External Commercial Borrowings (ECB) – Revised regulations and framework

Borrowing and lending between a person resident in India and outside India were regulated vide following Regulations:

- Foreign Exchange Management (Borrowing and Lending in Foreign Exchange) Regulations, 2000 – Notification no FEMA 3/2000-RB
- Foreign Exchange Management (Borrowing and Lending in Rupees) Regulations, 2000 – Notification no FEMA 4/2000-RB.

The Reserve Bank of India (‘RBI’) vide its Notification no 3(R)/2018-RB dated 17 December 2018 has subsumed both the Regulations into a consolidated Regulation viz. Foreign Exchange Management (Borrowing and Lending) Regulations, 2018. The revised Regulation provides scope for further amendments by the RBI in consultation with the Government of India (GoI).

In line with the changes introduced by the revised Regulation, a New ECB Framework has been issued vide A.P. (DIR Series) Circular No. 17 dated 16 January 2019 which is brought into force with immediate effect.

Key changes introduced vide FEMA 3(R) and New ECB Framework are summarised below:

1. **Removal of track-based ECB classification**
   
   Tracks I (medium-term foreign currency loans), Track II (long term foreign currency loan) and Track III (INR denominated ECB) and Rupee Denominated Bonds (‘RDB’ or ‘Masala Bonds’) from the existing framework have been merged and the new framework has the following simplified two categories:
   
   - Foreign currency denominated ECB
   - INR denominated ECB

Since RDBs have been merged into INR denominated ECBs, prior RBI approval is no longer required for issuing RDB provided all other conditions for an automatic route in respect of amount, maturity period, etc. are complied with.

2. **Forms of ECB**

FEMA 3(R) provides that presently certain hybrid instruments such as optionally convertible debentures presently covered under ECB would be governed by specific hybrid instruments Regulations when notified by the GoI.

3. **Amendment to the definition of Eligible Borrowers**

- FEMA 3(R) has amended the definition of an Indian entity to include a Limited Liability Partnership (LLP) formed and registered in India under the LLP Partnership Act, 2008, as amended from time to time.
- Further, the New ECB framework defines Eligible borrowers to include all ‘entities’ eligible to receive FDI under FEMA 20(R) and also includes Port Trusts, Units in SEZ, SIDBI, EXIM Bank and registered entities engaged in micro-finance activities viz., not for profit companies, registered societies/trusts /cooperatives and non-government organisations.

4. **Recognised lenders simplified**

The previous ECB framework defined recognized lender for each track. As per the revised ECB framework, the overseas lender needs to be a resident of FATF or IOSCO compliant country.
5. Minimum Average Maturity Period (MAMP)

The new framework has prescribed a uniform MAMP of three years for all types of ECB irrespective of the amount involved, except:

- Manufacturing sector companies raising ECB up to USD50 million or equivalent per financial year can have MAMP of one year and
- ECB raised from foreign equity holder lending for meeting working capital needs, general corporate purpose or repayment of rupee loan to have MAMP of five years.

The reduced MAMP may impact the borrowers in the infrastructure sector which earlier enjoyed MAMP of 10 years.

6. All-in-cost ceiling

The definition of all-in-cost as per the revised ECB framework specifies that various components of the all-in-cost have to be paid by the borrower without taking recourse to the drawdown of ECB/Trade Credit, i.e. ECB/Trade Credit proceeds cannot be used for payment of interest/charges.

7. Individual limits

The ECB framework prescribed the following borrowing limits basis the sector in which the borrower operates:

<table>
<thead>
<tr>
<th>Borrower Category</th>
<th>Eligible limit (USD in a million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Companies in infrastructure and manufacturing sectors, Non-Banking Financial Companies -Infrastructure Finance Companies (NBFC-IFCs), NBFCs-Asset Finance Companies (NBFC-AFCs), Holding Companies and Core Investment Companies (CICs)</td>
<td>750</td>
</tr>
<tr>
<td>Companies in the software development sector</td>
<td>200</td>
</tr>
</tbody>
</table>

The revised ECB framework has provided a single limit of USD 750 million or equivalent per financial year irrespective of the category of borrower. The limit for Startup remains constant at USD three million or equivalent per financial year either in INR or any convertible foreign currency or a combination of both.

8. ECB Liability - Equity Ratio

The revised ECB framework provides that the ECB liability: Equity ratio of 7:1 shall be applicable only in case of foreign currency denominated ECB.

9. End uses

The new ECB framework has defined the term Real estate as under:

"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 the 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 sectors' definition.

10. Hedging requirements

The previous ECB framework mandated the hedging requirement of 70 per cent of the ECB exposure for maturity period between three to five years for companies in infrastructure sector, NBFC-IFCs, NBFC-AFCs, Holding Companies and CICs and Housing Finance Companies, regulated by the National Housing Bank, Port Trusts constituted under the Major Port Trusts Act, 1963 or Indian Ports Act, 1908.

The revised framework has made the above hedging requirement mandatory for ‘Infrastructure space companies’ which has been defined as under:
Companies in infrastructure sector, Non-Banking Finance Companies (NBFCs) 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).

11. Revised reporting structure

Form ECB (for obtaining LRN under approval route) and Form 83 (for obtaining LRN under automatic route) has been subsumed under single Form ECB to be used for obtaining LRN both under the automatic and approval route.

12. Late Submission Fees (LSF) introduced

Delay in reporting of the drawdown of ECB proceeds before obtaining LRN or delay in submission of Form ECB 2 returns can now be regularised by payment of late submission fees as detailed below

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

13. Trade Credit

FEMA 3(R) has made following changes to the trade credit provisions:

- **Borrowing limit:** The amount of trade credit increased from USD 20 million to USD 50 million or equivalent per import transaction for import of capital or non-capital goods

- **Currency of borrowing:** It can be denominated in foreign currency as well as INR or any other currency as specified by the RBI in consultation with the GoI.

- **Maturity period:** The period of trade credit for import of capital goods has been reduced from five years to three years.

- **Cost of raising Trade Credit:** The all-in-cost ceiling for raising Trade Credit raised in foreign exchange has been reduced from 350 to 250 basis points over six months LIBOR (for the respective currency of credit or applicable benchmark).

For Rupee denominated Trade Credit, the all-in-cost shall be commensurate with the prevailing market conditions or as prescribed by the RBI in consultation with the GoI.

The revised ECB framework does not cover Trade Credit related provisions and it appears that a separate Trade Credit framework would be introduced.

**Our comments**

The revised ECB framework has simplified the provisions by removing track-based ECB classification, providing single borrowing limit for all borrowers and single MAMP irrespective of the amount involved.

Removal of prior RBI approval requirement for Rupee bonds would hopefully bring back momentum in raising Indian Masala Bonds.

Revised definition of Eligible Borrowers has allowed LLPs eligible to raise funds by way of ECBs. Further, even sectors such as trading, services, etc. eligible to receive FDI which could not access ECB earlier, would now be eligible under the revised framework.

The enhanced limit of USD 750 million or equivalent per financial year is a positive change for all borrowers.

The introduction of late submission fee would ensure stricter compliance with the reporting requirements and reduce the time taken in getting the delay regularised through compounding.