



JSA Prism Corporate (FDI)

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Recent Press Note 2 (2025 series) clarifies on the issuance of bonus shares by Indian companies engaged in Sectors Prohibited for Foreign Direct Investment

On April 7, 2025, the Department for Promotion of Industry and Internal Trade, through Press Note 2 (2025 series) (“**PN2**”), has issued a clarification concerning the issuance of bonus shares by Indian companies operating in sectors where Foreign Direct Investment (“**FDI**”) is prohibited.

As per Schedule I of the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 (“**NDI Rules**”), FDI is prohibited in lottery business, gambling and betting, chit funds, Nidhi companies, trading in transferable development rights (TDRs), real estate business or construction of farmhouses, manufacturing of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes, and activities/sectors not open to private sector investment (“**Sectors Prohibited for FDI**”).

There was ambiguity on whether Indian companies engaged in Sectors Prohibited for FDI could issue bonus shares to its shareholders (which, by implication would have included extending the bonus offer to non-resident (“**NR**”) shareholders) under the ‘automatic’ route. Pursuant to the PN2, the government clarified the position that such companies (i.e., Indian companies engaged in Sectors Prohibited for FDI) are allowed to issue bonus shares to NR shareholders. The PN2 provides clarity for the Indian companies operating in sectors where FDI was originally permitted but is now prohibited. For example, it was through Press Note 2, dated May 10, 2010, that FDI was prohibited in the manufacturing of cigarettes.¹

What has the government clarified?

The government has clarified that issuance of bonus shares by Indian companies engaged in Sectors Prohibited for FDI to its existing NR shareholders is permitted provided the Indian company fulfils the following conditions in connection with such issuance:

1. the shareholding pattern of the pre-existing NR shareholders will not change pursuant to the issuance of the bonus shares; and
2. the issuance of bonus shares must comply with all other applicable rules, laws, regulations, and guidelines.

Thus, issuance of bonus shares will need to be in accordance with the Companies Act, 2013 and rules thereunder and SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009 (in case of listed companies).

¹ [Press Note 2 \(2010 Series\).pdf](#).

The implication of this clarification is that such companies can proceed to issue bonus shares without having to obtain a prior government approval provided the aforesaid conditions are fulfilled by the Indian company.

Does PN2 have a retrospective application?

One of the interesting questions is whether this clarification can be applied retrospectively. Can previous issuances of bonus shares by such companies be grandfathered under this clarification? The language of PN2 reads “*following clarification is inserted*”, which is quite unlike previous Press Notes (including the famous Press Note 3) which amended the position of the law. Given the PN2 ‘clarification’, one could possibly argue that the position of law was always that such bonus issuance to NR shareholders was permitted under the extant FDI framework, and the current clarification merely puts the matter beyond doubt. While one could rely on certain judicial precedents to argue that a clarificatory amendment has retrospective application, it may be a slightly risky argument to advance in the context of FDI which is a highly regulated activity.² Accordingly, a cautious approach is suggested.

Impact of PN 2 vis-à-vis FDI from land-bordering countries (i.e., Press Note No. 3 (2020 Series))

Press Note No. 3 (2020 Series) (“**PN3**”), which was issued against the backdrop of the Covid pandemic, mandated that where an investing entity is situated in a country sharing land border with India or where the beneficial owner of an investment into India is situated in or is a citizen of any such country, FDI will be permitted only with prior government approval.

The basis of the clarification provided in PN2 seems to be the fact that a bonus issuance does not entail any inflows of funds nor would it under ordinary circumstance (unless there is a selective bonus issuance) alter the existing shareholding pattern of the Indian company. Given the rationale behind the clarification that resulted in the issuance of PN2, one could argue that a similar logic could also extend to the issue of bonus shares that could otherwise get caught within the restriction of PN3. Therefore, a similar clarification from the government in relation to PN3 would help.

Conclusion

While the PN2 ‘clarification’ sheds light on the regulator’s thought process, PN2 states that the clarification will be only effective from the date of issuance of the applicable notifications issued under the Foreign Exchange Management Act, 1999 (“**FEMA**”). The FEMA notification in this regard is still awaited and hence, on a literal interpretation, the PN2 is not effective as on date of this article.

From the date of the anticipated FEMA notification, the PN2 clarification will allow the Indian companies in Sectors Prohibited for FDI an additional avenue to effectively capitalise their existing reserves and such companies could explore bonus issuances as a means for cash distribution to their existing shareholders, including for Indian shareholders. Previously due to the restriction on issue of the bonus shares to NR shareholders, Indian companies in Sectors Prohibited for FDI largely shied away from undertaking issuance of bonus shares considering the commercial and governance related challenges especially those in relation to the dilution of the NR shareholder(s). The move is expected to ensure parity in shareholder rights and make exploring bonus issuances easier for Indian companies operating in the Sectors Prohibited for FDI.

² *Bengaluru Development Authority vs. Sudhakar Hegde and Ors.* (2020) 15 SCC 63; *State Bank of India vs. V. Ramakrishnan* (2018) 17 SCC 394; *CIT vs. Vatika Township* (2015) 1 SCC 1

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