Overview of FDIs and ECBs

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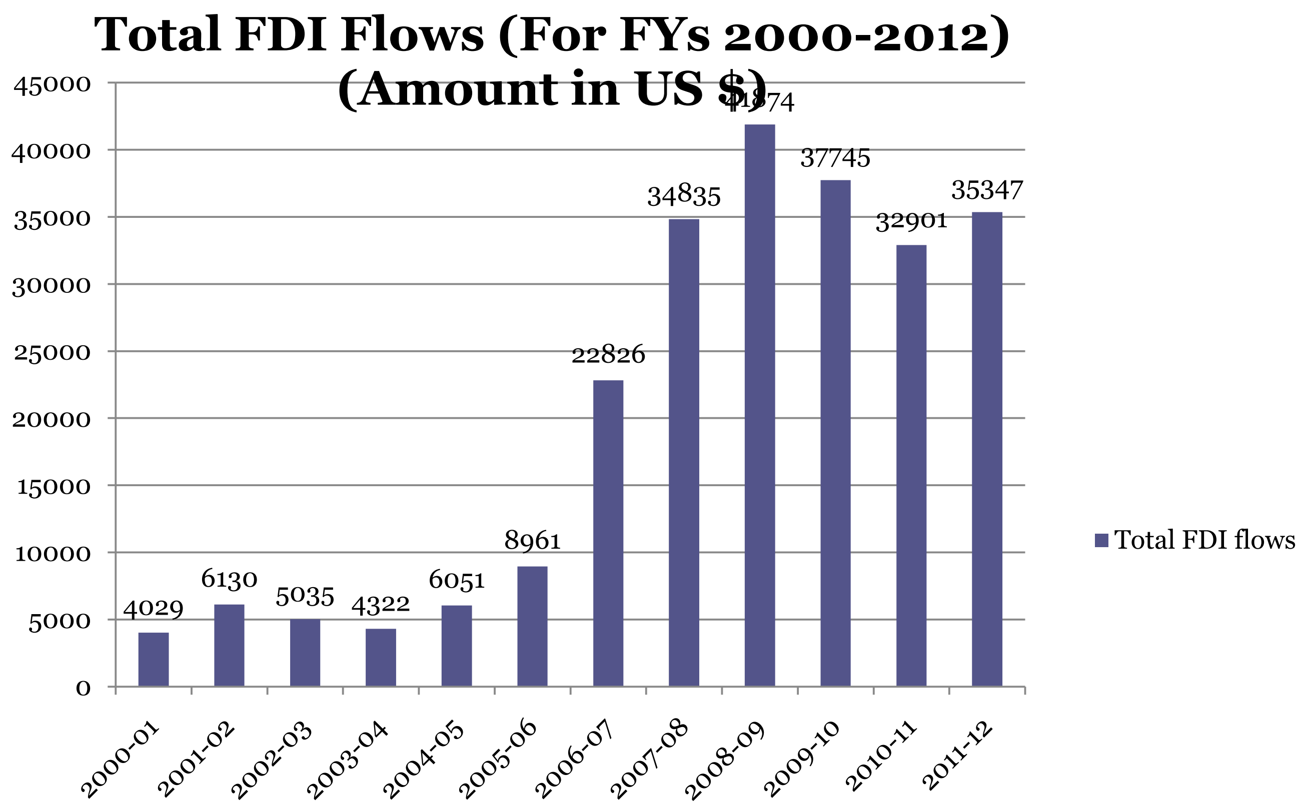
India as FDI destination

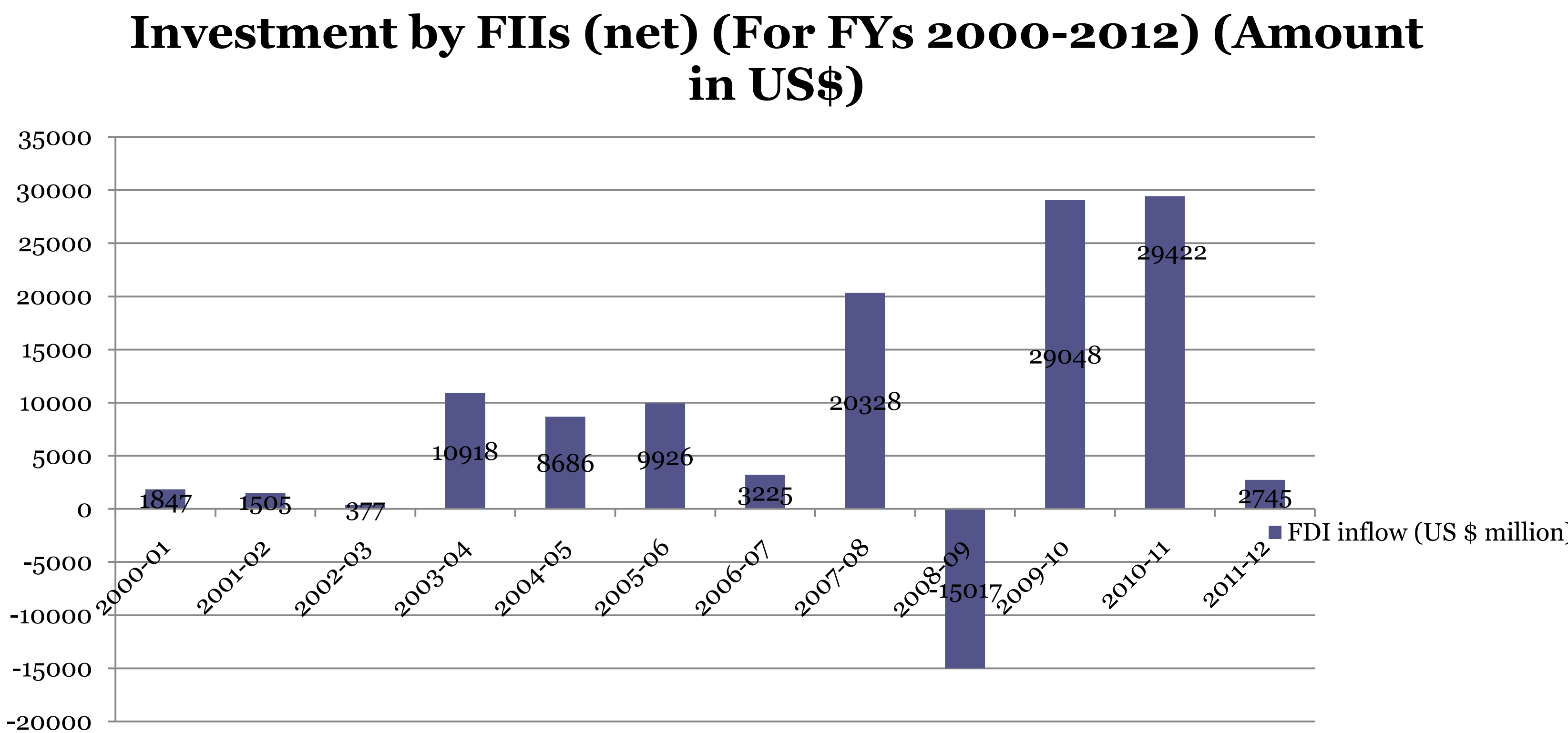
- As per UNCTAD data, India remains a strong FDI destination
  - India received a total inflow of USD 34 billion in 2011, compared to:
    - China: 124 billion
    - Russia: 50.8 billion
    - Brazil: 65.5 billion
  - Several clients confirm that it is much easier to set up business in Brazil than it is in India.
  - Taxation framework of India seems to be a big challenge
- Vodafone ruling is a big comfort to international investors; however, if the Govt opts to amend the law in the coming budget, it will add to the uncertainty.

FDI flows into India



Source: Fact Sheet on Foreign Direct Investment (FDI) from April 2000 to December 2011 (www.dipp.nic.in)

FII investments



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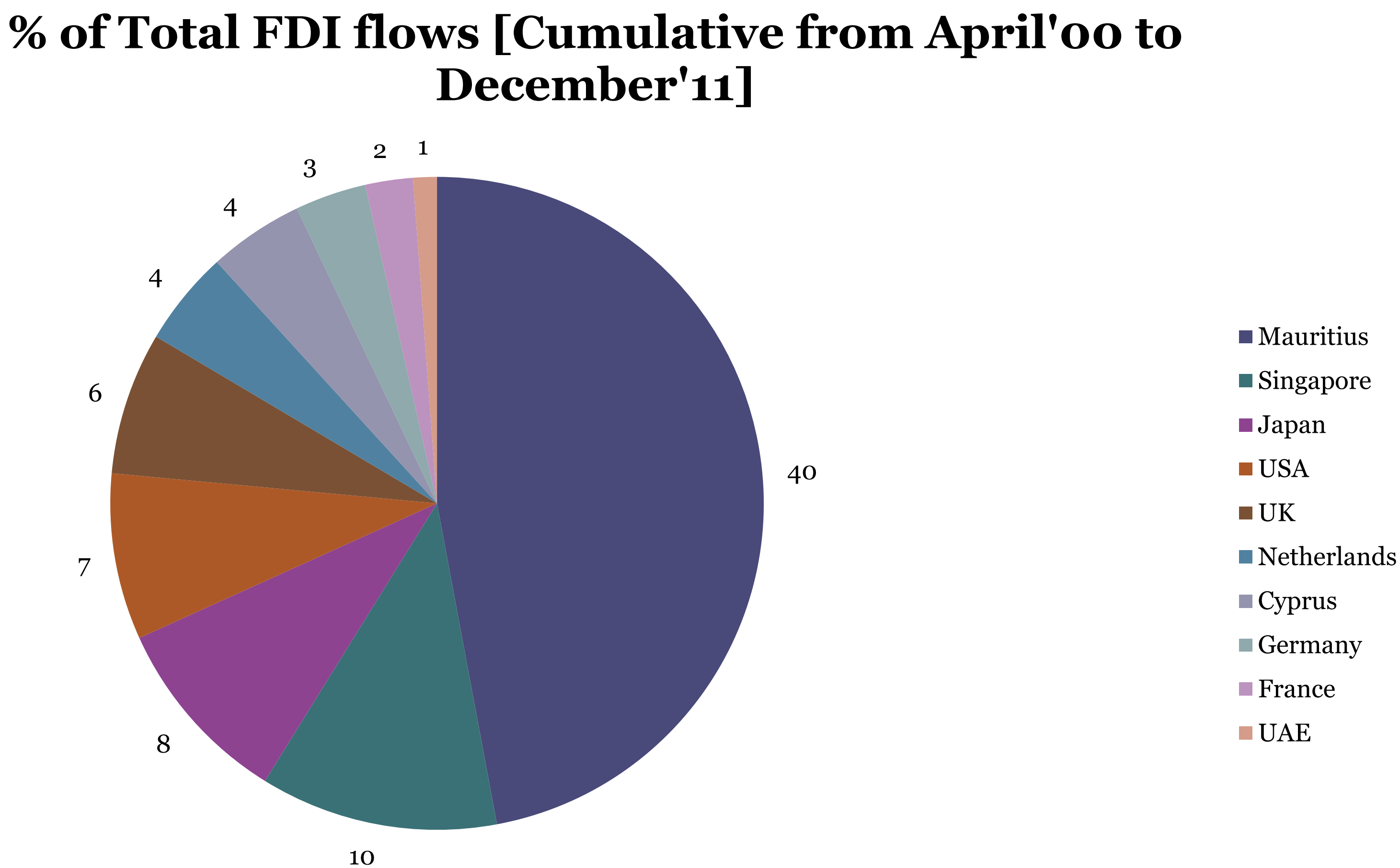
Where does the money come from?



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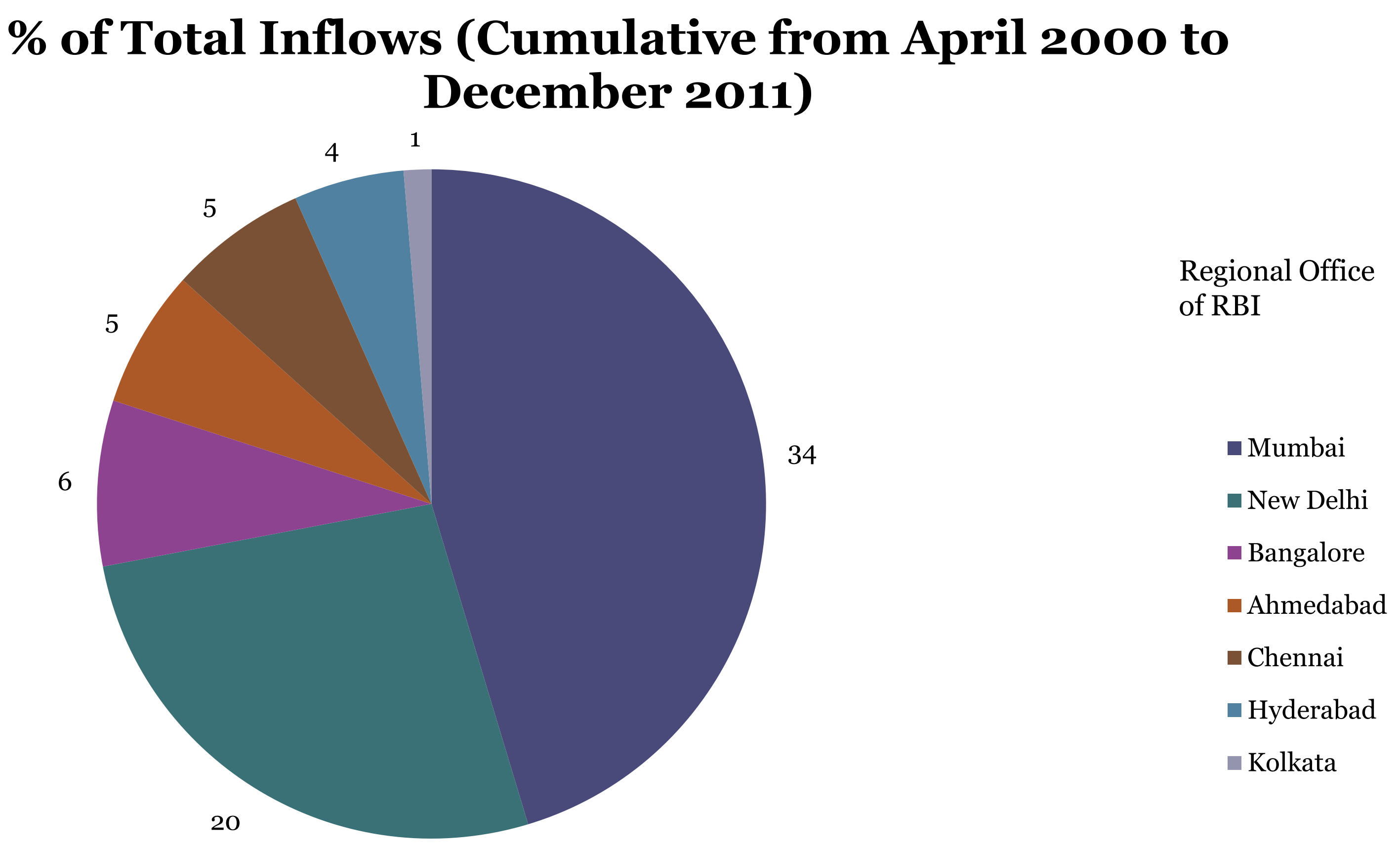
Which cities does the FDI go to



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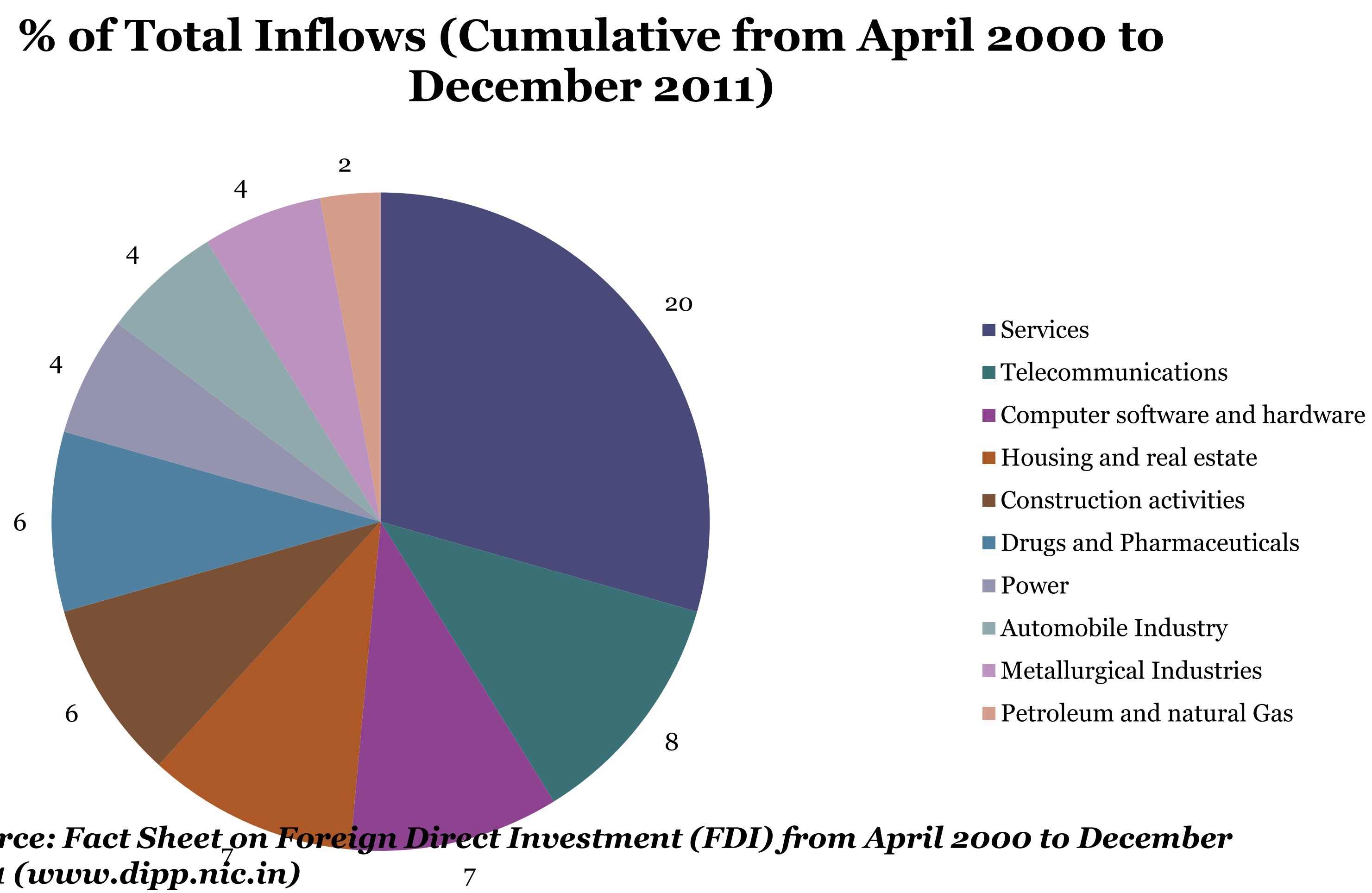
Which sectors does it go to



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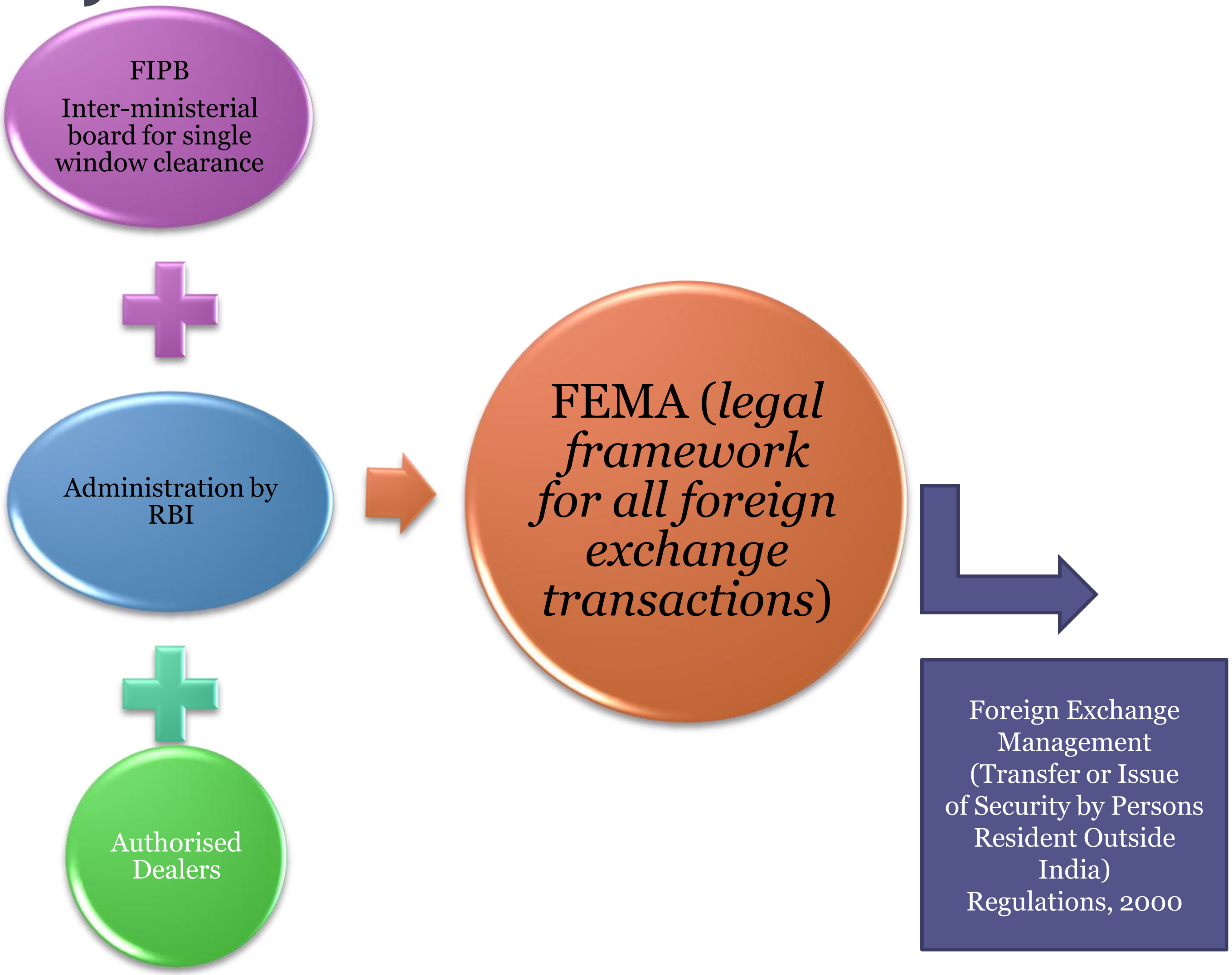
Regulatory framework for FDI in India



Classification of Foreign Investments

- Equity
  - Foreign Direct Investment
  - Foreign Portfolio Investment
  - Foreign Venture Capital Investment
- Debt
  - External Commercial Borrowings

What applies where

- Direct investment into shares of an Indian company:
  - FDI
    - Can be used for general corporate purposes; no end-use restrictions
  - Investments by FVCFs
- Secondary market transactions in company's equity:
  - Acquisition of shares from a resident by a non-resident
    - FIIs
    - NRIs/ PIOs
- Debt:
  - Short-term debt for imported goods
    - Supplier's credit
  - Short-term debt for imported capital goods
    - Buyer's credit
  - Loans/borrowings
    - ECBs – can be used only capital expenditure or permitted use
  - FCCBs
  - FCEBs

Why do foreign entities need FDI

- There are several ways an overseas entity may enter India:
  - Branch office
  - Liaison office
  - Project office
  - Site office
  - Alliances
- Branch and liaison offices: Foreign Exchange Management (Establishment in India of Branch or Office or other Place of Business) Regulations put blanket bar on branch or liaison offices, except with specific RBI approval
  - Separate rules for project offices, however, also closely regulated
- In addition, the activities of branches and liaison offices are closely controlled
- Therefore, if one wants to do business in India, the obvious choice is Indian subsidiary or JV

What is covered by FDI

- Equity shares
- Preference shares
  - Only if fully, mandatorily convertible into equity
- Bonds/debentures
  - Only if fully, , mandatorily convertible into equity
- Partly paid up shares:
  - Only covered under approval route
- Share warrants
  - Only covered under approval route
- Depository receipts
  - Also treated as FDI

Who can invest in India?

- Non-resident entity
  - Other than a citizen of Pakistan or an entity incorporated in Pakistan
- NRIs resident in Nepal and Bhutan as well as citizens of Nepal and Bhutan
- FIIs
- SEBI registered FII, NRIs, Foreign Venture Capital Investor (FVCI)

•***Bangladesh residents or companies can invest only through approval route.***

•

NRIs in Nepal and Bhutan

NRIs as well as citizens of Nepal and Bhutan are permitted to invest in the capital of Indian companies on repatriation basis

Subject to the condition that the amount of consideration for such investment shall be paid only by way of inward remittance in free foreign exchange through normal banking channels

Foreign Institutional Investors (FIIs)

- FII may invest in the capital of an Indian Company under the Portfolio Investment Scheme subject to
  - individual holding of 10% of the capital of the company
  - aggregate limit of 24% of the capital of the company
    - Aggregate limit can be increased to the sectoral cap by the Indian Company concerned through a resolution passed at BM and SR passed at GM
- The aggregate FII investment, in the FDI and Portfolio Investment Scheme, should be within the above caps
  - That is to say, the cap of 24% applies to holdings of FIIs both under FDI as also under portfolio investment scheme

Investments by NRIs

- Two types of investments:
  - Repatriable
  - Non repatriable
- Non-repatriable investments will generally be allowed except in agriculture, plantations, and print media
- Repatriable Investments by NRIs under the Portfolio investment scheme subject to the following:
- the total purchase of all NRIs/PIOs both, on repatriation and non-repatriation basis, are within the overall ceiling limit of
  - 24 per cent of the company's total paid up equity capital;
  - 24 per cent of the total paid up value of each series of convertible debenture; and
- the investment made on repatriation basis by any single NRI/PIO in the equity shares and convertible debentures not exceeding five per cent of the paid up equity capital of the company or five per cent of the total paid up value of each series of convertible debentures issued by the company.

SEBI registered Foreign Venture Capital Investor (FVCI)

FVCI may contribute up to 100% of the capital of an Indian Venture Capital Undertaking

- May also set up a domestic asset management company to manage the fund

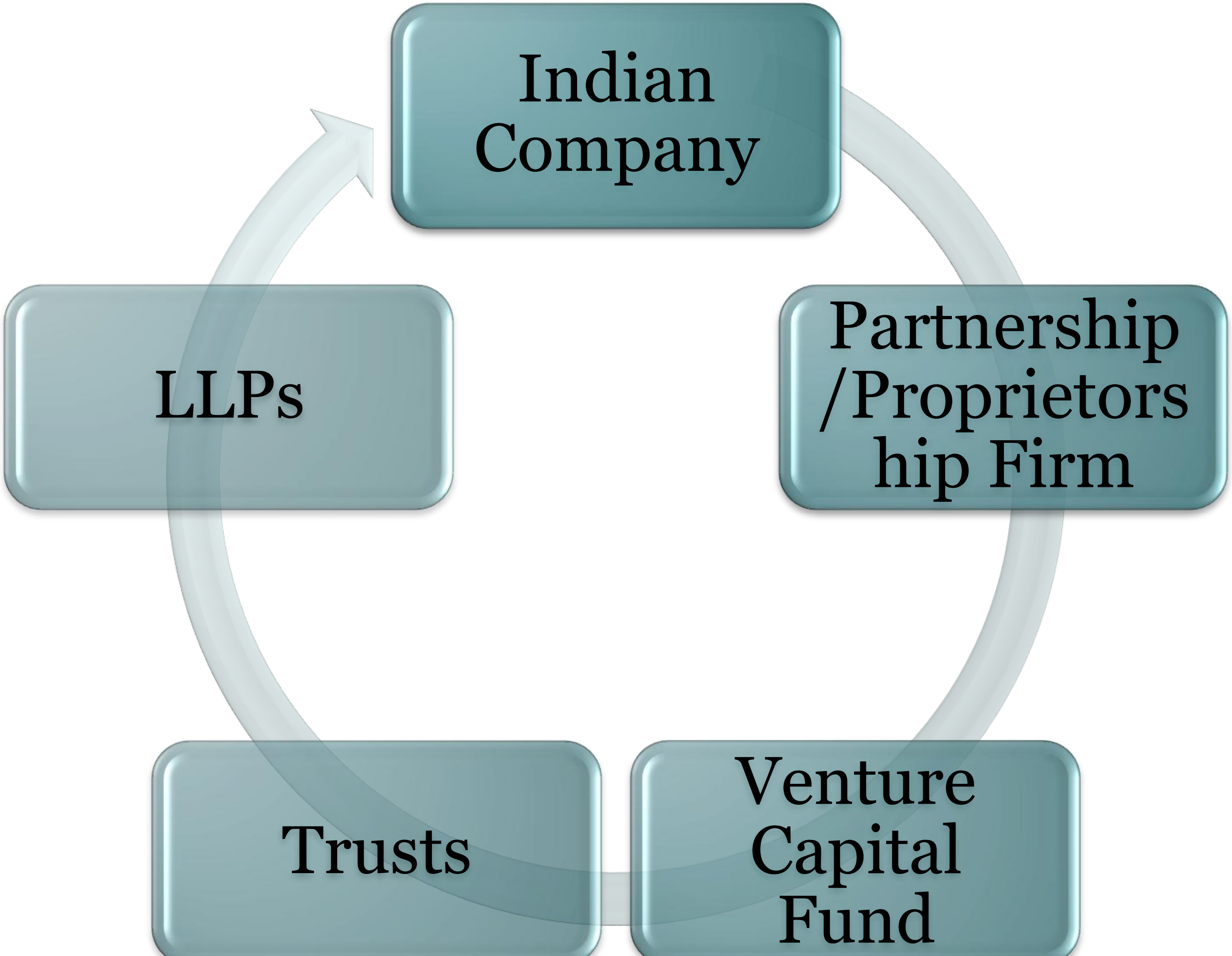
All such investments can be made under the automatic route in terms of FEMA Schedule 6

Can invest in a domestic venture capital fund non-resident entities and in other companies, subject to FDI Policy and FEMA regulations.

Investments by FVCI

- Investments may be made on in Venture capital undertaking (VCU)
- VCU is defined as an unlisted company not engaged in businesses negative listed under SEBI Regulations
- There are 2 regulations relevant here:
  - SEBI Regulations:
    - NBFCs, other than RBI registered leasing and hire purchase companies (now called asset finance companies)
    - Gold finance companies
    - Activities not permitted under Industrial policy
  - Tax rules:
    - No tax exemption available if the VCF invests in any sector other than 8 sectors.
    - In case of FVCIs, Indian taxation rules will be applicable to the extent of income arising in India

Entities into which FDI can be made



Entities into which FDI can be made contd..

Indian Companies	• Can issue shares against FDI
Partnership/Proprietor Firm	• NRI and PIO can invest on non-repatriation basis; repatriable investment only allowed on approval basis • Investments by persons other than NRIs/PIOs – based on specific approval of RBI
VCFs	• FVCIs can invest in domestic VCFs • Two types of VCFs: • Trusts: only on approval route • Companies – automatic route, subject to compliance with pricing guidelines

Entities into which FDI can be made contd..

Trusts

- FDI in Trusts other than VCF is not permitted

LLPs

- Allowed through Government Route only in LLPs operating in sectors/activities where 100% FDI is allowed, through the automatic route :
  - That is to say, no FDI in LLPs engaged in financial services
- LLPs with FDI not allowed to operate in agricultural/plantation activity, print media or real estate business
- LLPs with FDI not eligible to make any downstream investments
- Investment by FIIs and FVCIs not permitted
- Conversion of a company with FDI, into an LLP, will be allowed only if the above stipulations are met and with the prior approval of FIPB/Government

Entry routes for investments

- **Automatic Route**
  - No approval required, if invested within sectoral caps
  - In some sectors, 100% FDI allowed
- **Government Route**
  - Approval of FIPB required

Issue of CCDs, CCPS for FDI

- Note – only compulsorily convertible instruments are permitted as FDI
  - If optionally convertible, they are taken as ECBs
- Why convertible instruments:
  - Entities hope to get better pricing by deferring the equity issuance
  - Quite a common route to investing by VCFs
- Some key points about CCDs:
  - Any limit on time for conversion: none
  - Conversion terms: either the conversion price should be prefixed, or the conversion formula
    - In either case, price should not be lower than:
      - DCF value in case of unlisted shares
      - SEBI ICDR price, in case of listed shares
      - At the time of issuance of the instrument

Issue of shares by Indian Company under FCCB/ADR/GDR

- Companies which are eligible to issue shares to person resident outside India can issue in accordance with the Scheme for issue of Foreign Currency Convertible Bonds and Ordinary Shares (Through Depository Receipt Mechanism) Scheme, 1993
- Unlisted companies
  - which have not yet accessed the ADR/GDR route for raising capital in the international market, would require prior or simultaneous listing in the domestic market
  - which have already issued ADRs/GDRs in the international market, have to list in the domestic market on making profit or within three years of such issue of ADRs/GDRs, whichever is earlier
- No end-use restrictions except for a ban on deployment / investment of such funds in real estate or the stock market
- No monetary limit up to which an Indian company can raise ADRs / GDRs
- Erstwhile OCBs who are not eligible to invest in India and entities prohibited from buying, selling or dealing in securities by SEBI will not be eligible to subscribe
- Pricing to be done in accordance with the Scheme, 1993

Issue of Shares

Capital instruments should be issued within 180 days from the date of receipt of the inward remittance

- If not issued within 180 days, the amount of consideration so received should be refunded immediately
- Non compliance would attract penal provisions

Pricing of shares

- In case of FDI into equity sharse, price should not be less than:
  - Price calculated in accordance with SEBI, if issuing company is listed
  - Fair valuation of shares done by a SEBI registered Category - I Merchant Banker or a Chartered Accountant as per the discounted free cash flow method, where the shares of the company is not listed; and
  - Price as applicable to transfer of shares from resident to non-resident as per the pricing guidelines laid down by RBI, where the issue of shares is on preferential allotment
- Indian companies eligible to issue shares to persons resident outside India under the FDI Policy may be allowed to retain the share subscription amount in a Foreign Currency Account, with the prior approval of RBI

Acquisition route: Transfer of shares and convertible debentures under general permission

- Form FC-TRS to be submitted within 60 days from the date of receipt of the amount of consideration
- Transfers/sale by:
  - A person resident outside India
    - (other than NRI and erstwhile OCB) may transfer by way of sale or gift to any person resident outside India (including NRIs)
    - can transfer to a person resident in India by way of gift
    - sell the shares and convertible debentures on a SE
    - to a person resident in India under private arrangement subject to the FDI Guidelines
  - NRIs may transfer by way of sale or gift to another NRI

Transfer of shares and convertible debentures under general permission contd..

Person resident in India

- can transfer by way of sale of an Indian company in sectors other than financial services sectors under private arrangement to a person resident outside India, subject to the FDI Guidelines
- to a non-resident by transfer of shares/convertible debentures of an Indian company, engaged in an activity earlier covered under the Government Route but now falling under Automatic Route, as well as transfer of shares by a non-resident to an Indian company under buyback and/or capital reduction scheme of the company

Transfer of shares from non-resident to residents

- General guidelines (annex 2 of the FDI Circular)

Transfers requiring prior permission of RBI

- Following instances of transfer from resident to non-residents by way of sale:
  - Transfer of capital instruments of an Indian company engaged in financial services sector :
    - Banks, NBFCs, asset reconstruction companies, insurance companies, etc
  - Transactions falling under SEBI Takeover Regulations
  - Activity of issuing company is outside the automatic route and the approval of the Government has been obtained for the said transfer
  - Transfer at a price which falls outside the pricing guidelines specified by the RBI
  - Transfer where the non-resident acquirer proposes deferment of payment of the amount of consideration
- If approval granted, the same should be reported in Form FC-TRS, to an AD Category-I bank within 60 days from the date of receipt of the full and final amount of consideration

Transfers requiring prior permission of RBI contd..

- By a person resident in India, who intends to transfer any capital instrument, by way of gift to a person resident outside India
- Transfer of capital instruments of companies engaged in sectors falling under the Government Route from residents to non-residents by way of sale or otherwise

Issue of Rights/Bonus Shares

- Indian Companies can issue Rights/Bonus shares to existing non-resident shareholders, subject to adherence to sectoral cap, if any
  - Provisions of other Applicable Laws like Companies Act, SEBI ICDR Regulations, to be complied with
- The offer on right basis to the persons resident outside India shall be:
  - at a price as determined by the company, if shares are listed
  - at a price which is not less than the price at which the offer on right basis is made to resident shareholders , if shares are unlisted
- Issue to erstwhile OCBs will require prior approval of RBI

Acquisition of shares under scheme of arrangement

On approval of the scheme by the competent court, the transferee company or new company is allowed to issue shares to the shareholders of the transferor company resident outside India, subject to the conditions that:

- Shareholding in new/transferee company is within the sectoral cap
- the transferor company or the transferee or the new company is not engaged in activities which are prohibited under the FDI policy

Issue of shares under ESOP

- Listed companies can issue ESOP directly or through a Trust subject to the condition that:
  - The scheme has been drawn in terms of relevant regulations issued by the SEBI
  - The face value of the shares to be allotted under the scheme to the non-resident employees does not exceed 5 per cent of the paid-up capital of the issuing company
- Unlisted companies can issue in compliance with Companies Act
- The issuing company is required to report the details of granting options and thereafter the details of issue of shares subsequent to the exercise of such stock options within 30 days from the date of issue of shares in Form FC-GPR

Unusual methods of receiving consideration

- Swap of shares:
  - Irrespective of amount, valuation of the shares will have to be made by a Category I Merchant Banker registered with SEBI or an Investment Banker outside India registered with the appropriate regulatory authority in the host country .
  - Approval of FIPB is also required
- Conversion of ECB/ lump sum royalty:
  - ECBs can be converted into equity shares, subject to pricing norms, sectoral caps, etc.
  - Amount payable to foreign vendors such as lump sum fee, royalty can also be converted into equity based on entry route, sectoral and pricing restrictions
- Under government route, allowed against:
  - Import of machinery or capital goods:
    - Within 180 days of import
    - Capital goods have been valued by an independent valuer
  - Pre-operative or pre-incorporation exps

Pledge of shares

- Promoter of Indian borrowing company, which has raised ECB, may, for securing ECB, pledge shares of
  - borrowing company or
  - its associate resident companies
  - provided that a no objection for the same is obtained from the authorised dealer bank
- Non-resident holding shares of an Indian company, can pledge these shares in favour of the AD bank in India to secure credit facilities being extended to the resident investee company for bonafide business purpose, subject to following:
  - in case of invocation of pledge, transfer of shares should be in accordance with the FDI policy in vogue at the time of creation of pledge
  - submission of a declaration/ annual certificate from the statutory auditor of the investee company
  - Indian Company is to comply with SEBI disclosure norms
  - Pledge in favor of bank would be subject to Banking Regulation Act

Pledge of shares contd..

- Non-resident holding shares of an Indian company, can pledge in favour of an overseas bank to secure the credit facilities being extended to the non-resident investor / non-resident promoter of the Indian company or its overseas group company, subject to the following:
  - loan is availed of only from an overseas bank and utilized for genuine business purpose overseas
  - overseas investment should not result in any capital inflow into India
  - in case of invocation of pledge, transfer should be in accordance with the FDI policy in vogue at the time of creation of pledge
  - submission of a declaration/ annual certificate from a Chartered Accountant/ Certified Public Accountant of the non-resident borrower that the loan proceeds will be / have been utilized for the declared purpose

Transfer of ownership/control to non residents in sectors with caps

- FIPB approval requires in sectors with caps including:
  - defence production,
  - air transport services,
  - ground handling services,
  - asset reconstruction companies,
  - private sector banking,
  - broadcasting,
  - commodity exchanges, credit information companies, insurance,
  - print media,
  - telecommunications and satellites
- Approval requires if:
  - Indian company is established with foreign investment and is owned/controlled by non resident entity
  - Control/ownership is transferred to non resident entities by issuing new shares/transfer of shares through restructuring
- Approval not required if 100% FDI is permitted under automatic route

Entry routes to FDI

- Automatic route:
  - No approval of RBI required
  - Reporting mechanism
- Approval route:
  - Prior approval required
  - Approval to be sought from FIPB
- Transfer of control in all sectors where there are conditions will also require FIPB approval

FDI in Indian Companies engaged in investment business

Approval required irrespective of ownership/control of investing entity

FDI in NBFCs carrying on following activities would not require approval of FIPB, subject to capitalisation norms

- Merchant Banking
- Underwriting
- PMS
- Investment advisory services
- Financial consultancy
- Stock and Forex broking
- Asset Management
- Venture Capital
- Custodian Services
- Factoring
- Credit Rating Agencies
- Leasing and Housing Finance
- Credit Card business
- Money changing business
- Micro and Rural Credit

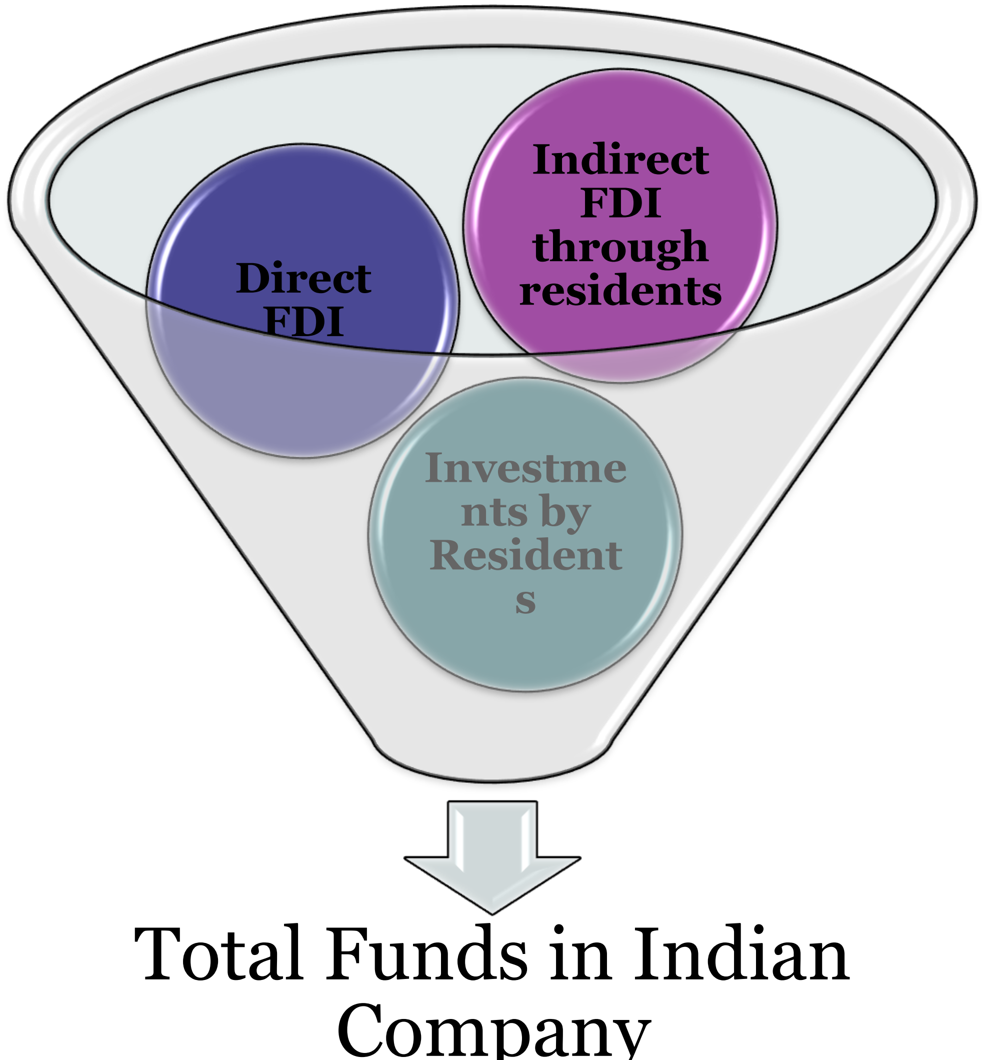
FDI in investment companies and entities without any operations

- FDI in Investment companies necessarily required FIPB approval
- In case of investment in infrastructure projects, investments through SPVs are allowed in limited cases
- In case of core investment companies, further requirements of RBI on CICs need to be satisfied
- In case of entities which do not have any operations, the case falls under approval route

Downstream investment by Indian Company owned/controlled by non residents

- Relevance of downstream investments:
  - In cases where there are sectoral caps, direct and “indirect” investments are counted
  - Indirect investments include downstream investments
  - Downstream investments also are subject to conditionalities
- Meaning of downstream investment:
  - Investments made in a company or LLP or partnership
- Investment shall be in accordance/compliance with the relevant sectoral conditions on entry route, conditionalities and caps, with regard to the sectors in which the latter Indian company is operating and shall be subject to:
  - company is to notify SIA, DIPP and FIPB of its downstream investment within 30 days
  - downstream investment by way of induction of foreign equity in an existing Indian Company would require BR and SR of the company
  - issue/transfer/pricing/valuation of shares shall be in accordance with applicable SEBI/RBI guidelines
  - investing Indian company can use funds from abroad, leverage funds from domestic market cannot be used

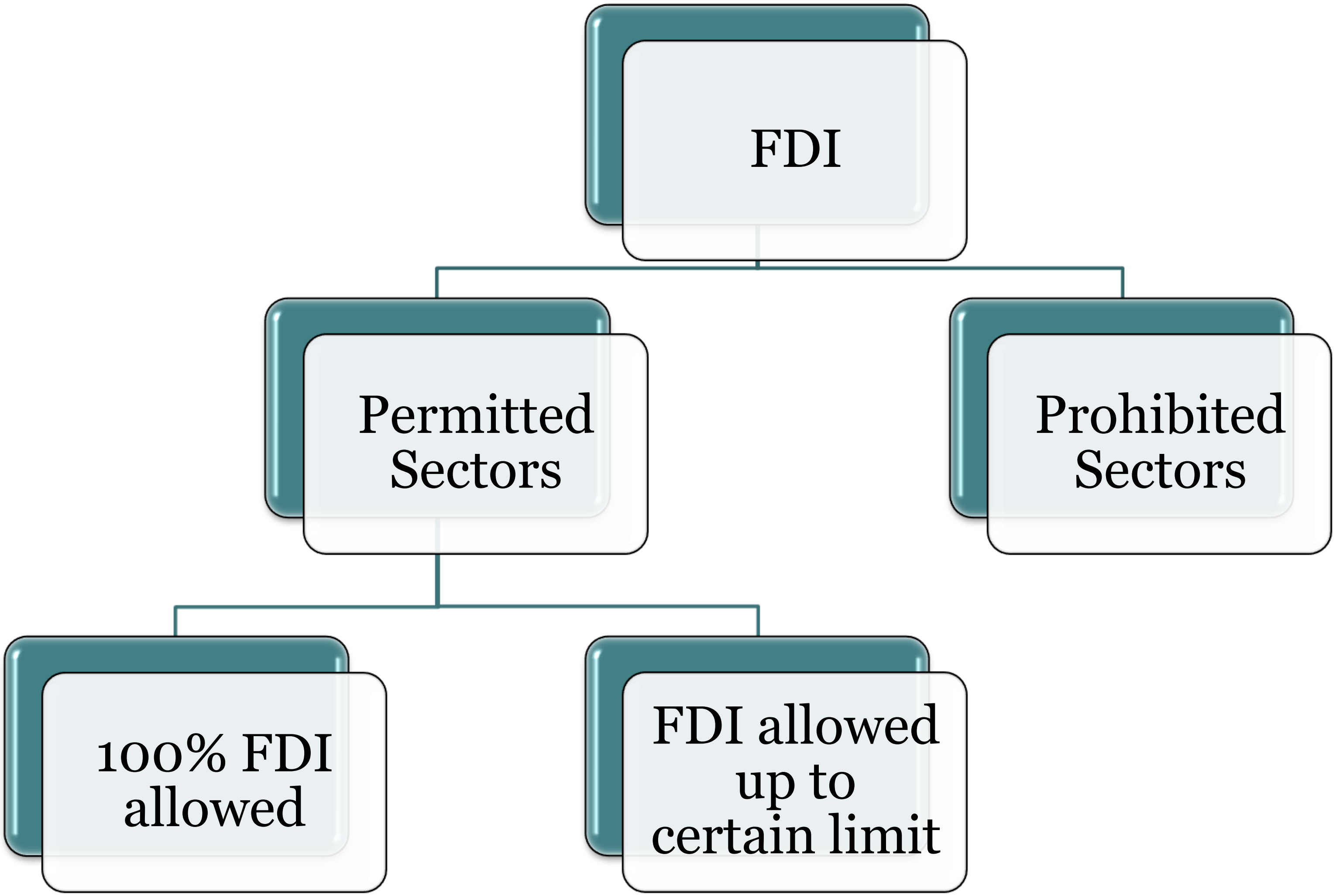
FDI in Indian Companies



Calculation of FDI in Indian Companies

- Counting of direct Foreign Investment
  - All investments directly made by non residents
- Counting of indirect Foreign Investment
  - investment through the investing Indian company would not be considered for calculation of the indirect foreign investment in case of Indian companies which are owned **and** controlled by resident
  - In other case, it would be treated as indirect foreign investment
    - Exception where the entire capital of the downstream subsidiary is owned by the holding company
- The above methodology do not apply to Insurance Sector

Sector specific Conditions on FDI



Prohibited Sectors

- Retail Trading (except single brand product retailing)
- Lottery Business including Government /private lottery, online lotteries, etc.
- Gambling and Betting including casinos etc.
- Chit funds and Nidhi company
- Trading in Transferable Development Rights (TDRs)
- Real Estate Business or Construction of Farm Houses
- Manufacturing of Cigars, cheroots, cigarillos and cigarettes, of tobacco or of tobacco substitutes
- Activities / sectors not open to private sector investment e.g. Atomic Energy and Railway Transport (other than Mass Rapid Transport Systems)
- Foreign technology collaboration in any form for Lottery Business and Gambling and Betting activities

Real estate sector

- Following are sectors where FDI is permitted:
  - Townships, housing, built-up infrastructure and construction-development projects (which would include, but not be restricted to, housing, commercial premises, hotels, resorts, hospitals, educational institutions, recreational facilities, city and regional level infrastructure)
  - Note – the activity must be construction and development. Trading in properties is not allowed
- Minimum built up area:
  - serviced housing plots, a minimum land area of 10 hectares
  - In case of construction-development projects, a minimum built-up area of 50,000 sq.mts
- In case of wholly owned subsidiary: $ 10 million, JVs - $ 5 million
- Lock in period of 3 years from completion of minimum capitalisation
- At least 50% of the project must be completed within 5 years

Remittance and Reporting Requirements

Remittance and Repatriation

- Sale proceeds on winding up/liquidation of companies
  - Can be remitted on submission of specified documents and certificate
- Repatriation of dividend
  - freely repatriable without any restrictions (net of taxes)
- Repatriation of interest
  - Interest on fully, mandatorily & compulsorily convertible debentures is also freely repatriable without any restrictions (net of applicable taxes)

Reporting Requirements

- Indian company receiving investment from outside India for issuing shares / convertible debentures / preference shares under the FDI Scheme to report to RO within 30 days

Reporting of Inflow

- Reporting in Form FC-GPR within 30 days from issuing shares and convertible securities

Reporting of issue of shares

- Reporting of transfer of shares between residents and non-residents and vice- versa is to be done in Form FC-TRS within 60 days

Reporting of Transfer of shares

Vinod Kothari

Reporting Requirements contd..

Issue of shares against conversion of ECB

To be reported to the Regional Office concerned of the RBI

In case of full conversion of ECB into equity, Form FC-GPR and Form ECB 2

In case of partial conversion of ECB, converted portion to be reported in Form FC-GPR and Form ECB 2

Reporting of FCCB/ADR/GDR Issue

Issuing company to report in Form specified within 30 days

Penalties for Non violation

- For contravention of FDI Regulations by an Individual
  - If amount is quantifiable
    - Penalty up to thrice the sum involved in such contraventions
  - Where the amount is not quantifiable
    - Up to two lakh Rupees
  - Where such contraventions is a continuing one, further penalty which may extend to five thousand Rupees for every day after the first day during which the contraventions continues
- If the company or other body corporate found guilty of offence, persons in charge at the time of violation are punishable
- Adjudicating Authority may confiscate any currency, security or any other money or property in respect of which the contravention has taken place

Compounding Proceeding

- Quantifiable offences are compoundable, second or subsequent offence shall be treated as first contravention after a period of three years
- Compounding application to be filed with concerned RO/Compounding Authority along with prescribed fee
- RO/Compounding Authority will pass the order within 180 days from the date of filing of application after giving an opportunity of being heard
- RO/Compounding Authority reserves rights to call for further information, documents and evidences

Recent Amendment in Compounding Regulations

- Powers of Compounding Authority delegated to RO for following offences:
  - Delay in reporting of inward remittance,
  - Delay in filing of form FC-GPR after allotment of shares
  - Delay in issue of shares beyond 180 days
- Offences punishable up to Rupees One hundred lakhs can be compoundable by following RO:
  - Bhopal, Bhubaneshwar, Chandigarh, Guwahati, Jaipur , Jammu, Kanpur, Kochi, Patna and Panaji
- Following ROs can compound contraventions punishable with whatever may be the amount
  - Ahmedabad, Bangalore, Chennai, Hyderabad, Kolkata, Mumbai and New Delhi

External Commercial Borrowings (ECBs)

Nature of ECBs

Commercial loans in the form of:

bank loans, buyers' credit, suppliers' credit, securitized instruments (e.g. floating rate notes and fixed rate bonds, non-convertible, optionally convertible or partially convertible preference shares)

availed of from non-resident lenders with a minimum average maturity of 3 years.

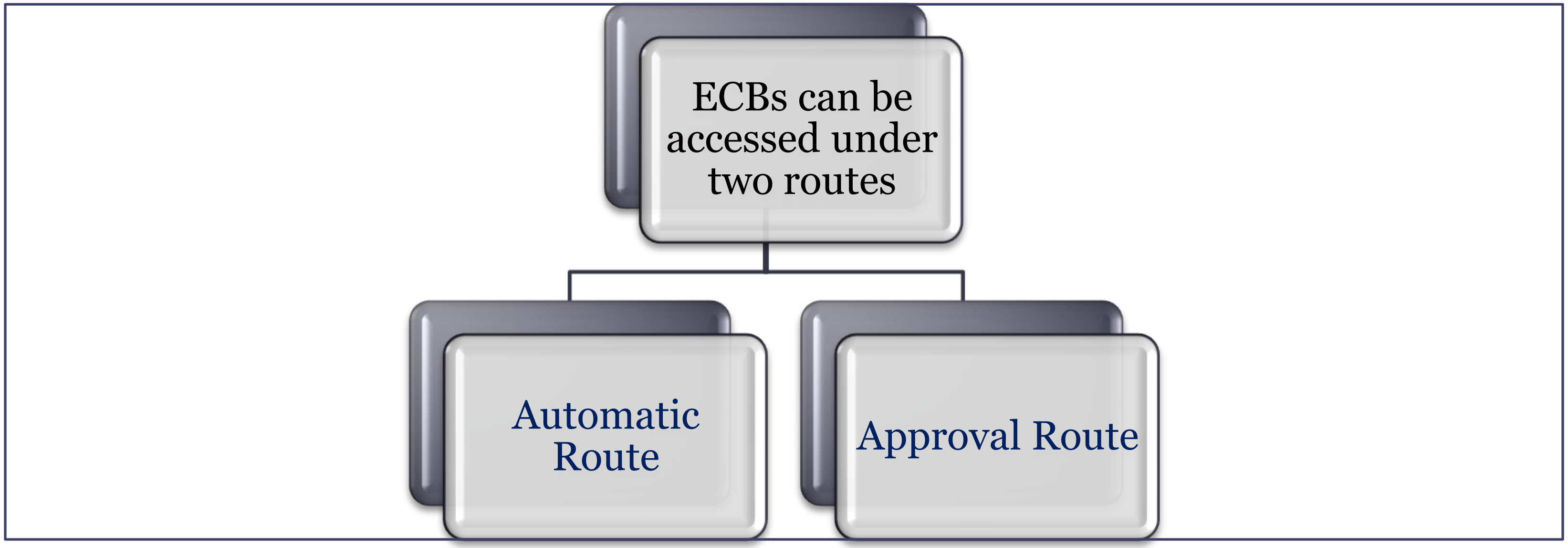
ECBs with a minimum maturity of 3 years

ECBs

Includes: optionally convertible debentures, non convertible bonds, FCCBs, FCEBs, securitized instruments, financial leases

Excludes: trade credit – supplier and buyers' credit compulsorily convertible debentures, compulsorily convertible preference shares, equity investments

How ECBs cab be availed?



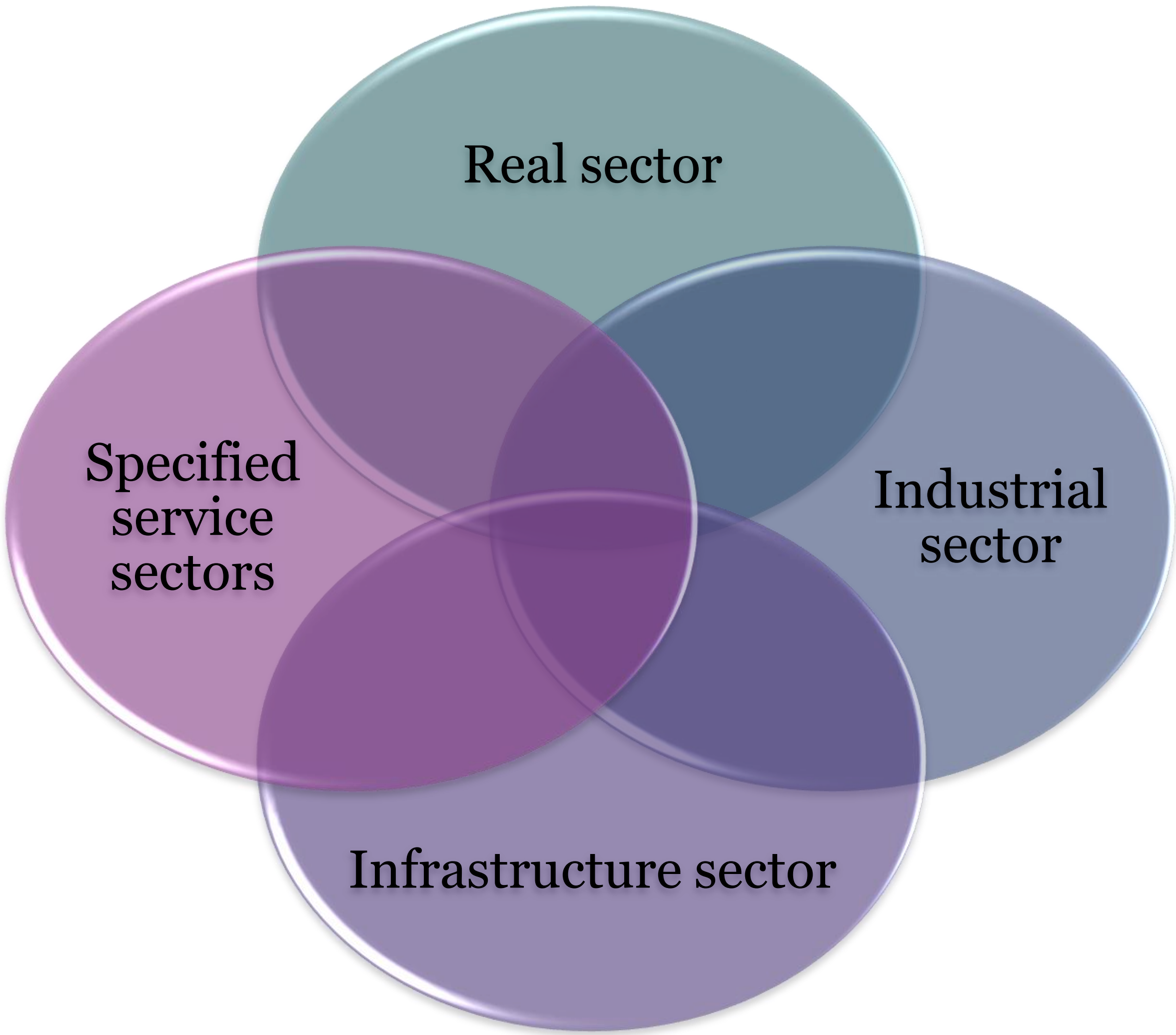
•Borrowings for the real sector and infrastructure sector are covered by automatic route
•Financial sector comes under approval route
•In case of any doubt whether automatic route applies, one may resort to approval route.

ECB under Automatic Route

Eligible Borrowers

- Eligible Borrowers are Corporates, IFCs
  - Banks, NBFCs, housing finance companies are not covered by automatic route
    - Microfinance companies – special permission given recently
  - Individuals, trusts, Non-profit making organizations not eligible
  - Units in SEZ can raise, but cannot transfer to sister concerns in DTA
  - NGOs in microfinance activities can avail
  - Service sector units – hospitals, hotels, software companies may avail ECBs
    - Only 3 service sectors covered by automatic route
    - Other service sectors fall under approval route; norms are more stringent,

Eligible Sectors



Recognized lenders

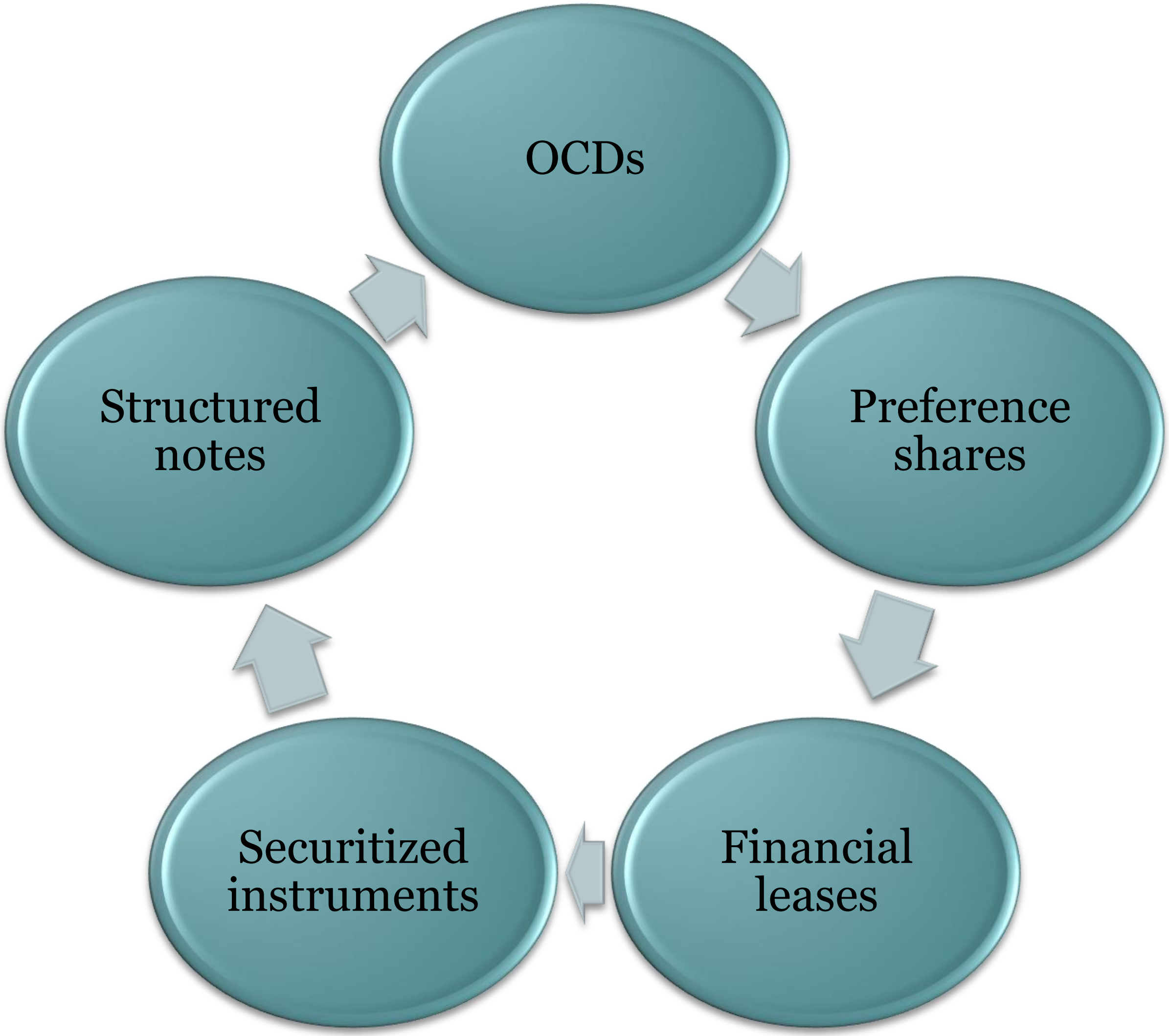
- International banks,
- International capital markets,
- Multilateral financial institutions (such as IFC, ADB, CDC, etc.) / regional financial institutions and Government owned development financial institutions,
- Export credit agencies,
- Suppliers of equipments,
- Foreign collaborators
- Foreign equity holders

- Can foreign NBFCs extend ECBs?
  - No

Foreign equity holders as lenders under ECBs

- Pre-condition for foreign equity holder giving ECBs
  - For amount upto $ 5 million – minimum 25% of paid up equity capital
  - For amount exceeding $ 5 million – minimum 25% of paid up equity capital, proposed ECB not to exceed 4 times of direct foreign equity
    - Whether held by the lender or not
  - Note:
    - The percentage refers only to paid up equity
    - CCDs and CCPS not included

Instruments to be treated as ECBs



Micro finance institutions and NGOs in microfinance

- As a special dispensation, MFIs and microfinance NGOs allowed to raise ECBs
  - Upto $ 10 million in a financial year
  - The exposure should be fully hedged

Instruments neither ECB nor FDI

- Perpetual Debt Instruments (PDIs)
- Cross border operating leases

- Is this ECB?
  - Borrowings denominated in INR:
    - Yes.
    - The cost ceilings will be swap rates + spread

How much ECB can be raised

- Corporates other than hotels, hospitals and software:
  - $ 750 million
- Hotels, hospitals and software:
  - $ 200 million
- If average maturity is 3 years: $ 20 million in a financial year
- Average maturity 3-5 years: maximum ceiling $ 500 as above
- That is to say, in case of average maturity of 3 years, the ceiling is $20 million per financial year

Procedure for raising ECB

Procedure

Borrowers to enter into a loan agreement with recognised lenders

Borrowers to obtain a Loan Registration Number (LRN) from the Reserve Bank of India before drawing down the ECB

Simplified Procedure for change in Lender

- The designated AD has been delegated the power to approve the request from the ECB borrowers when the original lender is
  - International bank
  - Multilateral financial institution
  - Regional financial institution
  - Government owned development financial institution
  - Export credit agency
  - Supplier of equipment
- subject to satisfaction of following conditions:
  - the new lender is a recognized lender as per the extant ECB norms
  - there is no change in the other terms and conditions of the ECB; and
  - the ECB is in compliance with the extant guidelines
- Earlier, change in the lender required RBI approval
- Change in recognised lender in case of foreign equity holder and foreign collaborator will continue to be examined by the Reserve Bank

Simplified Procedure for other changes in availed ECB

- In terms of *Notification dated February 7, 2012*, the designated AD Category-I bank may approve requests from ECB borrowers for the ECBs availed under the automatic route for the following subject to the specified conditions:
  - Reduction in amount of ECB availed
  - changes in the drawdown schedule where the original average maturity period is not maintained
  - reduction in the all-in-cost of the ECB after obtaining the LRN
- Previously, these changes required approval of RBI

Amount and Maturity

- Maximum amount for corporate other than those in the hotel, hospital and software sectors is USD 750 million or its equivalent during a financial year
- Corporates in the services sector viz. hotels, hospitals and software sector are allowed to avail of ECB up to USD 200 million or its equivalent in a financial year
  - Provided proceeds of the ECBs should not be used for acquisition of land
- NGOs engaged in micro finance activities can raise ECB up to USD 10 million or its equivalent during a financial year
  - AD to ensure that at the time of drawdown the forex exposure of the borrower is fully hedged
- Maturity
  - up to USD 20 million or its equivalent in a financial year with minimum average maturity of three years
  - above USD 20 million or equivalent and up to USD 750 million or its equivalent with a minimum average maturity of five years
- ECB up to USD 20 million or equivalent can have call/put option provided the minimum average maturity of three years is complied with before exercising call/put option

All-in-cost ceiling

- All-in-cost includes
  - rate of interest,
  - other fees and expenses in foreign currency
    - except commitment fee, pre-payment fee, and fees payable in Indian Rupees
    - Excludes withholding tax
- Ceilings over 6 months LIBOR are
  - For maturity upto 3-5 yrs – 350* basis points
  - For maturity more than 5 yrs -500 basis points
- In case of fixed rate loans, swap rates of the given maturity

**Revised from 300 basis points vide RBI/2011 -12/273 A. P. (DIR Series) Circular No. 51 dated November 23, 2011*

Permitted End Use

- ECB raised can be used in India for
  - investment [such as import of capital goods, new projects, modernization/expansion of existing production units] in real sector - industrial sector including small and medium enterprises (SME),
  - infrastructure sector
  - specified service sectors namely hotel, hospital, software in India
- ODI in JV/WOS subject to existing guidelines
- In case of infrastructure sector, also for interest during construction
- For first stage acquisition of shares in the disinvestment process and also in the mandatory second stage offer to the public under the Government's disinvestment programme of PSU shares
- For lending to self-help groups or for micro-credit or for bonafide micro finance activity including capacity building by NGOs engaged in micro finance activities
- Payment for Spectrum Allocation

Prohibited End Use

For on-lending or investment in capital market

- investment in SPVs, Money Market Mutual Funds etc., are also considered as investment in capital markets

For acquiring a company (or a part thereof) in India by a corporate

For real estate sector,

For working capital, general corporate purpose and repayment of existing Rupee loans.

Meaning of infrastructure

- power
- telecommunication,
- railways,
- roads including bridges
- sea port and airport,
- industrial parks,
- urban infrastructure (water supply, sanitation and sewage projects),
- mining, exploration and refining and
- cold storage or cold room facility, including for farm level pre-cooling for preservation or storage of agricultural and allied produce, marine products and meat

Meaning of capital goods

- Para 9.12 of Foreign Trade Policy:
- Capital Goods” means any plant, machinery, equipment or accessories required for manufacture or production, either directly or indirectly, of goods or for rendering services, including those required for replacement, modernisation, technological upgradation or expansion.
- Also includes packaging machinery and equipment, refractories for initial lining, refrigeration equipment, power generating sets, machine tools, catalysts for initial charge, equipment and instruments for testing, research and development, quality and pollution control. Capital goods may be for use in manufacturing, mining, agriculture, aquaculture, animal husbandry, floriculture, horticulture, pisciculture, poultry, sericulture and viticulture as well as for use in services sector.

ECBs in case of infrastructure finance companies

- Can borrow upto 50 per cent of owned funds
- Need to comply with DNBS Circular DNBS.PD.CCNo.168 / 03.02.089 / 2009-10 dated February 12, 2010
- Fully hedged basis

Parking of ECB Proceeds*

- ECB proceeds meant for foreign currency expenditure can be retained abroad pending utilisation
- ECB proceeds meant for Rupee expenditure should be brought immediately for credit to Rupee account
  - Rupee funds cannot be used for investment in capital markets, real estate or for inter-corporate lending
- Earlier borrowers could park their funds in liquid assets overseas and repatriated in India, credit to borrower's Rupee account pending utilisation for permissible end-uses.

* *Amended vide notification dated November 23, 2011*

Guarantee and Prepayment

Issuing guarantee

- Issuance of guarantee, standby letter of credit, letter of undertaking or letter of comfort by banks/FIs/NBFCs from India relating to ECB is not permitted

Prepayment

- Up to USD 500 million may be allowed by AD banks without prior approval of Reserve Bank subject to compliance with the stipulated minimum average maturity period as applicable to the loan

Refinancing of existing ECB

- By raising a fresh ECB subject to the condition
  - that the fresh ECB is raised at a lower all-in-cost
  - that the outstanding maturity of the original ECB is maintained

ECB from foreign equity holders

- Foreign equity holder is an eligible lender ***under automatic route***, with a minimum paid up equity capital as set below:

ECB	Minimum paid up equity
Up to USD 5 million	minimum paid-up equity of 25 per cent held directly by the lender
More than USD 5 million	•minimum paid-up equity of 25 per cent held directly by the lender •ECB liability'-equity ratio not exceeding 4:1 ** (for the purpose of calculation of ECB liability, the outstanding and proposed ECB from the same equity holder shall be reckoned)

ECB from foreign equity holders contd..

- For other eligible borrowers ECB proposals from foreign equity holders ***will come under the approval route***
  - Service sector units
  - ECB from indirect holders, holding at least 51% in the Indian company
  - ECB from a group company, provided both the borrower and the foreign lender are subsidiaries of the same parent.
- Total outstanding stock of ECBs (including the proposed ECBs) from a foreign equity lender does not exceed 7 times the equity holding, either directly or indirectly of the lender

ECB for MFIs and NGOs

- MFIs and NGOs in micro finance activities may be permitted to raise ECB up to USD 10 million or equivalent during a financial year for permitted end-uses ***under the Automatic Route***
- Designated AD is to certify the status of the borrower as eligible and involved in micro finance and ensure at the time of draw down that the forex exposure of the borrower is fully hedged
- **Eligible Borrowers** are:
  - MFIs registered under Societies Registration Act
  - MFIs registered under Indian Trust Act
  - MFIs registered under state/national level cooperative legislations
  - NBFC-MFIs
  - Section 25 companies engaged in micro finance activity
- The borrowers would further require:
  - A satisfactory borrowing relationship for at least 3 years with a scheduled commercial bank authorized to deal in foreign exchange
  - A certificate of due diligence on `fit and proper' status from AD Bank

Vinod Kothari

Recognized Lenders for MFIs

NBFC-MFIs will be permitted to avail of ECBs from multilateral institutions, such as IFC, ADB etc./ regional financial institutions/international banks / foreign equity holders and overseas organizations

Section 25 Companies can avail from international banks, multilateral financial institutions, export credit agencies, foreign equity holders, overseas organizations and individuals

Other MFIs will be permitted to avail of ECBs from international banks, multilateral financial institutions, export credit agencies, overseas organizations and individuals

Other ECB Parameters for MFIs

Permitted end use:

- For lending to self-help groups or for micro-credit or for bonafide micro finance activity including capacity building

Amount of ECB:

- USD 10 million during a financial year

Other ECB parameters:

- Minimum average maturity, all-in-cost ceilings, restrictions on issuance of guarantee, choice of security, parking of ECB proceeds, prepayment, refinancing of ECB, reporting arrangements under the Automatic Route should be complied with by MFIs/NGOs availing ECBs

ECBs under Approval Route

Eligible Borrowers

- On lending by the EXIM Bank
- Banks and financial institutions which had participated in the textile or steel sector restructuring package as approved by the Government
  - ECB availed for this purpose so far will be deducted from their entitlement
- NBFCs from multilateral financial institutions, reputable regional financial institutions, official export credit agencies and international banks to finance import of infrastructure equipment for leasing to infrastructure projects
  - Such ECB should be with minimum average maturity of 5 years
- IFCs beyond 50% of their owned funds, for on-lending to the infrastructure sector subject to compliance with guidelines prescribed
- FCCBs by HFCs provided:
  - the minimum net worth during the previous three years shall not be less than Rs. 500 crore,
  - listing on the BSE or NSE,
  - minimum size of FCCB is USD 100 million and
  - the applicant should submit the purpose / plan of utilization of funds

Eligible Borrowers contd..

- SPVs notified by RBI set up to finance infrastructure companies / projects exclusively
- Multi-State Co-operative Societies engaged in manufacturing activity
- SEZ developers can avail of ECBs for providing infrastructure facilities within SEZ
- Corporates in the services sector viz. hotels, hospitals and software sector availing beyond USD 100 million per financial year
- Any other cases falling outside the purview of the automatic route limits and maturity period
- Corporates in service sectors other than hotels, hospitals and software can avail ECBs only from equity holders

Eligible Lenders

- Eligible lenders are internationally recognized sources
  - international banks,
  - international capital markets,
  - multilateral financial institutions (such as IFC, ADB, CDC, etc.) / regional financial institutions and Government owned development financial institutions,
  - export credit agencies,
  - suppliers of equipments,
  - foreign collaborators and
  - foreign equity holders (other than erstwhile Overseas Corporate Bodies (OCBs), provided they have in borrower company
    - For ECB up to USD 5 million - minimum paid-up equity of 25 per cent held directly by the lender
    - For ECB more than USD 5 million - minimum paid-up equity of 25 per cent held directly by the lender and debt-equity ratio not exceeding 4:1

Amount and Maturity Period

Corporates in the services sector viz. hotels, hospitals and software sector are allowed to avail of ECB beyond USD 200 million or its equivalent in a financial year

- proceeds of the ECBs should not be used for acquisition of land

Corporates can avail of ECB of an additional amount of USD 250 million with average maturity of more than 10 years under the approval route

- This is over and above the existing limit of USD 500 million under the automatic route, during a financial year
- Prepayment and call/put options, however, would not be permissible for such ECB up to a period of 10 years

All-in-cost-ceiling

- All-in-cost includes
  - rate of interest,
  - other fees and expenses in foreign currency except commitment fee, pre-payment fee, and fees payable in Indian Rupees
    - Excludes withholding tax
- Ceilings over 6 months LIBOR are
  - For maturity upto 3-5 yrs – 350* basis points
  - For maturity more than 5 yrs -500 basis points

***Revised from 300 basis points vide RBI/2011 - 12/273 A. P. (DIR Series) Circular No. 51 dated November 23, 2011**

Permitted End Use

- ECB proceeds raised abroad meant for Rupee expenditure in India, should be brought immediately for credit to their Rupee accounts with AD *[Vide RBI/2011-12/274 A.P. (DIR Series) Circular No. 52 dated November 23, 2011]*
- Can be used in India for
  - investment [such as import of capital goods, new projects, modernization/expansion of existing production units] in real sector - industrial sector including small and medium enterprises (SME),
  - infrastructure sector
  - specified service sectors namely hotel, hospital, software in India
- ODI in JV/WOS subject to existing guidelines
- For first stage acquisition of shares in the disinvestment process and also in the mandatory second stage offer to the public under the Government's disinvestment programme of PSU shares
- Refinancing of spectrum allocation in Telecom Sector
- Repayment of existing rupee loans
  - In case of infrastructure companies,25% of ECBs may be used for repaying existing INR debt
  - The rupee loans must have been raised for capital expenditure

Prohibited End Use

- For on-lending or investment in capital market or acquiring a company (or a part thereof) in India by a corporate
- For real estate
- For working capital, general corporate purpose and repayment of existing Rupee loans

Guarantee and Prepayment of ECB

Issuing guarantee

- Issuance of guarantee, standby letter of credit, letter of undertaking or letter of comfort by banks/FIs/NBFCs from India relating to ECB is not permitted
- Guarantee in case of SME may be considered on merit basis
- Guarantee in respect of ECB by textile companies for modernization or expansion of textile units will be considered

Prepayment

- Exceeding USD 500 million would require prior approval of Reserve Bank

Refinancing of existing ECB

- By raising a fresh ECB subject to the condition
  - that the fresh ECB is raised at a lower all-in-cost
  - that the outstanding maturity of the original ECB is maintained

Foreign Currency Exchangeable Bond (FCEB)

- FCEBs, requiring prior approval of the Reserve Bank under the Approval Route for raising ECB, are bonds
  - expressed in foreign currency,
    - may be denominated in any freely convertible foreign currency
  - the principal and interest in respect of which is payable in foreign currency,
  - issued by an Issuing Company and subscribed to by a person who is a resident outside India, in foreign currency
  - exchangeable into equity share of another company (Offered Company)

Terms for issuing FCEB

Eligible Issuer	• Is the Issuing Company which shall be part of the promoter group of the Offered Company and shall hold the equity share/s being offered at the time of issuance of FCEB
Offered Company	• shall be a listed company, which is engaged in a sector eligible to receive FDI and eligible to issue or avail of FCCB or ECB
Entities not eligible	• An Indian company, which is not eligible to raise funds from the Indian securities market or restrained from accessing the securities market by the SEBI

Terms for issuing FCEB contd..

- Eligible Subscriber
  - Entities complying with the FDI policy and adhering to the sectoral caps at the time of issue of FCEB
    - Prior approval of the FIPB, wherever required under the FDI policy, should be obtained
- Entities not eligible to subscribe to FCEB
  - Entities prohibited to buy, sell or deal in securities by the SEBI
- End use of proceeds of FCEB
  - may be invested by the issuing company in promoter group companies or in JV/WOS abroad
    - Promoter group companies receiving investments may utilize the amount in accordance with end-uses prescribed under the ECB policy
  - Utilization prohibited in real estate or capital market in India

Pricing and Maturity of FCEBs

- At the time of issuance of FCEB the exchange price of the offered listed equity shares shall not be less than the higher of the following
  - The average of the weekly high and low of the closing prices of the shares of the offered company quoted on the stock exchange during the six months preceding the relevant date
  - The average of the weekly high and low of the closing prices of the shares of the offered company quoted on the stock exchange during the six months preceding the relevant date
- Minimum maturity shall be 5 years
  - exchange option can be exercised at any time before redemption
  - Cash (Net) settlement shall not be permissible

Conditions for conversion of ECB into Equity

- The activity of the company is covered under the Automatic Route and FIPB approval for foreign equity participation has been obtained by the company, wherever applicable
- The foreign equity holding after such conversion of debt into equity is within the sectoral cap, if any
- Pricing of shares is as per the pricing guidelines issued under FEMA, 1999
- Reporting to RBI
  - In form FC-GPR and ECB-2 within seven working days from the close of month to which it relates
    - NO reporting requirement in subsequent months
  - In form FC-GPR and ECB-2 clearly differentiating the converted portion from the unconverted portion
    - outstanding portion of ECB should be reported in ECB-2 in subsequent months

ECB for Infrastructure Sector

- Repayment of existing loan is not permissible end use under the ECB guidelines. However for companies in infrastructure sector, ***25% of the fresh ECB proceeds*** can be utilised for refinancing existing Rupee loans availed from domestic banks, ***under approval route***, subject to following conditions:
  - Atleast 75% of the fresh ECB proposed to raised is used towards capital expenditure towards a 'new infrastructure' project(s)
  - 25% remaining to be utilised for refinancing domestic loan availed for capital expenditure of earlier completed infrastructure project(s); ***and***
  - Refinance shall be utilised only for Rupee loans which are outstanding in the books of the financing bank concerned
- The designated AD bank shall monitor the end-use of funds and bank(s) in India will not be permitted to provide any form of guarantee(s)
- For the purpose of this amendment, definition of infrastructure would be the same as under the extant guidelines on ECB

ECB for NMIZs

Vide notification dated February 29, 2012 ECB has been allowed for infrastructure facilities within National Manufacturing Investment Zone (NMIZs) ***under approval route*** for providing infrastructure facilities

Other aspects of ECB policy such as, recognised lender, average maturity, all-in-cost, repayment, refinancing of existing ECB and reporting arrangements shall apply as applicable under approval route

ECB – Bridge finance for Infrastructure Sector

- Indian companies in the infrastructure sector can import capital goods by availing of short term credit (including buyers'/ suppliers' credit) in the nature of 'bridge finance', ***under the approval route***, subject to the following conditions-
  - bridge finance shall be replaced with a long term ECB
  - long term ECB shall comply with all the extant ECB norms; and
  - Prior approval to be sought for replacing bridge finance with long term ECB
- Companies in infrastructure sector can avail ECB in Renminbi (RMB) under the approval route subject to annual cap of USD 1 billion

Rationalization and Liberalization of ECB Guidelines

- ECB limit enhanced in certain cases:
  - borrowers in real sector-industrial sector-infrastructure sector can avail of ECB up to USD 750 million or equivalent per financial year under the automatic route as against the present limit of USD 500 million or equivalent per financial year
  - Corporates in specified service sector to avail ECB up to USD 200 million or equivalent during a financial year as against the present limit of USD 100 million or equivalent per financial year; provided proceeds not used for acquisition of land
- ECB designated in INR can be availed by NGOs engaged in microfinance activities under automatic route from overseas organizations and individuals
- All eligible borrowers can avail ECB designated in INR from foreign equity holders
- Interest during construction (IDC) to be considered as permissible end use for companies engaged in infrastructure sector, provided:
  - IDC is capitalized; and
  - Is a part of the project cost

Liberalized ECB policy - structured obligations for Infrastructure Sector

- Credit enhancement to be provided to companies in infrastructure sector and IFCs by foreign equity holders
  - Direct foreign equity holders holding minimum of 25% of the paid up capital; and
  - Indirect foreign equity holders holding at least 51% of the paid up capital
- Credit enhancement by all eligible non-resident entities to be permitted under the automatic route
- Earlier credit enhancements could be provided by multilateral/ regional financial institutions and Government owned development financial institutions for domestic debt raised through issue of capital market instruments

Trade Credits for Imports into India

Meaning

Trade Credit (TC) meaning credits extended for imports directly by the overseas supplier, bank and financial institution for maturity of less than three years

May be in form of

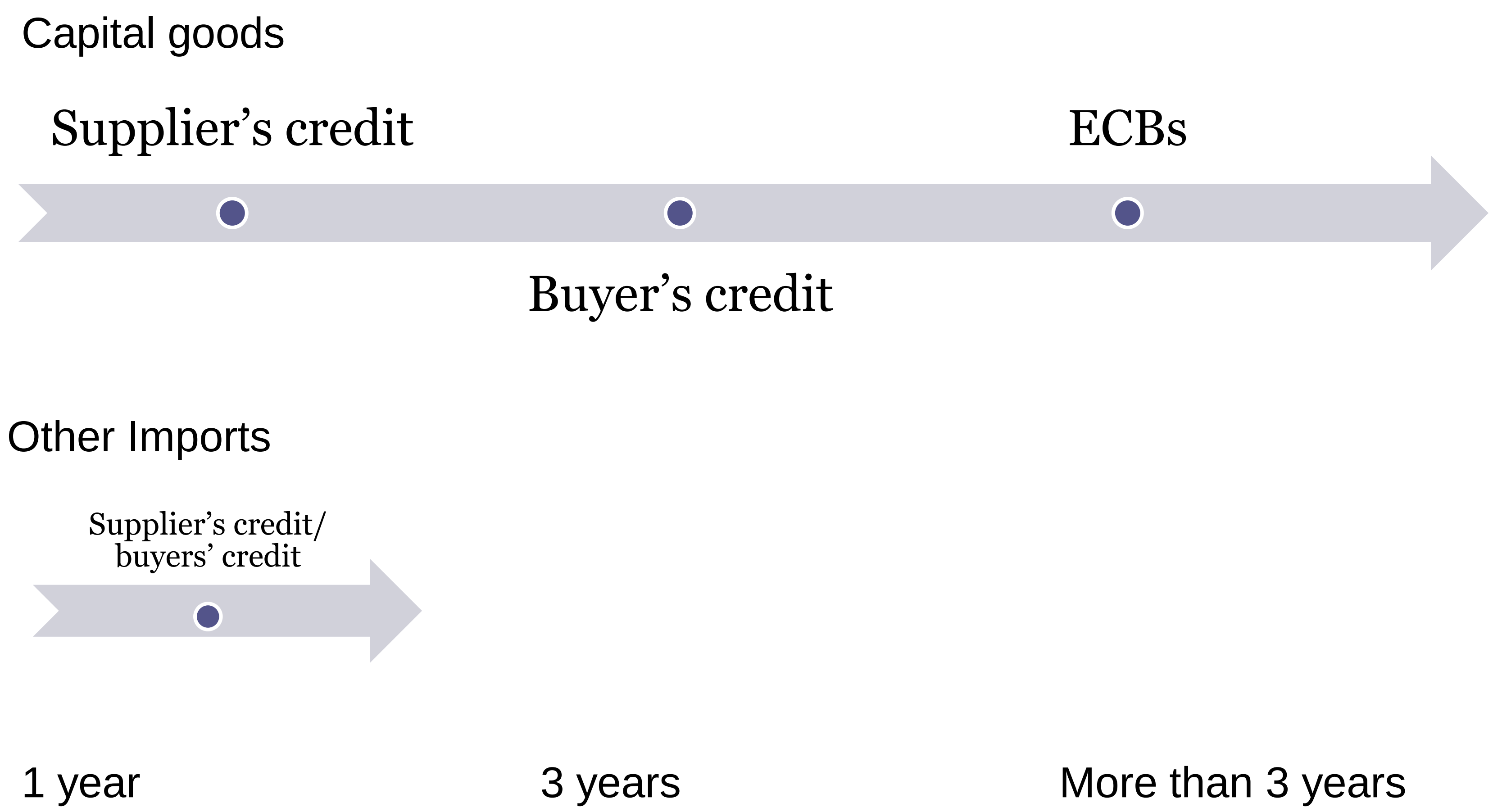
- Supplier's credit i.e. credit for imports into India extended by the overseas supplier
- Buyer's credit i.e. loans for payment of imports into India arranged by the importer from a bank or financial institution outside India for maturity of less than three years

•Note that TC for three years and above come under the category of ECB and are governed by ECB guidelines
•What about credit availed from Indian banks – not covered by FEMA at all
•Can trade credit be availed for import of services - No

Amount and Maturity of TC

- For imports permissible under the current Foreign Trade Policy
  - up to USD 20 million per import transaction
  - with a maturity period up to one year (from the date of shipment)
- For capital goods
  - What is capital goods
    - Capital goods as per DGFT classification
  - up to USD 20 million per import transaction
  - with a maturity period of more than one year and less than three years (from the date of shipment)
- No roll-over/extension will be permitted beyond the permissible period
- AD banks shall not approve trade credit exceeding USD 20 million per import transaction

So, this is how trade credits run



All-in-cost ceiling

- The all-in-cost ceilings include
  - arranger fee,
  - upfront fee,
  - management fee,
  - handling/ processing charges, out of pocket and legal expenses, if any
  - Note the difference in the definition in case of ECBs – the costs need not be foreign currency costs

Maturity period	All-in-cost ceilings over 6 months LIBOR
Up to 1 year	350 basis points
More than one year but less than three years	350 basis points

Guarantee for TC

- Letters of Credit/guarantees/Letter of Undertaking /Letter of Comfort in favour of overseas supplier, bank and financial institution up to USD 20 million per transaction for a period
  - up to one year for import of all non-capital goods permissible under FTP (except gold, silver, platinum, rodium etc)
  - up to three years for import of capital goods
    - Period to be reckoned from the date of shipment

Reporting Requirement

Reporting

Of details of approval, drawal, utilisation, and repayment of TC in Form TC on monthly basis


Thank You!