June 2025

Amendment to the foreign exchange management rules: Issuance of bonus shares to non-resident investors by companies engaged in sectors prohibited from receiving foreign direct investment

Bonus shares are issued under Section 63 of the Companies Act, 2013 and the Companies (Share Capital and Debentures) Rules, 2014. This process involves the issuance of additional shares in a pre-determined ratio to existing shareholders resulting in an increase in the total number of shares and a corresponding proportional decrease in the stock price. The issuance of bonus shares must be undertaken in compliance with the provisions of the Companies Act, 2013, rules thereunder, and applicable foreign exchange laws including the Foreign Exchange Management (Non-Debt Instruments) Rules, 2019 ("**NDI Rules**"). In the case of listed entities, it is also necessary to comply with the applicable regulations issued by the Securities and Exchange Board of India, including the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018.

Amendment to NDI Rules

On June 11, 2025, the Ministry of Finance ("**MoF**") has introduced amendments to Rule 7 of the NDI Rules ("**Amendment Notification**"). The Amendment Notification is accessible *here*.

The Amendment Notification allows resident companies (operating in sectors prohibited for Foreign Direct Investment ("**FDI**") or undertaking activities prohibited from receiving FDI as elaborated below) to issue bonus shares to existing non-resident shareholders with the condition that such non-resident shareholders' shareholding does not increase pursuant to such issuance. The Amendment Notification came into effect from June 11, 2025. The Amendment Notification is also retrospective in nature and applies to bonus issuance undertaken during the subsistence of the erstwhile Foreign Exchange Management (Transfer or issue of Security by a Person Resident outside India) Regulations, 2000 or the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017.

Prohibited sectors

The FDI Policy, 2020 restricts Foreign Direct Investment in the following sectors:

1. lottery business including government/private lottery, online lotteries, etc.;
2. gambling and betting including casinos etc.;
3. chit funds;
4. nidhi company;

5. trading in transferable development rights;
6. real estate business or construction of farm houses[1];
7. manufacturing of cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes; and
8. activities/sectors not open to private sector investment e.g. (a) atomic energy; and (b) railway operations (other than permitted activities mentioned in para 5.2 of the FDI Policy, 2020).

Related clarifications

Prior to the Amendment Notification, the Department for Promotion of Industry and Internal Trade, through Press Note 2 (2025 series) dated April 7, 2025 ("**PN 2**"), had issued a clarification concerning the issuance of bonus shares by Indian companies operating in sectors where FDI is prohibited. The PN 2 is accessible *here*. The clarification however did not include provisions relating to retrospective applicability of the clarification.

In addition to including the provision as substantive law, it may be noted that the deeming language under the Amendment Notification provides clarity relating to the fact that these relaxations are available retrospectively including relating to actions undertaken under the erstwhile Foreign Exchange Management (Transfer or issue of Security by a Person Resident outside India) Regulations, 2000 or the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2017.

Conclusion

The Amendment Notification eases the restrictions on companies while undertaking future issuance of bonus shares. This is particularly beneficial to foreign shareholders whose investments were 'grandfathered' (i.e. new rules restricting investments do not apply retroactively to existing investments) pursuant to any change in law which restricted their holding by means of a prohibition on foreign investment. Such shareholders may now be able to freely receive bonus shares without increasing their total shareholding percentage. Further, given that the Amendment Notification provides retrospective validation to bonus shares already issued, the Amendment Notification shall provide relief to several companies who may now be able to regularize outstanding non-compliance issues in this regard. The Amendment Notification is accordingly a welcome move for existing foreign investors in companies operating in FDI prohibited sectors and reduces legal complexity and uncertainty.

[1] 'Real estate business' does not include development of townships, construction of residential/commercial premises, roads or bridges and Real Estate Investment Trusts ("**REITs**") registered and regulated under the SEBI (REITs) Regulations, 2014.

Corporate Practice

JSA's corporate practice is centered around transactional and legal advisory services including day-to-day business, regulatory issues, corporate and governance affairs. We have an expert team of attorneys who advise on legal issues concerning inbound and outbound investments, strategic alliances, collaborations and corporate restructurings. We advise clients through all stages of complex and marquee assignments including restructuring, mergers and acquisitions (including those in the public space) to private equity and joint ventures. Our vast clientele includes multinational corporations and large Indian businesses in private, public and joint sector. We work closely with in-house counsel teams, investment banks, consulting and accounting firms along with multilateral agencies and policy making institutions on development of policy and legal frameworks. We provide assistance and counsel to start-ups and venture backed companies by drawing upon our in-depth understanding of how companies are incorporated, financed and grown. With an in-depth understanding of the industry combined with years of expertise, our attorneys provide innovative and constructive solutions to clients in complex transactional engagements. We emphasise teamwork across our wide network of offices across India. This allows us to benefit from the various specialisations available for the ultimate benefit of our clients. We also provide assistance in dealing with diverse corporate governance and compliance issues including FCPA /Anti-Bribery/Anti-Corruption matters and investigations.

This Prism has been prepared by:

Archana Tewary
Partner

Naveen Kumar
Associate

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