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EY Regulatory Alert

External Commercial Borrowings denominated in Indian Rupees- hedging facilities for non-resident entities



Background

The Reserve Bank of India (RBI) had amended the External Commercial Borrowings (ECB) guidelines and permitted all eligible borrowers and Non-Government Organisations engaged in micro finance activities to avail ECB in designated Indian Rupee under the automatic route from foreign equity holder and overseas organisations/ individuals respectively.

Amendment

The RBI, vide A.P. (DIR Series) Circular No.63, dated 29 December 2011, has decided to allow non-residents to hedge the currency risk retained in respect of ECBs denominated in Indian Rupees with Authorised Dealer Category-I banks (AD banks).

Conditions

Products to be used for hedging:

- ▶ Forward foreign exchange contracts with rupee as one of the currencies
- ▶ Foreign currency with Indian Rupee options
- ▶ Foreign currency Indian Rupee swaps

Operational Guidelines:

- ▶ The foreign equity holder/ overseas organisation or individual (lender) should

approach the AD bank in India with a request for forward cover in respect of underlying transaction, along with appropriate documentation, on a pre-deal basis to enable the AD bank in India to satisfy itself that there is an underlying ECB transaction, details of the overseas banker, address, etc.

- ▶ The following undertakings also need to be submitted by the lender to the AD bank:
 - Same underlying exposure has not been hedged with any other AD bank in India
 - Where underlying exposure is cancelled, the customer will cancel the hedge contract immediately
- ▶ The amount and tenure of the hedge should not exceed that of the underlying transaction and should be in agreement with the existing guidelines
- ▶ On due date, settlement is to be done through the correspondent bank's Vostro or the AD bank's Nostro accounts. AD banks in India may release funds to the beneficiaries only after sighting funds in Nostro/ Vostro accounts
- ▶ The contracts, once cancelled, cannot be rebooked
- ▶ The contracts may be rolled over on or before maturity subject to maturity of the underlying exposure

- ▶ On cancellation of the contracts, gains may be passed on to the customer subject to the customer providing a declaration that he is not going to rebook the contract or that the contract has been cancelled on account of cancellation of the underlying exposure

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