Foreign Funding Options for Indian Companies

- This note discusses the various routes typically available to foreign corporations for funding their Indian subsidiaries from overseas, post initial capitalisation.
- While we have sought to highlight the key features associated with each route, this is a general discussion of funding methods that may be of relevance to overseas investors, and should not be construed as specific legal advice.
- The assessment of a suitable option will additionally require tax advice on implications under the tax laws of India and of the jurisdiction of the investing entity.

Equity Capital

Equity shares constitute the common stock of a company, and may be issued as fully or partly paid. Equity capital represents ownership in a company, and entitles the holder to voting rights and a share in the success of the company (via dividends or capital appreciation, or both).

Equity share issuances by an Indian company to a foreign resident must comply with certain restrictions under the foreign direct investment ("FDI") regulations, particularly: (i) sectoral foreign shareholding caps and entry routes; and (ii) pricing norms.

Compulsorily Convertible Debentures ("CCD") or Compulsorily Convertible Preference Shares ("CCPS")

An Indian company may also receive foreign investments through the issue of CCDs and CCPS to non-resident investors. These are instruments that are mandatorily convertible into equity shares within a specified period of time. The price / conversion formula of CCDs and CCPS should be determined upfront at the time of issue of the instruments, and must not be lower than the fair market value of the shares as on the date of conversion.

CCDs and CCPS are considered to be an equity, rather than debt, route of investment, given the definite commitment to convert the instruments into common equity shares. As such, their issue and subscription is subject to the conditions and restrictions applicable under the FDI regulations

External Commercial Borrowings ("ECBs")

Indian companies can raise debt from recognised foreign lenders subject to the ("ECB") regulations. Such ECB can be raised under the automatic route or approval route (i.e. with prior approval of the Reserve Bank of India).

ECBs are commercial loans and include bank loans, buyers' and suppliers' credit, securitised instruments, preference shares / debentures which are not fully and mandatorily convertible, and foreign currency convertible bonds.

Conditions set out under the ECB regulations include specifications of borrowers eligible to raise, and lenders eligible to issue, debt through ECB. The ECB regulations also prescribe end-use restrictions, all - in - costs ceiling, minimum maturity,etc.

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Masala Bonds

'Masala bonds' are rupee denominated bonds issued by Indian companies in the overseas market. Indian corporates permitted to raise ECB are also permitted to issue masala bonds, following the same procedure and conditions specified under the ECB regulations.
To encourage the use of masala bonds, corporates have been provided leeway in respect of a number of requirements under the (Indian) Companies Act, 2013. However, the Reserve Bank of India has recently prohibited "related parties" from funding masala bonds. This could create complications for an Indian subsidiary seeking to raise funds from its foreign parent through this method.

American Depository Receipts (ADRs)/ Global Depository Receipts (GDRs)

ADRs/GDRs are instruments created by a foreign depository outside India which are listed and traded on foreign stock exchanges, and which represent a certain number of equity shares of an Indian company. These underlying equity shares are held in India by a local custodian on behalf of the depository.
The number of underlying equity shares offered for issuance of ADRs/GDRs must be determined upfront at the time of issuance. Companies issuing ADRs/GDRs are also subject to other conditions including disclosure and anti-money laundering requirements, and compliance with investment conditions under the FDI regulations.

Services Contract

An Indian subsidiary may provide services to its offshore parent under a commercial services contract, subject to certain conditions. An invoice will be raised against which monies will be advanced to the subsidiary in India.
This option is typically used as a measure to meet short-term cash flow requirements. If services are not provided, the Indian company will be required to repay the monies within a specified time period.

What BTG Legal can do for you

- Assess overseas and domestic funding options available to your Indian subsidiary, and provide structuring support.
- Provide tailored legal advice based on your requirements including sector of operations, quantum of funding, timeline and costs involved, repatriation, exit considerations etc.
- Connect you with tax advisors for assessing tax implications, or coordinate with them on your behalf.

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