Companies Act Series

July 14, 2025

NSDL CIRCULAR ON OFF-MARKET TRANSFERS: ALIGNING WITH COMPANIES ACT, 2013

- NSDL mandates prior company consent for off-market transfers of dematerialized shares held by shareholders of private limited companies.
- Alignment of depository operations with the Companies Act, 2013, giving effect to share transfer restrictions under Articles of Association and shareholder agreements.
- Currently, this requirement applies only to off-market transfers through NSDL, creating potential regulatory arbitrage in the absence of similar guidelines from CDSL

INTRODUCTION

The National Securities Depository Limited ("**NSDL**"), through the Participant Services CircularNo. NSDL/POLICY/2025/0071 dated June 03, 2025 ("**Circular**")[1], has introduced a critical compliance step while processing off-market transfers of dematerialized shares held by shareholders of private limited companies. The Depository Participants ("**DPs**") have been directed to ensure strict adherence to this requirement and to inform their clients accordingly. Subsequently, on June 05, 2025, NSDL issued Issuer Interface Circular No.: NSDL/CIR/II/17/2025[2] to bring the Circular to the attention of Issuers and Registrar and Share Transfer Agents ("RTAs"), and to instruct them to notify their client companies. The compliance requirement introduced under the Circular marks a significant step toward aligning depository practices with the statutory framework applicable to private companies under the Indian Companies Act, 2013 (the "**Act**").

THE PRE-CIRCULAR LANDSCAPE

Prior to the issuance of the Circular, shareholders of private companies were able to initiate off-market transfers of their dematerialized securities by simply submitting a Delivery Instruction Slip ("**DIS**") to their DP. This process, however, did not account for the complex legal and contractual restrictions typically applicable to share transfers in the private companies such as the restrictions contained in the Articles of Association ("**AoA**"), shareholders' agreements, and other binding inter-se arrangements.

While these restrictions were enforceable in theory, the depository system lacked any mechanism to vet or flag non-compliant share transfers in practice. In such cases, the companies were informed of such transfers only on post facto basis, by way of discovering such share transfers upon reviewing the updated BENPOS i.e., Beneficiary Position Statement, which is generally supplied on a weekly basis by the RTA. This disconnect between the legal and/or contractual restrictions and operational execution posed risks of unauthorized or disputed transfers, undermining the legal sanctity of transfer restrictions under the Act. To mitigate these risks, some well-advised private companies voluntarily adopted safeguards such as inserting restrictive clauses in their AoA specific to dematerialized share transfers, keeping RTAs apprised of such restrictions, requesting the freezing of the relevant ISIN in the depository system, or establishing joint demat accounts. These measures also played a critical role in controlling the actions of nominee shareholders, particularly in the context of nominee shareholdings held in wholly owned subsidiaries.

KEY CHANGE INTRODUCED BY THE CIRCULAR

To address this gap, the Circular mandates an additional compliance step as per which, the shareholder holding shares of a private limited company in demat form and intends to transfer shares will now have to mandatorily obtain and submit to their DP, a prior consent from the concerned private company confirming no objection for the proposed share transfer. This is in addition to depositing a duly executed DIS. This consent should be in the format prescribed in the Circular and include key details such as the names of the transferor and transferee, the number and class of shares being transferred, and the reason for the transfer. Without such a consent, the DPs are instructed not to process any off-market transfer of shares of private companies.

LEGAL RATIONALE BEHIND THE CIRCULAR

This requirement stems directly from the statutory framework under the Act, particularly Section 2(68) of the Act defines a private company as one which, inter alia, *restricts the right to transfer its shares through its Articles.* Further, Section 58 (1) of the Act stipulates that any refusal by a private company to register a transfer should be based on the restrictions contained in its Articles, thus reinforcing that private companies enjoy a legally recognized right to pre-approve or block share transfers.

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While the provisions to restrict share transfer in case of private companies long existed, enforcement was primarily relevant in the context of physical share transfers or in disputes before the National Company Law Tribunal (NCLT). With the increasing shift to dematerialized securities particularly that, all the private companies, other than small companies, are now mandated to issue securities and approve transfer of securities only in dematerialized form (Please see our hotline MCA's Digital Leap: Dematerialization of Securities by Private Companies for this), the Circular now bridges the gap by embedding the statutory restriction into the depository share transfer system.

This Circular strengthens private companies' ability to maintain control over its shareholder base by preventing any unvetted or potentially hostile changes in the ownership. The existing AoA restrictions and contractual arrangements if any will now be honored as this Circular has aligned depository processes with the statutory and internal governance norms.

From the shareholders perspective, though this additional compliance step intend to protect their interest, it can sometimes elongate share transfer timelines. This is since, unlike Sections 56 and 58 of the Act which impose a 30-day timeline for processing physical transfers, the Circular does not prescribe a timeline within which the companies have to respond to the consent requests. This creates uncertainty, particularly in time-sensitive transfers. Also, in contentious or control-sensitive scenarios, there may be a possibility that the company may try to delay or frustrate even the valid share transfers. To prevent such potential abuse, it may be advisable for the regulators to specify a timeline. In the interim, the companies and shareholders can consider addressing this by way of specifying a timeline in the AoA for the company to issue requisite consents for share transfers. Alternatively, the investment agreements can include specific obligation on the target company to issue such consent within a definite period, failing which the consequences to follow.

Separately, in situations involving pledge of shares, where the pledge has been invoked, the flow of shares from the pledgor's demat account to the pledgee's demat account may, on the face of it, constitute a share transfer within the scope of the Circular. However, such transfers are processed pursuant to a share pledge agreement and through an automatic transfer mechanism as per prescribed operational guidelines without requiring a DIS.

Accordingly, it can be reasonably argued that the consent requirement under the Circular should not extend to transfers effected upon pledge invocation. Imposing the consent requirement could potentially undermine the enforceability of security interests, which are otherwise protected under applicable laws.

Pertinent to note that this requirement currently applies only to off-market transfers through NSDL, and no corresponding compliance has yet been issued by the Central Depository Services (India) Limited("**CDSL**"). This discrepancy could result in regulatory arbitrage, where shareholders may opt to use the less restrictive depository for executing transfers. It remains to be seen whether CDSL will adopt a parallel framework to maintain regulatory parity.

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You can direct your queries or comments to the relevant member.

[1] https://nsdl.co.in/downloadables/pdf/2025-0071-Policy-Processing_of_off-market_transfer_instructions_in_shares_of_Private_Limited_Companies.pdf

[2] https://nsdl.co.in/downloadables/pdf/17_Circular_for_Processing_of_off-market_transfer_instructions_in_shares_of_Private_Limited_Companies.pdf

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