

The Institute of Chartered Accountants of India - WIRC

External Commercial Borrowings

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ECB

- ECB means: Commercial loans – i.e. bank loans, suppliers' credit, buyers' credit, floating rate notes & fixed rate bonds, finance leases - with minimum average maturity of three years.
- Borrowings for less than 3 years are considered as per Trade Credit rules.

ECB

- Preference shares and debentures – partly convertible, optionally convertible or non-convertible – will be considered as debt. Only fully convertible preference shares / debentures will be considered as equity.
- Ministry of Finance Guidelines & RBI Circular give ECB Guidelines. [AP 5 dt. 1.8.05, subsequent circulars and FEMA notification no. 3].

ECB

- There are two main routes - Automatic Route & Approval Route.

Most of the rules are same under both routes – except for “eligible borrowers” and “purpose of ECBs”.

- RBI is the monitoring authority. Ministry of Finance lays down policy matters.

ECB – Key Elements

- Eligible borrowers.
- Eligible lenders.
- Purpose of ECB.

- Other aspects.

ECB – Eligible borrowers

- Automatic route:
 - Indian companies (except Financial Institutions, banks, NBFCs); and
 - NGOs raising ECBs for micro finance activities.
- Approval Route:
 - FIs dealing exclusively with infrastructure or export finance.

ECB – Eligible borrowers

- Approval Route (contd.):
 - Housing Finance companies can raise FCCBs.
 - Multi-State Co-op. Soc. which are in manufacturing sector.
 - Bank & FIs which had participated in textile or steel sector restructuring package – to the extent of their investment in the package.

ECB – Eligible borrowers

- Cases falling outside the automatic route.
- IFC can borrow ECB subject to NBFC guidelines. Total ECB cannot exceed 50% of net owned funds.

ECB – Eligible borrowers

- **Borrowers not eligible:**
 - Individuals, Trusts & Non-profit organisations are not eligible for ECBs.
 - Partnerships, proprietorships, are also not eligible.
 - Co-operative Societies are not eligible. However Multi-State Co-operative Societies in manufacturing sector can raise ECBs under Approval route.

ECB – Eligible borrowers

- Proposed borrowers who have violated ECB guidelines, or are under investigation by RBI / ED are not eligible to borrow under automatic route.

ECB – Purpose

- ECB can be raised for **Real Sector** – i.e. industrial sector, especially infrastructure sector; expansion and modernisation; acquisition of shares under disinvestment process and second stage public offer of PSU shares;

ECB – Purpose

- Infrastructure means – power, telecommunication, railways, road including bridges, ports, industrial party, water supply, sanitation and sewage projects, mining, exploitation & refining, cold storage or cold room facility, farm lend pre-cooling for preparation of agricultural and allied produce, marine products and meat.

ECB – Purpose

- What is “Real Sector”?
Service industries are not eligible for ECBs.
- Software, Hotels and Hospitals are eligible for ECBs. [AP Circular 46 dt. 2.1.09]
- Refinancing of old ECBs is permitted provided outstanding maturity of original loans is maintained. (Minimum average maturity period for new ECB does not apply.)

ECB – Purpose

- ECBs can be used for JV/WOS abroad.
- ECB can be used for SEZ Development.
- ECB upto U.S. \$ 500 mn. Per borrower per financial year is permitted for rupee expenditure / foreign currency expenditure - for permitted end users.
(AP circular 26 dt. 22.10.2008)

ECB - Purpose

- ECB CANNOT be used for on-lending, investment in capital market, real estate business, working capital, general corporate purpose, repayment of existing rupee loans acquiring a company in India (or a part thereof)

ECB – Purpose

- ECBs cannot be raised for Real Estate development.
- ECB for Integrated Township development is permissible upto 31.12.2010.
- FIs, Banks, Housing Finance companies and IFCs can use ECBs for on-lending under Approval Route.
- ECB can be converted into FDI.

ECB – Recognised Lender

- Internationally recognised sources – International Banks, international capital markets, IFC, ADB, etc.; export credit agencies; suppliers of equipment; Foreign collaborators; Foreign equity holders.

ECB – Recognised Lender

- Foreign equity holders – They should hold directly at least 25% of the equity capital. (For ECB above US\$ 5 mn, the ECB cannot exceed 4 times the equity holding.)
OCBs cannot be lenders (even if they are equity holders.)
- Suppliers of equipment & Technical Collaborators – can they give funds, or only technology?

ECB – Recognised Lender

- Earlier, lenders could only be corporates.
Can individuals, trusts, partnerships give ECBs if they are shareholders?
- NGOs can borrow from individuals and overseas organisations subject to satisfying KYC guidelines.
- Certificate of Due Diligence from the foreign bank – which is regulated in the host country is required.

ECB – Amount & Maturity period

- ECBs upto U.S. \$ 20 millions – minimum average maturity of 3 years. It can have a put/call option subject to minimum average maturity of three years.

ECBs above U.S. \$ 20 millions & upto U.S. \$500 millions - minimum average maturity of 5 years.

Weighted average maturity should be seen.

ECB – Amount and Maturity period

- There is an annual cap of US\$ 500 mn.
Above US\$ 500 mn. can be raised under approval route.
- NGOs can raise upto US\$ 5 mn. p.a. for micro finance.

ECB – Cost ceilings

- Costs cannot exceed:

Minimum average maturity of 3-5 years – 3% over 6 months LIBOR in respective currency.

Minimum average maturity of more than 5 years – 5% over 6 months LIBOR in respective currency.

[where loan agreements have been signed on or after 1.1.2010.]

ECB – Cost ceilings

- All inclusive cost includes:
 - Interest,
 - Other fees & expenses in foreign currency except commitment fee, pre-payment fee & fees payable in rupees.
- Income-tax can be paid by borrower.
This is a bargaining tool for Indian resident.
- How does one calculate All in cost?**
- Penal interest cannot exceed 2% over regular rate of interest.

ECB – Guarantee / Security

- Any security can be given by borrower. Immovable property, financial securities, corporate & personal guarantees are possible.
Guarantee is possible after obtaining the Loan Registration Number.
- Corporate Guarantee is permissible for operating lease in respect of aircraft/ aircraft engine/ helicopter.

ECB – Guarantee / Security

- Guarantees are not permitted by banks, FIs & NBFCs. Under approval route, SMEs can get letter of comfort from banks. Banks can give guarantee to textile industry.

ECB – Other issues

- ECBs should be parked abroad until required in India.
- Vide AP circular 26 dt. 22.10.08, funds can be parked in India in banks. No investment in stock market.

ECB can be parked in top rated securities and treasury bills, & foreign branches of Indian banks.

ECB – Other issues

- Pre-payment upto U.S. \$ 400 million is permitted – subject to minimum average maturity.
- Forward Cover, Interest & Currency Swaps, Foreign Currency Option & Other contracts can be entered into with banks.
- After grant of LRN – any change in ECB requires RBI approval.

ECB – Other issues

Authorised dealer can approve the following:

- Change in drawdown/ repayment provided average maturity is maintained.
- Change in currency.
- Change of AD bank.
- Change in name of the Borrower company.

ECB – Documents

- Automatic Route:

File Form 83 in duplicate, certificate by CS or CA with 7 days from signing the loan agreement. RBI will allot loan registration number.

Then draw down the loan.

ECB - Documents

- Approval Route:

Application in Form ECB to be made by RBI. Empowered committee will look into it.

- File ECB-2 every month within 7 days from the close of the month. This requirement applies to old ECBs also. Is it sufficient to file it with AD?

Short term Foreign Currency Loans (Trade Credit)

- AP circulars 87 dt. 17.4.2004.
- Suppliers'/Buyers' credit upto U.S. \$ 20 millions per import transaction for maturity of less than 1 year.
- For import of capital goods, credit period can be more than 1 year, but less than 3 years.

Period applies from date of shipment. No roll-over/extension can be permitted.

Short term Foreign Currency Loans (Trade Credit)

- All in costs:

Credit upto 1 year – 2% above 6 months LIBOR.

Credit upto 3 years – 2% above 6 months LIBOR.

All in cost includes arranger fee, upfront fee, etc.

Can it be net of tax?

- ADs cannot issue any guarantee.

Foreign Currency Convertible Bonds (FCCBs)

- FEMA notification 120, Schedule I.
- FCCBs can be issued as per Euro issues guidelines.
- ECB guidelines apply to FCCBs.
- Only listed companies can issue FCCBs.
- Costs, maturity etc. should be as per ECB guidelines. No separate limits for merchant banker fees, legal fees, etc.

Foreign Currency Exchangeable Bonds (FCEBs)

- FCEBs can be issued by Indian companies. The bonds can be exchanged against shares of another group company of the borrower (offered company).
- The borrower & offered company should be listed.
- Borrower can invest funds in group companies. The group companies should use the funds as per ECB policy.

Borrowing from relatives.

- Upto U.S. \$ 250,000 can be borrowed from relatives. [Relatives can be Non-NRIs.]

Relative has been defined under Companies Act.

- Loan should be interest free.
- Minimum maturity in 1 year.

Borrowing from relatives.

- No end use conditions prescribed. [Clause 4(iv) of Schedule to Notification 3 has been deleted.]

Does it mean an Indian resident can borrow for any purpose?

Rupee Loans – Repatriable

- “Rupee loans” & “Deposits” are considered separately as per FEMA.
- Indian companies can issue NCDs to NRIs in a public issue.

Interest can be upto 3% above SBI's prime lending rate on the date on which General Body Resolution is passed.

Rupee Loans – Repatriable

- Minimum 3 year redemption period. Can the NRI sell on stock exchange before 3 year period?
- Indian company cannot do agricultural activities, real estate trading; reinvest; re-lend.

What about retail trading, working capital?

Rupee Loans – Repatriable

- Percentage of NCDs issued to NRIs shall not exceed sectoral caps or equity shares.
- No deposits can be accepted from NRIs from NRE a/c.;
- Can ECBs cover loans from NRE A/c?

Rupee Loans – Non-Repatriable

- Indian companies can issue NCDs to NRIs in a public issue. Conditions regarding sectoral caps does not apply.
- Any resident (except a company) can borrow in “rupees” from a non-resident.
 - Loan shall not exceed 3 years.
 - Interest can be upto 2% over bank rate.
 - Condition regarding no agricultural activities, etc. apply.

Rupee Loans – Non-Repatriable

- Proprietary concern, Partnership firms & Indian companies can accept “deposits” from NRIs.

Deposits cannot exceed 3 years.

Deposits from NRIs are not permissible from NRE a/c. but loans are permitted. [AP 89 dt. 24.4.04].

Rupee Loans are permitted for Real Estate Development business.

Projects exports

- Project outside India – Person can borrow from a foreign bank.

Terms & conditions should be approved by the relevant authority.

Commercial Paper

- NBFC guidelines should be adhered to
- CPs can be issued on non-repatriable basis.
- Only NRIs & FIIs can invest in CPs. FIIs can invest on repatriable basis.
- CPs are not transferable.

Borrowing against security of NRI deposits

- Borrowings can be made against deposits by NRIs – NRO / NRE / FCNR.
- Borrowing can be for personal use or business. No re-lending or use in agriculture or Real Estate is permitted.
- Against NRE / FCNR deposits, banks cannot lend more than Rs. 20 lakhs.

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- Thoughts, Questions and Comments are welcome.