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Newsflash: New External Commercial Borrowings (ECB) Regulations / Framework - Consolidation and Liberalisation

The external commercial borrowings regime provides for a framework for Indian corporates to avail foreign currency loans from an overseas lender. Over past few years, the ECB regulations have undergone various changes. As a part of on-going effort, The Reserve Bank of India (RBI) has consolidated and liberalised the regulatory provisions dealing with borrowing and lending in foreign exchange as well as Indian Rupees (INR), combined two separate regulations¹ on these aspects and notified the Foreign Exchange Management (Borrowing and Lending) Regulations, 2018 (also referred to as **New ECB Regulations, 2018**) on 17 December 2018 (Notification No. FE-MA.3(R)/2018-RB) effective from the said date.

Subsequent to the issue of the said **New ECB Regulations, 2018**, RBI, with the intention to rationalize the extant ECB Master Direction, has also issued the ECB Policy – New ECB Framework vide circular No. 17 dated 16 January 2019. (herein referred as **New ECB Framework**)

The amended policy, i.e. the New ECB Framework will come into effect from the date of issuance i.e. 16 January 2019. **However, the Master Direction No. 5 (FED Master Direction No.5/2015-16) dated 1 January 2016 is yet to be updated to reflected the changes in New ECB Framework.**

1.0 Certain regulatory changes made in the New ECB Regulations, 2018 and changes brought in the New ECB framework

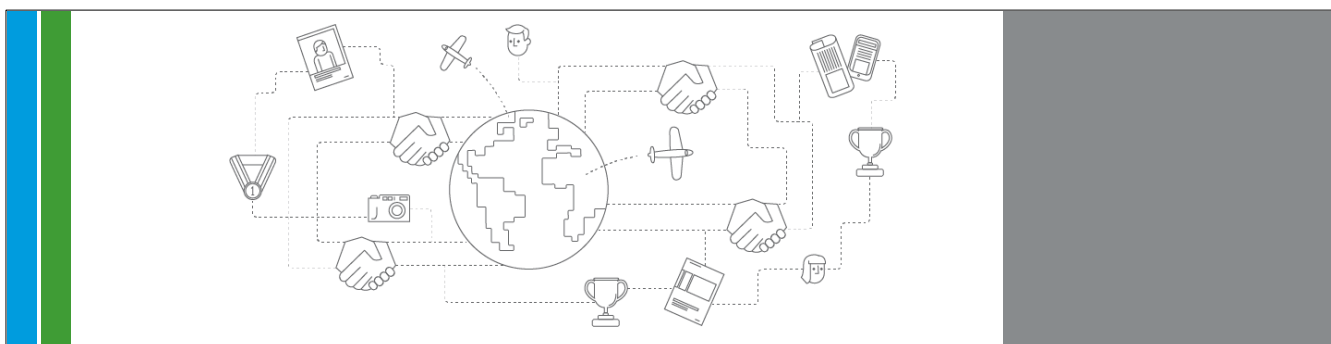
1.1 The New ECB Regulations, 2018 has introduced certain new definitions. Some of the important new definitions are provided hereunder.

- a. **“External Commercial Borrowings (ECB)”** means borrowing by an eligible resident entity from outside India in accordance with framework decided by the Reserve Bank in consultation with the Government of India.
- b. **“External Commercial Lending (ECL)”** means lending by a person resident in India to a borrower outside India in accordance with framework decided by the Reserve Bank in consultation with the Government of India;
- c. **“Foreign branches/subsidiaries of the Indian banks”** means entities established overseas in terms of provisions contained in the Banking Regulation Act, 1949, as amended from time to time;
- d. **“Overseas Citizen of India (OCI)”** Cardholder shall have the same meaning as assigned to it under Section 7(A) of the Citizenship Act, 1955, as amended from time to time;
- e. **“Restricted End Uses”** shall mean end uses where borrowed funds cannot be deployed and shall include the following:
 - a) In the business of chit fund or Nidhi Company;
 - b) Investment in capital market including margin trading and derivatives;
 - c) Agricultural or plantation activities;
 - d) Real estate activity or construction of farm houses; and
 - e) Trading in Transferrable Development Rights (TDR), where TDR shall have the meaning as assigned to it in the Foreign Exchange Management (Permissible Capital Account Transactions) Regulations, 2015.
- f. **“Real Estate Activity”** means any activity involving own or leased property for buying, selling and renting of commercial and residential properties or land and also includes activities either on a fee or contract basis assigning real estate agents for intermediating in buying, selling, letting or managing real estate. However, this would not include development of integrated township, purchase/ long term leasing of industrial land as part of new project / modernisation or expansion of existing units or any activity under ‘infrastructure sub-sectors’ as given in the Harmonised Master List of Infrastructure sub-sectors approved by the Government of India vide Notification F. No. 13/06/2009-INF, as amended/ updated from time to time;

The New Regulation has repealed the Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 and Foreign Exchange Management (Borrowing and Lending in Indian Rupees) Regulations, 2000 (**erstwhile Regulations**).

- g. **“Start-up”** means an entity which complies with the conditions laid down in Notification No. G.S.R 180(E) dated February 17, 2016, as amended/ updated from time to time, issued by Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, Government of India;
- h. **“Trade Credit”** refer to the credits extended by the overseas supplier, bank /financial institution for imports into India in accordance with the Trade Credit framework decided by the Reserve Bank in consultation with the Government of India;

Explanation: Depending on the source of finance, such trade credits include both suppliers' credit and buyers' credit. Suppliers' credit relates to the credit for imports into India extended by the overseas supplier, while buyers' credit refers to loans for payment of imports into India arranged by the importer from overseas bank or financial institution. Imports should be as permissible under the extant Foreign Trade Policy of the Director General of Foreign Trade (DGFT).



1.2 Amendment in the definition of ‘Indian Entity’

Erstwhile Regulations	New ECB Regulations, 2018
‘Indian Entity’ means a company or a body corporate or a firm in India	“Indian Entity” means a company incorporated in India under the Companies Act, 2013, as amended from time to time, or a Limited Liability Partnership formed and registered in India under the Limited Liability Partnership Act, 2008, as amended from time to time;

The New ECB Regulations, 2018 has removed ‘firm’ from the definition of Indian Entity and has expanded its scope to include limited liability partnerships.

In view of the said amendment entities formed under an Act of the Parliament, partnership firm formed under the partnership Act will not be regarded as Indian Entity. However, Indian LLPs are now eligible to raise ECB subject to conditions specified in the said regulation.

1.3 Borrowing in foreign currency from outside India by a Person resident in India (other than Authorised Dealers)

Borrowings by	New ECB Regulations, 2018	Erstwhile Regulations
Financial Institutions	Financial Institutions, set-up under an Act of the Indian Parliament, is permitted to raise foreign exchange borrowings with prior approval of the Government of India for onward lending. If borrowings are in the nature of ECB then the same shall be	There were no specific regulations
Resident Individual studying abroad	An individual resident in India studying abroad may raise loan outside India not exceeding USD 250,000/- or its equivalent, for the purposes of payment of education fees abroad and maintenance expenses subject to specified terms and conditions.	

1.4 Borrowing in Indian rupee from outside India by a Person resident in India (other than Authorised Dealers)

Borrowings by	New ECB Regulations, 2018	Erstwhile Regulations
Company incorporated in India	<p>Borrowing by Eligible resident entities in Rupee denominated ECBs from outside India through issuance of Non-Convertible Debentures (NCDs) other than through public offer is now permitted subject to compliance under the New ECB Regulations, 2018.</p> <p><u>The mandatory requirement of public offer of NCDs is no longer provided in New ECB Regulations, 2018.</u></p>	<p>A company incorporated in India may borrow in rupees on repatriation or non-repatriation basis, from a non-resident Indian or a person of Indian origin resident outside India or an overseas corporate body (OCB), by way of investment in NCDs subject to the following conditions;</p> <ul style="list-style-type: none"> • Issue of NCDs is made by public offer; • rate of interest on such NCDs does not exceed the prime lending rate of the SBI plus 300 basis points • Period for redemption of such NCDs is not less than 3 years
Person resident in India, not being a company incorporated in India	<p>A person resident in India, not being a company incorporated in India, may borrow in Indian Rupees from NRI / Relatives who are <u>OCI Cardholders</u> outside India, subject to such terms and conditions as specified by the Reserve Bank from time-to-time in consultation with the Government of India.</p>	<p>A person resident in India, not being a company incorporated in India, may borrow in rupees on non-repatriation basis from a <u>non-resident Indian</u> or a <u>person of Indian origin</u> resident outside India</p>

1.5 Lending in Indian rupee by a Person resident in India (other than Authorised Dealers)

Lending by	New ECB Regulations, 2018	Erstwhile Regulations
Non-banking financial company (NBFC) & Housing Finance Institution	<p>A registered non-banking financial company in India or a registered housing finance institution in India or any other financial institution as may be specified by RBI, may provide housing loan or vehicle loan, as the case may be, to a <u>NRI/OCI cardholder</u> subject to specified conditions</p>	<p>A housing finance institution in India approved by the National Housing Bank may provide housing loan to a <u>non-resident Indian</u> or a <u>person of Indian origin resident outside India</u>, for acquisition of a residential accommodation in India, subject to certain conditions</p>

1.6 Continuation of loan in the event of change in residential status of the lender / Borrower

A Change in residential status of the lender from resident to non-resident

New ECB Regulations, 2018	Erstwhile Regulations
<p>In case a loan was granted by a resident individual to another resident individual and the lender subsequently becomes a non-resident, the repayment of the loan by the resident borrower should be made by credit to the <u>Non-resident Ordinary (NRO) account</u> or <u>any other account</u> of the lender maintained with a bank in India as specified by the Reserve Bank from time-to-time, at the option of the lender.</p>	<p>In case a rupee loan was granted by a person resident in India to another person resident in India and the lender subsequently becomes a non-resident, the repayment of the loan by the resident borrower should be made by credit to the <u>NRO or Non-resident Special Rupee (NRSR) account</u> of the lender maintained with a bank in India, at the option of the lender.</p>

B Change in residential status of the lender from non-resident to resident

New ECB Regulations, 2018	Erstwhile Regulations
In case a loan was granted by a NRI/OCI Cardholder to a person resident in India and the lender subsequently becomes a resident, then repayment of the loan may be made to the designated account of the lender maintained with a bank in India as specified by the Reserve Bank from time-to-time, at the option of the lender.	There are no specific regulations

C Continuation of loan in the event of change in residential status of the borrower from non-resident to resident

New ECB Regulations, 2018	Erstwhile Regulations
A resident individual will be permitted to service loans taken overseas earlier as a person resident outside India subject to terms and conditions and limit specified by the Reserve Bank from time-to-time.	There were no specific regulations

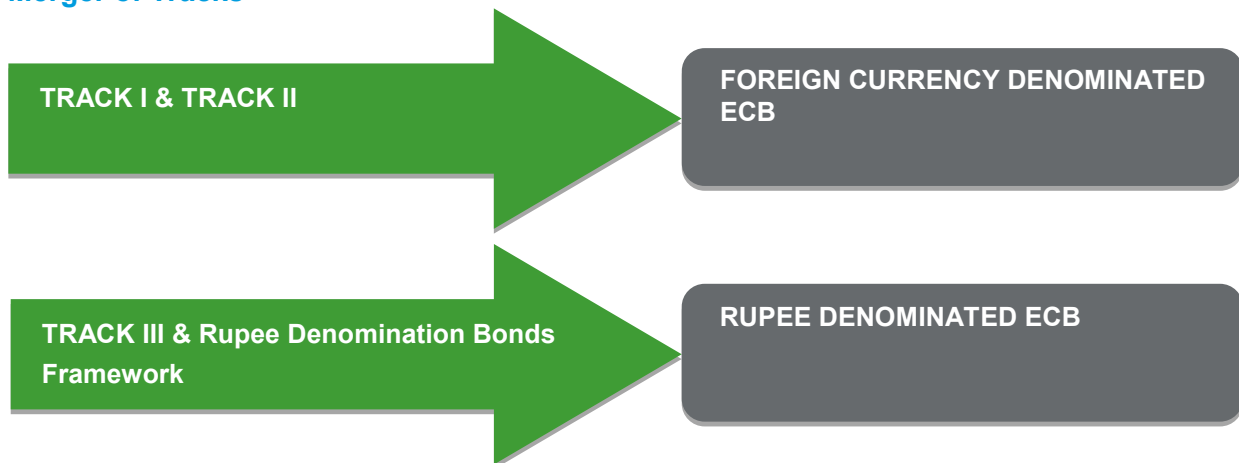
1.7 Trade credit for Imports

Particulars	New ECB Regulations, 2018	Erstwhile Regulations
Currency of borrowing	Importers can now raise trade credit from outside India in <u>freely convertible foreign currency or Indian Rupee</u>	Importer was permitted to raise trade credit <u>only in foreign currency</u>
Borrowing limit	Importers can raise <u>trade credit up to USD 50 million equivalent per import transaction</u> for import of capital or non-capital goods	Trade credit for import of non-capital and capital goods was permitted under automatic route up to <u>USD 20 million or equivalent per import transaction</u> .
Maturity period	Non-capital goods – up to <u>1 year and it is linked with operating cycle</u> Import of <u>capital goods - up to 3 years</u>	Non-capital goods - up to <u>1 year from the date of shipment or the operating cycle</u> whichever is less Capital goods - up to <u>5 years</u> from the date of shipment
Recognised Lenders	<u>Overseas suppliers, banks and other financial institutions, foreign equity holders and financial institutions in International Financial Services Centres (IFSCs) in India</u>	<u>Overseas supplier, bank and financial institution</u>
Cost of raising Trade Credit	<u>Trade Credit in foreign currency – reduced to 250 basis points over 6 month LIBOR</u>	<u>Upto 350 basis points over 6 months LIBOR</u>
	<u>Trade Credit in INR – cost shall be commensurate with prevailing market conditions</u>	

It is pertinent to note that the New ECB Framework does not cover provisions pertaining to Trade Credit. RBI may issue a separate notification for the same.

2.0 Certain regulatory changes in the New ECB Framework

2.1 Merger of Tracks



The New ECB Framework has merged earlier Tracks I and II ECB as “Foreign Currency denominated ECB” and merged Track III and Rupee Denominated Bonds (RDBs) framework as “Rupee Denominated ECB”. In view of the above merger of Track III and RDBs, prior RBI approval will now not be required for issuing RDB subject to compliances under the said regulations.

2.2 Few Important terms used in New ECB Framework

- **FATF compliant country**

A country that is a member of Financial Action Task Force (FATF) or a member of a FATF-Style Regional Body; and should not be a country identified in the public statement of the FATF as

- i. A jurisdiction having a strategic Anti-Money Laundering or Combating the Financing of Terrorism deficiencies to which counter measures apply; or
- ii. A jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with the Financial Action Task Force to address the deficiencies.

- **IOSCO compliant country**

A country whose securities market regulator is a signatory to the International Organization of Securities Commission's (IOSCO's) Multilateral Memorandum of Understanding (Appendix A Signatories) or a signatory to bilateral Memorandum of Understanding with the Securities and Exchange Board of India (SEBI) for information sharing arrangements.

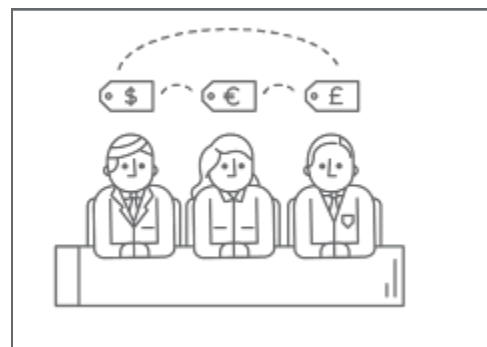
- **Infrastructure space companies**

Companies in infrastructure sector, Non-Banking Finance Companies (NBFCs) undertaking infrastructure financing, Holding Companies/ Core Investment Companies undertaking infrastructure financing, Housing Finance Companies (HFCs) regulated by National Housing Bank (NHB) and Port Trusts (constituted under the Major Port Trusts Act, 1963 or Indian Ports Act, 1908).

2.3 Eligible Borrowers

The list of Eligible Borrowers has been expanded to include **all entities eligible to receive FDI**. Further, the following entities are also eligible to raise ECB:

- Port Trusts;
- Units in SEZ;
- SIDBI;
- EXIM Bank; and
- Registered entities engaged in micro-finance activities, viz., registered Not for Profit companies, registered societies/trusts/cooperatives and Non-Government Organisations (permitted only to raise INR ECB).



2.4 Recognised Lenders

The Erstwhile Regulations had defined recognized lender for each track. As per the New ECB Framework the lender should be resident of FATF or IOSCO compliant country. The following are also considered as recognised lenders.

- Multilateral and Regional Financial Institutions where India is a member country
- Individuals as lenders can only be permitted if they are foreign equity holders or for subscription to bonds/debentures listed abroad;
- Foreign branches / subsidiaries of Indian banks only for ECB in foreign currency (except FCCBs and FCEBs).

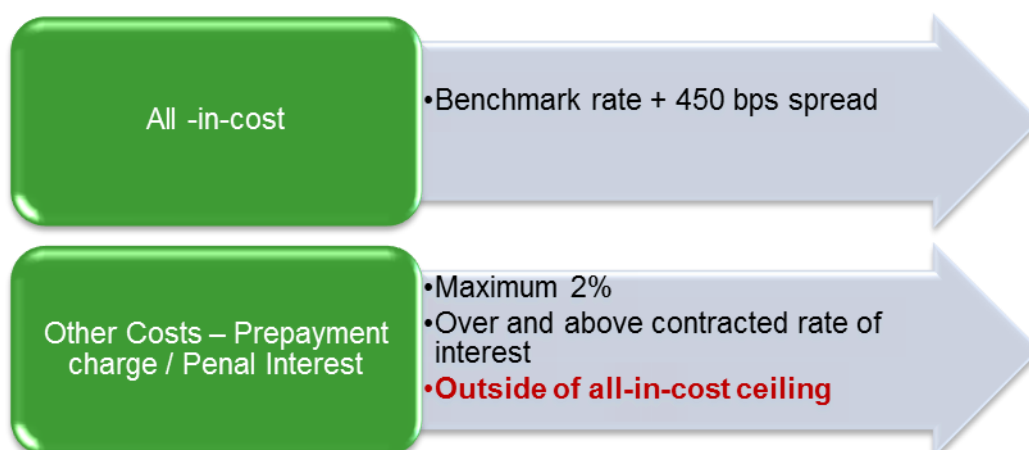
2.5 Minimum Average Maturity Period (MAMP)

As per the New ECB Framework, the MAMP for foreign currency denominated ECBs (including FCCBs and FCEBs) and INR Denominated ECBs is tabulated hereunder.

Manufacturing sector	1 year (for ECB up to 50 million or equivalent per FY)
Foreign Equity Holder	5 years (if utilized for working capital purpose, general corporate purpose or repayment of rupee loans)
Others	3 years

As per the Erstwhile Regulations, MAMP for borrowings of up to USD 50 million (or the equivalent) was 3 years and the MAMP for borrowings above USD 50 million was 5 years. The MAMP for FCCBs or FCEBs, irrespective of the amount of the borrowing, was 5 years.

2.6 All-in-cost and other cost

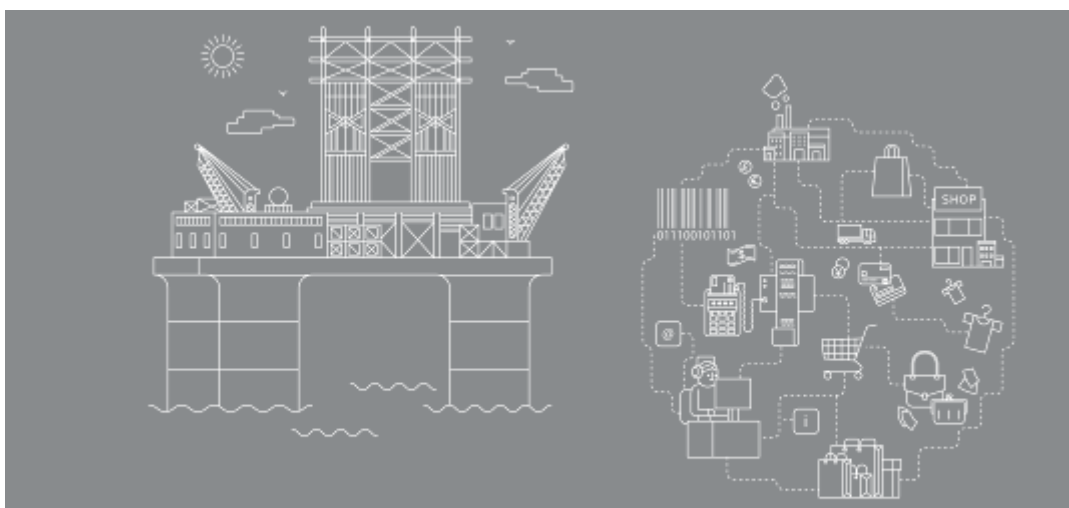


Benchmark rate in case of foreign currency denominated ECB/ TC refers to 6 month London Interbank Offered Rate (LIBOR) rate of different currencies or any other 6 month interbank interest rate applicable to the currency of borrowing, for e.g., Euro Interbank Offered Rate (EURIBOR). Benchmark rate in case of Rupee denominated ECB (INR ECB) will be prevailing yield of the Government of India securities of corresponding maturity.

2.7 End use negative list

- Real Estate activities (as defined in the New ECB Regulations, 2018)
- Investment in capital market
- Equity Investment
- Working capital purposes, General capital purpose and repayment of rupee loans except from foreign equity holder
- On-lending to entities for the above activities

As per the Master Direction No. 5 (pertaining to Erstwhile Regulations), proceeds from issuance of Rupee denominated bonds could be used for working capital or general corporate purposes or for repayment of rupee loans. However, under the New ECB Regulations, 2018 proceeds from the issuance of Rupee denominated bonds can be used for working capital or general corporate purposes or for repayment of rupee loans **only** if such RDBs are held by foreign equity holders.



2.8 Hedging provision

New ECB Regulations, 2018	Erstwhile Regulations
Under the New ECB Framework, infrastructure space companies are required to have a board approved risk management policy and such companies must <u>mandatorily hedge 70%</u> of their ECB exposure in case the average maturity period is less than 5 years.	<p>The below mentioned entities were required to have a board approved risk management policy and their ECB exposure shall be <u>hedged upto 100%</u> in case the average maturity is less than 5 years.</p> <ul style="list-style-type: none"> • Companies in infrastructure sector • Non-Banking Financial Companies - Infrastructure Port Trusts Act, 1963 or Indian Ports Act, 1908 Finance Companies (NBFC-IFCs), • NBFCs-Asset Finance Companies (NBFC-AFCs), • Holding Companies and • Core Investment Companies (CICs). • Housing Finance Companies, regulated by the National Housing Bank, Port Trusts constituted under the Major

2.9 End use negative list

Particulars	New ECB Regulations, 2018	Erstwhile Regulations
Individual borrowing limit	USD 750 million or equivalent per financial year to all categories of borrowers	USD 750 million – Infrastructure, manufacturing sectors and certain categories of NBFCs USD 200 million - Software development sector USD 100 million - Micro finance activities USD 500 million - remaining entities

2.10 Change in reporting requirement

As per the Erstwhile Regulations, for obtaining LRN under approval route, borrowers are required to submit duly certified Form ECB whereas in case the borrower desirous to raise ECB under the automatic route Form 83 must be filed with the AD bank.

The New ECB Regulations, 2018 has subsumed both the forms under one single **form ECB** to be used for obtaining LRN under automatic as well as approval route.



2.11 Delay in reporting – Late submission Fee (LSF)

The New ECB Framework has introduced the concept of LSF wherein the borrower is given an opportunity to regularize the following contraventions under the ECB regulations by making payment of late submission fees.

- Delay in reporting of drawdown of ECB proceeds before obtaining LRN or
- Delay in submission of Form ECB 2 returns,

The details of LSF are tabulated hereunder:

Sr. No.	Type of Return/Form	Period of delay	Applicable LSF
1	Form ECB 2	Up to 30 calendar days from due date of submission	INR 5,000
2	Form ECB 2/Form ECB	Up to 3 years from due date of submission/date of drawdown	INR 50,000 per year
3	Form ECB 2/Form ECB	Beyond 3 years from due date of submission/date of drawdown	INR 100,000 per year

2.12 Standard Operating Procedure (SOP) for Untraceable Entities

As per the New ECB Framework, any borrower who has raised ECB will be treated as 'untraceable entity', if entity/auditor(s)/director(s)/ promoter(s) of entity are not reachable/responsive/reply in negative over email/letters/phone for a period of not less than 2 quarters with documented communication/ reminders numbering 6 or more and it fulfills both of the following conditions:

- a. Entity not found to be operative at the registered office address as per records available with the AD Bank or not found to be operative during the visit by the officials of the AD Bank or any other agencies authorized by the AD bank for the purpose;
- b. Entities have not submitted Statutory Auditor's Certificate for last two years or more;

SOP has to be followed by designated AD Category-I banks in case of untraceable entities – **action required**

- a. File Revised Form ECB, if required, and last Form ECB 2 Return without certification from company with 'UNTRACEABLE ENTITY' written in bold on top. The outstanding amount will be treated as written-off from external debt liability of the country but may be retained by the lender in its books for recovery through judicial/ non-judicial means;
- b. AD bank not to examined/processed any fresh ECB application by the entity;
- c. Directorate of Enforcement should be informed whenever any entity is designated 'UNTRACEABLE ENTITY'; and
- d. No inward remittance or debt servicing will be permitted under automatic route.

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This newsflash is general in nature. In this newsflash we have analysed New ECB Regulations, 2018 (vide Notification No. FEMA.3(R)/2018-RB, 17 December 2018) and New ECB Framework vide circular No. 17 dated 16 January 2019. (herein referred as New ECB Framework). It may be noted that nothing contained in this newsflash should be regarded as our opinion and facts of each case will need to be analyzed to ascertain applicability or otherwise of the said notification and appropriate professional advice should be sought for applicability of legal provisions based on specific facts. We are not responsible for any liability arising from any statements or errors contained in this newsflash.

5 Feb 2019