ECB and Compounding under the FEMA

29th February 2020

KPNB & Associates
Chartered Accountants

External Commercial Borrowings
- An overview

ECB Contents

- Framework
- Forms & Routes
- Key Parameter
- ECB Liability – Equity Ratio & Parking ECB proceeds
- Refinancing & Conversion
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- Security / Creation of charge
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Framework

Act

Foreign Exchange Management Act, 1999 – Section 6 – Capital Account Definition

Regulations

Permissible Capital Account Transaction Regulations 2000 [FEMA 1] and Borrowing and Lending Regulations 2000 [FEMA 3R]

Circulars (A.P. DIR Series Circulars) and Notifications amending the Regulations issued by RBI from time to time

External Commercial Borrowings (ECB) Policy – New ECB Framework dated 16 January 2019

Master Direction

No. 11/2017-18 dated 26 March 2019 updated from time to time (last updated on 8 August 2019)

FAQs

RBI issued FAQs on ECB dated 29 May 2019

Thumb Rule - ECB is a Capital Account Transaction – permissible only as stipulated - In case of doubt, always avail the Approval Route

Forms and Routes

ECB = Commercial loans raised by eligible resident entities from recognized non-resident entities conforming to **cumulative** parameters such as minimum maturity, permitted and non-permitted end uses, maximum all-in-cost ceiling etc.

FCY / INR

ECB Routes

Automatic Route

- No approval required
- Obtain LRN from RBI by filing Form ECB through AD Bank (earlier Form 83)
- Monthly filings with RBI through AD Bank in Form ECB-2
- Includes entities under Investigation under FEMA on without prejudice basis

Bank / Other Loans

Securitized instruments **

FCCBs / FCEB

Finance Lease

Trade Credit > 3 years

Approval Route

- Prior application to the RBI through AD Bank (Form ECB)
- Recommendation of RBI Empowered Committee (Internal RBI & External Members) for application above certain threshold and final decision by RBI
- Factors: merits, macroeconomic situations and overall guidelines
- Post approval, obtain LRN, monthly filings as Automatic Route

All other forms of ECBs for instance, beyond individual limits

*** Securitized instruments (such as bonds, non-convertible, optionally convertible or partially convertible preference shares or debentures)*

Key Parameters (Cumulative)

1. **Eligible Borrowers**
2. **Recognized Lenders**
3. **Minimum Average Maturity Period**
4. **End-use prescriptions**
5. **All-in-cost Ceiling**
6. **Limits**
7. **Currency**

Eligible Borrowers and Recognised Lenders

Eligible Borrowers

- All entities eligible to receive FDI
- Further, following entities are also eligible to raise ECB:
  a) Port Trusts;
  b) Units in SEZ;
  c) SIDBI;
  d) EXIM Bank and
  e) Registered entities engaged in micro-finance activities, viz., registered Not for Profit companies, registered societies / trusts / cooperatives and Non- Government Organizations (permitted only to raise INR ECB).

LLPs not eligible borrower as not eligible to receive FDI

Recognized Lenders

- The lender should be resident of FATF or IOSCO compliant country, including on transfer of ECBs.
- Additionally, following are also recognized lenders:
  - Multilateral and Regional Financial Institutions where India is a member country;
  - Individuals can only be permitted if they are foreign equity holders or for subscription to bonds / debentures listed abroad; and
  - Foreign branches / subsidiaries of Indian banks only for FCY ECB (except FCCBs and FCEBs)

Minimum Average Maturity Period (MAMP)

MAMP for ECB will be 3 years. Call and put options, if any, shall not be exercisable prior to completion of MAMP. However, for the specific categories mentioned below, the MAMP will be as prescribed therein:

Sr. No.	Category	MAMP (Years)
1.	ECB raised by manufacturing companies up to USD 50 million or its equivalent per FY	1
2.	ECB raised from foreign equity holder for working capital purposes, general corporate purposes or for repayment of Rupees loans	5
3.	ECB raised for working capital purposes or general corporate purposes and on- lending by NBFCs for working capital purposes or general corporate purposes	10
4.	ECB raised for repayment of Rupee loans availed domestically for capital expenditure and on-lending by NBFCs for the same purpose	7
5.	ECB raised for repayment of Rupee loans availed domestically for purposes other than capital expenditure and on-lending by NBFCs for the same purpose	10

For categories mentioned at (b) to (e) – i) ECB cannot be raised from foreign branches / subsidiaries of Indian banks; ii) the prescribed MAMP will have to be strictly complied with under all circumstances.

Foreign equity holder means a) Direct foreign equity holder of minimum 25% equity holding by the lender in the borrowing company; b) Indirect equity holder with minimum 51%; and c) Group company with common overseas parent.

(Foreign Equity Holding condition to be fulfilled throughout the tenure of the ECB wherever applicable)

End-use (Negative List)

The negative list, for which the ECB proceeds cannot be utilized include:

a) Real estate activities;
b) Investment in capital market
c) Equity investment
d) Working capital purposes*
e) General corporate purposes *
f) Repayment of Rupee loans*
g) On-lending to entities for the above activities, except in case of ECB raised by NBFCs as prescribed

Other non-permissible utilization

a) Contribution in an LLP
b) Indirect Equity investment through Purchase of Goodwill
c) Reimbursement of expenditure incurred in the past

Investment in Overseas WOS / JV permissible

Real Estate Activities: Any real estate 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, *(i) construction / development of industrial parks / integrated townships/SEZ (ii) purchase / long term leasing of industrial land as part of new project / modernisation of expansion of existing units and (iii) any activity under 'infrastructure sector' definition*

All-in-Cost ceiling

- **Benchmark Rate**
  - (6 months LIBOR or 6 months interbank interest rate applicable to currency of borrowing for eg., EURIBOR) plus 450 bps spread
  - Benchmark rate in case of Rupee denominated ECB / TC will be prevailing yield of the Government of India securities of corresponding maturity.
- **All-in-cost Components –**
  - Rate of Interest, other fees, expenses, charges, guarantee fees, ECA charges whether in FCY or INR
- **Specific Exclusions :**
  - Commitment Fees
  - Withholding Tax paid in Indian Rupees
- **Penal interest for default of any covenants: Not be more than 2% over the contracted rate of interest on outstanding principal amount and will be outside the all-in-cost ceiling.**

All-in-cost should be within the applicable ceiling at all times-

for eg., giving interest breaching the ceiling in first year and much lower in second year so as to comply on an average, is not permitted)

Limits & Currency

- **Individual limit of borrowing**
  - ECB up to USD 750 million or equivalent per financial year irrespective of the category of borrower under automatic route
- **Currency:** ECB can be raised in any freely convertible foreign currency as well as in Indian Rupees as stipulated
- **Change of currency of ECB**
  - ECB from one convertible foreign currency to any other convertible foreign currency as well as to INR is freely permitted (at an exchange rate prevailing on the date of agreement or less than that rate with consent of ECB Lender).
  - Change of currency from INR to any foreign currency is, however, not permitted.

ECB Liability : Equity Ratio & Parking ECB proceeds

ECB Liability : Equity Ratio

- In case of FCY ECB from direct foreign equity holder - Ratio not to exceed 7:1.
- Not applicable if outstanding ECB (including proposed ECB) is upto USD 5 million
- Borrowing entities to be governed by guidelines on debt equity ratio issued, if any, by the sectoral or prudential regulator concerned
- Proposed ECB to be added to all the outstanding ECB for ECB Liability : Equity ratio – except ECB raised for refinancing
- Equity includes - paid-up capital plus free reserves (incl. proportionate share premium received in FC) as per latest audited balance sheet.

Non-convertible Preference Shares not to be included in Equity

Parking ECB proceeds

Abroad

- ECB for foreign currency expenditure can be parked abroad pending utilization;
- Till utilisation, can be invested in liquid assets (certificate of deposits, Treasury bills, deposits with foreign branches / subsidiaries of Indian banks abroad)

Domestically

- ECB for Rupee expenditure to be immediately repatriated to India;
- Can be invested in term deposits for maximum period of 12 months.

(It cannot be extended beyond this period. Funds have to be shifted to non-interest-bearing account or returned back to the lender beyond 12 months)

Refinancing & Conversion

Refinancing existing ECB

- Refinancing of existing ECB by raising fresh ECB is permitted provided:
  - No reduction in outstanding maturity of the original borrowing;
  - all-in-cost of fresh ECB to be lower than all-in-cost of existing ECB
- Refinancing of ECBs raised under the previous ECB framework – permitted
- Fresh ECB is not availed from overseas branches / Subsidiaries of Indian banks except for highly rated corporates (AAA) and Maharatna / Navratna public sector undertakings

Refinancing of INR ECB with FCY ECB is not permitted.

Conversion of ECB into equity: Permitted subject to following:

- Activity of borrowing company covered under automatic route or required approval is obtained for FDI;
- Conversion not to breach applicable sectoral cap under FDI policy;
- Compliance with pricing guidelines (FV on date of conversion);
- Consent of other lenders; and
- Conversion at exchange rate on the date of agreement or any lesser rate with mutual Consent
- Compliance with filing requirement in Form FC-GSPR and ECB 2

ECB interest also permitted to be converted into equity subject to applicable conditions

Hedging Requirements

Hedging Framework:

Foreign Currency Denominated:

- To follow guidelines for hedging issued, if any, by the concerned sectoral or prudential regulator
- For Infrastructure space companies
  - Requires board approved risk management policy
  - Mandatory hedge of 70% of ECB exposure if average maturity < 5 years

Operational aspects of Hedging:

- **Coverage:** Hedge required to cover principal and interest from the day liability created in books of borrower
- **Tenor and rollover:** Minimum tenor of 1 year of financial hedge required with periodic rollover to ensure ECB exposure is not unhedged at any point
- **Natural Hedge:** Natural hedge, in lieu of financial hedge, to be considered to the extent of offsetting projected cash flows / revenues in matching currency net off projected outflows within same accounting year

INR Denominated

- Hedging through permitted derivative products with AD Category I banks in India
- Foreign investor can also access domestic market through branches / subsidiaries of Indian banks abroad or branches of foreign banks with Indian presence on back to back basis

Security / Creation of charge

Security for Raising ECB :

AD Banks are permitted to allow creation of charge on i) immovable assets, ii) movable assets, iii) financial securities, and iv) issue of corporate and/ or personal guarantees in favor of overseas lender / security trustee, to secure the ECB to be raised / raised by the borrower. The creation of security to be co-terminus with underlying ECB subject to security clause in Loan Agreement and NOC from Indian Lenders

Creation of Charge on Movable Assets

In case of enforcement / invocation of charge, the claim of the lender will be restricted to outstanding claim against ECB. (NOC from Indian lenders for moving encumbered movable assets outside India)

Creation of charge on Immovable Property

- Security shall be subject to FEMA (Acquisition and Transfer of Immovable Property in India) Regulations 2000;
- Permission should not be construed as permission to acquire immovable property by overseas lender / security trustee;
- In case of enforcement / invocation, property should be sold to person resident in India and proceeds shall be repatriated to liquidate the outstanding ECB

Creation of Charges over Financial securities:

Below arrangements are permitted – **to be in compliant with FDI policy on invocation:**

- Pledge of shares of the borrowing company held by the promoters as well as in domestic associate companies of the borrower
- Pledge on other financial securities, viz. bonds and debentures, mutual funds etc. in the name of ECB borrower / promoter
- Security interest over all current and future loan assets and all current assets of the borrower

Guarantee

Issue of Corporate and Personal Guarantee - Possible subject to below conditions / documents:	Issuance of Guarantee, etc. by Indian Banks and Financial Institutions
• A copy of Board Resolution with details specified for corporate guarantee. • Specific requests from individuals to issue personal guarantee indicating details of the ECB should be obtained. • Compliance with the Foreign Exchange Management (Guarantees) Regulations, 2000. • ECB can be credit enhanced / guaranteed / insured by overseas party if it is recognised lender under extant ECB guidelines	• Issuance of Guarantee, Letter of credit, letter of undertaking or letter of comfort by Indian banks, All India Financial Institutions and NBFCs (financial intermediaries) relating to ECB is not permitted. • Indian financial intermediaries (Banks, NBFCs or All India Financial Institutions) cannot invest in FCCBs / FCEBs in any manner.

Non-resident guarantee for domestic fund based and non-fund based facilities:

- The non-resident guarantor may discharge the liability by: i) payment out of rupee balance held in India or ii) by remitting the funds to India or iii) by debit to FCNR(B) / NRE account
- Non-resident guarantor may enforce his claim against resident borrower to recover the amount and on recovery amount can be repatriated subject to certain conditions
- General permission to resident to make payment to non-resident who has met the liability under a guarantee

Reporting Requirement

Form ECB: Borrower is required to submit Form ECB in duplicate with AD Bank. AD Bank will forward one copy to the Director, Balance of payments statistics division, Department of Statistics and Information Management, RBI.

Loan Registration Number: Any draw-down in respect of ECB as well as payment of any fee / charges for ECB should happen only after obtaining LRN from RBI.

Changes in terms and conditions of ECB: – revised Form ECB should be submitted with DSIM within 7 days of such changes

Monthly filings: Borrower to submit Form ECB-2 on monthly basis with AD Bank so as to reach to DSIM within 7 days from the close of the month. All filings up to date for past ECB / FCCB before new ECB / FCCB, etc. It requires compliance certificate from CS / CA apart from that of AD-Bank.

Reporting on Conversion of ECB into equity :

- Partial Conversion – Converted portion to be reported in Form FC-GPR and appropriately reported in monthly Form ECB2 – "ECB Partially converted into Equity"
- Full Conversion – Entire portion to be reported in Form FC-GPR and appropriately reported in monthly Form ECB2 – "ECB fully converted into Equity"
- For conversion of ECB into equity in phases, reporting through ECB 2 Return will also be in phases.

Late Submission Fees (LSF)

Delay in reporting of drawdown of ECB proceeds before obtaining LRN or delay in submission of Form ECB 2 returns can be regularized by payment of LSF as under:

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 three years from due date of submission / date of drawdown	INR 50,000 per year
3	Form ECB 2 / Form ECB	Beyond three years from due date of submission / date of drawdown	INR 100,000 per year

- With this change, borrowers who are otherwise in compliance can regularize their reporting delays without having to go to the RBI for compounding contraventions
- Non-payment of LSF will be treated as a contravention of reporting provision and shall be subject to compounding or adjudication as provided in FEMA
- Form ECB and Form ECB 2 reporting contraventions will be treated separately.

Powers delegated to AD Banks (not for FCCB / FCEB)

i. Change / Modification in Drawdown / Repayment Schedule ii. Change in Currency of Borrowing iii. Change in AD Bank (subject to no objection certificate from earlier AD Bank) iv. Change in name of borrower Company v. Transfer of ECB (on re-organization at the borrower level – merger/demerger/ acquisition as per law) vi. Change in Recognised Lender	vii. Change in name of Lender viii. Prepayment of ECB (provided MAMP is maintained) ix. Cancellation of LRN (only if no draw-down) x. Reduction in amount of ECB xi. Refinancing of existing ECB (provided the fresh ECB is raised at a lower all-in-cost and residual maturity is not reduced)

While permitting changes, AD Bank should ensure –

- Revised average maturity / all-in-cost are in conformity with applicable guidelines
- RBI DBR Prudential guidelines complied for credit facilities from Indian Banks or their Overseas Branches / Subs
- ECB continues to be in compliance with applicable guidelines and the change are with consent of lender
- Changes to be communicated in Form ECB / ECB-2 within 7 days of the changes being effected.

Start Ups - Special dispensation under ECB

Eligibility	• An entity recognised as a Startup by the Central Government as on date of raising ECB
Amount, Average Maturity & All-in-costs	• Amount - The limit of startup remains constant at USD 3 million or equivalent per financial year either in INR or any other convertible foreign currency or a combination of both • Ratio - Leverage ratio and ECB Liability – Equity Ratio is not applicable. • Maturity - Minimum average maturity period of 3 years • All-in-cost - Mutually agreed between the borrower and lender
Recognised Lender	• Lender / investor to be a resident of FATF compliant country • Not permissible - Overseas branches / subsidiaries of Indian banks and overseas WOS / JV of an Indian company
Form and End-use	• Form - Loans or non-convertible or optionally convertible or partially convertible preference shares. • End Use - For any expenditure in connection with the business of borrower
Currency and conversion	• Denominated in any freely convertible currency or in INR or a combination thereof (Hedging recommended but not mandatory) • Conversion of ECB into equity is freely permitted – rate as per date of agreement
Security and Guarantee	• Security = movable, immovable, intangible assets (including patents, IPRs), financial securities, etc. • Issuance of corporate or personal guarantee is allowed. NR guarantee only if Eligible Lender as above. Banks / FIs / NBFCs cannot issue any guarantee, LoC, etc.

Standard Operating Procedure (SOP) for Untraceable Entities

- New concept
- Action plan to be undertaken by the AD Banks and RBI against untraceable entities in contravention of reporting provisions under the New ECB Framework, for eight quarters or more
- Stricter compliance requirements in relation to ineligibility for untraceable entities

Untraceable Entities: 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/reply in negative for a period of not less than two quarters with documented communication/reminders numbering 6 or more; and it fulfills both the following conditions:

  a) Entity not found to be operative at the registered office during the visits by the officials; and

  b) Entities have not submitted Statutory Auditor's Certificate for last two years or more

Action: The followings actions are to be undertaken in respect of 'untraceable entities':

– 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;

– No fresh ECB application by the entity should be examined/processed by the AD bank;

– Directorate of Enforcement to be informed whenever any entity is designated 'UNTRACEABLE ENTITY'; and

– No inward remittance or debt servicing will be permitted under auto route.

Trade Credits

Trade credits refer to credits extended directly by the overseas supplier, bank and financial institution for a maturity period up to 3 years for imports into India. Trade credit includes Suppliers credit (Overseas Supplier himself) & Buyers credit (By Overseas Banks & Financial Institutions)

Routes

Automatic Route – AD Bank is permitted to approve TC for import of capital and non-capital goods upto USD 50 million or equivalent per import transaction.

Approval Route - TC for import of capital and non-capital goods beyond USD 50 million per import transaction.

Maturity Prescription (with no roll / extension beyond the permitted period)

- **Import of non-capital goods -** Up to 1 year from the date of shipment or operating cycle whichever is less.
- **Import of capital goods** - Up to 3 years from date of shipment.

Reporting- Monthly reporting in Form TC by AD Category 1 Banks (not later than 10th of the following month) / Quarterly reporting – Issuance of Bank Guarantees.

Other points

- All in costs: up to 250 basis points + 6 months LIBOR. Includes rate of interest, other fee, expense, charges, guarantee fee whether in FCY or INR
- AD Banks permitted to issue Guarantee in favor of overseas supplier, bank or financial institution not exceeding the amount of TC and the period cannot exceed the maximum permissible period for TC.

Selected ECB Issues

RBI Guidelines on Funds raised overseas by overseas holding / association / subsidiary / group companies

- Indian companies or their AD banks are not allowed to issue direct or indirect guarantee or create any contingent liability or offer any security for borrowings by overseas holding / association / subsidiary / group companies except for purposes explicitly permitted in the relevant regulations
- Funds raised overseas by above entities with support from Indian companies and AD Banks cannot be used in India (except general or special permission outside India).
- Strict penal action for violation

Items of Compounding

- End-use not complied
- Eligible lender conditions not complied
- Loans from un-recognised borrowers
- MAMP not complied
- ECB compliances not undertaken
- Deemed ECB
  - Overdue imports payables
  - Overdue current account payables
  - On-behalf payments by overseas entities
  - Exports Advance

Minimum Average Maturity Period ('MAMP')

Illustration for calculating Minimum Average Maturity as available in the RBI circular

Calculation of Average Maturity- An Illustration

ABC LTD. Loan Amount = USD 2 million

Date of drawal / repayment (MM/DD/YYYY)	Drawal	Repayment	Balance	No. of Days** balance with the borrower	Product= (Col.4 * Col. 5)/ (Loan amount * 360)
Col. 1	**Col. 2**	**Col. 3**	**Col. 4**	**Col. 5**	**Col. 6**
11/05/2007	0.75		0.75	24	0.0250
05/06/2007	0.50		1.25	85	0.1476
31/08/2007	0.75		2.00	477	1.3250
27/12/2008		0.20	1.80	180	0.4500
27/06/2009		0.25	1.55	180	0.3875
27/12/2009		0.25	1.30	180	0.3250
27/06/2010		0.30	1.00	180	0.2500
27/12/2010		0.25	0.75	180	0.1875
27/06/2011		0.25	0.50	180	0.1250
27/12/2011		0.25	0.25	180	0.0625
27/06/2012		0.25	0.00		

Average Maturity= 3.2851 years

** Calculated by = DAYS360 (firstdate, seconddate, 360)

Infrastructure Space Companies

Definition:

- Companies in the infrastructure sector*;
- NBFC undertaking infrastructure financing;
- Holding Companies / Core Investment Companies undertaking infrastructure financing;
- Housing Financing Companies regulated by National Housing Bank; and
- Port Trusts (constituted under the Major Port Trusts Act, 1963 or Indian Ports Act, 1908)

** Infrastructure Sector: It has the same meaning as given in the Harmonised Master List of Infrastructure sub-sectors, approved by Government of India vide Notification No. 13/06/2009-INF, as amended / updated from time to time. For ECB, "Exploration, Mining and Refinery" sectors will be deemed as in the infrastructure sector.*

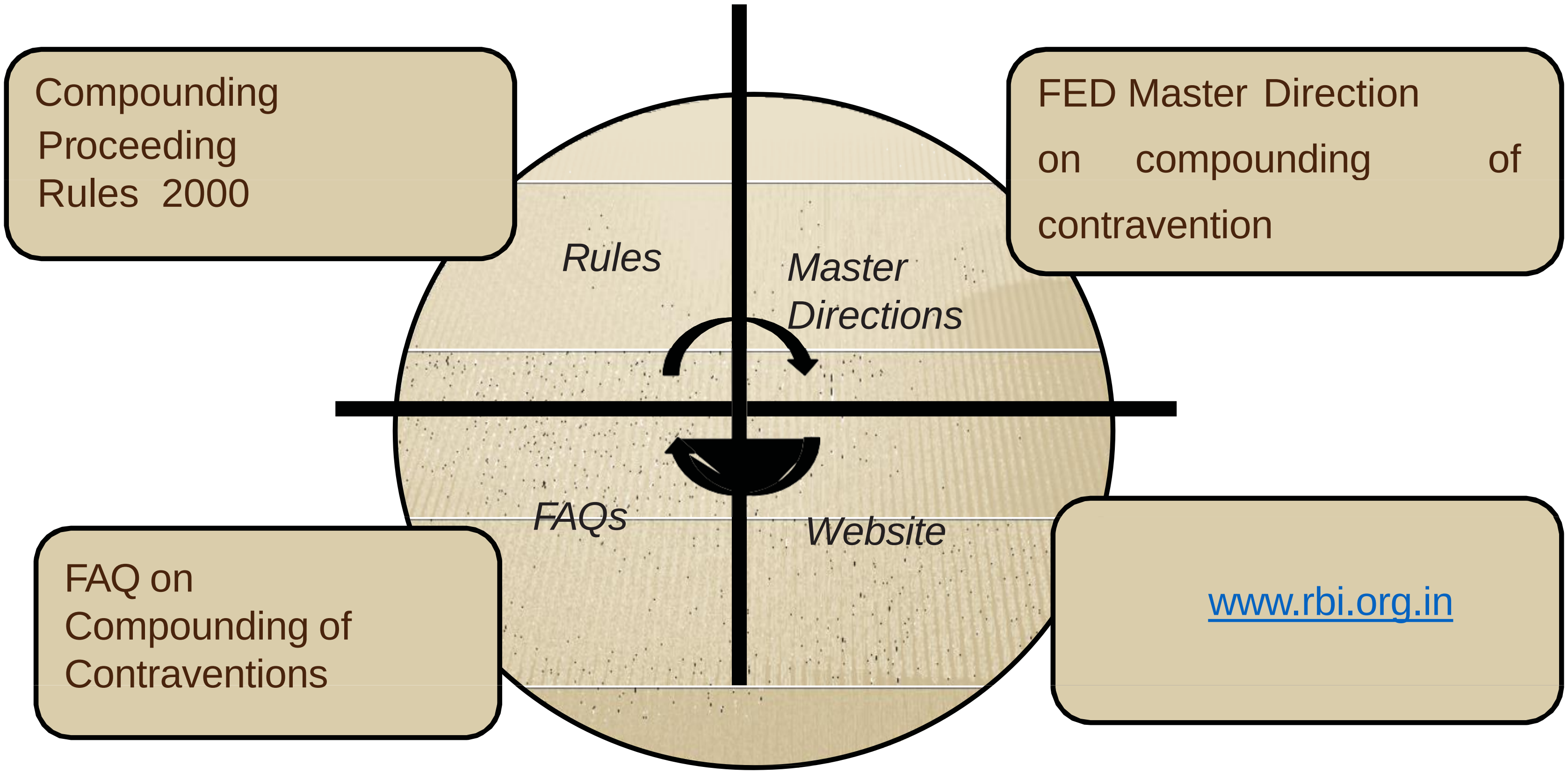
Overview on Compounding of Contraventions under FEMA, 1999

KPNB & Associates
Chartered Accountants

Compounding - Contents

- Framework of Compounding under FEMA
- Meaning of contravention and Compounding
- Detection of Contravention and Benefits of Compounding
- Generally committed contraventions under FEMA
- Who and when can apply for Compounding
- Pre-requisite for Compounding Process
- Compounding process
- Compounding Application and Documents
- Scope and procedure of compounding
- Guidance Note on Computation Matrix
- Issue of Compounding order and Payment of Fees
- Q&A

Framework of Compounding under FEMA



Total compounding orders passed in FY 2019

Amount imposed under Compounding(in INR)	No of cases	%
Less 25,000	217	26
25,000 - 50,000	126	15
50,000 - 75,000	128	15
75,000 - 100,000	66	8
100,000 - 150,000	106	12
150,000 - 250,000	65	8
250,000 - 350,000	31	4
Above 350,000	111	13
Total	**850**	**100**

Meaning of contravention and Compounding

- Section 15 of FEMA 1999 covers powers to compound contraventions and section 13 of FEMA provides for penalty under FEMA
- RBI is empowered to compound contraventions under FEMA except for under section 3(a) of FEMA

Contravention is a breach of the following:

- Provisions of the FEMA, 1999
- Rules made under FEMA
- Regulations
- Notifications
- Orders
- Directions
- Circulars , issued under the Foreign Exchange Management Act (FEMA), 1999.

- ‘Compound’ or 'compounding’ not defined in the Act or in the Rules:

  ✓ Compounding refers to the process of voluntarily admitting the contravention, pleading guilty and seeking redressal

  ✓ It is a voluntary process in which an individual or a corporate seeks compounding of an admitted contravention.

Detection of Contravention and Benefits of Compounding

Detection of contravention

- Voluntary disclosure
- Analysis of data
- Market intelligence
- Information from ADs
- RBI's inspection
- Through complaint
- Other-Media reporting

Benefits of Compounding

- It is a voluntary process
- Comforts - citizens and corporates
- Personal hearing is not mandatory
- Minimizing transaction costs
- Time -bound disposal (180 Days)
- Changing dynamics of our economy
- Simple and hassle - Free procedure
- No proceeding or further proceedings initiated or continued
- Absolutely transparent
- It saves time and energy
  - ✓ One Application - One hearing - One order

Generally committed contraventions under FEMA

FDI Regulations

- Not / delay I reporting - inward remittance
- Not allotting equity instruments or not refunding the amount within 60 days.
- Delay or non submission of form FC-GPR
- Delay or non submission of form FC-TRS
- Issue of instruments other than permitted instruments

ODI Regulations

- Non/ delay in submission of Form OD after investment and UIN not allotted
- Not permitted method of funding
- Not obtaining share certificate within time period
- Delay or non-submission of Annual Performance Report (APR) every year

Setting-up of LO/ BO/ PO

- Non/ delay in seeking approval for setting office in India
- Delay or non submission of AAC
- Carrying activity not permissible under prescribed regulations

ECB Regulations

- Non/ delay in obtaining LRN
- Delay or non submission of ECB 2
- Utilizing ECB proceeds for activities permissible under prescribed regulations
- Other miscellaneous non-compliance under regulations

Who and when can apply for Compounding

- Any person can apply for compounding to the ReserveBank under following situations:
  - *Person who contravenes any provision of the FEMA, 1999 [except section 3(a)] or contravenes any rule, regulation, notification, direction or order issued in exercise of the powers under this Act or*
  - *contravenes any condition subject to which an authorization is issued by the Reserve Bank,*
- Applications seeking compounding of contraventions under section 3(a) of FEMA, 1999 may be submitted to the Directorate of Enforcement.

<u>When should one apply for Compounding</u>

- When a person become conscious of the contravention of the provisions of FEMA, 1999 by the Reserve Bank or any other statutory authority or the auditors or by any other means, she/he may apply for compounding.
- *One can also make an application for Compounding, suo moto, on becoming aware of the contravention.*

All requisite approvals should be <u>obtained</u> and compliances should be completed before seeking compounding of contravention

Pre-requisite for Compounding Process

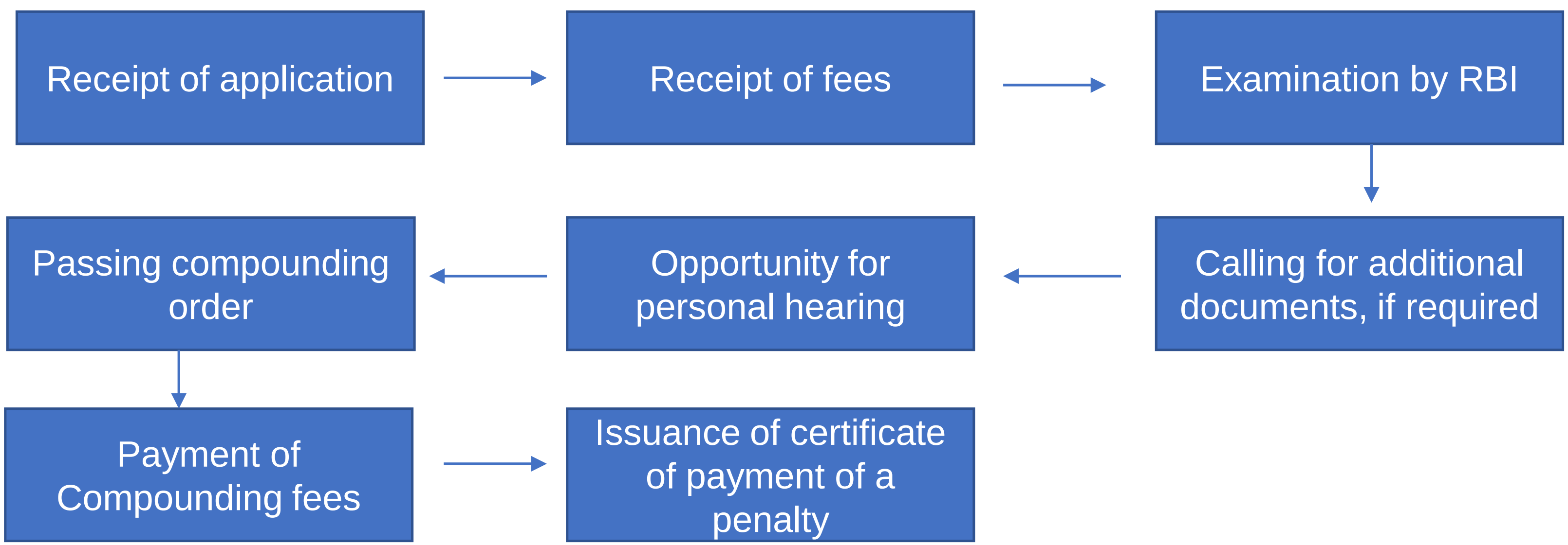
- Contravention committed by any person *within a period of three years from the date on which a similar contravention committed by him was compounded* - such contraventions would not be compounded
  - ➢ Any subsequent contravention committed after the expiry of a period of 3 years from the date of compounding - shall be deemed to be a first contravention.

If a party who has been compounded earlier applies for compounding again for similar contravention - the Compounding fees shall be enhanced by 50%

- Contraventions relating to any transaction where proper approvals or permission from the Government or any statutory authority concerned not been obtained **- such contraventions would not be compounded unless the required approvals are obtained**
- Contraventions having serious contravention suspected of money laundering, terror financing or affecting sovereignty and integrity of the nation or where the contravener fails to pay the sum for which contravention was compounded within the specified period in terms of the compounding order - **shall be referred to the Directorate of Enforcement for further investigation**

Compounding process

- Application, along with fee and documents to be submitted to The Compounding Authority, Central Office or the Regional Office concerned depending on the amount / nature of contravention
- The application fee of Rs 5,000 shall be paid by a DD in favour of the "Reserve Bank of India" and payable at Mumbai or the Regional Office location
- The proceedings would be concluded and order issued by the Compounding Authority within 180 days from the date of receipt of complete application



Compounding Application and Documents…

Application for Compounding

- The application in prescribed format
- Details Required for contravention relating to FDI, ECB, ODI and BO/LO/ PO – In the format prescribed
- Undertaking that the applicant is not under investigation of any agency such as DOE, CBI, etc. in order to complete the compounding process within the time frame – Format prescribed
- ECS Mandate and details of bank account - in case the application has to be returned for any reason, the application fees of Rs.5000/- received along with the application fees is also returned

…Compounding Application and Documents

Format of Application

Part XI: Annex I

Format of Application Form

(See Rule 4 or 5)

(To be filled in duplicate and shall be accompanied by certified copy of the Memorandum issued)

1. Name of the applicant (in BLOCK LETTERS)
2. Full address of the applicant (including Phone and Fax Number and email id)
3. Whether the applicant is resident in India or resident outside India [Please refer to Section 2(v) of the Act]
4. Name of the Adjudicating Authority before whom the case is pending
5. Nature of the contravention [according to sub-section (1) of Section 13]
6. Brief facts of the case
7. Details of fee for application of compounding
8. Any other information relevant to the case

I/We declare that the particulars given above are true and correct to the best of my/our knowledge and belief and that I/We am/are willing to accept any direction/order of the Compounding Authority in connection with compounding of my/our case.

Dated :
Name

(Signature of the Applicant)

PAN and the activity as per NIC codes – 1987 also required to be reported

Scope and procedure of compounding

- On receipt of the application for compounding - RBI shall examine the application based on the documents and submissions made in the application and assess whether contravention is quantifiable and amount of contravention
- The Compounding Authority (CA) may call for any information, record or any other documents relevant to the compounding proceedings - In case additional information/documents not submitted within the specified period, the application for compounding will be rejected
- The following factors are considered for the purpose of passing compounding order and adjudging the sum compounding fees
  - ✓ the amount of gain of unfair advantage, wherever quantifiable, made as a result of the contravention
  - ✓ the amount of loss caused to any authority/ agency/ exchequer as a result of the contravention
  - ✓ economic benefits accruing to the contravener from delayed compliance or compliance avoided
  - ✓ the repetitive nature of the contravention, the track record and/or history of non-compliance of the contravener
  - ✓ **contravener's conduct in undertaking the transaction and in disclosure of full facts in the application and submissions made during the personal hearing;**

Guidance Note on Computation Matrix…

Sr NO	Type of contravention	Existing Formula
A	Reporting Contraventions	
	• Under FDI Regulation • Under ECB Regulations • Under ODI Regulations • Any other reporting contraventions (except in B below)	Fixed amount : Rs10,000/- (applied once for each contravention in a compounding application) + Variable amount as under: Up to Rs 10 lakhs - Rs 1,000 per year Above Rs.10 lakhs & below Rs. 40 lakhs: - Rs 2,500 per year Above Rs.40 lakhs & below Rs. 100 lakhs: - Rs 7,000 per year Rs.1 crore to Rs10 crore - Rs 50,000 per year Above Rs.10 crore to Rs100 crore - Rs 100,000 per year Above 100 crore - Rs 200,000 per year
	• Reporting contraventions by LO/BO/PO	As above, subject to ceiling of Rs. 2 lakhs. In case of Project Office, the amount imposed shall be calculated on 10% of total project cost.

…Guidance Note on Computation Matrix…

Sr NO	Type of contravention	Existing Formula
B	Reporting Contraventions	
	• In case of non-submission/ delayed submission of APR/ share certificates (ODI Regulations) or AAC (LO/ BO/ PO) or FLA Returns	Rs.10,000/- per AAC/APR/FCGPR (B) /FLA Return delayed. Delayed receipt of share certificate – Rs.10,000/- per year, the total amount being subject to ceiling of 300% of the amount invested.
C	Non-allotment of shares or allotment/ refund after the stipulated 180 days in FDI	Rs.30000/- + given percentage: 1st year – 0.30% 1 to 2 year – 0.35% 2 to 3 year – 0.40% 3 to 4 year – 0.45% 4 to 5 year – 0.50% Above 5 year – 0.75% (For project offices the amount of contravention shall be deemed to be 10% of the cost of project).
	LO/BO/PO - (Other than reporting contraventions)	
D	All other contraventions except Corporate Guarantees but including all contraventions of FDI other than FLA	Rs.50,000/- + given percentage: 1st year – 0.50% 1 to 2 year – 0.55% 2 to 3 year – 0.60% 3 to 4 year – 0.65% 4 to 5 year – 0.70% Above 5 year – 0.75%

…Guidance Note on Computation Matrix

Sr NO	Type of contravention	Existing Formula
E	Corporate Guarantees	
	• Issue of Corporate Guarantees without UIN/ without permission wherever required /open ended guarantees or any other contravention related to issue of Corporate Guarantees.	Rs.500,000/- + given percentage: 1st year – 0.50% 1 to 2 year – 0.55% 2 to 3 year – 0.60% 3 to 4 year – 0.65% 4 to 5 year – 0.70% Above 5 year – 0.75%

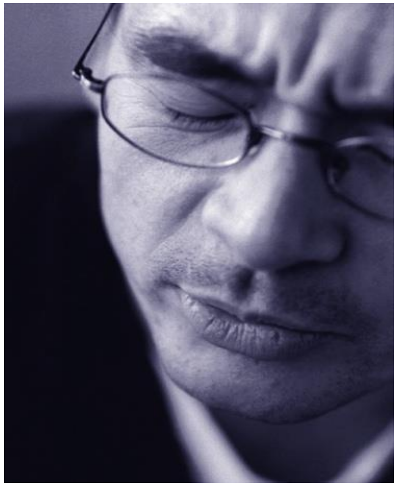
Please note that Compounding for delay in compliance reporting under FDI and ECB is alternative to payment of Late Submission Fee under respective regulations

- The above amounts are presently subject to the following provisos, viz.
  - the amount imposed should not exceed 300% of the amount of contravention;
  - In case the amount of contravention is less than Rs. 1 lakh - the total amount imposed not exceed by simple interest @5% p.a. calculated on the amount of contravention in case of reporting contraventions and @10% p.a. in respect of all other contraventions
  - For contravention with respect to issue of non-allotment of shares or allotment/ refund of share application money
    - ✓ *If the shares are allotted after 180 days without the prior RBI approval, 1.25 times the amount calculated as per table above*
    - ✓ *If the shares are not allotted and the amount is refunded after 180 days with the RBI's permission: 1.50 times the amount calculated, and if w/o RBI approval 1.75 times of amount calculated as per table above*

Issue of Compounding order and Payment of Fees

- The Compounding Authority shall pass an order of compounding after affording an opportunity of being heard to all the concerned as expeditiously as possible
- If the authorized representative of the applicant is unavailable for the personal hearing, the Compounding Authority may pass the order based on available information/ documents
- The Compounding order specify the provisions of the FEMA in respect of which contravention has taken place
- To ensure more transparency and greater disclosure, it has been decided to host the compounding orders passed on or after June 1, 2016
- The Compounding fees shall be paid by way of demand draft in favour of the "Reserve Bank of India" <u>within 15 days from the date of the order of compounding</u> of such contravention
- In case of failure to pay the sum compounded within the time specified – it shall be deemed that the contravener had never made an application for compounding of any contravention
- On realization of the sum - a certificate in this regard shall be issued by RBI

Q&A



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Questions

Answers

Thank you

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KPNB & Associates
Chartered Accountants