

Remodelling of External Commercial Borrowing Framework

written by Shreya Dasgupta | September 2, 2019

ECB Framework - Post the enormous victory of the Bhartiya Janta Party and its allies in the Centre in 2019, this year has been witnessing substantial modifications in the existing laws of India. The Modi government has been a constant advocate of own business and thus, in the past few years, we have observed a sudden burst of start-ups in the Indian market. In order to continue and encourage the Indian start-ups further, the government and the Reserve Bank of India ("RBI") brought in extensive amendments by the notifications dated January 16, 2019[1], February 08, 2019[2] and March 13, 2019 [3] and subsequently amended Master Direction - External Commercial Borrowings, Trade Credits and Structured Obligations dated March 26, 2019 (collectively referred as "Amended Framework"). External Commercial Borrowing ("ECB") are the debts availed by Indian commercial entities from foreign lenders. We have enumerated below the vital alternations:

- **Consolidation of tracks:** The earlier Master Director dated January 01, 2016 ("Erstwhile Framework") had 4 types of ECB under it, in which Track 1 and 2 were for medium-term and long-term foreign currency ("FCY") denominated ECB. The Track 3 and Masala Bonds were medium-term and long-term Rupee ("INR") denominated ECB. In the Amended Framework, the Track I and II have been merged as 'FCY denominated ECB' and further Track III and Masala Bonds have been merged as 'INR denominated ECB'.
- **Expansion of forms of ECB:** The Amended Framework has expanded the forms by which ECB can be given for both the ECBs viz: inclusion of trade credits beyond 3 years. It further states that plain vanilla INR denominated ECB can either be placed privately or listed on exchanges as per host country regulations.
- **Standardisation of Recognised Lenders:** Unlike Erstwhile Framework, the Amended Framework has uniformed the criteria of lenders who can lend in India throughout all kind of ECBs. The lender has to be a member of FATF or International Organization of Securities Commissions ("IOSCO") and also includes multilateral and regional financial institutions of which India is a member. Further, for both the denominations of ECB, foreign individuals will be only considered as a lender if the bond is listed in the host country. The foreign branches/subsidiaries of Indian banks can also be considered as an eligible lender, however, underwriting by such foreign branches/subsidiaries cannot be considered as eligible lender.
- **Changes in the 'Eligible Borrowers':** The Erstwhile Framework had a list of eligible borrowers for every track, however the same has been simplified in the Amended Framework. All entities who are eligible to raise Foreign Direct Investment ("FDI") will be considered eligible under the current ECB norms, which includes port trusts, unit in Special Economic Zone, Small Industries Development Bank of India and Export-Import Bank of India while for INR denominated ECB, eligible lenders include all eligible

lenders under FCY denominated ECB and registered entities engaged in micro-financing in India.

- **Uniformity in Minimum Average Maturity Period (“MAMP”):** The Amended Framework has uniformed the MAMP as 3 years for all ECBs, contrasting the Erstwhile Framework wherein every track had an individual MAMP.
The exception to the above-mentioned standardised MAMP in the Amended Framework is that the manufacturing companies may raise ECBs with MAMP of 1 year for ECB up to USD 50,000,000 or its equivalent per financial year. Further, if the ECB is raised from foreign equity holder and utilized for working capital purposes, general corporate purposes or repayment of Rupee loans, MAMP will be 5 years. The call and put option, if any, shall not be exercisable prior to completion of MAMP.
- **Consistency in the individual limits:** The Amended Framework has created a uniform limit of USD 750,000,000 for both FCY and INR denominated ECB under the automatic route. However, the provision regarding raising ECB from direct foreign equity holder has been rephrased, not amended.
- **Changes in exchange rates of ECB:** As per the Erstwhile Framework, the exchange rate was the rate which was prevalent on the day of settlement, whereas in the Amended Framework, the exchange rate for FCY denominated ECB will be the rate prevailing on the date of agreement or any rate agreement by the lender and for INR denominated ECB, the exchange rate of the Erstwhile Framework will prevail.
- **Variations in hedging provisions:** The hedging provision of the Erstwhile Framework was optional and was permitted through derivative products with Authorized Dealer (“AD Bank”) Category I banks or through branches/subsidiaries of Indian banks abroad or branches of foreign banks with Indian presence on a back-to-back basis. According to the Amended Framework, 70% of the total borrowing has to be compulsorily hedged if the MAMP is less than 5 years for FCY denominated ECB. For the INR denominated ECB, the external lender is eligible to hedge their exposure in Rupee through permitted derivative products with AD Category I banks in India. The investors can also access the domestic market through branches/subsidiaries of Indian banks abroad or branches of foreign banks with Indian presence on a back to back basis.
- **Deviation in reporting:** In the Erstwhile Framework, the entities desirous to raise ECB under the automatic route had to approach an AD Bank with their proposal along with duly filled Form 83, however for approval route cases, the borrowers had to approach the RBI with an application in Form ECB for examination through their AD Bank. However, in the Amended Framework, Form 83 and ECB have been merged to Form ECB. Further, the borrower under the Erstwhile Framework has to file Form ECB-2 monthly with the Department of Statistics and Information Management (DSIM) and in case of failure to file the same, the Loan

Registration Number ("LRN") was being instantly cancelled. In the Amended Framework, the late submission of Form ECB-2/ECB can now be compounded by paying late fees of:

- INR 5,000 for delay of submission of 30 days from the due date;
- INR 50,000 per year for delay up to 3 years;
- INR 1,00,000 per year for delay beyond 3 years;
- Alternation in Trade Credit norms: Trade-credit limit for the automatic route for import of non-capital and capital goods has been increased from USD 20,000,000 to USD 50,000,000 for import of non-capital and capital goods and for beyond USD 50,000,000, the RBI approval is required. Further, for oil/gas refining & marketing, airline and shipping companies, the limit is set up to USD 150,000,000 or equivalent per import transaction and beyond it, RBI approval is required. The MAMP for trade credits of capital goods has been reduced from 5 years to 3 years. The all-in-cost ceiling per annum has been reduced from 350 basic points over 6 months LIBOR to 250 basic points over 6 months LIBOR.
- Other modifications: The other relevant modifications include the following:
- The Amended Framework introduced the 'Standard operating procedure for untraceable entities' wherein if the AD Bank does not receive any response from any means of communication by a particular entity for more than two quarters or the entity has stopped operating in its registered office or the entity is not filing the statutory auditor's report for than 2 years, the AD Bank has to immediately file Form ECB/ECB-2 and mark it as 'Untraceable entity'. The AD Bank should not further examine/process any fresh ECB application or any inward remittance and debt servicing will be permitted under the automatic route.
- The Amended Framework further states that an entity which is under restructuring scheme/ CIRP under Insolvency and Bankruptcy Code, 2016 can raise ECB only if specifically permitted under the resolution plan and they can raise ECBs from all recognized lenders, except foreign branches/subsidiaries of Indian banks, for repayment of Rupee term loans of the target company. Such ECBs will be considered under the approval route only.
- As per the Amended Framework, trade credit can henceforth be raised by a unit or a developer in SEZ[4] including FTWZ[5] for purchase of non-capital and capital goods within an SEZ including FTWZ or from a different SEZ including FTWZ subject to compliance with parameters of ordinary trade credit and provisions of SEZ Act, 2005. Further, an entity in DTA is also allowed to raise trade credit for the purchase of capital / non-capital goods from a unit or a developer of an SEZ including FTWZ. For such trade credit transactions, the date of transfer of ownership of goods will be

treated as trade credit date. As there will be no bill of entry for sale transactions within SEZ, the inter-unit receipt generated through National Securities Depository Limited can be treated as an import document.

- The Amended Framework allows bank guarantees to be given by the AD Bank, on behalf of the importer, in favour of overseas lender of trade credit not exceeding the amount of trade credit, within the maximum permissible period. Trade credit may also be secured by an overseas guarantee issued by foreign banks/overseas branches of Indian banks. The importer may also offer the security of movable assets (including financial assets) / immovable assets (excluding land in SEZs) / corporate or personal guarantee for raising trade credit, with prior scrutiny of the AD Bank.
- Part IV (Borrowing and Lending in foreign currency by an Authorised Dealer) and Part V (Borrowing and Lending in foreign currency by persons other than an authorised dealer) of the Erstwhile Framework has been removed in the Amended Framework.
- Amendment as per notification dated July 30, 2019[6]: The notification enables the eligible borrowers and NBFCs[7] with ECB of MAMP of 10 years for the purpose of working capital and general corporate purposes and for on-lending for the above purposes, respectively. Further, this notification enumerates that eligible borrowers with ECB of MAMP of 7 years can utilise the funds for repayment of rupee-denominated loans raised for capital expenditure and also NBFC can further lend for the same purpose if their ECB is with MAMP of 7 years. The notification also states that eligible borrowers in manufacturing & infrastructure sector which have been classified as 'special mention account-2'[8] can also repay their domestically availed rupee-denominated loans used for capital expenditure by their ECB loans through any one-time settlement arrangement with lenders. Domestic lenders have also been permitted to sell, through assignment, such loans to eligible ECB lenders, except foreign branches/ overseas subsidiaries of Indian banks, provided, the resultant ECB complies with all-in-cost, MAMP and other laws of the ECB framework.

CONCLUSION

On analysis of the above-cited amendments, we have observed that the government is enabling Indian businesses to obtain capital in a simpler form, with necessary compliances. The amendments have liberalized the Indian borrowing market further with an aim to devise easier capital access to the start-ups and the promoters, who are not willing to dilute their shareholding in their companies, however, had to take recourse of FDI, due to the stringent policies in the Erstwhile Framework. Nevertheless, by this policy, the government has opened the debt market of India considerably and thus, the government needs to be stringent with the

compliances as in the absence of the same, India might drown in the morass of debt in the foreign market. Such liberalisation of the debt market is like a 'two-edged sword' which shall act as a boon to the Indian market, if administered

meticulously and as an irrevocable bane, if not.

- [\[1\]](#) Bearing A. P. (DIR Series) Circular No. 17
- [\[2\]](#) Bearing A. P. (DIR Series) Circular No. 18
- [\[3\]](#) Bearing A. P. (DIR Series) Circular No. 23
- [\[4\]](#) Special Economic Zone
- [\[5\]](#) Free Trade and Warehousing Zone
- [\[6\]](#) Bearing A.P. (DIR Series) Circular No. 04
- [\[7\]](#) Non-banking Financial Company
- [\[8\]](#) where principal or interest payment is overdue between 61-90 days

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