Reserve Bank of India issues guidance on foreign exchange rules

On 4 September 2013, the Reserve Bank of India (RBI) issued the A.P. (DIR Series) Circular No. 30, 31 &32 liberalizing the end use restrictions under the External Commercial Borrowing (ECB) Regulations and providing further clarifications on circulars issued on 14 August 2013 amending the investment conditions prescribed under the Overseas Direct Investment (ODI) Regulations and Liberalized Remittance Scheme (LRS).

Background

RBI had formalized the Overseas Investment norms aimed at moderating the Foreign Exchange Outflows and to stop the rupee slide by controlling the outflow of foreign exchange.

After issuance of the Circular amending the ODI guidelines, the stakeholders needed further clarity on the applicability of the regulations. To address these concerns, RBI has now issued clarifications on certain aspects of ODI and LRS. RBI has also issued a circular liberalizing the ECB policy by permitting companies to avail ECB under the approval route from Foreign Equity Holder for the purpose of general corporate purposes which was previously prohibited.

Announcements

**Clarifications on ODI**

In the past, an Indian Party was permitted to invest up to 400% of its net-worth in its joint ventures and/or wholly owned subsidiaries abroad under the automatic route.

RBI vide AP Dir Circular No. 23 dated 14 August 2013 reduced the existing investment limit to 100% of net worth of the Indian Party under the automatic route. Any ODI in excess of 100% of the net worth is now considered under the approval route by the RBI.
In this regard, RBI has issued the following clarifications:

- The Financial Commitment (which includes investment made in the form of equity, loan and guarantees) made on or before 14 August 2013, in compliance with the earlier limit of 400% of the net worth of the Indian party under the automatic route will continue to be allowed and will not require any further approval.

- The limit of 100% of net-worth will not apply to the financial commitments funded out of EEFC (Exchange Earners Foreign Currency) account of the Indian Party or out of the funds raised by issuing ADRs/GDRs by the Indian Party.

- RBI has decided to continue with the limit of 400% of the net worth of the Indian Party for the financial commitments funded by way of ECB raised by the Indian Party.

Clarifications on LRS

Under the existing LRS guidelines, a resident individual is allowed to remit US$75,000 (previously US$200,000) in one financial year (April-March) for any permitted current and capital account transaction or combination of both.

RBI has issued certain clarifications pursuant to queries raised from various stakeholders and authorized dealers:

- LRS can be used to acquire both listed and unlisted shares of an overseas company. The master circular dated 1 July 2013 has been suitably modified to provide for the same.

- RBI has clarified that the following remittances can be made by a resident individual over and above the annual limit of US$75,000 permissible under the modified LRS:
  - Meeting expenses for medical treatment abroad up to the estimate from a doctor in India or hospital/doctor abroad.
  - Up to US$25,000 for maintenance expenses of a patient going abroad for medical treatment or check-up abroad or for accompanying as attendant to a patient going abroad for medical treatment/check-up.
  - Remittances for studies abroad, up to the estimates from the institutions abroad or US$100,000, whichever is higher.
  - Other remittances (other than donation and gifts) as stipulated under Schedules III to FEMA Current Account Transaction Rules, 2000.

- Resident individual is also permitted to carry out other permissible current account transactions (transactions which are not explicitly prohibited under Schedule I, or restricted under Schedules II and III, to FEMA Current Account Transaction Rules, 2000) without any limits subject to the AD bank verifying the good faith of the transaction.

- RBI has clarified that the revised LRS limit of US$75,000 shall be effective from the date of publication of notification in the Official Gazette. Accordingly, the effective date of the notification is 5 August 2013 (the date of publication of notification in the Official Gazette) and not 5 March 2013.

- The existing LRS scheme does not permit acquisition of immovable property directly or indirectly outside India. It is now clarified that Resident individuals are permitted to make remittances for acquiring immovable property within the annual limit of US$75000 for those contracts which were entered on or before the date of the circular, i.e., 14 August 2013 which prohibited acquisition of immovable property, subject to satisfaction of the genuineness of the transactions by the AD bank, which have to be immediately reported post facto to the RBI by the AD banks.
Liberalization in the ECB policy
As per the existing ECB guidelines, an eligible borrower is prohibited to utilize the ECB proceeds for its general corporate purpose.

RBI has liberalized the end use restrictions under the ECB policy by permitting eligible borrowers to avail ECB under the approval route from the foreign equity holder company for general corporate purposes subject to the following conditions:

- Minimum paid up equity of 25% should be held directly by the lender.
- ECB should not be used for purposes not permitted by the ECB guidelines including on-lending to the group companies/step down subsidiaries in India.
- Repayment of the principal shall commence only after completion of minimum average maturity of seven years. No repayment will be allowed before maturity.

Implications
RBI while issuing these circulars has tried to indicate that restrictive ODI guidelines were issued keeping the macro economic situation in mind and they do not intend to restrict any bona-fide and genuine ODI transactions. Allowing ECB for the general corporate purposes will meet the dual objective, on one hand it will provide liquidity to Indian companies with foreign shareholders to meet their day to day expenses through inexpensive loans and at the same time India will receive valuable foreign exchange on a long term basis.
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