- i. the proportionate net asset value of the target company as a percentage of the consolidated net asset value of the entity or business being acquired; or
- ii. the proportionate sales turnover of the target company as a percentage of the consolidated sales turnover of the entity or business being acquired; or
- iii. the proportionate market capitalisation of the target company as a percentage of the enterprise value for the entity or business being acquired; is in excess of 80%, on the basis of the most recent audited annual financial statements, then an indirect acquisition would be regarded as a direct acquisition under the Takeover Code for the purposes of the timing of the offer, pricing of the offer etc.

Voluntary open offer

An acquirer who holds between 25% and 75%⁴⁸ of the shareholding/ voting rights in a company is permitted to voluntarily make a public announcement of an open offer for acquiring additional shares of the company subject to their aggregate shareholding after completion of the open offer not exceeding 75%.⁴⁹ In case of a voluntary offer, the offer must be for at least 10% of the voting rights in the target company, but the acquisition should not result in a breach of the maximum non-public shareholding limit of 75%. Any person who has been declared as a willful defaulter or is a fugitive economic offender cannot make an open offer or enter into any transaction that would attract obligations to make a public announcement of open offer.⁵⁰

a. Minimum Offer Size

- i. **Mandatory Offer⁵¹:** Mandatory open offer for acquiring shares must be for at least 26% of the shares of the target company. It is also possible for the acquirer to provide that the offer to acquire shares is subject to a minimum level of acceptance.⁵² If an open offer is subject to a minimum level of acceptance, then during the offer period, the acquirer and any persons acting in concert with them can only acquire shares of the target company through the open offer or through the underlying agreement that triggered the open offer. In the event the required minimum level of acceptance is not reached, the acquirer shall face no obligation to acquire any shares pursuant to the open offer.⁵³
- ii. **Voluntary Open Offer⁵⁴:** In case of a voluntary open offer by an acquirer holding 25% or more of the shares/voting rights, the offer must be for at least 10% of the voting rights in the target company. While there is no maximum limit, the shareholding of the acquirer post-acquisition should not exceed 75%. In case of a voluntary offer made by a shareholder holding less than 25% of shares or voting rights of the target company, the minimum offer size is 26% of the total shares of the company.

46 Regulation 5, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

47 Regulation 5(2), SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

48 The maximum permissible non-public shareholding limit.

49 Regulation 6(1) of Takeover Code.

50 Regulation 6A and 6B of Takeover Code.

51 Regulation 7 (1) of Takeover Code.

52 Regulation 19 of Takeover Code.

53 Regulation 19(1) and 19(2) of Takeover Code.

54 Regulation 7 (2) of Takeover Code.

b. **Pricing of Offer**⁵⁵

Regulation 8 of the Takeover Code sets out the parameters to determine offer price to be paid to the public shareholders, which is the same for a mandatory open offer as well as a voluntary open offer. There are certain additional parameters prescribed for determining the offer price when the open offer is made pursuant to an indirect acquisition. Please see Annexure 2 for the parameters as prescribed under Regulation 8 of the Takeover Code. It is important to note that an acquirer cannot reduce the offer price but an upward revision of offer price is permitted, subject to certain conditions. Furthermore, the impact of material price movement and confirmation of events on the target company's share price can be excluded when determining the offer price under Regulation 30 (11) of the Listing Regulations.⁵⁶

c. **Competitive Bid/Revision of offer/bid**⁵⁷

The Takeover Code also permits a person other than the acquirer (the first bidder) to make a competitive bid, by a public announcement, for the shares of the target company. This bid must be made within 15 (fifteen) working days from the date of the detailed public announcement of the first bidder. The competitive bid must be for at least the number of shares held or agreed to be acquired by the first bidder (along with PAC), plus the number of shares that the first bidder has bid for. Each bidder (whether a competitive bid is made or not) is permitted to revise his bid, provided such revised terms are more favourable to the shareholders of the target company.⁵⁸ The revision can be made up to 3 (three) working days prior to the commencement of the tendering period.

d. **Take private mechanism**

The SEBI (Delisting of Equity Shares) Regulations, 2021 ("SEBI Delisting Regulations") prescribe the method and conditions for delisting of a company. The SEBI Delisting Regulations allow an acquirer in addition to the promoter of the company to initiate delisting of such company. Pursuant to Regulation 5A of the Takeover Code, an acquirer may delist the company pursuant to an open offer in accordance with the SEBI Delisting Regulations provided that the acquirer declares upfront his intention to delist.⁵⁹ Prior to the inclusion of Regulation 5A, an open offer under the Takeover Regulations could not be clubbed with a delisting offer, making it burdensome for acquirers to delist the company in the future.

The Takeover Code provided for a 1 year cooling off period between the completion of an open offer under the Takeover Code and a delisting offer in situations where on account of the open offer the shareholding of the promoters exceeded the maximum permissible non-public shareholding of 75%.⁶⁰ This restriction is not affected by Clause 5A in that the acquirer will continue to be bound by this restriction if the acquirer's intent to delist the company is not declared upfront at the time of making the detailed public statement.

⁵⁵ Regulation 8, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

⁵⁶ Regulation 8, SEBI (Substantial Acquisition of Shares and Takeovers) Amendment Regulations, 2024.

⁵⁷ Regulation 20, SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011.

⁵⁸ Regulation 20 of Takeover Code.

⁵⁹ Regulation 5A, SEBI (Delisting of Equity Shares) Regulations, 2021.

⁶⁰ Regulation 7(5) of the Takeover Code.

C. Listing Regulations

On September 2, 2015, the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“**Listing Regulations**”) were notified and constitute the applicable law in this domain. The Listing Regulations provide a comprehensive framework governing various types of listed securities.

Regulation 30 of Listing Regulations deals with disclosure of material events by the listed entity whose equity and convertibles securities are listed. Such entity is required to make disclosure of events specified under Schedule III of the Listing Regulations. The Listing Regulations divide the events that need to be disclosed broadly in two categories. The events that have to be necessarily disclosed without applying any test of materiality are indicated in Para A of Schedule III of the Listing Regulation.⁶¹ Para B of Schedule III indicates the events that should be disclosed by the listed entity, if considered material.⁶²

D. SEBI (Prohibition of Insider Trading) Regulations, 2015 (“PIT Regulations”)

The PIT Regulations prohibit the following in case of a listed company (or a company that is proposed to be listed)⁶³:

- i. an insider from communicating unpublished price sensitive information (“UPSI”);
- ii. any person from procuring UPSI from an insider; and,
- iii. an insider from trading in securities⁶⁴ when in possession of UPSI.

Therefore, the PIT prohibits the dissemination as well as the receipt of UPSI.

a. Who is an Insider?

Insider: Under the PIT Regulations, an ‘insider’ is a person who is (i) a connected person; or (ii) in possession of or having access to UPSI.⁶⁵ Since “generally available information” is defined in the PIT Regulations, anyone who possesses or has access to UPSI (explained below) is considered an “insider,” regardless of how they came into possession of such information. This broad definition ensures that any individual with access to UPSI falls within the scope of insider trading rules. The responsibility to prove that someone had access to or was in possession of UPSI at the time of trading lies with the person making the allegation. Once that is established, the person accused of insider trading may defend themselves by showing they were not in possession of the information, did not trade on the basis of it, or that their actions fall under permitted exceptions.

Connected Person: A connected person is one who is directly or indirectly associated with the company (i) by reason of frequent communication with its officers; or (ii) by being in a contractual, fiduciary or employment relationship; or (iii) by holding any position including a professional or business relationship with the company whether temporary or permanent that allows such person, directly or indirectly, access to UPSI or is reasonably expected to allow such access.⁶⁶

61 Para A, Schedule III, SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015; Regulation 30(4), SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

62 Para B, Schedule III, SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015; Regulation 30(4), SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015.

63 Regulation 3, SEBI (Prohibition of Insider Trading) Regulations, 2015.

64 For the purpose of the PIT Regulations the term ‘securities’ does not include units of mutual funds.

65 Regulation 2(g) of the PIT Regulation.

66 Regulation 2(d) of the PIT Regulation.

Therefore, any person who has any connection with the company that is expected to put him in possession of UPSI is considered to be a connected person. Persons who do not seemingly occupy any position in a company but are in regular touch with the company will also be covered. Certain categories of persons are all deemed to be connected, such as ‘immediate relatives’,⁶⁷ a holding, associate or subsidiary company, etc.

b. What is Unpublished Price Sensitive Information?⁶⁸

UPSI means any information relating to a company or its securities, directly or indirectly, that is not generally available, and which upon becoming available is likely to materially affect the price of the securities. It includes: financial results; dividends; change in capital structure; mergers, demergers, acquisitions, de-listing, disposals and expansion of business and such other transactions, changes in key managerial personnel, changes in ratings other than ESG rating, fund raising proposed to be undertaken, management or control impacting agreements, frauds/defaults by the company, promoter, director, key managerial personnel, etc., resolution plan/restructuring/one-time settlement relating to loans or borrowings from banks/financial institutions, admission of winding up proceedings or initiation of CIRP proceedings, initiation of forensic audit for detecting mis-statement in financials, orders by regulatory or enforcement authorities within or outside India, outcome of litigations, giving of guarantees or indemnity not in the normal course of business, or, granting, withdrawal, surrender, cancellation or suspension of key licenses or regulatory approvals. The term ‘generally available’⁶⁹ means information that is accessible to the public on a non-discriminatory basis.

c. Defenses/Exceptions

The communication of UPSI by an insider and the procurement of UPSI by a person from an insider is permitted if such communication, procurement is in furtherance of legitimate purposes, performance of duties or discharge of legal obligations.⁷⁰ The following are valid defenses available to a person who trades in securities when in possession of UPSI:⁷¹

General

An off-market transaction or a block deal between persons who:

- were in possession of the same UPSI (without being in breach of Regulation 3 and the UPSI was not obtained under Regulation 3(3)); and
- both counterparties made a conscious and informed trade decision.

The transaction was carried out pursuant to a statutory or a regulatory obligation to carry out a bona fide trade.

The transaction was undertaken pursuant to exercise of stock options in respect of which the exercise price was pre-determined in compliance of applicable regulations.

Specifically for non-individual insiders

- Individuals who executed the trade were different from individuals in possession of UPSI and were not in possession of such UPSI;

⁶⁷ Regulation 2(f) of the PIT Regulations, a spouse of a person, parent, sibling, and child of such person or of the spouse, any of whom is dependent financially on such person, or consults such person in taking decisions relating to trading in securities.

⁶⁸ Regulation 2 (n) of the PIT Regulations.

⁶⁹ Regulation 2(e) of the PIT Regulation.

⁷⁰ Regulation 3(1) of the PIT Regulation.

⁷¹ Regulation 4(1) of the PIT Regulation.

- Chinese wall arrangements were in place and there was no leakage of information and the PIT Regulations were not violated; or
- Trades were made pursuant a trading plan.

Therefore, as long as the board is of the informed opinion that the transaction is in the best interest of the company, due diligence may be lawfully conducted. In case a particular transaction does not entail making an open offer to the public shareholders, the board of directors would be required to cause public disclosures of the UPSI prior to the proposed transaction to rule out any information asymmetry in the market. Additionally, a duty has been cast on the board of the company to cause the parties to execute confidentiality and non-disclosure agreements for the purpose of this provision. Therefore, introduction of Regulation 3(3) under the PIT Regulations has amply clarified that the communication or procurement of UPSI for the purpose of due diligence shall be permitted, subject to the conditions set out in the PIT Regulations.

d. Trading Plans⁷²

A key aspect in the framework of PIT Regulations is the concept of trading plans. Typically, ‘insiders’ who are liable to possess UPSI round the year are permitted to formulate trading plans with appropriate safeguards. Every trading plan is required to have a designated outer time limit (the PIT Regulations do not specify an exact coverage period), and in this period it must be reviewed and approved by the compliance officer of the company and then publicly disclosed. Trading cannot begin for a period of 120 days after the plan is publicly disclosed.⁷³ Trading plans should set out certain parameters for each trade to be executed, which includes the trade’s value or quantity of securities to be traded, nature of trade, either specific date or time period not exceeding five consecutive trading days and optionally, an upper price limit for buy trades and a lower price limit for sell trades, set within 20% of the closing price the day before the plan submission. Trades outside these price limits cannot be executed, protecting insiders from unexpected price movements. Insiders can deviate from the trading plan in cases of permanent incapacity, bankruptcy, or operation of law. In cases of inability to implement the plan due to price limits or inadequate liquidity, the compliance officer must be notified within two days after the trading plan’s tenure ends, with reasons and evidence. The compliance officer will present the information to the audit committee, which will decide if the non-implementation was bona fide. The compliance officer will then notify the stock exchanges of the audit committee’s decision. If the audit committee rejects the submission, the compliance officer will take action as per the code of conduct. Adjustments to the trading plan due to corporate actions like bonus issues or stock splits are allowed with compliance officer approval and must be notified to the stock exchanges. Contra trades are not permissible under the approved trading plan. A restriction of at least six months will apply according to the code of conduct requirements. Trading plans are a defense and do not provide absolute immunity from investigation under the PIT Regulations.

⁷² Regulation 5 of the PIT Regulation.

⁷³ Regulation 5(2), SEBI (Prohibition of Insider Trading) Regulations, 2015.

e. Due-Diligence Carve-Out

The PIT Regulations contain a specific carveout for communication and procurement of information (conduct of due-diligence) in connection with transactions involving mergers and acquisitions.⁷⁴ Therefore, based on whether or not a transaction entails making an open offer under Takeover Code, information may be communicated, provided, allowed access to or procured on the following conditions:

Open Offer Obligation under Takeover Code⁷⁵

Where the board of directors of the listed company is of the informed opinion that sharing of such information is in the best interest of the company.

No Open Offer Obligation under Takeover Code⁷⁶

Where the board of directors of the listed company is of the informed opinion that sharing of such information is in the best interest of the listed company. Information that constitutes UPSI is to be made generally available at least 2 trading days prior to the proposed transaction being effected in such form as the board of directors may determine to be adequate and fair to cover all relevant and material facts.

f. Disclosures

A significant aspect of the insider trading norms is disclosure requirements for different categories of persons involved in the affairs of the company. It is important to bear in mind that going forward, Every person on appointment as a key managerial personnel or a director of the company or upon becoming a promoter or member of the promoter group would be required to disclose to the company his holding of securities of the company as on date of appointment/date of notification of the PIT Regulations i.e., May 15, 2015. More importantly, every promoter, member of promoter group, designated persons or director would be required to make continual disclosures (within 2 trading days of such transaction) in case the traded value of securities over a calendar quarter exceeds the monetary threshold of INR 1 million (USD 11.5 thousand approx.) or such other value as may be specified. The company is also required to notify the stock exchanges in case such transactions by the promoter, employee or director exceeds this monetary threshold or in case of any incremental changes after such disclosure within 2 days of receipt of such information. These records will be required to be maintained by the company for at least 5 years.⁷⁷

g. Code of Conduct and Fair Disclosures

The board of every company is required to formulate and publish a code of practices and procedures to be followed for fair disclosure of UPSI in accordance with the principles set out in Schedule A to the PIT Regulations. Schedule A of the PIT Regulations sets out certain minimum standards such as equality of access to information, publication of policies such as those on dividend, inorganic growth pursuits, calls and meetings with analysts, publication of transcripts of such calls and meetings etc.⁷⁸ Additionally, the board of directors of every listed company and the board of directors or head(s) of the organisation of every intermediary shall ensure that the chief executive officer or managing director of every listed company and market intermediary shall formulate a code of conduct to regulate, monitor and report trading by designated persons and immediate relatives of designated persons.⁷⁹

⁷⁴ Regulation 3(3) of the PIT Regulation.

⁷⁵ Regulation 3(3)(i), SEBI (Prohibition of Insider Trading) Regulations, 2015.

⁷⁶ Regulation 3(3)(ii), SEBI (Prohibition of Insider Trading) Regulations, 2015.

⁷⁷ Regulation 7 (1) of the PIT Regulation.

⁷⁸ Regulation 8 of the PIT Regulation.

⁷⁹ Regulation 9 of the PIT Regulation.

h. Compliance Officer

The PIT Regulations have enhanced the role of a compliance officer's role with respect to monitoring and regulating trading by employees and connected persons, in particular monitoring and approving trading plans. The PIT Regulations prescribe specific qualification criteria for a compliance officer who shall report to the board of directors of the company or the head of the organization, as the case may be.

i. Pre-Clearance of Trades

A condition may be imposed on the insiders that they can deal in the securities of the company only after obtaining a prior approval in accordance with the procedure and policy prescribed by the company in that regard. In addition, it may also be prescribed that a preapproved trade will have to be undertaken within the stipulated time period, failing which the approval would lapse.

j. Notional Trading Windows

Usually, the trading windows are closed to eliminate any risk of insider trading and monitor compliant trading within a company. The trading window shall be closed when the compliance officer determines that a designated person or class of designated persons can reasonably be expected to have possession of unpublished price sensitive information. Trading restriction period shall be made applicable from the end of every quarter till 48 hours after the declaration of financial results.

k. Chinese Walls

To prevent the misuse of confidential information the organization/firm shall adopt a 'Chinese Wall' policy which separates those areas of the organization/firm which routinely have access to confidential information, from those areas which deal with sale/marketing/ investment advice or other departments providing support services. In order to monitor Chinese Wall procedures and trading in client securities based on UPSI, the organization/firm shall restrict trading in certain securities and designate such list as restricted/grey list. Securities of a listed company shall be put on the restricted/grey list if the organization/firm is handling any assignment for the listed company and is privy to UPSI.

Competition Law

The Competition Act, 2002 (“**Competition Act**”) which replaced the Monopolies and Restrictive Trade Practices Act, 1969 primarily covers (i) anti-competitive agreements (Section 3), (ii) abuse of dominance (Section 4), and (iii) combinations (Section 5, 6, 20, 29, 30 and 31).

The Competition Commission of India (Procedure in regard to the Transaction of Business relating to Combinations) Regulations, 2011 (“**Combination Regulations**”) govern the manner in which the CCI will regulate combinations which have caused or are likely to cause an appreciable adverse effect on competition (“AAEC”) in India.

I. Anti-Competitive Agreements

The Competition Act essentially contemplates 2 kinds of anti-competitive agreements – Horizontal Agreements i.e., agreements between entities engaged in similar trade of goods or provisions of services, and Vertical Agreements i.e., agreements between entities in different stages/levels of the chain of production, in respect of production, supply, distribution, storage, sale or price of goods or services. Anticompetitive agreements that cause or are likely to cause an AAEC within India are void under the provisions of the Competition Act.

A horizontal agreement that (i) determines purchase/sale prices, or (ii) limits or controls production supply, markets, technical development, investment or provision of services, or (iii) shares the market or source of production or provision of services, by allocation of geographical areas/type of goods or services or number of customers in the market, or (iv) results in bid rigging / collusive bidding, is presumed to have an AAEC. Additionally, an enterprise or association of enterprises or a person or association of persons though not engaged in identical or similar trade shall be presumed to be part of an anti-competitive agreement, if it participates or intends to participate in the furtherance of such a horizontal agreement.¹ On the other hand, vertical agreements, such as tie-in arrangements,² exclusive dealing³ or distribution agreements, etc., are examples where they can be considered to have an AAEC.⁴

II. Abuse of Dominant Position

An entity is considered to be in a dominant position if it is able to operate independently of competitive forces in India, or is able to affect its competitors or consumers or the relevant market in India in its favor. The Competition Act prohibits an entity from abusing its dominant position.⁵ Abuse of dominance would

¹ Inserted to Section 5, through the Competition (Amendment) Act, 2023.

² A tie-in arrangement would include any agreement where the purchaser of goods, (as a condition of such purchase) is made to purchase some other goods. A classic example of this on a global scale may be Microsoft’s bundling of its web browser Internet Explorer along with the Windows operating system, limiting Netscape’s web browser, Navigator, from having a significant presence in the market.

³ Section 4(b)(ii), Competition (Amendment) Act, 2023; Exclusive dealing agreements have been defined as “any agreement restricting in any manner the purchaser or the seller, as the case may be, in the course of his trade from acquiring or selling or otherwise dealing in any goods or services other than those of the seller or the purchaser or any other person, as the case may be.”

⁴ Section 3(4), Competition Act, 2002.

⁵ Section 4, Competition Act, 2002.

include imposing unfair or discriminatory conditions or prices in purchase/sale of goods or services and predatory pricing, limiting or restricting production/provision of goods/ services, technical or scientific development, indulging in practices resulting in denial of market access, etc.

III. Regulation of Combinations

In terms of Section 5 of the Competition Act, a ‘combination’ involves:

- i. the acquisition of control, shares, voting rights or assets of an enterprise by a person;
- ii. acquisition of control of an enterprise where the acquirer already has direct or indirect control of another enterprise engaged in identical business; or
- iii. a merger or amalgamation between or amongst enterprises; that cross the financial thresholds set out in Section 5.

The financial thresholds for a combination are determined with reference to (i) the combined asset value and the turnover⁶ of the acquirer and the target in the event of an acquisition, and the combined asset value and the turnover of the combined resultant company, in the event of an amalgamation or merger, and (ii) the combined asset value and the turnover of the “group” to which the target/resultant company will belong pursuant to the proposed acquisition/merger.⁷

Under Section 32 of the Competition Act, the CCI has been conferred with extra-territorial jurisdiction, meaning that any acquisition where assets/turnover are in India, and exceed specified limits, would be subject to the scrutiny of the CCI, even if the acquirer and target are located outside India.

The CCI and MCA have, along with bringing into force certain sections of the Competition (Amendment) Act, 2023, notified certain new rules and regulations on September 09, 2024. This includes the (i) CCI (Combination) Regulations, 2024, (“**2024 Combination Regulations**”), (ii) CCI (Minimum Value of Assets and Turnover) Rules, 2024, (“**MVAT Rules**”), (iii) CCI (Criteria for Combinations) Rules, 2024, (“**Green Channel Rules**”) and (iv) CCI (Criteria of Exemptions) Rules, 2024 (“**Exemption Rules**”). These new rules and regulations have taken into effect from September 10, 2024 onwards.

A. Financial Thresholds

The Competition Act prescribes financial thresholds linked with assets/turnover for the purposes of determining whether a particular transaction qualifies as a ‘combination’. These thresholds have been revised vide a circular released by the Ministry of Corporate Affairs, which proposed to enhance the thresholds stated in the original language of the Competition Act by 150%.⁸ Keeping this enhancement in mind, a transaction that satisfies any of the following tests shall be treated as a ‘Combination’:

⁶ The turnover shall be certified by the statutory auditor in the financial year immediately preceding the financial year in which the notice is filed, and such turnover in India shall be determined by excluding intra-group sales, indirect taxes, trade discounts and all amounts generated through assets or business from customers outside India.

⁷ Section 5, Competition Act, 2002.

⁸ Notification S.O. 1130 (E) No. 1073 dated March 7, 2024.

An acquisition where the parties to the acquisition, i.e., the acquirer and the target, should jointly have:

- **Test 1 / India Asset Test and India Turnover Test** - in India (i) assets higher than INR 25 billion (USD 288.3 million approx.); or (ii) turnover higher than INR 75 billion (USD 864.9 million approx.); or
- **Test 2 / Global Asset Test and Global Turnover Test** - Total assets in India or outside India, higher than USD 1.25 billion (INR 108.4 billion approx.) of which assets in India should be higher than INR 12.5 billion (USD 144.1 million approx.); or (ii) total turnover in India or outside is higher than USD 3.75 billion (INR 325.2 billion approx.) of which turnover in India should be higher than INR 37.5 billion (USD 432.4 million approx.); or

The acquirer group⁹ has:

- **Test 1 / India Asset Test and India Turnover Test** - in India (i) assets higher than INR 100 billion (USD 1.2 billion approx.); or (ii) turnover higher than INR 300 billion (USD 3.5 billion approx.); or
- **Test 2 / Global Asset Test and Global Turnover Test** - (i) Total assets in India or outside higher USD 5 billion (INR 433.6 billion approx.) of which assets in India are higher than INR 12.5 billion (USD 144.1 million approx.); or (ii) total turnover in India or outside is higher than USD 15 billion (INR 1.3 trillion approx.) of which turnover in India should be higher than INR 37.5 billion (USD 432.4 million approx.).

B. Deal Value Thresholds

Pursuant to an amendment¹⁰ to the Competition Act, the addition of clause (d) in Section 5 of the original act introduced a deal value threshold, which requires an approval from CCI for any transaction in connection with acquisition of any control, shares, voting rights or assets of an enterprise, merger or amalgamation, the deal value¹¹ of which exceeds INR 20 billion (USD 230.6 million approx.) and if such enterprise (i.e. the enterprise being acquired / taken control of / merged / amalgamated) has 'substantial business operations in India'. In accordance with the 2024 Combination Regulations, an enterprise would be deemed to have 'substantial business operations in India' if:

- a. for digital services provided, the number of its business users or end users in India is 10% or more of its total global number of such users; or,
- b. its gross merchandise value for the period of twelve months preceding the relevant date in India is:
 - i. 10% or more of its total global gross merchandise value; and
 - ii. More than INR 5 billion (USD 57.7 million approx.) or

9 A 'group' for the above purposes would mean two or more enterprises which, directly or indirectly, are in position to – (i) Exercise of not less than 26% or more of the voting rights in the other enterprise; or (ii) Appoint more than fifty per cent of the members of the board of directors in the other enterprise, or (iii) Control the management or affairs of the other enterprise.

10 Section 5(d) of the Competition Act, 2002 (as amended).

11 As per Regulation 4(1) of the 2024 Combination Regulations, the value of transaction shall include every valuable consideration, whether direct or indirect, immediate or deferred, cash or otherwise, including but not limited to, the following consideration: – (a) for any covenant, undertaking, obligations or restrictions imposed on seller or any other person, if such consideration is agreed separately; (b) for all inter-connected steps and transactions, as provided in sub-regulation (4) and (5) of regulation 9 of these regulations; (c) payable during two years from the date on which the transaction would come into effect for arrangement(s) entered into as a part of the transaction or incidental thereto including but not limited to technology assistance, licensing of intellectual property rights, usage rights of any product, service or facility, supply of raw materials or finished goods, branding and marketing; (d) for call option and shares to be acquired thereof assuming full exercise of such option; (e) payable, as per best estimates, based on the future outcome specified under the transaction documents.

- c. its turnover during the preceding financial year in India is:
 - i. 10% or more of its total global turnover derived from all the products and services; and
 - ii. More than INR 5 billion (USD 57.7 million approx).

However, each clause (ii) of clauses (b) and (c) above, are not applicable to digital services.¹²

Additionally, the CCI has illustrated the method of estimating the ‘value of a transaction’ in the 2024 Combination Regulations. Value of a transaction shall include every valuable consideration, whether direct or indirect, immediate or deferred, cash or otherwise, including but not limited to the consideration, (a) for any covenant, undertaking, obligation or restrictions imposed on seller or any other person, if such consideration is agreed separately; (b) for all inter-connected steps and transactions; (c) payable during two years from the date on which the transaction would come into effect for arrangement(s) entered into as a part of the transaction or incidental thereto; (d) for call option and shares to be acquired thereof assuming full exercise of such option; (e) payable, as per best estimates, based on the future outcome specified under the transaction documents. However, the 2024 Combination Regulations further provide that in the event a best estimate cannot be arrived at by the board of directors, the deal value threshold shall be deemed to be breached.

C. Minimum Value of Assets and Turnover

The CCI, through the MVAT Rules, continues to exempt certain enterprises from the provisions of Section 5 of the Act. Such enterprises are those that are party to any form of combination described under Section 5 of the Act – acquisitions and mergers / amalgamations alike – and, where the value of assets of the target entity or the merged entity is not more than INR 4.5 billion (USD 51.9 million approx.) in India or turnover is not more than INR 12.5 billion (USD 144.1 million approx.) in India.¹³ Further, the exemption also extends to specific situations where a portion of an enterprise or division or business is being acquired, taken control of, merged or amalgamated with another enterprise. In such cases, the value of assets and turnover of the said portion will be the relevant assets and turnover to be taken into account for the purposes of this exemption. This results in the entire enterprise value being disregarded in cases where it is the commercial intent for the acquirer to acquire only a portion of an enterprise. Further, it is essential to understand the applicability of the MVAT Rules in light of the DVT rule. Essentially, if the value of a transaction breaches the deal value threshold, the applicability of MVAT will cease to exist for such a transaction.

D. Pre-Filing Consultation

Any enterprise which proposes to enter into a combination may submit a request in writing to the CCI, for a consultation with the officials of the CCI about whether their proposed transaction qualifies as a combination or if such transaction is required to be notified to the CCI in Form I or Form II. However, advice provided by the CCI during such pre-filing consultation is not binding on the CCI.

¹² Explanation 1 to Regulation 4(2) of the 2024 Combination Regulations.

¹³ Rule 3, MVAT Rules, 2024.

E. Mandatory Reporting before Consummation of the Combination

Section 6 makes void any combination which causes or is likely to cause an AAEC within India. Accordingly, Section 6 of the Competition Act requires every acquirer to notify the CCI of a combination prior to consummating the proposed combination, but only after (i) receiving approval from the Board of Directors of the concerned enterprises; or (ii) execution of any agreement or other document for acquisition or acquisition of control.¹⁴ The CCI must form a prima facie opinion on whether a combination has caused or is likely to cause an AAEC within the relevant market in India. The combination can be consummated only after the expiry of 150 days from the date on which notice is given to the CCI, or after the CCI has passed an order approving the combination. The newly added Section 6A of the Competition (Amendment) Act, 2023 grants open offers or an acquisition of shares or securities convertible into other securities (through a series of transactions on a regulated stock exchange) an exemption from the requirements of Section 6(2A) as long as: (i) notice was filed with the Commission in the prescribed manner and time; and (ii) the acquirer does not exercise any ownership or beneficial rights or interest in such securities including voting rights, receipt of dividends or any other distributions, except those specified by the regulations, until approval from the Commission has been received.¹⁵

F. Inter-connected transactions

In order to ensure that all the combinations arising from small individual transactions which otherwise in isolation may not qualify the financial thresholds mentioned above but along with inter-connected or inter-dependent transactions¹⁶ may qualify the financial thresholds are notified to CCI, the 2024 Combinations Regulations provide that in a situation where the ultimate intended effect of a business transaction is achieved by way of a series of steps or smaller individual transactions which are interconnected or inter-dependent on each other, one or more of which may amount to a combination, a single notice, covering all these transactions, may be filed by the parties to the combination.¹⁷

G. Green Channel

In furtherance of the Government of India's ease of doing business initiatives, the CCI introduced certain important amendments to its Combination Regulations on August 13, 2019 ("2019 Amendment Regulations") which came into effect from August 15, 2019. These amendments have now taken the form of the Green Channel Rules, 2024.

The Green Channel Rules provide for a deemed approval route, whereby parties that meet the criteria described below need not wait for the approval of the CCI to consummate a notifiable transaction ('Green Channel'). Once the acknowledgment of the form filed under this Green Channel route has been received by the parties, the transaction will be deemed approved, and parties will be able to consummate the transaction immediately.¹⁸

¹⁴ Section 6(2) of the Competition Act.

¹⁵ Section 6A, Competition (Amendment) Act, 2023; Section 6(2A), Competition Act, 2002.

¹⁶ Regulation 5(9) and 9(4), Competition Commission of India (Procedure in regard to the Transaction of Business relating to Combinations) Regulations, 2011.

¹⁷ Regulation 9(4).

¹⁸ Regulation 5(A), Competition Commission of India (Procedure in regard to the Transaction of Business relating to Combinations) Regulations, 2011.

To avail of the benefit of the Green Channel route, the qualifying criteria is that the parties to the combination, their group entities and their affiliates¹⁹ should not: (i) produce/provide similar or identical or substitutable product or service or; (ii) engage in any activity relating to production, supply, distribution, storage, sale and service or trade in product or service which are at different stage or level of production chain or; (iii) engage in any activity relating to production, supply distribution, storage, sale and service or trade in product or service which are complementary to each other. Notably, the term “commercially sensitive information” remains undefined in both the Competition Act and the revised merger control regime. Additionally, the Green Channel Rules confirms CCI’s practice that requires parties to identify and report overlaps between the acquirer’s ultimate controlling entity (along with its affiliates or group) and the target enterprise. This analysis will also have to be undertaken while considering all plausible alternative market definitions.

The acquirer would also be required to make a positive declaration confirming that the combination falls under the Green Channel (meaning there are no overlaps at any level as discussed above). If it is found that either such declaration or any other statement made by the acquirer in the form is incorrect then the form and deemed approval of the CCI shall both be considered void ab initio. The parties will however have an opportunity to be heard before the CCI renders the approval *void ab initio*.

H. Criterion for Exemption to Combinations

The Exemption Rules²⁰ replaced Schedule I of the Combination Regulations, which previously outlined exemptions from the requirement to notify, such as for minority share acquisitions, intra-group transactions, bonus issues, stock splits, and creeping acquisitions. The key changes brought by the Exemption Rules are as follows:

■ Revised Minority Share Acquisition Exemption

The former exemption for minority share acquisitions has been divided into two distinct exemptions:

i. *Acquisitions in the Ordinary Course of Business (OCB):*

- This applies to acquiring shares in the OCB. Earlier, the CCI interpreted OCB as transactions driven by short-term price movements in securities. Now, Rule 1 limits OCB to acquisitions by underwriters, stockbrokers, and mutual funds.
- The exemption applies provided the acquirer does not exceed the following thresholds:
 - Underwriters: <25% of unsubscribed shares
 - Stockbrokers: <25% of shares
 - Mutual funds: <10% of shares

¹⁹ (a) the parties to the combination and their respective group entities means— (i) the ultimate controlling person of the acquirer and other entities forming part of the same group; (ii) the enterprise being acquired and its downstream entities forming part of its group; (iii) enterprises being merged or amalgamated, their controlling persons, and entities forming part of their group.
(b) an enterprise is considered to be an affiliate of another enterprise if that another enterprise has— (i) ten per cent. or more of the shareholding or voting rights of the enterprise; or (ii) right or ability to have a representation on the board of directors of the enterprise either as a director or as an observer; or (iii) right or ability to access commercially sensitive information of the enterprise.

²⁰ CCI (Criteria for Exemption of Combinations) Rules, 2024.

ii. *Acquisitions undertaken ‘solely as an investment’:*

- This relates to acquiring less than 25% of shares or voting rights in the target without gaining control or the ability to access commercially sensitive information (CSI), strictly for investment purposes, provided:
 - The acquirer does not obtain board representation or observer rights.
 - There are no horizontal, vertical, or complementary overlaps. If overlaps exist, the exemption is allowed only if the acquirer holds less than 10% of shares or voting rights after the acquisition.
- **Exemption for Incremental Shareholding or Voting Rights**
 - a) Existing shareholders with less than 25% of shares or voting rights may acquire additional shares without notification, provided it does not result in control or access to CSI or the acquirer or its group do not gain a right to have representation on the board of directors (either as a director or an observer).
 - b) If no overlaps exist, the acquirer may acquire up to 25%.
 - c) If overlaps exist, there is a 5% cap on additional acquisitions.
 - d) If the acquirer’s shareholding increases from below 10% to above 10% due to overlaps, the exemption is unavailable.
- **Intra-group Transactions Exemption**
 - a) A “group” under the Competition Act, 2002, includes entities that hold 26% or more voting rights, control board appointments, or manage another entity’s affairs.
 - b) *Share and Voting Rights:* Acquisitions by a group entity holding 50% or more shares or voting rights in the target are exempt, provided control does not change.
 - c) *Asset Acquisitions:* Acquisitions within the same group are exempt unless control over the assets changes.
 - d) *Mergers and Amalgamations:* Intra-group mergers or amalgamations are exempt if they do not result in a change in control.
- **‘Change in Control’ Test**

The Amendment Act introduces the “material influence” standard into the definition of control. Previously, exemptions like bonus issues or stock splits were based on a change in control from joint to sole control. The Exemption Rules now apply a uniform test of ‘change in control’ for these exemptions, meaning they are valid as long as no change in control occurs. Whether changes between different levels of control (not just joint to sole) qualify remains to be clarified.

- **Demerger Exemption**

The Exemption Rules now cover demergers and the issuance of shares to the demerged company or its shareholders as consideration for the demerger.

The Exemption Rules, as well as the Green Channel Rules, lay down a specific definition for ‘group’ and ‘affiliate’, as follows:

- a. the parties to the combination and their respective group entities means;
 - i. the ultimate controlling person of the acquirer and other entities forming part of the same group;
 - ii. the enterprise being acquired and its downstream entities forming part of its group;

- iii. enterprises being merged or amalgamated, their controlling persons, and entities forming part of their group.
- b. an enterprise is considered to be an affiliate of another enterprise if that another enterprise has;
 - i. ten per cent. or more of the shareholding or voting rights of the enterprise; or,
 - ii. right or ability to have a representation on the board of directors of the enterprise either as a director or as an observer; or,
 - iii. right or ability to access commercially sensitive information of the enterprise.

I. Miscellaneous Changes Brought About by the New Merger Control Regime

Some of the key changes to the merger control regime, such as the inclusion of the Deal Value Thresholds, substantial business operations' and 'value of transactions' illustration, etc. were discussed above. Some other changes to the merger control regime to bear in mind are as follows:

- i. **Open Offer Exemptions** – The Competition Amendment Act permits implementation of (a) an open offer; or (b) the acquisition of convertible securities through a series of transactions on a regulated stock exchange forming part of a combination prior to the approval by CCI, if (i) the notice of the acquisition is filed with the CCI in the manner set out in the Competition Act, and (ii) the acquirer, in the aforesaid case, shall not exercise any ownership or beneficial rights or voting rights or receive dividends / any other distributions, unless otherwise specified in the regulations till the CCI approves such acquisition. Further, as per the 2024 Combination Regulations, prior to obtaining the CCI's approval, the acquirer can undertake the following actions: (i) avail economic benefits such as dividend or any other distribution, subscription to rights issue, bonus shares, stock-splits and buy-back of securities; and (ii) exercise voting rights in matters related to liquidation or insolvency proceedings. However, the acquirer or any of its group entities or affiliates shall not, directly or indirectly, influence the enterprise whose shares or securities are being acquired, in any manner whatsoever.
- ii. **Increased Filing fees for Form I and Form II** – The filing fees for notifying the CCI of a proposed combination in Form I and Form II was previously INR 2 million (USD 23 thousand approx.) and INR 6.5 million (USD 75 thousand approx.) (USD 78,000) respectively. Form I filing fees is proposed to be increased to (USD 34.6 thousand approx.) (USD 36,000) and Form II fees is proposed to be increased to INR 9 million (USD 103.8 thousand approx.) (USD 108,000) under the Draft Regulations.
- iii. **Prima Facie Opinion** – The CCI is now required to form a prima facie opinion on a combination within 30 calendar days and in the event that the CCI does not form a prima facie opinion within the above timelines, the combination shall be deemed to have been approved.
- iv. **Material Influence** – The definition for "control" has now included within its ambit the aspect of "material influence". This is in line with the decisional practice of the CCI. Material influence implies the presence of factors that give an enterprise/person the ability to influence the affairs and management of the other enterprise, including factors such as shareholding, special rights, status and expertise of an enterprise or person, board representation, structural/financial arrangements, etc.

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I. Foreign Investment

India's story with respect to exchange control is one of a gradual, deliberate and carefully monitored advance towards full capital account convertibility. Though significant controls have been removed and foreign companies can freely acquire Indian companies across most sectors, these are subject to strict pricing and reporting requirements imposed by the Central Government and the RBI.

Investments in and acquisitions (including deferred) of Indian companies by non-resident entities and individuals are governed by the terms of the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 (**"Non-Debt Instruments Rules"**), and the press notes issued by the Department of Industrial Policy and Promotion, Government of India.

The Ministry of Finance, on October 15, 2019 notified Sections 139, 143 and 144 of the Finance Act, 2015 which had proposed amendments to certain sections of the Foreign Exchange Management Act, 1999 (**"FEMA"**), being Section 6 (Capital Account Transactions), Section 46 (Power of Central Government to make rules) and Section 47 (Power of RBI to make regulations) respectively.

The Non-Debt Instrument Rules were notably amended on January 24, 2024 (**"Amendment Rules 2024"**) and subsequently on August 16, 2024 (**"Fourth Amendment Rules"**) (Amendment Rules 2024 and Fourth Amendment Rules will cumulatively be referred to as the **"Amendments to Non-Debt Instruments Rules"**). The Amendment Rules 2024 brought about a new definition of the term **"International Exchange"**, revamped the definition of **"listed Indian company"**, added a new chapter (Chapter X) on investment in equity shares of public Indian companies listed or to be listed on International Exchanges, alongside Schedule XI to provide for a framework for public Indian companies to issue or offer equity shares on specified International Exchanges, to name a few.¹

The Fourth Amendment Rules have been introduced pursuant to the Finance Minister's announcement in the Union Budget 2024-25 to simplify the rules and regulations governing foreign investment. One of the key amendments through the Fourth Amendment Rules is the insertion of Rule 9A, where the transfer of equity instruments of an Indian company between a person resident in India and a person resident outside India may be conducted through a swap of equity instruments, subject to compliance with the rules prescribed by the Central Government and the regulations specified by the Reserve Bank of India (RBI) from time to time. Additionally, a swap of equity capital of a foreign company is permitted, provided it adheres to the rules set by the Central Government, including the Foreign Exchange Management (Overseas Investment) Rules, 2022, and the relevant RBI regulations. In instances where Government approval is necessary, it must be obtained prior to the transfer in all applicable cases.

The Non-Debt Instruments Rules segregate foreign investments into various types: person resident outside India, foreign portfolio investor (FPI), non-resident Indian (NRI) or an Overseas Citizen of India (OCI), other nonresident investors and foreign venture capital investments (FVCI).²

¹ Foreign Exchange Management (Non-Debt Instruments) Amendment Rules, 2024.

² Chapter III-VII, Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.

A. Key definitions in the Non-Debt Instruments Rules

- **“Non-Debt Instruments”** has been defined as: (i) all investments in equity instruments in incorporated entities: public, private, listed and unlisted; (ii) capital participation in LLP; (iii) all instruments of investment recognized in the FDI Policy notified from time to time; (iv) investments in units of AIFs, REITs and InvITs; (v) investment in units of mutual funds of Exchange-Trade Fund which invest more than 50% in equity; (vi) junior-most layer (i.e. equity tranche) of securitization structure; (vii) acquisition, sale or dealing directly in immovable property; (viii) contribution to trusts; and (ix) depository receipts issued against equity instruments. It must be noted that FI Regulations did not allow for foreign direct investment in trusts except VCF and investment vehicles. The Non-Debt Instruments Rules specifically include contribution to trusts in the definition of non-debt instruments.
- **“Debt Instruments”** has been defined to mean all instruments other than non-debt instruments as defined above.
- **“Equity Instruments”** means equity shares (including partly paid-up), convertible debentures, preference shares and share warrants issued by an Indian company.
- **“Hybrid Securities”** has been introduced in the Non-Debt Instruments Rules to mean hybrid instruments such as optionally or partially convertible preference shares or debentures and such other instruments as specified by the Central Government from time to time, issued to a person resident outside India by an Indian company or a trust. However, the term ‘Hybrid Security’ has not been used anywhere in the Non-Debt Instruments Rules.
- **‘Foreign Investment’**, means any investment made by a person resident outside India on a repatriable basis in equity instruments of an Indian company or to the capital of a LLP. The definition further includes an explanation that in the event any declaration is made by a person as per the provisions of the CA, 2013, stating that the beneficial interest in the securities is being held by a person resident outside India, then even though the investment is made by a resident Indian citizen, the same shall be counted as foreign investment.
- **‘Investment’** means to subscribe, acquire, hold or transfer any security or unit issued by a person resident in India.
- **‘Foreign Portfolio Investment’** means any investment made by a person resident outside India through equity instruments where such investment is less than ten percent of the post issue paid-up share capital on a fully diluted basis of a listed Indian company or less than ten percent of the paid-up value of each series of equity instrument of a listed Indian company.
- **‘Foreign Direct Investment’** means investment through equity instruments by a person resident outside India in an unlisted Indian company; or in ten per cent or more of the post issue paid-up equity capital on a fully diluted basis of a listed Indian company
- The definition of **‘Sectoral Cap’** has been amended under the Amendment to the Non-Debt Instruments Rules to omit “debt” meaning the composite sectoral cap under the Non-Debt Instruments Rules will now include only (i) foreign investment on a repatriable basis by persons resident outside India in equity instruments of a company or capital of an LLP; and (ii) indirect foreign investment.
- The definition of **‘Control’** has been modified in the Fourth Amendment Rules to ensure consistency with other legislations, namely the Companies Act 2013. The definition of “Control” under the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 was amended by the Fourth Amendment Rules, 2024, to align it with the Companies Act, 2013. The revised definition now includes the right to appoint a majority of directors or to control management or policy decisions, whether exercised directly or indirectly, individually or in concert, through shareholding, management rights, shareholders’

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agreements, voting agreements, or any other means. This amendment ensures consistency across Indian corporate and foreign investment laws, providing greater clarity and uniformity in determining control for regulatory and compliance purposes.

- The definition of 'Startup' under the Fourth Amendment Rules have been aligned with the definition set out in the notification of the Government of India number G.S.R. 127 (E), dated the 19th February, 2019 issued by the Department for Promotion of Industry and Internal Trade, Ministry of Commerce and Industry.
- The definition of 'International Exchange' has been added through the Amendment Rules 2024, to mean permitted stock exchange in permissible jurisdictions which are listed under the newly added 'Direct Listing of Equity Shares of Companies Incorporated in India on International Exchanges Scheme' under Schedule XI of the Rules.

B. Foreign Direct Investment (FDI)

FDI means investment through equity instruments by a person resident outside India in an unlisted Indian company; or in 10% or more of the post-issue paid-up equity capital on a fully diluted basis of a listed Indian company. In case an existing investment by a person resident outside India in equity instruments of a listed company falls to a level below 10%, of the post-issue paid-up capital on a fully diluted basis, the investment shall continue to be treated as FDI.

Schedule I of the Non-Debt Instruments Rules contains the Foreign Direct Investment Scheme ("FDI Scheme") and sets out the conditions for FDI in India. Sectors in which FDI is prohibited include lottery business, gambling and betting including casinos, chit funds, Nidhi company, trading in transferable development rights and real estate business or construction of farm houses, manufacturing of cigars or tobacco, sectors not open to private sectors such as atomic energy, railway operations, foreign technology collaborations such as franchise, trademark, brand name, management contract is also prohibited for lottery business and gambling and betting activities.³ Entry routes and sectoral caps are prescribed for sectors specifically permitted under the FDI Scheme. In sectors or activities not listed under the FDI Scheme or prohibited, foreign investment is permitted up to 100% through the automatic route, subject to applicable laws and specified conditionalities.

Automatic Route and Government Approval Route: Automatic route means the entry route where investment by a person resident outside India does not require the prior approval of the RBI or the Central Government. Government route, on the other hand, requires prior government approval and foreign investment received under this route is subject to conditions stipulated by the government in its approval.

Earlier, the determination of automatic route or approval route was made based on the sector in which the investee company operates. However, pursuant to Press Note 3 published on April 17, 2020,⁴ the Government of India has prescribed mandatory government approval route for all investments made by any entity of a country that shares land border with India, i.e., Bangladesh, China (including Hong Kong), Pakistan, Nepal, Myanmar, Bhutan and Afghanistan. Further, this requirement shall also be applicable in case where any beneficial owner of an investment into India is situated in or is a citizen of any such countries. Accordingly, all investments from neighbouring countries, regardless of the sector in which the investee company operates, would require prior government approval.

³ Schedule I, Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.

⁴ Press Note 3 (2020 Series) Available at https://dipp.gov.in/sites/default/files/pn3_2020.pdf.

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The onus of compliance with sectoral or statutory caps on foreign investment and attendant conditions, if any, is on the company receiving foreign investment. A foreign investor can acquire equity shares, compulsorily convertible preference shares, convertible debentures or share warrants⁵ in an Indian company up to the investment (or sectoral) caps for each sector provided in the FDI Scheme. Subsequent to the abolition of the Foreign Investment Promotion Board (“FIPB”), which provided prior approval as required for certain sectors, the Government of India, vide an Office Memorandum dated June 5, 2017, has entrusted the work of granting government approval for foreign investments to the concerned administrative ministries/departments of the Government and for certain specific situations, to the DIPP, now renamed as DPIIT, in accordance with the standard operating procedure for processing FDI.⁶

Issuance by Indian company:⁷ An Indian company may issue equity instruments to a person resident outside India subject to entry routes, sectoral caps, pricing guidelines and attendant conditionalities prescribed in the FDI Scheme.

Issuance by listed Indian company:⁸ A person resident outside India may purchase equity instruments of a listed Indian company on a stock exchange in India, provided that the person making the investment has already acquired control of such company in accordance with SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011 and continues to hold such control and the amount of consideration may be paid as per the mode prescribed by RBI or out of the dividend payable by the Indian investee company; provided further that such dividend is credited to a specially designated non-interest bearing rupee account for acquisition of shares on the recognized stock exchange.

Issuance against pre-incorporation expenses:⁹ A wholly owned subsidiary set up in India by a non-resident entity, operating in a sector where 100% foreign investment is allowed under the automatic route and there are no FDI linked performance conditions, may issue equity instruments to the said non-resident entity against pre-incorporation or pre-operative expenses incurred by the non-resident entity up to a limit of 5% of its authorized capital or USD 500 thousand (INR 43.4 million approx.), whichever is less.

Issuances by Indian company for other consideration:¹⁰ An Indian company may issue equity instruments to a person resident outside India, against –

- a. swap of equity instruments; or
- b. import of capital goods or machinery or equipment (excluding second-hand machinery); or
- c. pre-operative or pre-incorporation expenses (including payments of rent etc.)
- d. swap of equity capital of a foreign company in compliance with the rules prescribed by the Central Government including Foreign Exchange Management, (Overseas Investment) Rules 2022, and the Regulations specified by the Reserve Bank from time to time.

In case of swap of equity instruments, valuation involved in the swap arrangement is required to be made by a merchant banker registered with SEBI or an investment banker outside India registered with the appropriate authority in the host country.

5 A foreign investor may also subscribe to preference shares. However, in order to fall under the automatic route, the preference shares / debentures must be compulsorily convertible into equity, failing which the investment will be treated as a debt and the External Commercial Borrowings (ECB) policy will be applicable.

6 <https://fipb.gov.in/Forms/SOP.pdf>.

7 Schedule I (1)(a), Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.

8 Schedule I (1)(b), Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.

9 Schedule I (1)(c), Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.

10 Schedule I (1)(d), Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.

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An Indian company may issue equity shares against any funds payable by it to a person resident outside India, the remittance of which is permitted under FEMA, the Non-Debt Instrument Rules and corresponding rules.

C. Foreign Portfolio Investors

Foreign portfolio investors registered with the SEBI as per the SEBI (Foreign Portfolio Investment) Regulations, 2019 are permitted to invest in equity instruments of an Indian company listed or to be listed on a recognized stock exchange in India subject to the conditions set forth under Schedule II of the Non-Debt Instruments Rules:

- a. Total holding by each FPI or an investor group, is less than 10% of the total paid-up equity capital on a fully diluted basis or less than 10% of the paid-up value of each series of debentures or preference shares or share warrants issued by Indian company (individual limits), and the total holdings of all FPIs put together, is not exceeding 24% of paid-up equity capital on a fully diluted basis or paid-up value of each series of debentures or preference shares or share warrants (aggregate limit); provided this aggregate limit may be increased by the Indian company up to the sectoral cap/statutory ceiling, with approval of its board of directors and general body through a resolution and a special resolution, respectively. Once the aggregate limit has been increased to a higher threshold, the Indian company cannot reduce the same to a lower threshold; provided further that the aggregate limit with respect to an Indian company in a sector where FDI is prohibited shall be 24%.
- b. An FPI may purchase equity instruments of an Indian company through public offer or private placement, subject to individual and aggregate limited specified.
- c. An FPI may purchase units of domestic mutual funds or Category III Alternative Investment Fund or offshore fund for which no objection is issued in accordance with SEBI (Mutual Fund) Regulations, 1996, which in turn invest more than 50% in equity instruments on repatriation basis subject to the terms and conditions specified by the SEBI and the RBI.
- d. An FPI may purchase units of REITs and InVITs on repatriation basis subject to terms specified by SEBI.

D. Non-Resident Indian (“NRI”) or Overseas Citizen of India (“OCI”) on Repatriation Basis

An NRI or OCI may purchase or sell equity instruments of a listed company on repatriation basis, on a recognized stock exchange in India through a branch designated by an Authorised Dealer for the purpose; and the total holding by any individual NRI or OCI shall not exceed 5% of the total paid-up equity capital on a fully diluted basis or shall not exceed 5% of the paid-up value of each series of debentures or preference shares or share warrants issued by Indian company; and the total holdings of all NRIs and OCIs put together shall not exceed 10% of the total paid-up equity capital on a fully diluted basis or shall not exceed 10% of the paid-up value of each series of debentures or preference shares or share warrants; provided that this 10% limit may be raised to 24% if a special resolution to that effect is passed by the general body of the Indian company.

An NRI or OCI may without limit purchase or sell units of domestic mutual funds which invest more than 50% in equity.

E. NRI or OCI on Non-Repatriation Basis

An NRI or OCI, including a company, a trust and a partnership firm incorporated outside India and owned and controlled by NRIs or OCIs, may purchase or contribute towards the following, on a non-repatriation basis, and such investment is deemed to be domestic investment made at par with the investment by residents:

- a. Equity instrument issued by a company without any limit either on the stock exchange or outside it; and/or
- b. Units issued by an investment vehicle without any limit, either on the stock exchange or outside it; and/or
- c. Capital of a limited liability partnership without any limit; and/or
- d. Convertible notes issued by a startup entity.

An NRI or OCI, including a company, a trust and a partnership firm incorporated outside India and owned and controlled by NRIs or OCIs are not permitted to make any investment in equity instruments or units of a Nidhi company or a company engaged in agricultural or plantation activities or real estate business or construction of farm houses or dealing in transfer of development rights.

F. Investment by Other Non-Resident Investors

Long term investors like sovereign wealth funds (“SWFs”), multilateral agencies, endowment funds, insurance funds, pension funds and foreign central banks may purchase securities subject to terms specified by the RBI and the SEBI.

G. Investment in a Limited Liability Partnership (“LLP”)

A person resident outside India or an entity incorporated outside India, not being an FPI or an FVCI, may contribute to the capital of an LLP operating in sectors or activities where foreign investment up to 100% is permitted under automatic route and there are no FDI linked performance conditions.

H. Foreign Venture Capital Investors (“FVCI”)¹¹

An FVCI registered with the SEBI can invest in:

- a. Securities issued by an Indian company in the following sectors, and whose securities are not listed on a recognized stock exchange at the time of issue of securities:
 - i. Biotechnology;
 - ii. IT related to hardware and software development;
 - iii. Nanotechnology;
 - iv. Seed research and development;

¹¹ Schedule VII, Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.

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- v. Research and development of new chemical entities in pharmaceutical sector;
 - vi. Dairy industry;
 - vii. Poultry industry;
 - viii. Production of bio-fuels;
 - ix. Hotel-cum-convention centers with seating capacity of more than 3000;
 - x. Infrastructure sector.
- b. Units of a VCF or a category I Alternative Investment Fund (“Cat-I AIF”) or units or a scheme or of a fund set up by a VCF or Cat-I AIF.
 - c. Equity or equity linked instrument or debt instrument issued by an Indian ‘start-up’ irrespective of the sector in which the start-up is engaged. The definition of ‘start-up’ is as per the DPIIT’s notification;¹² provided that if the investment is in equity instruments, then sectoral caps, entry routes and attendant conditions apply.

An FVCI may purchase securities or instruments either from issuer of securities/instruments or from any person holding these securities or instruments. FVCI may invest in securities on a recognized stock exchange subject to the provisions of Securities and Exchange Board of India (FVCI) Regulations, 2000.

The FVCI may acquire, by purchase or otherwise, from or transfer by sale or otherwise, to any person resident in or outside India, any security or instrument it is allowed to invest in, at a price that is mutually acceptable to the buyer and the seller/issuer. The FVCI may also receive proceeds of liquidation of VCF or of Cat-I AIF or of schemes or funds set up by the VCFs or Cat-I AIFs.

I. Investment by a Person Resident Outside India in an Investment Vehicle

A person resident outside India (other than a citizen of Pakistan or Bangladesh) or an entity incorporated outside India (other than an entity incorporated in Pakistan or Bangladesh) may invest in units of investment vehicle.¹³ Investment vehicle may issue its units to a person resident outside India against swap of equity instruments of a special purpose vehicle proposed to be acquired by such investment vehicle.

Investment made by an investment vehicle into an Indian entity is considered as indirect foreign investment for the investee Indian entity if the Sponsor or Manager or Investment Manager (a) is not owned and not controlled by resident Indian citizens; or (b) is owned or controlled by person’s resident outside India.

¹² While the definition of ‘startup’ under the rules still refer to the Department for Promotion of Industry and Internal Trade’s Notification No.G.S.R. 364(E), dated the 11th April, 2018, Notification G.S.R. 127(E), February 19, 2019 provides the latest definition of startup as below (which needs to be aligned under the rules): An entity shall be considered as a Startup: i. Up to a period of ten years from the date of incorporation/ registration, if it is incorporated as a private limited company (as defined in the Companies Act, 2013) or registered as a partnership firm (registered under section 59 of the Partnership Act, 1932) or a limited liability partnership (under the Limited Liability Partnership Act, 2008) in India. ii. Turnover of the entity for any of the financial years since incorporation/ registration has not exceeded INR 1 billion (USD 11.5 million approx.). iii. Entity is working towards innovation, development or improvement of products or processes or services, or if it is a scalable business model with a high potential of employment generation or wealth creation. Provided that an entity formed by splitting up or reconstruction of an existing business shall not be considered a ‘Startup’.

¹³ Investment Vehicle means an entity registered and regulated under the regulations framed by the SEBI or any other authority designated for that purpose and shall include, namely: (i) Real Estate Investment Trusts (REITs) governed by the Securities and Exchange Board of India (REITs) Regulations, 2014;(ii)Infrastructure Investment Trusts (InvIts) governed by the Securities and Exchange Board of India (InvIts) Regulations, 2014 (iii) Alternative Investment Funds (AIFs) governed by the Securities and Exchange Board of India (AIFs) Regulations, 2012;.

J. Issue of Convertible Notes by an Indian Startup Company

A person resident outside India (other than an individual who is a citizen of Pakistan or Bangladesh or an entity which is registered or incorporated in Pakistan or Bangladesh) may purchase convertible notes issued by an Indian startup company for an amount of INR 2.5 million (USD 28.9 thousand approx.) or more in a single tranche. Such issuance is required to comply with the entry route, sectoral caps, pricing guidelines and other conditions for foreign investment. Similarly, transfers of a convertible note between a person resident outside India and a person resident in or outside India is also permitted subject to compliance with entry route, sectoral caps, pricing guidelines and other conditions as prescribed. An NRI or an OCI may acquire convertible notes on non-repatriation basis subject to certain conditions of the Non-Debt Instruments Rules.

K. Acquisition of Rights Shares/ Bonus Shares

A person resident outside India may subscribe to shares issued on a rights basis/bonus issuance by an Indian company provided that the offer of shares is in compliance with the provisions of CA 2013, and does not result in breach of sectoral caps applicable to the company, and the price at which the shares are offered to the person resident outside India is not less than the price offered to the resident shareholders. These conditions are also applicable in case a person resident outside India makes investment in shares issued by an Indian company (other than share warrants) as a rights issue that are renounced to a person to whom it was offered, provided however that, if a person resident in India renounces the shares in favour of a person resident outside India, then the pricing guidelines of FEMA must be complied with.

L. Issue of Shares Under Merger/ Amalgamation / Demerger

A transferee company may issue shares to the shareholders of a transferor company under a scheme of merger or amalgamation approved by an Indian court, provided that the sectoral caps mentioned above are not exceeded.

M. Issue of Partly-Paid up Shares and Share Warrants

Currently, only equity shares, compulsorily convertible preference shares and compulsorily convertible debentures and share warrants are permitted under the FDI route as equity instruments.

Partly paid-up equity shares can be issued to person resident outside India if (i) pricing of partly paid shares is determined up front and at least 25% of the total consideration amount (including share premium) is paid up front; and (ii) the remaining amount is invested within a period of 12 months of issuance. As regards the issuance of share warrants, the following conditions must be complied with: (i) pricing and conversion formula / price is required to be determined up front and 25% of the total consideration is required to be paid up front; and (ii) the remaining amount is required to be brought in within a period of 18 months. Further, the price at the time of conversion should not be less than the fair value of the shares as calculated at the time of issuance of such warrants.

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It must also be noted that only companies in which investment can be made under the automatic route can issue partly paid-up equity shares or share warrants. For companies under the approval route, prior approval of concerned administrative ministries/departments of the Government will be required to issue partly paid-up equity shares or share warrants.

N. ESOP and Sweat Equity Shares

An Indian company may issue ‘employees’ stock option’ and/or ‘sweat equity shares’ to its employees or directors or employees or directors of its holding company or joint venture or wholly owned overseas subsidiary or subsidiaries who are resident outside India; provided that (i) the scheme has been drawn in terms of the SEBI (Share Based Employee Benefits and Sweat Equity) Regulations, 2021 under the SEBI Act, 1992 or the Companies (Share Capital and Debentures) Rules, 2014; (ii) such employee stock options or sweat equity shares are in compliance with the sectoral cap applicable to the said company; (iii) issue of employee stock option or sweat equity shares in a company that requires prior government approval should procure such approval prior to issuance (this includes issue of employee stock option or sweat equity shares to a citizen of Bangladesh/ Pakistan or any other country sharing land border with India).

O. Pricing Under the Automatic Route

Acquisition of shares of an Indian company by a person resident outside India under the automatic route may only be made in accordance with the pricing requirements provided in the Non-Debt Instruments Rules. The price of shares issued to non-residents cannot be less than:

- a. the price worked out in accordance with the SEBI guidelines in case of a listed Indian company or in case of a company going through a delisting process as per the SEBI (Delisting of Equity Shares) Regulations, 2021;
- b. the fair value of shares determined as per any internationally accepted pricing methodology for valuation of shares on arm’s length basis duly certified by a chartered accountant or a merchant banker registered with SEBI or a practicing cost accountant, in case of an unlisted Indian company.

P. Investment in Depository Receipts

Any security or unit in which a person resident outside India is allowed to invest under the Non-Debt Instruments Rules are eligible instruments for issue of depository receipts¹⁴ in terms of Depository Receipts Scheme, 2014 (“DR Scheme”).

Companies incorporated outside India may issue Indian Depository Receipts¹⁵ (IDRs) through a domestic depository, to persons resident in India and outside India subject to such issue being in compliance with the Companies (Registration of Foreign Companies) Rules, 2014 and the ICDR Regulations, be denominated

¹⁴ Depository receipt means a foreign currency denominated instrument, whether listed on an international exchange or not, issued by a foreign depository in a permissible jurisdiction on the back of eligible securities issued or transferred to that foreign depository and deposited with a domestic custodian and includes ‘global depository receipt’ as defined in the Companies Act, 2013 (18 of 2013);.

¹⁵ Indian Depository Receipts means any instrument in the form of a depository receipt created by a domestic depository in India and authorised by a company incorporated outside India making an issue of such depository receipts;.

in Indian rupee only and the proceeds of issue of IDRs be immediately repatriated outside India by companies issuing such IDRs. Any issue of IDRs by financial or banking companies having presence in India, either through a branch or subsidiary, requires prior approval of the sectoral regulator.

Q. Investment in Equity Shares of Indian Incorporated Companies on International Exchanges

Pursuant to an amendment made to the Non-Debt Instrument Rules,¹⁶ a public company is allowed to issue or offer equity shares of existing shareholders, subject of fulfillment of eligibility criteria¹⁷ and qualification as a ‘permissible holder’,¹⁸ so long as such issuance or offer of equity shares of existing shareholders is:

- i. permitted and such shares are listed on any of the specified International Exchange;¹⁹
- ii. subject to prohibited activities, and sectoral caps as specified in Schedule I of Non-Debt Instruments Rules; and
- iii. such issue/offer on International Exchange is in dematerialised form and ranks pari passu with equity shares listed on a recognised stock exchange in India

Provided that prior Government approval, wherever applicable, shall be obtained.

II. Indirect Foreign Investment

Foreign investment may be direct or indirect. Generally speaking (and subject to certain exceptions) if:

- a. an Indian investing company is (i) not “owned” and “controlled” by resident Indian citizens; or (ii) is owned or controlled by persons resident outside India; or
- b. an investment vehicle whose sponsor or manager or investment manager (i) is not owned and not controlled by resident Indian citizens; or (ii) is owned or controlled by person resident outside India;

then the entire investment by the investing company into the subject downstream Indian investee company would be considered as indirect foreign investment.

An Indian entity that has received indirect foreign investment is required to comply with entry route, sectoral caps, pricing guidelines and other conditions as applicable for foreign investment. Further, it has been clarified that an investment made by an Indian entity which is owned and controlled by NRI(s), on a non-repatriation basis, shall not be considered for calculation of indirect foreign investment.²⁰ Subsequent to the August 16, 2024 amendment to the Non-Debt Instruments Rules (Foreign Exchange Management (Non-Debt

¹⁶ Schedule XI, as added through Foreign Exchange Management (Non-Debt Instruments) Amendment Rules, 2024.

¹⁷ Such as the public Indian company/its promoters/directors etc. not being a willful defaulter, not debarred from accessing the capital market, not under inspection or investment under the Companies Act, 2013 etc.: Schedule XI (3), as added through Foreign Exchange Management (Non-Debt Instruments) Amendment Rules, 2024.

¹⁸ “Permissible holder means a holder of equity shares of the Company which are listed on International Exchange, excluding its beneficial owner”; Further, if the holder is a citizen of a country sharing land border with India, or an entity incorporated in such a country, or an entity whose beneficial owner is from such a country, then it shall hold equity shares of such public Indian company only with the approval of the Central Government.

¹⁹ International Financial Services Centre in India – India International Exchange, NSE International Exchange: Annexure, Foreign Exchange Management (Non-Debt Instruments) Rules, 2019.

²⁰ Notification S.O. 3206(E), dated August 06, 2021 issued by Department of Economic Affairs, Ministry of Finance.

Instruments) Fourth Amendment Rules, 2024), an investment made by an Indian entity which is owned and controlled by a Non-Resident Indian or an Overseas Citizen of India including a company, a trust and a partnership firm incorporated outside India and owned and controlled by a Non-Resident Indian or an Overseas Citizen of India, on a non-repatriation basis in compliance with Schedule IV of the Fourth Amendment Rules, shall not be considered for calculation of indirect foreign investment.²¹

III. Transfer of Equity Instruments of an Indian Company by or to a Person Resident Outside India

The Non-Debt Instruments Rules have detailed the provisions in relation to transfer of equity instruments of an Indian company by or to a person resident outside India. A person resident outside India, holding equity instruments of an Indian company, or units of a person resident in India, may transfer such equity instruments or units so held by him in compliance with the conditions specified:

- a. Transfer by non-resident (not NRI / OCI / erstwhile overseas body corporate) to non-resident: a person resident outside India, not an NRI or an OCI or an erstwhile overseas corporate body, may transfer by way of sale or gift the equity instruments of an Indian company or units held by him to any person outside India; this may also include transfer of equity instruments of an Indian company pursuant to liquidation, merger, de-merger, amalgamation of entities or companies incorporated or registered outside India.

Where the equity instruments are held by person resident outside India on a non-repatriable basis, the transfer by way of sale where the transferee intends to hold the equity instruments on a repatriable basis, is required to comply with the entry routes, sectoral caps or investment limits, pricing guidelines, documentation and reporting requirements for such transfers, as prescribed from time to time.

- b. Transfer by sale or gift or sale on stock exchange: Person resident outside India, holding equity instruments of an Indian company or units may transfer the same to person resident in India by way of sale or gift or may sell the same on a recognized stock exchange in India in the manner specified by SEBI; provided that such transfer is required to comply with entry routes, sectoral caps or investment limits, pricing guidelines, documentation and reporting requirements for such transfers, as prescribed from time to time.
- c. Transfer by sale: A person resident in India holding equity instruments of an Indian company or units, may transfer the same to a person resident outside India by way of sale, subject to sectoral caps, investment limits, pricing guidelines or other conditions as applicable for investment by person resident outside India.
- d. Gift by Resident to Non-resident: A person resident in India holding equity instruments or units of an Indian company may transfer the same to a person resident outside India by way of gift with the prior approval of the RBI and subject to the following conditions:
 - i. the donee is eligible to hold such security under the Non-Debt Instruments Rules;
 - ii. gift does not exceed 5% of the paid-up capital of the Indian company or each series of debentures or each mutual fund scheme;
 - iii. the applicable sectoral cap in Indian company is not breached;
 - iv. the donor and donee are 'relatives' as defined under Section 2(77) of Companies Act, 2013;

²¹ Foreign Exchange Management (Non-Debt Instruments) Fourth Amendment Rules, 2024.

Exchange Control

- v. value of the security to be transferred by donor together with any security transferred to any person residing outside India as gift during the financial year does not exceed the rupee equivalent of USD 50 thousand (INR 4.3 million approx).
- e. Transfer of equity instruments with optionality clause: Person residing outside India holding equity instruments of an Indian company containing an optionality clause and exercising the option or right, may exit without any assured return, subject to pricing guidelines and a minimum lock-in period of 1 year or as prescribed, whichever is higher.
- f. Deferred consideration: Transfer of equity instruments between a person resident in India and a person outside India structured as a deferred payment is permitted in the following manner: an amount not exceeding 25% of the total consideration may be paid by the buyer (i) on a deferred basis, within a period not exceeding 18 months from the date of the transfer agreement; or (ii) may be settled through an escrow arrangement between the buyer and seller for a period not exceeding 18 months from the date of the transfer agreement; or (iii) may be indemnified by the seller for a period not exceeding 18 months from the date of payment of the full consideration, if the total consideration has been paid by the buyer to the seller. Provided that the total consideration finally paid is required to comply with the applicable pricing guidelines.
- g. Transfer by pledge: Transfer of equity instruments of an Indian company or units of an investment vehicle by way of pledge is subject to: (i) any person being promoter of a company that has raised ECB in compliance with the Foreign Exchange Management (Borrowing and Lending in Foreign Exchange) Regulations, 2000, may pledge the shares of the borrowing company or of its associate resident companies subject to certain conditions; (ii) any person resident outside India holding equity instruments in an Indian company or units of an investment vehicle may pledge the equity instruments or units in favour of a bank in India/nonbanking financial company to secure credit facilities for bona fide purposes or in favour of an overseas bank to secure credit facilities extended to such person who is the promoter of the Indian company or overseas group company of such Indian company.

In case of invocation of pledge, transfer of equity instruments is required to comply with sectoral caps, pricing guidelines and other conditions at the time of creation of pledge.

- h. Transfer by FPI²²: An FPI holding equity instruments of an Indian company or units may transfer such equity instruments or units held by him in compliance with the conditions specified in Schedule II of the Non-Debt Instruments Rules and by SEBI, provided that, Government approval is sought for relevant sectors requiring the same and also when the acquisition of equity instruments by FPI has resulted in a breach of applicable aggregate FPI limits or sectoral limits.
- i. Pricing guidelines: Price of equity instruments of an Indian company, when such instruments are being transferred from a resident in India to a person resident outside India, cannot be less than:
 - i. The price worked out in accordance with the SEBI guidelines in case of a listed Indian company;
 - ii. The price at which a preferential allotment of shares can be made under the SEBI guidelines, in case of a listed company or in case of a company going through a delisting process as per the Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2009;
 - iii. Valuation of equity instruments done as per any internationally accepted pricing methodology for valuation on an arm's length basis duly certified by a Chartered Accountant or a Merchant Banker registered with SEBI or a practicing Cost Accountant, in case of an unlisted Indian company.

22 Rule 11, as amended by Foreign Exchange Management (Non-Debt Instruments) Amendment Rules, 2019.

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On the other hand, the price of equity instruments of an Indian company, when such instruments are being transferred by a person resident outside India to a person resident in India, cannot exceed:

- i. Price worked out in accordance with the SEBI guidelines in case of a listed Indian company;
- ii. The price at which a preferential allotment of shares can be made under the SEBI guidelines, in case of a listed company or in case of a company going through a delisting process as per the Securities and Exchange Board of India (Delisting of Equity Shares) Regulations, 2009;
- iii. Valuation of equity instruments done as per any internationally accepted pricing methodology for valuation on an arm's length basis duly certified by a Chartered Accountant or a Merchant Banker registered with SEBI or a practicing Cost Accountant, in case of an unlisted Indian company.

The guiding principle being that the person resident outside India is not guaranteed any assured exit price at the time of making such investment or agreement and is required to exit at the price prevailing at the time of exit.

Further, in case of convertible equity instruments, the price or conversion formula of the instrument should be determined upfront at the time of issue of the instrument. The price at the time of conversion should not in any case be lower than the fair value worked out, at the time of issuance of such instrument²³.

IV. Overseas Investment

An Indian company that intends to acquire or invest in a foreign company outside India must comply with the Foreign Exchange Management (Overseas Investment) Rules, 2022 ("OI Rules"), Foreign Exchange Management (Overseas Investment) Regulations, 2022 ("OI Regulations") and Foreign Exchange Management (Overseas Investment) Directions, 2022 ("OI Directions") (collectively referred to as the "OI Laws").

The OI Laws, released by the Government of India and the RBI, overhauled, *inter alia*, the erstwhile Foreign Exchange Management (Transfer or Issue of any Foreign Security) Regulations, 2004, and can be seen as an extension of the process of liberalization initiated by the Government of India in the 1990s. The OI Laws contain detailed provisions governing investments made by an Indian company in a foreign company by grant of 'general permission' to make an 'overseas direct investment ("ODI")' or an 'overseas portfolio investment ("OPI")' in bona fide business activities, subject to compliance with the applicable rules and regulations. While the term ODI has been defined as 'investment by way of acquisition of unlisted equity capital²⁴ of a foreign entity,²⁵ or subscription as a part of the memorandum of association of a foreign entity, or investment in 10%, or more of the paid-up equity capital of a listed foreign entity or investment with control where investment is less than 10% of the paid-up equity capital of a listed foreign entity', the term OPI means 'investment, other than ODI, in foreign securities, but not in any unlisted debt instruments or any security issued by a person resident in India who is not in an IFSC, provided that OPI by a person resident in India in the equity capital of a listed entity, even after its delisting shall continue to be treated as OPI until any further investment is made in the entity'.

23 Notification S.O. 4355(E), dated December 05, 2019 issued by Department of Economic Affairs, Ministry of Finance.

24 "equity capital" means equity shares or perpetual capital or instruments that are irredeemable or contribution to non-debt capital of a foreign entity in the nature of fully and compulsorily convertible instruments.

25 "foreign entity" means an entity formed or registered or incorporated outside India, including International Financial Services Centre that has limited liability, provided that the restriction of limited liability shall not apply to an entity with core activity in a strategic sector.

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The Indian party may choose to fund the ODI out of balances held in Exchange Earner's Foreign Currency (EEFC) account, by drawing funds from an authorized dealer subject to certain limits, or using the proceeds of an ADR/GDR issue, swap of shares, capitalization of exports, or using the proceeds of external commercial borrowings (ECBs).

It has been clarified that the OI Laws shall not apply to acquisition or transfer of any investment outside India made (a) out of Resident Foreign Currency Account; or (b) out of foreign currency resources held outside India by a person who is employed in India for a specific duration irrespective of length thereof or for a specific job or assignment, duration of which does not exceed three years; or (c) foreign currency acquired when the person resident in India was resident outside India or has inherited from a person who was resident outside India.

A. ODI in a Foreign Entity

An Indian company is permitted to invest in all the foreign entities taken together at the time of undertaking ODI up to 400% of its net worth as on the date of the last audited balance sheet²⁶ or as directed by the RBI, in consultation with the Government of India from time to time, without seeking the prior approval of the RBI.

An Indian company making ODI in a foreign entity is required to route all its transactions relating to such investment through the AD bank designated by it. However, different AD banks may be designated, if required, for different foreign entities.

ODI cannot be made if the foreign entity is engaged in real estate activity; gambling in any form or dealing with financial products linked to the Indian rupee without specific approval of the RBI. The term 'real estate activity' means 'buying and selling of real estate or trading in Transferable Development Rights but does not include the development of townships, construction of residential or commercial premises, roads or bridges for selling or leasing.

Any financial commitment in a foreign entity exceeding USD 1 billion (INR 86.7 billion approx.) (or its equivalent) in a financial year will require the prior approval of the RBI even when the total financial commitment of the Indian entity is within the eligible limit under the automatic route (i.e., 400% net worth as per the last audited balance sheet).

ODI by an Indian entity engaged in financial or non-financial services activity into a foreign entity engaged in financial services activities is subject to special requirements.

B. Investment by Way of Capitalization Due to the Indian Company

The OI Laws provide for ODI by way of capitalization, within the time period, if any, specified for realization under FEMA, of any amount due towards the Indian entity from the foreign entity, the remittance of which is permitted under FEMA or does not require prior approval of the Government of India or the RBI.

²⁶ "last audited balance sheet" means audited balance sheet as on date not exceeding eighteen months preceding the date of the transaction.

Exchange Control

The financial commitment limit of 400% of the net worth does not include capitalization of retained earnings.

In case where the proceeds are overdue beyond the period specified for realization/repatriation, before permitting such capitalization, AD bank may grant necessary extension making the requisite application post proper due diligence.

C. Transfer of Shares

An Indian company may transfer equity capital of a foreign entity by way of a sale - either to a person resident in India who is eligible to make such investments under the OI Rules or to a person resident outside India.

If the transfer is on account of merger, amalgamation, demerger or on account of buy-back of foreign securities, such transfer shall have the approval of the competent authority as per the applicable laws in India or the laws of the host country, as the case maybe.

In the event where the disinvestment by the Indian company pertains to ODI - (i) the transferor, in case of full divestment (other than by way of liquidation), shall not have any outstanding dues to be received from the foreign entity; (ii) the transferor, in case of any divestment must have stayed invested for at least one year from the date of making the ODI.

The abovementioned conditions are not applicable in case of transfer by way of merger, demerger or amalgamation between two or more foreign entities that are wholly owned, directly or indirectly, by the Indian company, or where there is no change or dilution in aggregate equity holding of the Indian company in the merged, demerged or amalgamated entity.

Further, unlike the erstwhile regime, disinvestment involving write-off is now permitted under the automatic route.

Furthermore, the OI Laws have, inter alia, dispensed with the requirement of approval for (a) investment / divestment by persons resident in India under investigation by any investigative agency / regulatory body; and (b) write-off on account of disinvestment.

The equity capital of the foreign entity may also be pledged by the Indian company as security, to avail of fund/non-fund-based credit facilities for itself or for the foreign entity.

D. Guarantee by Indian Party

The Indian entity may issue corporate, personal or bank guarantee, subject to certain conditions, to or on behalf of the foreign entity or any of its step-down subsidiary in which the Indian entity has acquired control through the foreign entity.

In case of a guarantee extended by a group company, it is counted towards the utilization of its financial commitment limit independently and in case of a resident individual promoter, the same is counted towards the financial commitment limit of the Indian entity; provided that where the commitment is extended by a group company, any fund-based exposure to or from the Indian entity is deducted from the net worth of such group company for computing its financial commitment limit.

Further, no guarantee is permitted to be open-ended, and the guarantee invoked shall not be a part of the non-fund-based commitment but be considered as lending.

Where a guarantee has been extended jointly and severally by two or more Indian entities, 100% of the amount of such guarantee is reckoned towards the individual limits of each of such Indian entities.

In case of performance guarantee, 50% of the amount of guarantee is reckoned towards the financial commitment limit.

E. Investment by Individuals

The Liberalized Remittance Scheme (“LRS”)²⁷ was introduced on February 4, 2004, as a liberalization measure to facilitate foreign remittance by Indian resident individuals for permitted current or capital account transactions or a combination of both.

An individual may draw from an authorized person, foreign exchange not exceeding USD 2.5 thousand (INR 21.7 million approx.) per financial year (April to March)²⁸ or such amount as decided by RBI from time to time for permitted capital account transactions.

An Indian resident individual may make ODI by way of investment in equity capital or OPI, subject to the overall ceiling under the LRS. Investors can reinvest the income earned from investments made under the LRS.

An Indian resident individual may make ODI in an operating foreign entity not engaged in financial services activity and which does not have subsidiary²⁹ or step down subsidiary where the Indian resident individual has control in the foreign entity; provided that ODI can be made by an Indian resident individual with control in a foreign entity engaged in a financial or a non-financial services activity, regardless of having a subsidiary or a step down subsidiary, by way of (i) inheritance; (ii) acquisition of sweat equity shares; (iii) acquisition of minimum qualification shares issued for holding a management post in the foreign entity; and (iv) acquisition of shares or interest under ESOP or Employee Benefits Scheme:

Provided that the OI Directions permits the Indian resident individuals to make OPI in the units of any investment fund overseas, duly regulated by the regulator for the financial sector in the host jurisdiction, within the overall limit for LRS.

Further, acquisition of less than 10% of the equity capital, whether listed or unlisted, of a foreign entity without control by way of (i) acquisition of sweat equity shares; (ii) acquisition of minimum qualification shares issued for holding a management post in the foreign entity; and (iii) acquisition of shares or interest under ESOP or Employee Benefits Scheme, shall be treated as an OPI.

27 A.P. (DIR Series) Circular No. 64 dated February 4, 2004 (as amended from time to time).

28 Also see Para A1 of Master Direction – LRS (No. 7/2015-16) – Updated as on December 22, 2023.

29 ‘Subsidiary’ or ‘step-down subsidiary’ of a foreign entity means an entity in which the foreign entity has control.

Taxes and Duties

I. Income Tax Act, 1961

Taxation of income in India is governed by the provisions of the ITA as amended by the Finance Acts every year. The ITA contains separate rules for taxation of residents and non-residents. Residents are taxable on worldwide income, while non-residents are taxable only on India-sourced income i.e., only and to the extent that such income accrues or arises or is deemed to accrue or arise in India or is received or deemed to be received in India.¹

The ITA contains specific provisions which govern the classification and computation of income. There are 5 heads of income under which income is chargeable to tax under the ITA, one of them being “Capital Gains”.²

Section 45 of the ITA is the charging provision for capital gains. Section 45 of the ITA levies tax on capital gains arising on the transfer of a capital asset. Section 2(14) of the ITA defines capital asset to mean property of any kind held by an assessee, whether or not connected with his business or profession. Section 2(47) of the ITA defines the term ‘transfer’ in relation to a capital asset to include:

- i. sale, exchange or relinquishment of the asset; or
- ii. extinguishment of any rights therein; or
- iii. compulsory acquisition thereof under any law; or
- iv. in a case where the asset is converted by the owner thereof into, or is treated by him as, stock-in-trade of a business carried on by him, such conversion or treatment; or
- v. maturity or redemption of a zero-coupon bond; or
- vi. any transaction involving the allowing of the possession of any immovable property to be taken or retained in part performance of a contract of the nature referred to in section 53A of the Transfer of Property Act, 1882; or
- vii. any transaction (whether by way of becoming a member of, or acquiring shares in, a co-operative society, company or other association of persons or by way of any agreement or any arrangement or in any other manner whatsoever), which has the effect of transferring, or enabling the enjoyment of, any immovable property.

Income chargeable to tax as capital gains is computed by deducting the following from the value of the consideration received – (a) expenditure incurred wholly and exclusively in connection with such transfer, and (b) cost of acquisition of the capital asset and any cost of improvement of the capital asset.³

Section 48 of the ITA provides for the benefit of indexation of the cost of acquisition for computation of long term capital gain arising on transfer of property, gold, unlisted assets etc. in the hands of the residents (to account for inflation). The Finance Act, 2024 has removed the indexation benefit for computation of long term capital gains considering the reduction in tax rates for long term capital gains (explained in the later sections).

¹ Section 4 read with section 5 of the ITA.

² Section 14 of the ITA.

³ Section 48 of the ITA.

Section 9 of the ITA is the deeming provision relating to the income of non-residents that is considered to have its source in India. As per Section 9(1)(i) of the ITA, income accruing or arising in India (directly or indirectly) through transfer of capital assets situated in India shall be deemed to accrue or arise in India and shall be taxable as such. Hence, if the capital asset is situated in India, it is irrelevant whether the transferor is resident or non-resident for the purpose of taxation under the ITA. A capital asset is deemed to be situated in India if it substantially derives its value (directly or indirectly) from assets situated in India.

The ITA contains several provisions that deal with the taxation of different categories of M&A. The ways in which M&A transactions can be undertaken are:

- Amalgamation (i.e., a merger which satisfies the conditions mentioned below)⁴ or merger;
- Demerger or spin-off;
- Share Sale;
- Slump Sale; and
- Asset Sale

If a merger or any other kind of restructuring results in a transfer of a capital asset (as referred above) for a resident or a capital asset that is situated in India for a non-resident, it may lead to a taxable event.⁵

A. Amalgamation

The ITA defines an ‘amalgamation’ as the merger of one or more companies with another company, or the merger of two or more companies to form one company. The ITA also requires that the following conditions must be met by virtue of the merger, for such merger to qualify as an ‘amalgamation’ under the ITA⁶:

- all the property of the amalgamating company(ies) becomes the property of the amalgamated company;
- all the liabilities of the amalgamating company(ies) become the liabilities of the amalgamated company; and
- shareholders holding not less than 75% of the value of the shares of the amalgamating company become shareholders of the amalgamated company. There is a specific carve out from the satisfaction of this condition in case of amalgamation of a subsidiary into its parent, as it is impossible for the condition to be satisfied in such cases.

Section 47 of the ITA sets out certain transfers that are exempt from the provisions of Section 45 (the charging provision for tax on capital gains) and such transfers are exempt from tax on capital gains. The relevant exemptions are provided below:

- For an amalgamating company (transferor)

⁴ Section 2(1B) of the ITA.

⁵ Capital gains characterization under the ITA also depends on accounting treatment of the transferred asset as ‘capital asset’, frequency of sale, period of holding etc. In case the asset is held as a trading asset and is transferred as part of business, income arising may also be categorized as ‘business income’ under the ITA.

⁶ Section 2(1B) of the ITA.

Section 47(vi): The transfer of a capital asset in a scheme of amalgamation by the amalgamating company to the amalgamated company is exempt from tax on capital gains, provided the amalgamated company is an Indian company.⁷ Please note that for this exemption to be applicable to a merger, it is essential that the merger falls within the definition of ‘amalgamation’ provided above. Special exemptions have also been included in case of amalgamations involving banking companies.⁸

- For the shareholders of the amalgamating company

Section 47(vii): Transfer by the shareholders of an amalgamating company, in a scheme of amalgamation, of shares of the amalgamating company (i.e., the capital asset), as consideration for the allotment of shares of the amalgamated company - is exempt from tax on capital gains, provided that the amalgamated company is an Indian company.⁹ The exemption from tax on capital gains would only be to the extent that the transfer is for the consideration (being shares of the amalgamated company). If any consideration other than shares of the amalgamated company, such as cash or bonds, was paid to the shareholders of the amalgamating company, it may be considered liable to tax on capital gains.¹⁰ If any of the conditions specified above are not satisfied (including the conditions specified in the definition of ‘amalgamation’), the transfer of capital assets in a merger would be subject to tax on capital gains.

- For a foreign amalgamating company (transferor) in connection with transfer of shares in an Indian company

Section 47(via): When a foreign holding company (being the amalgamating company) transfers its shareholding in an Indian company to another foreign company (being the amalgamated company), as a result of a scheme of amalgamation, such a transfer of the capital asset (i.e. shares in the Indian company), should be exempt from tax on capital gains in India (at the foreign amalgamating company), if it satisfies the following conditions:

- i. at least 25% of the shareholders of the amalgamating foreign company continue to be the shareholders of the amalgamated foreign company, and
- ii. such transfer does not attract capital gains tax in the country where the amalgamating company is incorporated.

It may be noted that while the definition of ‘amalgamation’ under Section 2(1B) of the ITA requires that 75% (in terms of value of shares) of the shareholders of the amalgamating company should become the shareholders in the amalgamated company, this section specifies 25% of the number of shareholders as the corresponding figure. The above provisions also indicates that an Indian company amalgamating into a foreign company would lead to the attraction of capital gains tax liability in India.

7 This section only requires that the amalgamated (or the surviving) company must be an Indian company. The amalgamating company may be an Indian company or a foreign company. In this connection it is useful to note that the meaning of the term ‘company’ under the Companies Act differs considerably from the meaning under the ITA. Under the Companies Act, ‘company’ would generally refer to an Indian company (unless specifically provided otherwise). Under the ITA, the term ‘company’ has a much broader meaning and inter alia includes an Indian company and a foreign body corporate (i.e., including a foreign company).

8 Sections 47(viaa), 47(vica), 47(vicb) of the ITA.

9 In this scenario, the shareholders get shares of the amalgamated company in exchange for their shareholding in the amalgamating company, and the amalgamating company is dissolved. It should be noted that the term transfer is used here in the context of the definition of this term under the ITA, which includes the extinguishment of any right in a capital asset. So if the rights of the shareholders in the shares of the amalgamating company are extinguished, it would amount to a transfer (which is exempt from capital gains tax if the conditions specified are complied with).

10 The Gujarat High Court, in CIT v. Gautam Sarabhai Trust, [1988] 173 ITR 216 (Guj) had held that a shareholder receiving any other property other than shares by virtue of a merger would not qualify for the exemption under Section 47(vii).

- For the shareholders/interest holders of a foreign amalgamating company in relation to indirect transfer tax

Section 47(viab) of the ITA provides that any transfer by the shareholders, in a scheme of amalgamation, of shares/interests of a foreign amalgamating company (the capital asset) that derive their value ‘substantially’ from Indian assets¹¹ (indirect transfer), is exempt from tax on capital gains, if it satisfies the following conditions:

- at least 25% of the shareholders of the amalgamating foreign company continue to be the shareholders of the amalgamated foreign company, and
- such transfer does not attract capital gains tax in the country where the amalgamating company is incorporated.

The above, thus, only contemplates a horizontal merger (between two foreign companies), and not a vertical merger of a foreign company merging into its parent (also being a foreign company), as in such an instance, the first condition set out above, cannot possibly be met.

Section 49(1)(iii)(e) of the ITA provides that the cost of acquisition of assets transferred by way of a scheme of amalgamation that are covered by the exemptions under Section 47 mentioned above would be deemed to be the cost of acquisition of the assets in the hands of the amalgamating company (i.e., a cost step-up is not available in the case of amalgamations). Similarly, Section 49(2) provides that the cost of acquisition for a shareholder, of shares of the amalgamated company, is deemed to be the cost of acquisition of the shares of the amalgamating company.

B. Demerger

The term ‘demerger’ in relation to companies is defined in Section 2(19AA) of the ITA to mean the transfer, pursuant to a scheme of arrangement under the Merger Provisions by a demerged company¹² of its one or more undertakings, to any resulting company,¹³ in such a manner that:

- All the property of the undertaking,¹⁴ being transferred by the demerged company, immediately before the demerger becomes the property of the resulting company by virtue of the demerger;
- All the liabilities¹⁵ relating to the undertaking, being transferred by the demerged company, immediately before the demerger, become the liabilities of the resulting company by virtue of the demerger;
- The property & the liabilities of the undertaking/undertakings being transferred by the demerged company are transferred at values appearing in its books of account immediately before the demerger. In other words, the resulting company should record property and the liabilities of the undertaking at the value appearing in the books of accounts (book value) of the demerged company. This condition is impossible

11 Explanation 6 to Section 9(1)(i) of the ITA clarifies that the term ‘substantial’ would mean the foreign shares/interest would need to have a minimum value of INR 100 million (USD 1.2 million approx.) and have to derive at least 50% of their value from Indian assets.

12 Section 2(19AAA) of the ITA defines the term “demerged company” to mean a company, whose undertaking is transferred, pursuant to a demerger, to a resulting company.

13 Section 2(41A) defines a “resulting company” to mean one or more companies (including a wholly owned subsidiary thereof) to which the undertaking of the demerged company is transferred in a demerger and, the resulting company in consideration of such transfer of undertaking, issues shares to the shareholders of the demerged company and includes any authority or body or local authority or public sector company or a company established, constituted or formed as a result of demerger.

14 The term ‘undertaking’ would include any part of an undertaking, any unit or division of an undertaking or a business activity as whole, but does not include individual assets or liabilities which do not constitute a business activity.

15 The term ‘liabilities’ would include liabilities and specific loans/borrowings incurred or raised for the specific business activity of the undertaking. In case of a multipurpose loan, such value of the loan will be included, that bears the same proportion as the value of the demerged assets to the total assets of the company.

to be met by resulting companies that follow Indian accounting standards, since they are required to record the property and liabilities of the undertaking at fair value. In order to facilitate tax neutral demerges involving companies following Indian accounting standards, Finance Act, 2019 (No.2) amended Section 2(19AA) of the ITA to provide that the requirement of recording property and liabilities of the undertakings received by the resulting company at book value shall not be applicable in a case where the property and liabilities of the undertakings received by the resulting company are recorded at fair value, due the application of Indian accounting standards;

- The resulting company issues, in consideration of the demerger, its shares to the shareholders of the demerged company on a proportionate basis, except where the resulting company itself is a shareholder of the demerged company;
- The shareholders holding not less than 3/4ths in value of the shares in the demerged company (other than shares already held therein immediately before the demerger, or by a nominee for, the resulting company or its subsidiary) become shareholders of the resulting company(ies) by virtue of the demerger, otherwise than as a result of the acquisition of the property or assets of the demerged company or any undertaking thereof by the resulting company;
- The transfer of the undertaking is on a going concern basis;

The demerger is in accordance with the conditions, if any, notified under subsection (5) of section 72A by the Central Government in this behalf.

The ITA contains certain tax beneficial provisions in the case of a demerger. The relevant exemptions are provided below:

- When the resulting company is an Indian company

Section 47(vib): The transfer of assets by the demerged company to the resulting company, if the resulting company is an Indian company is exempt from capital gains if the demerger fulfils the conditions listed above.

- When both the demerged and resulting companies are foreign

In case of a demerger of a foreign company, whereby both the demerged and resulting companies are foreign, but the assets demerged include or consist of shares in an Indian company, the transfer of these shares is exempt from capital gains tax in the hands of the demerged company under Section 47(vic) of the ITA, if the following conditions are satisfied:

- a. The shareholders holding at least 3/4ths in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company; and
- b. Such transfer does not attract tax on capital gains in the country, in which the demerged foreign company is incorporated.

However, since both the demerged and the resulting companies in the aforesaid example are based outside India, hence the provisions of the CA 2013 (as the case may be) would not be applicable.

- Indirect transfer of a capital asset in a demerger

As in the case of a merger, a specific exemption provision covers demergers in an ‘indirect transfer’ situation i.e., Section 47(vicc) of the ITA, whereby any transfer of a foreign company’s shares, that derive their value ‘substantially’ from Indian assets (i.e., indirect transfer), as part of a demerger should be exempt from capital gains tax (in the hands of the demerged company), provided the following conditions are satisfied:

- a. The shareholders holding at least 3/4ths in value of the shares of the demerged foreign company continue to remain shareholders of the resulting foreign company; and
- b. Such transfer does not attract tax on capital gains in the country, in which the demerged foreign company is incorporated.

However, while this exempts the transfer at the level of the demerged and resulting companies, there is no explicit exemption with respect to tax on capital gains at the hands the shareholders of the demerged company (on account of the receipt of shares of the resulting foreign company).

C. Share Sale¹⁶

Taxation of capital gains is dependent on (i) nature of capital gains i.e. whether the gain is short term capital gain (“STCG”) or long term capital gains (“LTCG”) and (ii) the type of the asset being transferred. Determination of nature of capital gain is dependent on the period of holding of the asset. Section 2(42A) of the ITA provides for determination of period of holding depending on the asset being transferred,

The period of holding for a gain to be classified as STCG upon the transfer of capital assets held by a taxpayer (till the introduction of Finance Act, 2024) was (a) 36 months or less before the date of transfer of any asset, (b) 12 months or less in the case of securities listed on a recognized stock exchange in India, and (c) 24 months in the case of unlisted shares of an Indian company). Any holding of such assets beyond the abovementioned threshold would qualify the gains from the transfer of such assets as long term capital gains (“LTCG”).

In order to simplify the provisions for determination of period of holding, the Finance Act 2024 amended section 2(42A) of the ITA to provide for two holding periods. STCG will arise upon the transfer of capital assets held by a taxpayer for a period of (a) equal to or less than 24 months in case of unlisted shares of an Indian company (or any other assets), and (b) equal to or less than 12 months for securities listed on Indian stock exchange. The Finance Act 2024 has also amended section 50AA of the ITA. Under the Finance Act, 2024 the amount received upon maturity /redemption of bonds/ debentures is deemed to STCG in nature under the provisions of ITA (and taxable as such). In case of non-residents, where redemption premium is specifically included in definition of interest under the relevant tax treaty, one will have to analyze whether (i) non-resident can offer such amount received on redemption of bonds / debenture as interest (instead of STCG under section 50AA) or (ii) can claim exemption (if any) under capital gains article.

The Finance Act, 2024 also rationalized the tax rates on capital gains arising from transfers undertaken on or after July 23, 2024 for all category of assets,

¹⁶ All tax rates mentioned in this chapter are exclusive of applicable surcharge and cess.

Taxes and Duties

The table below sets out the rates at which capital gains are currently taxable under the ITA (i.e., prior to the introduction of Finance Act, 2024) and the changes after the Finance Act, 2024 for different forms of share sales:¹⁷

For short-term capital assets:

Type of Asset	Residents		Non-Residents	
	Before the 23rd day of July, 2024	On or after the 23rd day of July, 2024	Before the 23rd day of July, 2024	On or after the 23rd day of July, 2024
Sale of listed equity shares (Securities Transaction Tax ("STT") paid)	15% ¹⁸	20%	15%	20%
Sale of unlisted shares	No change – STCG taxable at applicable tax rate.			

For Long-term capital assets:

Type of Asset	Residents		Non-Residents	
	Before the 23rd day of July, 2024	On or after the 23rd day of July, 2024	Before the 23rd day of July, 2024	On or after the 23rd day of July, 2024
Sale of listed equity shares ¹⁹ (listed on Indian Stock exchange and STT paid) (on gains exceeding Rs.1,25,000/-)	10% (without indexation)	12.5% (without indexation)	10% (without indexation and without foreign exchange fluctuation benefit) ²⁰	12.5% (without indexation and without foreign exchange fluctuation benefit) ²¹

¹⁷ Surcharge, and, a health and education cess at 4% on the aggregate amount of tax and surcharge applies. Rates of surcharge are:

Taxable income	Foreign Companies	Domestic companies	Individuals
Up to INR 5 million	Nil	Nil	Nil
Above INR 5 million up to INR 10 million	Nil	Nil	10%
Above INR 10 million up to INR 20 million	2%	7%	15%
Above INR 20 million to INR 50 million	2%	7%	25%
Above INR 50 million to INR 100 million	2%	7%	37%
Above INR 100 million	5%	12%	37%

¹⁸ Section 111A of the ITA.

¹⁹ Section 112A of the ITA.

²⁰ Proviso 3 to Section 48 of the ITA

²¹ Ibid.

Taxes and Duties

Sale of unlisted equity shares and securities ²²	20% (with indexation)	12.5% (without indexation)	10% (without indexation and without foreign exchange fluctuation benefit) ²³	12.5% (without indexation and without foreign exchange fluctuation benefit) ²⁴
Unlisted bonds / debentures	20% (with indexation)	Deemed as STCG taxable at applicable rates	10% (without indexation)	Deemed as STCG taxable at applicable rates

All transactions entered into on a recognized stock exchange in India will be subject to STT, which is levied on the transaction value. In the case of sale of equity shares on a delivery basis, STT is generally levied at the rate of 0.1% on the value of the transaction on both the buyer and seller of the equity shares.²⁵

Further, India has entered into tax treaties with several jurisdictions that allow for allocation of taxation rights in a cross-border transactions. In case where a non-resident is resident of a jurisdiction with a beneficial tax treaty with India (such as Netherlands), subject to fulfilment of other requirements, they may claim benefits under the tax treaty to neutralize capital gains tax exposure in India. Recently, India and Mauritius have signed a protocol (though not notified yet) amending the India-Mauritius tax treaty to include the principal purposes test (“PPT”). The PPT denies tax benefit in case where one of the principal purposes of the transaction was to obtain tax benefit, unless, it is established that granting of such benefit is in accordance with the object and purpose of the relevant provisions of the treaty (i.e., in such situations, the PPT will not disallow such benefits being availed under the treaty). This amendment may have an impact on availing the benefits of capital gains exemption under Mauritius treaty on the transfer of grandfathered shares (i.e., shares acquired pre April 1, 2017).

Moreover, in case unlisted shares of a company are transferred at less than the fair market value (“FMV”) then the FMV shall be deemed to be the full value consideration for the purposes of computing capital gains tax in the hands of the transferor.²⁶ Further, in case of transfer of shares at less than FMV, even the transferee may be subject to tax on the difference between the FMV and the consideration paid under the head ‘income from other sources’.²⁷

Lastly, in the case of a secondary issuance, previously under section 56(2)(viib) of the ITA, if a private company issued shares to a resident at a premium (above the face value), then the difference between the consideration received for such shares and their FMV would be taxable in the hands of the issuing company, commonly referred as Angel Tax.

The Finance Act, 2023 had previously enlarged the scope of the Angel Tax to cover investments received by non-residents as well.

²² Section 112 of the ITA

²³ Section 112(1)(c) and as explained in Legatum Ventures Limited (Taxpayer) [ITA No. 1627/2022] which held that Section 112(1)(c)(iii), being a special provision would prevail over Section 48 of the ITA and thus foreign exchange fluctuation benefit would not be available.

²⁴ Section 112(1)(c) and as explained in Legatum Ventures Limited (Taxpayer) [ITA No. 1627/2022] which held that Section 112(1)(c)(iii), being a special provision would prevail over Section 48 of the ITA and thus foreign exchange fluctuation benefit would not be available.

²⁵ Section 98 of the Finance Act (No. 2), 2004.

²⁶ Section 50CA of the Income Tax Act, 1961.

²⁷ Section 56(2)(x) of the Income Tax Act, 1961.

However, this provision was not applicable to consideration for issuance of shares received: (i) by a venture capital undertaking from a venture capital company or a VCF; or (ii) by a specified fund;²⁸ or (iii) by a company from a class or classes of persons as may be notified by the Government in this behalf. 'Eligible start-ups', (i.e., start-ups that qualify the prescribed conditions and are recognized as 'eligible start-ups' by Government) too were exempt from section 56(2)(viib).

The introduction of Angel Tax created a lot of controversies (from a technical, as well as policy perspective) and posed substantial challenges for companies as well as investors. As an answer to several industry representations, the Finance Act, 2024 has abolished Angel Tax from April 1, 2025 and the provisions of the said clause (i.e., section 56(2)(viib) shall not apply from April 1, 2025).

D. Slump Sale

A slump sale is defined under the ITA as transfer of one or more undertaking(s) by any means for a lump sum consideration, without assigning values to the individual assets and liabilities of the undertaking.²⁹ 'Undertaking' has been defined to include an undertaking, or a unit or a division of an undertaking or business activity taken as a whole. However, undertaking does not mean a combination of individual assets which would not constitute a business activity in itself.³⁰

A simplified computation method, and potentially lower tax rate make slump sales attractive. For example, a seller can avail a concessional tax rate for capital gains where the business undertaking being sold has been held for more than 3 years (even if the assets of that undertaking have been held for a shorter period). Further, exemption from Goods and Services Tax makes a slump sale a popular mechanism of business transfers. Additionally, the taxable 'gains' in case of a slump sale are computed as the difference between the sale consideration and the net worth of the business undertaking, as opposed to the underlying cost of acquisition of each asset.³¹ The 'net worth' of the undertaking shall be determined by calculating the difference between the aggregate value of total assets and aggregate value of total liabilities as per the books of accounts of the seller.

For the purpose of such calculation, the aggregate value of total assets is:

- in the case of depreciable assets, the written down value of the block of assets determined in accordance with the ITA;³²
- in the case of capital asset being goodwill of a business or profession, which has not been acquired by the assessee by purchase from a previous owner, nil;
- in the case of capital assets in respect of which the whole of the expenditure has been allowed or is allowable as a deduction under section 35AD, nil; and
- in the case of other assets, the book value of such assets.

If the undertaking, which is being sold under slump sale was held by the transferor Indian company for more than 36 months, the capital gains realized on such sale would be taxed as LTCG, i.e., at the rate of 12.5%

28 As defined under clause (aa) in explanation to Section 56 (2)(viib) of the ITA.

29 Section 2(42C) of the ITA.

30 Explanation 1 to Section 2 (19AA).

31 Section 50B of the ITA.

32 Section 43(6)(C)(i)(c) of the ITA.

(exclusive of surcharge and education cess). If, however, the undertaking was held for 36 months or less by the transferor Indian company, the capital gains realized would be taxed as STCG, i.e., at the rate of 20% (exclusive of surcharge and education cess). For the purposes of computation, The full value of consideration is deemed to be the fair market value (“FMV”) of the undertaking to be determined as per prescribed rules. The Central Board of Direct Taxes (“CBDT”) has set out specific valuation rules³³ for computing capital gains arising from a slump sale.

A slump sale is useful in situations when it would not be feasible to go through the process of amalgamation or demerger under the Merger Provisions. Further, it is also a useful restructuring tool in case of transactions such as externalizations as an undertaking may be transferred by an Indian company at ‘net worth’ to another Indian company in a tax neutral manner. Time taken for a slump sale is substantially less than the time taken for merger.

It would also be useful to note that the ITA defines the term ‘slump sale’ to include the transfer of an undertaking “by any means”. The term ‘transfer’ has been defined broadly under the ITA to include specifically an ‘exchange’, ‘relinquishment’ and ‘extinguishment’. Thus, as was previously the case (prior to FY 21), slump sales are no more restricted to transfer exclusively by way of ‘sales’.

E. Asset Sale (itemized sale)

In an asset sale, the acquirer only purchases the assets of the seller. This does not amount to the transfer of the business as a going concern and specific values are attributed to each of the assets. The capital gains tax payable by the seller will depend on the period that the seller has held each of the assets that are transferred. This method of acquisition is usually used where the acquirer does not want to acquire the liabilities of the seller and more so if the acquirer believes that the seller has not disclosed certain liabilities or there is a distinct possibility that unforeseen liabilities could arise in the future. The ITA provides separate computation provisions for asset sale, depending upon whether the asset is depreciable or non – depreciable.

- **Non – depreciable assets:**

- a) **Long term capital assets**

As mentioned above, if the assets which are being sold were held by the transferor Indian company for more than 24 months, the capital gains realized on such sale would be taxed as LTCG, i.e., at the rate of 12.5% (exclusive of surcharge and education cess). Further, in case of sale of immovable property, LTCG will be taxed at 12.5% (without indexation).

- b) **Short term capital assets**

If the assets were held for 24 months or less by the transferor Indian company, the capital gains realized would be taxed as STCG, i.e., at the rate of 20% (exclusive of surcharge and education cess) in case listed equity shares, units of equity oriented mutual fund and units of business trust. In all other cases STCG will be taxable at applicable tax rate.

³³ Rule 11 UAE of the Income-tax Rules, 1962.

■ Depreciable assets:

Capital gains is determined based on whether the block of assets (“Block”)³⁴ continues to exist post transfer or not.

a) Capital gains when the Block continues to exist post transfer

Capital gains from the transfer would be deemed to be STCG and should be taxable in hands of transferor at the applicable tax rate, irrespective of the period of holding of such asset. The capital gains will be determined as the difference, if any, between (1) the full value of sale consideration from the transfer of the concerned assets, together with the full value of consideration for the transfer of any other asset within that Block (during the previous year), and (2) the aggregate of:

- i) Expenditure incurred wholly and exclusively in connection with such transfers;
- ii) Written Down Value (“WDV”) of the Block at the beginning of the previous year; and
- iii) Actual cost of any asset acquired during the previous year and forming part of that Block.³⁵

b) Capital gains when the Block ceases to exist post transfer

Where all assets from a Block are transferred during the previous year such that the Block ceases to exist, capital gain from such transfer should be deemed to be STCG and should be taxable in hands of transferor at the applicable tax rate, irrespective of the period of holding of such asset.

The capital gain from such transfer should be determined as the difference, if any, between (1) the full value of the sale consideration from the transfer of the concerned assets, together with the transfer of any other asset within that Block in the same financial year, and (2) the aggregate of:

- i) WDV of the Block at the beginning of the previous year; and
- ii) Actual cost of any asset acquired during the previous year and forming part of that Block.³⁶

Applicable surcharge on Indian companies would be 7% if income is between INR 10 million (USD 115.3 thousand) - INR 100 million (USD 1.2 million approx) and 12% if income exceeds INR 100 million (USD 1.2 million approx). Further, 4% cess on the quantum of income-tax and surcharge is applicable to all taxpayers.

F. Buy-Back of Shares

Special provisions were introduced by the Finance Act, 2013 to tax the income distributed by a domestic company from buy-back of shares. The income distributed (until the introduction of Finance Act 2024) was taxed in the hands of the domestic company at the rate of 20% plus surcharge and cess. To this extent, shareholders were exempt from tax on the income received from the buyback of shares and buybacks were specifically excluded from the scope of deemed dividend under ITA. The Finance Act, 2024 taxes the consideration paid on buy back of shares as dividend in the hands of the shareholders with effect from October 01, 2024. To this extent, a new sub clause (f) has been added in the definition of ‘dividends’ under the ITA. The

34 ‘Block of assets’ is defined in Section 2(11) of the ITA as a group of assets falling within a class of assets in respect of which the same percentage of depreciation is prescribed. Such block of assets may comprise of (a) tangible assets such as buildings, machinery, plant or furniture; (b) intangible assets such as know-how, patents, copyrights etc.

35 Section 50(1) of the ITA.

36 Section 50(2) of the ITA.

rationale for bringing this amendment is to bring parity in the taxation of incomes distributed to shareholders since both (a) dividend distribution and (b) income distributed on buyback are different methods for the company to distribute accumulated reserves.

Further, section 46A of the ITA has been amended wherein full value of consideration of such shares has been deemed as nil; thereby allowing a capital loss to be booked in the hands of the shareholder (which they may carry forward as per the ITA). An amendment has also been introduced in section 194 of the ITA which states that payments made by the company on buybacks will be subject to withholding tax in their hands.

Since the redemption of preference shares (taking place under section 55 of CA 2013) is arguably covered with the scope of section 115QA of the ITA, the taxability of consideration received on such redemption should be taxes as capital gains. The explicit characterization of payments on buyback of shares as dividends may also imply that the taxpayer can take the benefit of reduced tax rates for dividend income under the treaty.

Transfer Pricing

Please note that any cross-border transaction between related parties that is liable to tax under the ITA would also be subject to ‘transfer pricing’ requirements under Indian law (i.e., Chapter X of the ITA), mandating the transaction to be undertaken at an ‘arm’s length price’ and other documentation requirements.

G. Other Considerations

i. Indirect Transfer

Gains earned by a resident company from the transfer of capital assets situated anywhere in the world are taxable in India. However, in the case of non-residents, only those gains arising out of the transfer of a capital asset situated in India should be taxable.³⁷

The source rule pertaining to a ‘capital asset situated in India’ was examined by the Supreme Court of India in Vodafone International Holdings B.V. v. Union of India,³⁸ which dealt with the transfer of shares of a non-resident company between two non-residents. The Supreme Court held that a share is legally situated at the place of incorporation/ registration of the company or where the shares may be effectively dealt with. Therefore, while the shares of an Indian company would be considered as situated in India, the shares of a company incorporated outside India would ordinarily be viewed as situated outside India. Subsequent to the abovementioned Vodafone judgment, the Government of India introduced indirect transfer tax rules through introduction of Explanation 5 to Section 9(1)(i) of the ITA (“Indirect Transfer”). This insertion clarified that the transfer of shares of a foreign company which derives its value substantially from assets located in India shall be subject to capital gains tax in India.

As per Explanation 6 to section 9(1)(i) of the ITA,³⁹ the shares or interest in a foreign company is deemed to derive its value substantially from assets located in India if the value of such assets (“Indirect Transfer Test”):

37 Section 9 of the Income Tax Act, 1961. Further, India also introduced a rule to tax non-residents on the transfer of foreign securities the value of which are substantially (directly or indirectly) derived from assets situated in India (Indirect Transfer Tax).

38 (2012) 341 ITR 1(SC).

39 Explanation 6 to section 9(1)(i) was introduced through Finance Act, 2015.

- i) exceeds INR 100 million (USD 1.2 million approx.); and
- ii) represents at least 50% of the value of all the assets owned by the company or the entity, as the case may be.

Additionally, Rule 11UB (of the ITR) also provides the valuation methodologies prescribed for the purposes of valuing the shares/interest of the overseas entity, as well as its assets in India.

Further, as per clause (d) of Explanation 6, value of the assets for the purposes of determining whether the Indirect Transfer Test is satisfied should be computed as on a specified date (“Specified Date”). Specified date has been defined in the ITA to mean

- a) date on which the accounting period of the foreign company / entity ends preceding the date of transfer of a share or an interest; or
- b) date of transfer, if the book value of the assets of the foreign company/ entity on the date of transfer exceed the book value of the assets as on the date referred in (a) above by 15%

In addition to the above, Explanation 7 to Section 9(1)(i), provides for an exemption from the indirect transfer provisions to small shareholders, who together with associated enterprises hold a de minimis shareholding (less than 5%).

The demands raised by the Indian Government under the indirect transfer tax provisions spurred investment treaty arbitration cases against India – among which are Vodafone International Holdings BV v. The Republic of India (“Vodafone arbitration”) and Cairn Energy Plc and CUHL v the Republic of India (“Cairn arbitration”). The arbitral tribunals have ruled in favour of the foreign investors against India in the Vodafone and Cairn arbitrations.

In this backdrop, the Indirect Transfer provisions were amended by the Taxation Laws (Amendment) Act, 2021 (“2021 Act”) to remove its retrospective applicability. The 2021 Act made following changes in the Indirect Transfer provisions:

- **An embargo on future tax demands:** The 2021 Act provided that the Indirect Transfer provisions would not apply to income accruing or arising as a result of an Indirect Transfer undertaken prior to May 28, 2012. The 2021 Act added a proviso to Explanation 5 to section 9(1)(i) of the ITA for non-application of Indirect Transfer provisions on (i) assessments or reassessments initiated under specified sections, (ii) orders passed enhancing a tax assessment or reducing a refund and (iii) orders passed deeming a person to be an assessee-in-default for not withholding taxes in respect of indirect transfers prior to May 28, 2012.
- **Nullification of tax demands raised:** The 2021 Act also provided that demands raised for indirect transfers of Indian assets made prior to May 28, 2012 shall be nullified, subject to fulfilment of the following conditions⁴⁰ by the person in whose case such demand has been raised:
 - withdrawal or an undertaking for withdrawal of appeal filed before an appellate forum or a writ petition filed before a High Court or the Supreme Court of India;
 - withdrawal or an undertaking for withdrawal of any proceedings for arbitration, conciliation or mediation initiated by such person such as under a bilateral investment treaty; and
 - furnishing of an undertaking waiving their rights to seek or pursue any remedy or any claim in relation to such income whether in India or outside India.

40 On August 28, 2021, the Government has notified the draft rules for public consultation to specify the conditions to be fulfilled and the process to be followed to give effect to the amendment made by the 2021 Act.

Refund of amounts paid: The 2021 Act also provided that the Government shall refund the taxes paid in cases where the application of Indirect Transfer provisions is being withdrawn due to fulfilment of the conditions mentioned above. However, no interest, cost or damage shall be paid by the Government on such refund of taxes.

The 2021 Act saw moves towards settlement of quite a few cases including the Indian tax authorities withdrawing their petition before the SC over taxability in the Sanofi case⁴¹ and reports regarding the Indian Government settled the long-running tax disputes arising from the Indirect Transfer provisions with Vodafone Group⁴² and Cairn Energy.⁴³

ii. Tax on Business Income – Carry Forward of Losses

Section 72A of the ITA provides that in case of amalgamation of a company owning an industrial undertaking or a ship or a hotel⁴⁴ with another company, or a baking company with a specified bank or one or more public sector company or companies with one or more public sector company or companies or any other amalgamation as specified in the stated provision, the accumulated loss and the unabsorbed depreciation of the amalgamating company is deemed to be the loss / allowance for depreciation, of the amalgamated company. The amalgamated company would then be entitled to carry forward such loss and depreciation and set off such amounts against its future profits. However, the following conditions must be satisfied for availing the above entitlement:

- a) The amalgamated company:
 - i. Holds 3/4ths of the book value of the fixed assets which it acquired from the amalgamating company continuously for a minimum period of 5 years from the date of amalgamation;
 - ii. Continues to carry on the business of the amalgamating company for a minimum period of 5 years from the date of amalgamation. This would imply that if the amalgamating company were engaged in more than one business prior to amalgamation, the amalgamated company would be required to carry on all of those businesses; and
 - iii. Fulfills such other conditions as may be prescribed to ensure the revival of the business of the amalgamating company or to ensure that the amalgamation is for genuine business purpose.
- b) The amalgamating company:
 - i. has been engaged in the business, in which the accumulated loss occurred or depreciation remained unabsorbed, for 3 or more years; and
 - ii. has held continuously, on the date of amalgamation, at least 3/4ths of the book value of the fixed assets held by it 2 years prior to the date of amalgamation.

For amalgamations effected on or after 01.04.2025, losses of the amalgamating company can be carried forward and set off by the amalgamated company for not more than eight years immediately succeeding the assessment year for which such loss was first computed for the amalgamating company.⁴⁵ Thus, unlike the amalgamations effected prior to 01.04.2025, the time limit of eight years shall not restart when the new entity is formed.

41 SLP(C) No. 19856-58 of 2013.

42 <https://economictimes.indiatimes.com/news/economy/policy/vodafone-files-for-retro-tax-settlement-with-india/articleshow/88061385.cms>.

43 <https://www.livemint.com/companies/retrospective-tax-india-refunds-rs-7-900-cr-to-cairn-to-settle-dispute-11645706981790.html>.

44 Industrial undertaking means an undertaking engaged in manufacture or processing of good, manufacture of computer software, generation/ distribution of electricity/ power, telecommunications services etc. This does not cover undertakings in the software service sector and certain other service sectors.

45 Section 72A(6B) of the ITA, inserted vide the Finance Act, 2025.

Section 72A(4) of the ITA provides a similar benefit for demergers. However, in the case of a demerger, the company does not need to satisfy any conditions similar to those applicable to mergers. In the case of a demerger, the accumulated loss and the allowance for unabsorbed depreciation of the demerged company shall:

- a) where such loss or unabsorbed depreciation is directly relatable to the undertakings transferred to the resulting company, be allowed to be carried forward and set off in the hands of the resulting company;
- b) where such loss or unabsorbed depreciation is not directly relatable to the undertakings transferred to the resulting company, be apportioned between the demerged company and the resulting company in the same proportion in which the assets of the undertakings have been retained by the demerged company and transferred to the resulting company, and be allowed to be carried forward and set off in the hands of the demerged company or the resulting company, as the case may be.

In a case where these conditions are not met, carry-forward and set-off of losses will not be allowed to the amalgamated or the resulting company (as the case maybe). Section 79 of the ITA provides that in order for a company to claim carry-forward and set-off of losses for a particular assessment year, 51% of the voting power of the company must be beneficially held during that assessment year by the same shareholders who held such voting right on the last day of the year or years in which the loss was incurred. However, this provision shall not be applicable in a case where there is a change in shareholding of an Indian company, that is a subsidiary of a foreign company, as a result of amalgamation or demerger of a foreign company, subject to the condition that 51% shareholders of the amalgamating or demerged foreign company continue to be the shareholders of the amalgamated or the resulting foreign company.⁴⁶ Further, domestic transfer pricing rules have also been introduced under the ITA (as 'Specified Domestic Transactions' in Chapter X) by which expenses may be disallowed in case of transactions between related parties.

iii. Transfers declared void under Section 281

Where there are assessment proceedings or tax litigations under the ITA pending on any person, including a company, any charge created on or transfer envisaged of any assets of such person shall be considered void as per section 281 of the ITA –

- i. if it is not made for adequate consideration and there is a notice of the pendency of such proceeding or with a notice of such tax or other sum payable by such person; or
- ii. if it is not made with the previous permission of the assessing officer.

A certificate under section 281 is key in a merger or acquisition situation in a case where the transferor has pending assessment proceedings or tax litigation under the ITA at any level.

iv. Assessment post succession of business

Section 170 of the ITA provides the manner of taxation (i.e., who is assessable) in cases of succession of a business (or profession) to a person who succeeds and carries on the business (from its predecessor). It envisages separate assessments on both, the predecessor and the successor (for which they both separately compute their taxes, apply deductions, and pay taxes as per their applicable rates). The issue regarding the validity of assessment / re-assessment proceedings initiated on predecessor entities during the pendency of reorganization proceedings before the adjudicating authorities have been subject to litigation in the past. In order to clarify this issue, the Finance Act, 2022, amended Section 170 of the ITA (with effect from April 1, 2022) to provide that where

⁴⁶ Special exemptions are also provided in case of death of a shareholder, gift of shares to relatives.

assessment / re-assessment proceedings are initiated on predecessor entity during the pendency of reorganization proceedings, such proceedings shall be deemed to have been made on the successor entity. The amendment to Section 170 of the ITA ended further litigation on this issue going forward. The amendment was also in line with the spirit of the definition of 'demergers' in Section 2(19AA), and 'amalgamation' in Section 2(1B) which envisage all assets and liabilities of the demerging/amalgamating entity (predecessor) to stand transferred to the resulting entity (successor).

II. Goods and Services Tax

From July 1, 2017, the Goods and Services Tax ("GST") regime has come into force, which replaced the erstwhile indirect tax regime. Under the GST regime, Central GST and State GST is levied on all intra-state supplies of goods and/ or services, and Integrated GST is levied on imports and all supplies of goods and/or services undertaken in the course of inter-state trade or commerce. The slab rates for the levy of GST on the supply of goods/services are fixed at 5%, 12%, 18% or 28%.

In an asset purchase depending on the type of asset being sold, the rate of GST will vary. Since a 'business' per se does not qualify as 'goods' or 'services' under the GST Act, no GST is levied on slump sale transactions. Further, since 'shares' are covered under the definition of 'securities' and 'securities' are specifically excluded from the ambit of 'goods' under the GST law, there would be no GST incidence upon transfer of shares, including in case of amalgamations and demergers.

III. Stamp Duty

Stamp duty is a duty payable on certain specified instruments/documents. Broadly speaking, when there is a conveyance or transfer of any movable or immovable property, the instrument or document effecting the transfer is liable to payment of stamp duty.

A. Stamp Duty on Court Order for Mergers/Demergers

Since the order of the Court merging two or more companies, or approving a demerger, has the effect of transferring property to the surviving /resulting company, the order of the NCLT may be required to be stamped. The stamp laws of most states require the stamping of such orders. The amount of the stamp duty payable would depend on the state specific stamp law.

B. Stamp Duty on Share Transfer

With effect from July 1, 2020, share transfers of listed and unlisted securities both in physical and dematerialized form are subject to stamp duty at 0.015% of the purchase consideration.

C. Stamp Duty on Shareholder Agreements/Joint Venture Agreements

Stamp duty will be payable as per the state specific stamp law.

D. Stamp Duty on Share Purchase Agreements

Stamp duty may be payable on an agreement that records the purchase of shares/debentures of a company. This stamp duty is payable in addition to the stamp duty on the share transfers mentioned above.

E. Transaction Costs for Asset Purchase vs. Slump Sale vs. Share Purchase

Transaction related costs are generally higher in the case of an asset purchase as compared to a share purchase or slump sale. This is primarily because in a share purchase or slump sale, there would usually be no incidence of GST, which may be levied on different aspects of an asset purchase. Further, the rate of stamp duty is also usually higher in an asset purchase and slump sale, and it is dependent on the nature of the assets being transferred. While for tax purposes, no values are assigned to the individual assets of the undertaking being transferred (in a slump sale), it is necessary to assign values to assets for the purpose of determining the stamp duty payable.

The stamp duty on a transfer of shares is currently 0.015% of the consideration payable for the shares, which rate is usually far less than the stamp duty rates applicable for transfer of movable/immovable assets which may vary from 3% to 5% from state to state.

Conclusion

As Dale Carnegie¹ said “Flaming enthusiasm, backed by horse sense and persistence, is the quality that most frequently makes for success”. A quote that holds good for M&A in India, and a credo to which Indian companies seem to subscribe given their successes to date in completing acquisitions. There is little to stop Indian companies that desire to be global names for playing the merger and acquisition game globally. With a plethora of financing options, this aspiration has become a reality for many corporate houses, who can now boast of having the best in the industry under their wings. Indian companies have often surpassed their foreign counterparts in corporate restructuring both within and beyond the national frontiers. Mergers and acquisitions are powerful indicators of a robust and growing economy. The legal framework for such corporate restructuring must be easy and facilitative and not restrictive and mired in bureaucratic and regulatory hurdles. The biggest obstacle in the way of completing a merger or an amalgamation remains the often long drawn out court procedure required for the sanction of a scheme of arrangement.

As George Bernard Shaw² is reputed to have said “we are made wise not by the recollection of our past, but by the responsibility for our future”, and the future of India is bright indeed.

Team M&A

1 November 24, 1888 – November 1, 1955.

2 106. July 26, 1856 – November 2, 1950, Nobel Prize for Literature 1925.

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At Nishith Desai Associates, we have earned the reputation of being Asia's most Innovative Law Firm — and the go-to specialists for companies around the world, looking to conduct businesses in India and for Indian companies considering business expansion abroad. In fact, we have conceptualized and created a state-of-the-art Blue Sky Thinking and Research Campus, Imaginarium Aligunjan, an international institution dedicated to designing a premeditated future with an embedded strategic foresight capability.

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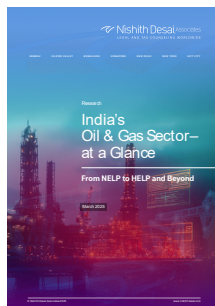
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