

NO. #1

**CS Coaching at
Laxmi Nagar**

**CS EXECUTIVE
MODULE - 2**

**NEW
ECB**

**For
SECURITIES
LAW &
EBCL**

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"Senior Qualified CS" Faculty



CHAPTER

7

New
EXTERNAL
COMMERCIAL
BORROWINGS (ECB)

Covering-

- External Commercial Borrowings (ECB)
- Type of ECB
- Reporting Requirements
- Advance Your Knowledge
- Self Test Questions

EXPECTED
MARKS COVERAGE
(1 to 5)

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EXTERNAL COMMERCIAL BORROWINGS (ECB)

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ECB – MEANING

External Commercial Borrowings are

1. commercial loans
2. raised by eligible resident entities
3. from recognised non-resident entities

ECB – LEGAL FRAMEWORK

ECB should conform to parameters such as minimum maturity, permitted and non-permitted end-uses, maximum all-in-cost ceiling, etc. Transactions on account of External Commercial Borrowings (ECB) are governed by Section 6(3) (d) of the **Foreign Exchange Management Act, 1999 (FEMA)**. Various provisions in respect of borrowings from overseas are included in the **Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2018** and the **Foreign Exchange Management (Guarantees) Regulations, 2000** as amended from time to time framed under FEMA. Within the contours of the Regulations, **Reserve Bank of India also issues directions** to Authorised Persons.

ECB FRAMEWORK

The framework for raising loans through ECB **comprises the following two options:**

PARAMETERS	FOREIGN CURRENCY DENOMINATED ECB	INDIAN RUPEE DENOMINATED ECB
1.Currency of Borrowing	Any <u>freely convertible</u> Foreign Currency	Indian Rupee (INR)
2.Forms of ECB	Loans including bank loans; floating/ fixed rate notes/ bonds/ debentures (other than fully and compulsorily convertible instruments); Trade credits beyond 3 years; Foreign	Loans including bank loans; floating/ fixed rate notes/bonds/ debentures/ preference shares (other than fully and compulsorily convertible instruments); Trade credits

	Currency Convertible Bonds;(FCCB) Foreign Currency Exchangeable Bonds(FCEB) and Financial Lease.	beyond 3 years; and Financial Lease. Also, plain vanilla Rupee denominated bonds issued overseas, which can be either placed privately or listed on exchanges as per host country regulations.
3. Eligible Borrowers	All entities eligible to receive Foreign Direct Investment (FDI). Further, the following entities are also eligible to raise <u>ECB</u> : (i) Port Trusts; (ii) Units in SEZ; (iii) SIDBI; and (iv) EXIM Bank of India.	(a) All entities eligible to raise Foreign Currency ECB ; and (b) Registered entities engaged in micro-finance activities, viz., registered Not for Profit companies, registered societies/trusts/cooperatives and Non-Government Organisations.

4. RECOGNISED LENDERS

The lender should be **resident of Financial Action Task Force (FATF)** or International Organisation of Securities Commission's **IOSCO compliant country**, including on transfer of ECB.

However,

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

5. MINIMUM AVERAGE MATURITY PERIOD (MAMP)

Minimum Average Maturity Period (MAMP) for ECB **will be 3 years**.

However, for the specific categories mentioned below, the Minimum Average Maturity Period (MAMP) are as under:

Category	Minimum Average Maturity Period (MAMP)
ECB raised by <u>manufacturing companies</u> up to USD 50 million or its equivalent per financial year	1 year
ECB raised <u>from foreign equity holder</u> for	5 year

<p>working capital purposes, general corporate purposes or for repayment of Rupee loans.</p>	
<p>ECB raised for</p> <p>(a) Working capital purposes or general corporate purposes</p> <p>(b) on-lending by NBFCs for working capital purposes or general corporate purposes.</p> <p>It may be noted that:</p> <p>(a) ECB cannot be raised from foreign branches / subsidiaries of Indian banks</p> <p>(b) the prescribed MAMP will have to be strictly complied with under all circumstances</p>	10 year
<p>ECB raised for</p> <p>(a) repayment of Rupee loans availed domestically for capital expenditure</p> <p>(b) on-lending by NBFCs for the same purpose.</p> <p>It may be noted that:</p> <p>(a) ECB cannot be raised from foreign branches / subsidiaries of Indian banks</p> <p>(b) the prescribed MAMP will have to be strictly complied with under all circumstances.</p>	7 year
<p>ECB raised for</p> <p>(a) repayment of Rupee loans availed domestically for purposes other than capital expenditure</p> <p>(b) on-lending by NBFCs for the same purpose.</p> <p>It may be noted that:</p> <p>(a) ECB cannot be raised from foreign branches / subsidiaries of Indian banks</p> <p>(b) the prescribed MAMP will have to be strictly complied with under all circumstances.</p>	10 years

6. ALL-IN-COST CEILING PER ANNUM

All-in-cost ceiling per annum is the **Benchmark rate plus 450 bps spread.**{Basis points (BPS)}

It may be noted that All-in-Cost includes rate of interest, other fees, expenses, charges, guarantee fees, ECA charges, whether paid in foreign currency or INR but will not include commitment fees and withholding tax payable in INR.

7. OTHER COSTS

Prepayment charge/ Penal interest, if any, for default or breach of covenants, should not be more than 2 per cent over and above the contracted rate of interest on the outstanding principal amount and will be outside the all-in-cost ceiling.

8. END-USES (NEGATIVE LIST)

The negative list, for which the ECB proceeds cannot be utilised, would include the following:

(a) Real estate activities.
(b) Investment in capital market.
(c) Equity investment.
(d) Working capital purposes, except ECB raised from foreign equity holder for working capital purposes,
(e) General corporate purposes, except in case of ECB raised from foreign equity holder for working capital purposes
(f) Repayment of Rupee loans, except in case of ECB raised for (i) repayment of Rupee loans availed domestically for capital expenditure (ii) on-lending by NBFCs for the same

9. EXCHANGE RATE

Change of currency of Foreign Currency ECB into Indian Rupee ECB can be **at the exchange rate prevailing on the date of the agreement** for such change between the parties concerned **or at an exchange rate, which is less than the rate prevailing on the date of the agreement, if consented to by the ECB lender.**

10. HEDGING PROVISION

The entities raising ECB are required to follow the guidelines for hedging issued, if any, by the concerned sectoral or prudential regulator in respect of foreign currency exposure.

The following operational aspects with respect to hedging should be ensured:

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| ➤ Coverage: The ECB borrower will be required to cover the principal as well as the coupon through financial hedges. |
| ➤ Tenor: A minimum tenor of one year for the financial hedge would be required |

11. CHANGE OF CURRENCY OF BORROWING

Change of currency of ECB from one freely convertible foreign currency to any other freely convertible foreign currency as well as to Indian Rupee is **freely permitted**.

Change of currency from Indian Rupee to any freely convertible foreign currency is **not permitted**.

12.LIMIT AND LEVERAGE

All eligible borrowers can raise ECB **up to USD 750 million** or equivalent per financial year under the **automatic route**. Further, in case of Foreign Currency denominated ECB raised from direct foreign equity holder, **ECB liability-equity ratio** for ECB raised under the automatic route **cannot exceed 7:1**.

13.ISSUANCE OF GUARANTEE, ETC. BY INDIAN BANKS AND FINANCIAL INSTITUTIONS

Issuance of any type of guarantee by Indian banks, All India Financial Institutions and NBFCs relating to ECB is **not permitted**

14.PARKING OF ECB PROCEEDS

ECB proceeds are permitted to be parked abroad as well as domestically in **the manner given below:**

Parking of ECB proceeds abroad:

ECB proceeds meant only for foreign currency expenditure can be parked abroad pending utilisation. Till utilisation, these funds can be invested in the following liquid assets

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| (a) deposits or Certificate of Deposit or other products offered by banks rated not less than AA (-) by Standard and Poor/Fitch IBCA or Aa3 by Moody's; |
| (b) Treasury bills and other monetary instruments of one-year maturity having minimum rating as indicated above and |
| (c) deposits with foreign branches/subsidiaries of Indian banks abroad. |

Parking of ECB proceeds domestically:

- | |
|--|
| (a) ECB proceeds meant for Rupee expenditure should be repatriated immediately for credit to their Rupee accounts with AD Category I banks in India. |
| (b) ECB borrowers are also allowed to park ECB proceeds in term deposits with AD Category I banks in India for a maximum period of 12 months cumulatively. |

15.PROCEDURE OF RAISING ECB

Automatic route

All ECB can be raised under the automatic route if they conform to the parameters prescribed under this framework. Entities desirous to raise ECB under the automatic route **may approach an AD Category I** bank with their proposal along with duly filled in Form ECB.

Approval route

For approval route cases, the borrowers **may approach the RBI** with an application in prescribed format (Form ECB) for examination through their AD Category I bank..

16.REPORTING REQUIREMENTS

Borrowings under ECB Framework are subject to following reporting requirements apart from any other specific reporting required under the framework:

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| <p>1. <u>Loan Registration Number (LRN):</u> Any draw-down in respect of an ECB should happen only after obtaining the LRN from the Reserve Bank. To obtain the LRN, borrowers are required to submit duly certified Form ECB in duplicate to the designated AD Category I bank. In turn, the AD Category I bank will forward one copy to the Director, Reserve Bank of India, Department of Statistics and Information Management, External Commercial Borrowings Division, Bandra-Kurla Complex, Mumbai 400 051.</p> |
| <p>2. <u>Changes in terms and conditions of ECB:</u>Changes in ECB parameters should be reported to the Department of Statistics and Information Management through revised Form ECB at the earliest, in any case not later than 7 days from the changes effected.</p> |
| <p>3. <u>Monthly Reporting of actual transactions:</u>The borrowers are required to report actual ECB transactions through Form ECB 2 Return through the AD Category I bank on monthly basis so as to reach Department of Statistics and Information Management within seven working days from the close of month</p> |

17.CONVERSION OF ECB INTO EQUITY

Conversion of ECB, including those which are matured but unpaid, into equity is permitted subject to the following conditions:

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| <p>(i) The activity of the borrowing company is covered under the automatic route for Foreign Direct Investment or Government approval is received, wherever applicable,for foreign equity participation as per extant Foreign Direct Investment policy.</p> |
| <p>(ii) The conversion, which should be with the lender's consent and without any additional cost, should not result in contravention of eligibility and breach of applicable sector cap on the foreign equity holding under Foreign Direct Investmentpolicy;</p> |
| <p>(iii) Applicable pricing guidelines for shares are complied with;</p> |

(iv) In case of partial or full conversion of ECB into equity, the reporting to the Reserve Bank will be as under:

- (a)** For partial conversion, the converted portion is to be reported in **Form FC-GPR** prescribed for reporting of FDI flows, while **monthly reporting to DSIM in Form ECB 2 Return** will be with suitable remarks, viz., "ECB partially converted to equity".

- (b) For full conversion, the entire portion is to be reported in Form FC-GPR, while reporting to DSIM in Form ECB 2 Return should be done with remarks “**ECB fully converted to equity**”. Subsequent filing of Form ECB 2 Return is not required.
- (c) For conversion of ECB into equity **in phases**, reporting through Form FC-GPR and Form ECB 2 Return will also be **in phases**.

18. SECURITY FOR RAISING ECB

AD Category I banks are permitted to allow creation/cancellation of charge on immovable assets, movable assets, financial securities and issue of corporate and/or personal guarantees in favour of overseas lender / security trustee, to secure the ECB to be raised/ raised by the borrower, subject to satisfying themselves that:

(a) the underlying ECB is in compliance with the extant ECB guidelines,
(b) there exists a security clause in the Loan Agreement requiring the ECB borrower to create/cancel charge, in favour of overseas lender/security trustee, on immovable assets/movable assets/financial securities/issuance of corporate and/or personal guarantee, and
(c) No objection certificate, as applicable, from the existing lenders in India has been obtained in case of creation of charge:

ECB FACILITY FOR OIL MARKETING COMPANIES

Public Sector Oil Marketing Companies (OMCs) can raise ECB for working capital purposes with **minimum average maturity period of 3 years** from all recognised lenders under the automatic route without mandatory hedging and individual limit requirements. The overall ceiling for such ECB shall be **USD 10 billion** or equivalent.

ECB FACILITY FOR STARTUPS

AD Category-I banks are permitted to allow Startups to raise ECB under the automatic route as per the following framework:

Eligibility: An entity recognised as a Startup by the Central Government as on date of raising ECB.
Maturity: Minimum average maturity period will be 3 years.
Recognised lender: Lender / investor shall be a resident of a FATF compliant country. However, foreign branches/subsidiaries of Indian banks and overseas entity in which Indian entity has made overseas direct investment as per the extant Overseas Direct Investment Policy will not be considered as recognised lenders under this framework.
Forms: The borrowing can be in form of loans or non-convertible, optionally convertible or partially convertible preference shares.
Currency: The borrowing should be denominated in any freely convertible currency or in Indian Rupees (INR) or a combination thereof. In case of borrowing in INR, the non-resident lender, should mobilise INR through swaps/outright sale undertaken through an AD Category I bank in India.

Amount: The borrowing per Startup will be limited to **USD 3 million** or equivalent **per financial year** either in INR or any convertible foreign currency or a combination of both.

All-in-cost: Shall be mutually agreed between the borrower and the lender.

End uses: For any expenditure in connection with the business of the borrower.

Conversion into equity: Conversion into equity is freely permitted subject to Regulations applicable for foreign investment in Startups.

Security: The choice of security to be provided to the lender is left to the borrowing entity. Security can be in the nature of movable, immovable, intangible assets (including patents, intellectual property rights), financial securities, etc.

Hedging: The overseas lender, in case of INR denominated ECB, will be eligible to hedge its INR exposure through permitted derivative products with AD Category I banks in India.

Conversion rate: In case of borrowing in INR, the foreign currency INR conversion will be at the market rate as on the date of agreement.

Other Provisions: Other provisions like parking of ECB proceeds, reporting arrangements, powers delegated to AD banks, borrowing by entities under investigation, conversion of ECB into equity will be as included in the ECB framework.

BORROWING BY ENTITIES UNDER INVESTIGATION

All entities against which investigation / adjudication / appeal by the law enforcing agencies for violation of any of the provisions of the Regulations under FEMA pending, may raise ECB as per the applicable norms, The **borrowing entity shall inform about pendency** of such investigation / adjudication / appeal to the **AD Category-I bank / RBI** as the case may be.

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