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REVISED GUIDELINES FOR EXTERNAL COMMERCIAL BORROWING

The Reserve Bank of India (the “**RBI**”) has recently brought in significant changes to the external commercial borrowing guidelines (the “**ECB Guidelines**”) with respect to companies in the infrastructure and other related sectors, pursuant to a circular dated March 30, 2016 (the “**March 2016 Circular**”).¹

A summary of the key changes brought in by the March 2016 Circular is set out below, together with our view on the implications of the changes to the ECB Guidelines.

1. BACKGROUND

The term ‘*infrastructure sector*’, for the purpose of the ECB Guidelines, is defined in the Harmonised Master List of Infrastructure sub-sectors² approved by the Government of India as amended from time to time.

Pursuant to circular dated September 18, 2013³, the term ‘*infrastructure sector*’, under the ECB Guidelines, includes companies engaged in the following activities:

- (a) Energy;
- (b) Communication;
- (c) Transport;
- (d) Water and sanitation;
- (e) Mining, exploration and refining; and
- (f) Social and commercial infrastructure.

Furthermore, the RBI, pursuant to its circular dated November 30, 2015⁴ (the “**November 2015 Circular**”) revised the ECB Guidelines, classifying external commercial borrowing into the following 3 (three) categories based on the tenure and the currency of the borrowings:

¹ RBI/2015-16/349 A.P. (DIR Series) Circular No.56 dated March 30, 2016:
<https://rbidocs.rbi.org.in/rdocs/notification/PDFs/APDIR563092BC2342FA494ABB58D5044F0D9FA6.PDF>

² See Notification F. No. 13/06/2009-INF dated March 27, 2012

³ RBI/2013-14/270 A.P. (DIR Series) Circular No. 48 dated September 18, 2013:
<https://rbidocs.rbi.org.in/rdocs/Notification/PDFs/APR48180913F.pdf>

⁴ RBI/2015-16/255 A.P. (DIR Series) Circular No. 32 dated November 30, 2015:

- (a) Track I: Medium term foreign currency denominated ECB with minimum average maturity of 3/5 years (“**Track I**”);
- (b) Track II: Long term foreign currency denominated ECB with minimum average maturity of 10 years (“**Track II**”); and
- (c) Track III: Indian Rupee denominated ECB with minimum average maturity of 3/5 years (“**Track III**”).

In addition to the minimum average maturity, the November 2015 Circular sets out in detail the list of eligible borrowers, recognized lenders and investors, all-in-cost requirements, permitted end-uses, individual limits and other prescriptions with respect to companies covered under each track.

2. KEY CHANGES

The RBI has made the following changes to the ECB Guidelines.

2.1 Inclusion under Track I

The RBI has specified that:

- Non-Banking Financial Companies (“**NBFCs**”);
- Infrastructure Finance Companies (“**NBFC-IFCs**”);
- Non-Banking Financial Companies, Asset Finance Companies (“**NBFC-AFCs**”);
- Holding Companies; and
- Core Investment Companies (“**CICs**”),

will be eligible to raise ECB under Track I of the framework with a minimum average maturity period of 5 (five) years, subject to 100% (one hundred percent) hedging.

Prior to the March 2016 Circular, these companies were categorized under Track II of the ECB Guidelines.

These companies will now qualify under all the three tracks to raise foreign debt.

This will allow infrastructure companies to secure debt funding for both short and long term perspectives.

2.2 Exploration, Mining and Refinery

The exploration, mining and refinery sectors which were not included in the Harmonised List of the infrastructure sector but were eligible to take external commercial borrowing under the ECB

<https://rbidocs.rbi.org.in/rdocs/notification/PDFs/A320084163A24434DB5905EEB3F3296EBEC.PDF>

Guidelines⁵ are now explicitly deemed to qualify under the definition of 'infrastructure sector'. Therefore, exploration, mining and refinery activities now have explicit recourse to foreign debt funding.

2.3 Clarification on Permitted Use

Companies in the infrastructure sector are permitted to utilize external commercial borrowing proceeds raised under Track I for the end uses permitted for Track I.

NBFC-IFCs and NBFC-AFCs are permitted to raise external commercial borrowing *only* for financing infrastructure.

The list of permitted uses for companies in the infrastructure sector are as follows:

- (a) import of capital goods including payment towards import of services, technical know-how and license fees, provided they are part of these capital goods;
- (b) local sourcing of capital goods;
- (c) new projects;
- (d) modernisation or expansion of existing units;
- (e) overseas direct investment in joint ventures or wholly owned subsidiaries;
- (f) acquisition of shares in public sector undertakings at any stage of disinvestment under the disinvestment programme of the Government of India;
- (g) refinancing of existing trade credit raised for import of capital goods;
- (h) payment of capital goods already shipped or imported but unpaid; and
- (i) refinancing of existing external commercial borrowing provided the residual maturity is not reduced.

It is further clarified that Holding Companies and CICs shall use ECB proceeds only for on-lending to infrastructure Special Purpose Vehicles (SPVs).

The individual limits on borrowing under the automatic route for the aforesaid companies shall be the same as for companies in the infrastructure sector (currently USD 750 million).

2.4 Compliance Requirements

Companies which have been added under Track I should have a board approved risk management policy and the designated AD Category-I Bank shall verify that the 100% (one hundred percent)

⁵ RBI/2013-14/270 A.P. (DIR Series) Circular No. 48 dated September 18, 2013:
<https://rbidocs.rbi.org.in/rdocs/notification/PDFs/APR48180913F.pdf>

hedging requirement is complied with during the term of the external commercial borrowing and report the position to the RBI through ECB 2 returns.

2.5 Revisions to the ECB Guidelines

(a) Refinancing

Designated AD Category-I banks may now, under powers delegated to them, allow refinancing of ECBs raised under the previous ECB Guidelines, provided that:

- (i) the refinancing is at a *lower* all-in-cost; and
- (ii) the borrower is eligible to raise ECB under the extant ECB Guidelines and the residual maturity of the loan is not reduced (i.e. it is either maintained or elongated).

(b) Non-Convertible Debentures

It has further been clarified that the ECB Guidelines are not applicable to investment in non-convertible debentures in India made by Registered Foreign Portfolio Investors.

(c) Minimum Average Maturity

The minimum average maturity of Foreign Currency Convertible Bonds (“**FCCBs**”) or Foreign Currency Exchangeable Bonds (“**FCEBs**”) is 5 (five) years *irrespective* of the amount of borrowing.

Further, any call or put option for FCCBs shall not be exercisable prior to 5 (five) years.

(d) NBFCs

Only NBFCs which are regulated by the RBI are permitted to raise ECB. Further, under Track III, NBFCs may raise ECB for on-lending for any activities including infrastructure as permitted by the concerned regulatory department of the RBI.

(e) Delegated Powers

The provisions regarding delegation of powers to designated AD Category-I banks is not applicable to FCCBs or FCEBs.

(f) Reference to *Loans*

In relation to the forms of ECB, the term *Bank loans* shall be read as *loans* as foreign equity holders or institutions other than banks, also provide ECB as recognized lenders.

3. INDUSLAW VIEW

The March 2016 Circular allows infrastructure companies to access foreign debt with a *shorter* term. Further, it *broadens* the option for project companies to seek funding from *varied* sources.

The March 2016 Circular generally aims to complement the government's focus on the infrastructure sector, by making it easier for Indian corporates to access foreign debt. With the recent re-allocation of coal blocks, the clarification on exploration and mining activities will come as a welcome change, expressly allowing bidders to use external commercial borrowing to fund their activities.

While hedging is fundamentally important, the cost of it erodes the advantage of lower interest rates commonly seen in the international market and it remains to be seen whether *all in* costs will be substantially different to the local market.

Generally, the policy changes making ECB more attractive are to be welcomed, but it remains to be seen whether foreign lenders will be more willing to lend to Indian corporates before deeper structural issues relating to the enforcement of security and the bankruptcy process are addressed.

With non-performing loans on domestic bank balance sheets of increasing concern, foreign commercial lenders will expect to see deeper structural reforms and a reduction in the risk of projects becoming stalled, before committing debt to the Indian projects market.

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