



Review Article

FROM BLANKET SCREENING TO CALIBRATED SCRUTINY: SHOULD INDIA CODIFY A CFIUS-STYLE NATIONAL SECURITY REVIEW FOR INBOUND M&A?

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ABSTRACT

"India's Press Note 3, introduced in April 2020 to screen foreign direct investment from land-border countries, was framed as a national security measure but functioned as a blunt, nationality-based filter with no sectoral discrimination, no published criteria, and no statutory timeline. This article traces its evolution through the partial liberalization introduced in March 2026, which opened an automatic route for passive, non-controlling stakes under ten percent while leaving controlling acquisitions by land-border entities subject to the same discretionary approval process that has governed such deals since 2020.

Drawing on official data showing Chinese investment frozen at roughly 0.3% of India's cumulative FDI inflows despite a formal easing of the regime, the article situates India's approach against the Committee on Foreign Investment in the United States (CFIUS) and the European Union's FDI Screening Regulation, both of which trigger review based on the sector and nature of a transaction rather than the investor's nationality alone.

The article argues that India's regime remains structurally deficient even after the 2026 amendments, particularly with respect to controlling stakes in mergers and acquisitions and proposes a codified National Security Review of Foreign Investment framework built around sector-specific triggers, a dedicated statutory review body, a control-based test independent of shareholding percentage, and mandatory beneficial-ownership disclosure.

INTRODUCTION

Press Note 3 was issued before the June 2020 Galwan Valley clash and expressly linked its policy objective to preventing opportunistic takeovers and acquisitions during the COVID-19 pandemic. The notification required investments by entities from countries sharing a land border with India, and investments in which the beneficial owner was situated in or a citizen of such a country, to proceed through the Government route. The design was therefore capable of capturing transactions across sectors and at different levels of economic significance, rather than limiting review to businesses connected with identified national-security assets.

The difference in effect was obvious. While Chinese investments that had accounted for roughly two percent of total FDI in India prior to the onset of the coronavirus crisis dropped to insignificance and have stayed there, the same time interval saw the trade link between India and China take a completely different turn with Chinese imports becoming increasingly larger despite restrictions imposed on their capital. This paradox of curbing capital and failing to stop goods constitutes the crux of the current study, while also forming the basis of argument that supports creation of a more sophisticated, industry-specific national security review process along the lines of the American CFIUS process or the EU FDI Screening Regulation.

In March 2026, India reversed course, at least in part. The Cabinet cleared changes that turned Press Note 3 into the informal “Press Note 2 of 2026” by creating an automatic route for passive, non-controlling foreign investments under ten percent and a sixty-day approval time frame for a pre-defined list of manufacturing-based sectors. At first sight, this may appear to be liberalization, but in reality, it is a government realizing that its catch-all measure was economically counterproductive, but still unwilling to design the necessary fix in the form of a proper security screening mechanism right away.

In this article, the author argues that the Indian system is still inferior to the screening systems used by India's major trading partners despite the amendments made in 2026. This article looks into the development of Press Note 3 from the time it was introduced during the pandemic period until the 2026 recalibration, compares India's system with CFIUS and the EU system and advocates for legislation that will provide a robust national security review system in India for inbound M&A transactions.

Introduction of a Blunt Instrument

Press Note 3 is often wrongly recalled as the Indian system introduced after the June 2020 Galwan Valley clash. It is not the case because the notification was introduced on 17 April 2020, about two months before the Galwan clash. It was a time when equity markets in many parts of the world were experiencing a downturn and Indian businesses were struggling under the influence of the pandemic. It was a concern for most finance ministries that foreign opportunistic investors, especially those affiliated with China, would use the time of the economic downturn to acquire Indian businesses at low prices, which was something happening with Europe-based companies.

For transaction counsel, the principal difficulty was not simply the existence of an approval requirement but the breadth of the trigger. A transaction involving a non-sensitive commercial enterprise could fall within the same Government-route architecture as a transaction involving strategically significant infrastructure. This created a need for regulatory analysis at the investor and ownership level even where the target company's business presented little apparent national-security sensitivity. The central issue is therefore one of calibration: a national-security regime must be capable of screening high-risk transactions intensively without imposing the same degree of scrutiny on every transaction merely because of the investor's country connection. The publicly available policy framework also provided less procedural detail than the mature statutory and regulatory architecture found in jurisdictions such as the United States. In terms of the legal professionals involved in designing cross-border deals, this created an especially burdensome challenge: a requirement that could be easily stated, but not anticipated when planning, because there was no published criteria against which the deal team could measure its own risk. Approval or rejection was determined by an inter-ministerial committee headed by the Home Secretary, without any

statutory deadline, or requirement for stating the reasons for its decisions. Out of a total of 526 filings made under the regime of Press Note 3 up until April 2024, only 124 have been approved, and 201 outrightly rejected, leaving the rest uncertain. It does not serve as any sort of screening process from a legal perspective. It amounts to a veto power masquerading as regulation.

The Numbers Tell Their Own Story

The available investment figures illustrate the scale of the policy change but should not be treated as proof of causation. The manuscript's earlier figures reported Chinese FDI at approximately USD 2.51 billion between April 2000 and December 2025, or about 0.32% of cumulative FDI inflows. Those figures are useful for describing the observed investment position, but the decline in Chinese-origin investment cannot automatically be attributed to Press Note 3 alone. A rigorous assessment must account for diplomatic relations, global market conditions, corporate investment strategies, sectoral restrictions, and other regulatory interventions. The relevant policy lesson is therefore narrower: where a screening mechanism materially reduces investment flows, the State should be able to demonstrate that the additional scrutiny is directed toward transactions presenting identifiable security or public-order risks. National-security screening and investment promotion pursue different but overlapping public objectives. A government may legitimately accept a reduction in certain categories of foreign capital where security risks justify it. At the same time, a screening system that cannot distinguish between passive capital and acquisition of strategic control may impose compliance costs without necessarily improving the quality of national-security assessment. The case for reform therefore rests less on restoring any particular level of Chinese investment and more on developing a transparent, risk-based method for differentiating transactions.

From the standpoint of law, what is important about this measure is not only the scope of it but rather the imprecision of its definition. The trigger mechanism under Press Note 3, based on the investor's nationality, affected venture capital firms, private equity entities and even portfolio managers whose investments had only some incidental affiliation with Chinese limited partners, putting them in the same category as a strategic buyer wanting to have a controlling interest in a company operating in the defence industry. The trigger could not differentiate between a state-owned enterprise from Shenzhen trying to gain control of an Indian port operator and a global investment firm with five percent investments from Chinese sovereign wealth aiming to buy out a minority stake in an Indian fintech startup.

Before Press Note 3, the share of investments of Chinese origin was close to 2%; now it stands somewhere from 0.27% to 0.34% and has stayed roughly at the lower bound. Even in the latest financial year for which official figures are available, i.e., FY 2025-26, only one FDI proposal from China has been sanctioned, totalling a meagre one crore rupees, while 13 such proposals from Hong Kong have been approved along with it. In the same financial year, the number of sanctioned proposals worth more than ten thousand crore rupees was 63 in total; and Singapore, United Kingdom and Thailand were at the forefront of those countries whose investments were sanctioned in that year.

These numbers do not represent the results of a balanced bilateral investment relationship by the two most populous countries in the world and two of its biggest economic powers. Instead, these are the results of six years of complete freeze without regard to the general atmosphere of diplomacy in existence between New Delhi and Beijing.

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The March 2026 Recalibration Success, But Limited Implementation So Far

The 10 March 2026 Union Cabinet decision introduced a more defined framework for certain investments from countries sharing a land border with India. The Government stated that the changes were intended to unlock FDI, provide greater certainty, and facilitate manufacturing, technology collaboration, and supply-chain integration while retaining scrutiny under the Government route where required. The official announcement emphasized a 60-day decision timeline for investments in specified areas.

The significance of the 2026 change is procedural as well as economic. A stated decision period improves transaction planning because parties can incorporate the regulatory process into conditions precedent, long-stop dates, financing arrangements, and closing mechanics. It also creates a benchmark against which administrative delay can be assessed. Nevertheless, a time limit alone does not establish a complete national-security screening regime. A mature framework also requires published criteria, institutional responsibility, information requirements, confidentiality protections, reasoned outcomes, and mechanisms to address circumvention or material changes in ownership.

The distinction between passive investment and control is especially important for M&A. A small investment without governance rights may create materially different security risks from an acquisition that provides board representation, veto rights, access to sensitive technology, control over data, or operational influence. CFIUS itself demonstrates that percentage ownership is not the sole measure of jurisdiction: FIRRMA expanded CFIUS authority to certain non-controlling investments involving sensitive U.S. businesses. The appropriate Indian lesson is therefore not simply to replace one numerical threshold with another, but to combine ownership thresholds with functional indicators of control, access, and strategic significance.

The interaction between investment screening and trade policy also warrants caution. Restrictions on foreign capital may coexist with continued dependence on imported components, technology, or intermediate goods. This does not make either policy inherently inconsistent, but it demonstrates why investment screening should be designed around clearly articulated national-security objectives rather than assumed to substitute for industrial, trade, or supply-chain policy. The legal framework should identify what risk is being addressed and which regulatory instrument is capable of addressing it.

At the same time, the exception contained in the same regulation reveals that this liberalization is limited. Global funds registered in China or Hong Kong (but not global investment vehicles with incidental Chinese ownership of less than ten percent) still need to go through the discretionary prior-approval process. This means that the 2026 liberalization has solved the problem of passive investments, but left the problem of M&A transactions unchanged as compared to April 2020. In other words, the current M&A process is no different from what it used to be six years ago for a Chinese strategic acquirer willing to purchase a majority stake in an Indian company. Given that this paper is focused on M&A transactions specifically (as opposed to portfolio or venture-capital flows), this is an important distinction to make.

It is essential to highlight another aspect of the matter to be considered by those keeping an eye on the Indian trade policy. On October 2025, China filed a dispute at the World Trade Organization concerning the PLI programs that favor advanced battery chemistry, automobiles, and electric vehicles with domestic value addition requirements allegedly violating WTO subsidies and trade-related investments regulation, discriminating against Chinese suppliers. Dispute resolution panels were set up in February 2026 following failed bilateral consultations. Such an incident highlights the following crucial point. India's investment screening posture with regard to China cannot be viewed separately from the country's trade remedy posture. Manufacturing industry, which is supposed to be protected from the Chinese capital, becomes heavily reliant on Chinese parts imported through those very PLIs that come under criticism in the context of the WTO dispute. Such a consideration needs to be taken into account in any legal reform proposals in this area rather than the assumption that two matters are completely separated from each other.

LESSONS LEARNED FROM CFIUS AND THE EU SCREENING REGULATION

The Committee on Foreign Investment in the United States (CFIUS) provides a useful comparative model because its jurisdiction is connected to specified categories of transactions, U.S. businesses, critical technologies, critical infrastructure, sensitive personal data, and certain real-estate transactions. FIRMA expanded CFIUS jurisdiction beyond controlling acquisitions to certain non-controlling investments and specified real-estate transactions. The U.S. Treasury describes CFIUS as an interagency committee authorized to review covered foreign investment transactions for national-security implications, supported by detailed regulations under 31 C.F.R. parts 800 and 802.

The European Union framework is structurally different. Regulation (EU) 2019/452 establishes a cooperation framework rather than a single centralized EU approval authority. It identifies factors that Member States and the Commission may consider, including critical infrastructure, critical technologies, critical inputs, sensitive information, and whether the foreign investor is directly or indirectly controlled by a third-country government. It also emphasizes information sharing, confidentiality, timeframes, and recourse against screening decisions.

The comparative lesson is therefore not that investor nationality should be ignored. Nationality, state ownership, government financing, and beneficial ownership can be relevant indicators of risk. The stronger lesson is that nationality should ordinarily operate alongside transaction-specific and target-specific factors. An Indian regime can retain enhanced scrutiny for investments connected with land-border jurisdictions while also asking whether the transaction concerns defence, telecommunications, critical infrastructure, strategic minerals, sensitive data, dual-use technology, or other assets whose compromise could materially affect national security. Such a framework would preserve the State's ability to respond to genuine strategic risks while reducing unnecessary aggregation of materially different transactions.

The Problem of the Legal Framework

Apart from the substantive trigger, the existing framework raises institutional and procedural questions. Press Note 3 operates through the FDI policy and Government-route architecture rather than through a standalone national-security screening statute equivalent to the U.S. CFIUS framework. This distinction matters because a national-security regime involves decisions that can affect valuation, financing, closing conditions and the allocation of regulatory risk in M&A agreements. A dedicated statute could define jurisdiction, information powers, review periods, confidentiality, mitigation, prohibited outcomes and recourse in a single coherent framework.

First, procedural certainty is important. Investors and Indian target companies should know when a filing is required, what information must be supplied, the expected review period, and what happens if additional investigation is required. Second, institutional expertise matters: a body reviewing semiconductor, defence, telecommunications, port, data and critical-mineral transactions should have access to technical and sectoral expertise rather than applying a single geographic test. Third, the system should permit proportionate remedies. Not every security concern requires prohibition; mitigation measures, governance restrictions, access controls, data segregation, ring-fencing, or restrictions on particular rights may in some cases address the identified risk.

Beneficial ownership and circumvention require particular attention. Press Note 3 already extends its policy to beneficial ownership, which demonstrates that the legal system recognizes the possibility of indirect structures. A statutory framework should build this principle into the filing process through ownership-chain disclosure, identification of ultimate beneficial owners, disclosure of government or sovereign-wealth interests, and continuing obligations to notify material changes. The EU framework similarly recognizes the need to prevent circumvention, while CFIUS requires detailed information concerning the transaction and ownership structure.

What a Codified Indian Framework Should Look Like

A proposed Indian National Security Review of Foreign Investment Act should be designed as a risk-based screening statute rather than as a simple replacement for Press Note 3. The following elements would provide a workable institutional architecture.

Second, the statute should establish a dedicated National Security Review Authority or an appropriately constituted inter-ministerial statutory body. Its composition should combine national-security, finance, commerce, technology, infrastructure and legal expertise. The body should have written rules of procedure; a secure electronic filing mechanism; power to request information; authority to coordinate with sectoral regulators; and a statutory review period. A proposed model could provide an initial 30-day screening stage, followed where necessary by a detailed review of up to 60 days, with a narrowly defined extension for exceptional cases. The parties should receive a written outcome clearance, clearance subject to mitigation, or prohibition within the statutory framework. This is a design proposal, not a claim that the present Indian law already contains these institutional features.

Third, the statute should use a functional control test in addition to any percentage-based safe harbour. Board appointment rights, veto rights over material corporate decisions, access to sensitive technology or personal data, rights to appoint key managerial personnel, and contractual arrangements conferring decisive influence should be considered. A ten-percent or other numerical threshold may provide an administrative safe harbour for genuinely passive investment, but it should not immunize a transaction that confers substantive control or sensitive access. Conversely, a small passive investment without governance or sensitive-access rights should not automatically receive the same scrutiny as an acquisition of strategic control.

Fourth, beneficial-ownership disclosure should be mandatory before a transaction receives automatic-route treatment. The filing should disclose the ownership chain up to the ultimate beneficial owner, material government or state-linked interests, financing arrangements relevant to control, and any shareholder or governance agreement that could confer influence. Misrepresentation should attract proportionate civil and regulatory penalties, and a complete transaction should remain subject to review where material ownership or control information was concealed. The statute should also include confidentiality protections and a clear mechanism for challenging procedural illegality or seeking review of a final order, while preserving the government's authority to protect genuinely sensitive national-security information.

CONCLUSION

The comparative analysis of CFIUS and the EU framework suggests several principles that can inform Indian law without requiring institutional transplantation. Review should be triggered by a combination of sectoral and transaction-specific factors; nationality and state-linked ownership should remain relevant aggravating factors; control should be assessed functionally rather than solely through shareholding; beneficial ownership should be transparent; and the review process should operate within defined timelines, confidentiality rules, reasoned outcomes, and proportionate remedies. A dedicated statutory framework would also allow Parliament and the executive to define the relationship between national-security review and existing FDI, FEMA, competition, sectoral, data, and corporate-law regimes.

The proposed National Security Review of Foreign Investment Act is therefore intended as a framework for calibrated scrutiny rather than a presumption either for or against foreign capital. Its objective would be to make the Indian M&A environment more predictable for legitimate transactions while preserving a strong governmental response where foreign investment creates a demonstrable national-security concern. Such a framework would better align regulatory intervention with the nature and severity of the risk being addressed.

India need not treat foreign investment and national security as mutually exclusive objectives. The principal challenge is to design a legal mechanism capable of distinguishing transactions that create

material security risks from transactions that do not. Press Note 3 responded to an exceptional economic and geopolitical context by using a broad approval trigger. The 2026 recalibration introduces greater procedural certainty for specified categories, but the continuing importance of controlling acquisitions demonstrates the need for a more complete screening architecture.

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CONFLICT OF INTEREST

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