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**PSL Release**

Gov issues FEMA Notification to increase FDI in defence sector through automatic route from 49% to 74%

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## 1. Introduction


- 1.1 The Department for Promotion of Industry and Internal Trade, Ministry of Commerce and Industry (“**DPIIT**”) had earlier on 17.09.2020 announced the increase in the Foreign Direct Investment (“**FDI**”) limit for the defence sector from earlier 49% to 74% under automatic route (i.e. without any Government approval). The said decision was to be enforced from the date of FEMA notification.
- 1.2 Hence, now vide the notification dated 08.12.2020, the Department of Economic Affairs, Ministry of Finance has amended the Foreign Exchange Management (Non-debt Instruments) Rules, 2019 (“**FEMA Rules**”) in exercise of its powers under Section 46 of the Foreign Exchange Management Act, 1999 (“**FEMA Act**”) to bring into force the revised FDI limit under automatic route.

## 2. Conditions prescribed:

- 2.1 The amended FEMA Rules stipulates for Government approval, where FDI goes beyond 74% and is likely to result in access to modern technology, or for other reasons that should be recorded. Currently, the sectoral cap for Defence sector is set as 100%.<sup>1</sup>
- 2.2 FDI upto 74 percent under automatic route will be permitted for companies seeking new industrial licences (new projects).
- 2.3 Infusion of fresh foreign investment up to 49%, in a company not seeking industrial licence or which already has Government approval for FDI in Defence, would require submitting a declaration with the Ministry of Defence in cases of change in equity, or shareholding pattern or transfer of stake by existing investor to new foreign investor, for FDI up to 49%, within a period of thirty days of such change.
- 2.4 Further, any proposal for raising FDI beyond 49% from such companies should require Government approval.
- 2.5 All applications for new licence will be considered by the Department for Promotion of Industry and Internal Trade, Ministry of Commerce and Industry, in consultation with Ministry of Defence and Ministry of External Affairs.
- 2.6 Any new FDI in defence sector would be subject to security clearance by Home Ministry and as per the guidelines of Ministry of Defence.
- 2.7 All the foreign investments in defence sector will be subject to scrutiny on grounds of national security and the Government of India may review any foreign investment in defence sector that affects or may affect national security.

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<sup>1</sup> FDI in defence sector is subject to industrial license under the Industries (Development and Regulation) Act, 1951 and manufacturing of small arms and ammunition under the Arms Act, 1959.



2.8 The investee company (in which the investment is being made) must have resources and sound infrastructure in the areas of product design and development. The investee company, or the Joint Venture Company (“**JVC**”) along with the manufacturing facility, shall also have maintenance capacity and life cycle support facility for the product being manufactured in India.

**3. PSL Comment:**

3.1 To deal with the economic stress posed by the Covid-19 Pandemic, the Government of India has taken a right step to give acceleration to growth in the defence sector while also introducing various checks to ensure there isn't sudden flood of foreign investors in defence sector, which might clog up this sector. The revised FDI limits can be seen as the Government of India's continuous progressive steps under the *Aatma Nirbhar Bharat Abhiyan*, India's vision to become self-reliant.