



C N K Knowledge Tracker

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RBI and FEMA

April 2018

C N K & Associates LLP

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Reserve Bank of India (RBI)/Foreign Exchange Management Act, 1999 (FEMA)

Notifications

▪ Master Direction on Foreign investment in India

Notification- RBI/FED/2017-18/60 dated 4th January 2018

The RBI has issued Master Directions on Foreign investment in India. Among other matters, it deals with the following:

- ♦ Issue of employees' stock options scheme (ESOP) and sweat equity shares
- ♦ Issue of Convertible Notes by an Indian startup company
- ♦ Merger or demerger or amalgamation of Indian companies

For details refer: https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=11200

▪ Refinancing of ECB by Indian Corporates through overseas branches/subsidiaries of Indian banks

Notification- RBI/2017-18/116 dated 4th January 2018

In order to provide a level playing field, Government of India, has permitted the overseas branches/subsidiaries of Indian banks to refinance ECBs having AAA ratings as well as Navratna and Maharatna PSUs, provided the outstanding maturity of the original borrowing is not reduced and all-in-cost of fresh ECB is lower than the existing ECB.

For details refer: <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11198&Mode=0>

▪ Discontinuation of Letters of Undertaking (LoUs) and Letters of Comfort (LoCs) for Trade Credits

Notification- RBI/2017-18/139 dated 13th March 2018

On a review of the extant guidelines, the RBI has been decided to discontinue the practice of issuance of LoUs/ LoCs for Trade Credits for imports into India by AD Category –I banks with immediate effect. LoC and Bank Guarantees for Trade Credits for imports into India may continue to be issued subject to compliance with the provisions contained in Master Circular (https://rbi.org.in/Scripts/BS_ViewMasCirculardetails.aspx?id=9879) dated 1st July 2015 on

Guarantees and Co-acceptances, as amended from time to time issued by Department of Banking Regulation.

For details refer: <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11227&Mode=0>

■ Cross Border Merger

Notification - FEMA.389/2018-RB dated 20th March 2018

The RBI vide the notification on Foreign Exchange Management (Cross Border Merger) Regulations, 2018 (‘the regulation’), has come out with FEMA regulations on cross border mergers.

The Section 234 of the Companies Act 2013 was notified on 13th April 2017. The said Section along with amended Rule 25A of Companies (Compromises, Arrangements and Amalgamation) Amendment Rules, 2017 (**the Rule**) deals with Cross border mergers of Indian and foreign companies. It provides that prior approval of RBI is required before the cross border merger is approved by NCLT. Accordingly, the RBI came out with the regulation on cross border mergers and merger. The said RBI regulation states that, if the conditions stated in the said regulations are satisfied, the approval will be deemed to have been granted by RBI, and that no separate approval would be required.

The Key features of the said regulation are as under:

Key Definitions:

- ♦ “**Cross border merger**” means any merger, amalgamation or arrangement between an Indian company (**IC**) and foreign company (**FC**), in accordance with Rule notified under the Companies Act, 2013.
- ♦ “**Foreign company**” means any company or body corporate incorporated outside India whether having a place of business in India or not.
- ♦ “**Indian company**” means a company incorporated under the Companies Act, 2013 or under any previous company law
- ♦ “**Resultant Company**” means an IC or a FC, which takes over the assets and liabilities of the companies involved in the cross border merger.

Particulars	Inbound Merger	Outbound Merger
Definition	A cross border merger where the resultant company is an IC; i.e. merger or amalgamation of FC with an IC	A cross border merger where the resultant company is a FC; i.e. merger or amalgamation of IC with a FC
For issue of security by the	The resultant company may issue or transfer any securities to	A ‘person resident in India’ may acquire or hold securities of the

Particulars	Inbound Merger	Outbound Merger
Resultant Company under cross-border merger	<p>person resident outside India in accordance with the pricing guidelines, entry routes, sectoral caps, attendant conditions and reporting requirements as laid down in FEMA regulations.</p> <p>Further, the conditions as laid down in FEMA regulation on ODI needs to be complied by IC:</p> <ul style="list-style-type: none"> ♦ Where transferor FC is joint venture (JV)/ wholly owned subsidiary (WOS) of IC; or ♦ Where the merger of the JV/ WOS results into acquisition of step down subsidiary (SDS) of JV/ WOS of the Indian party 	<p>resultant company (FC) in accordance with the FEMA regulation on Overseas Direct Investment (ODI).</p> <p>In case a 'Resident Individual' is acquiring securities outside India, the fair market value of such securities should be within the limits prescribed under the Liberalized Remittance Scheme ("LRS").</p>
Office of transferor company	<p>Any office of the transferor FC outside India will be deemed to be the branch/ office outside India of the resultant IC.</p> <p>Relevant FEMA regulations w.r.t Branch office outside India needs to be complied.</p>	<p>Any office of the transferor IC in India will be deemed to be the branch/ office in India of the resultant FC</p> <p>Relevant FEMA regulations w.r.t branch office in India has to be complied.</p>
Treatment of guarantee and borrowings of a transferor company.	<p>Any borrowing or guarantees of the FC from overseas source, which becomes the borrowing of the Resultant Company (IC). The resultant IC shall comply following:</p> <ul style="list-style-type: none"> ♦ Comply with External Commercial Borrowing (ECB) norms, Trade Credit norms, or other foreign borrowing norms, as laid down in the relevant FEMA regulations, within the period of 2 years. 	<p>The guarantees or outstanding borrowings of the IC which become the liabilities of the resultant company (FC). The resultant FC shall comply with the following:</p> <ul style="list-style-type: none"> ♦ It shall be liable to repay outstanding borrowings or guarantees of transferor IC as per the Scheme sanctioned by NCLT. ♦ It shall not acquire any liability payable towards lender in India in Rupees, which is not in

Particulars	Inbound Merger	Outbound Merger
	<ul style="list-style-type: none"> ♦ During the said period of 2 years, the IC will not be able to make remittance for repayment of the foreign liability. ♦ For such borrowings, the end use restrictions for such shall not apply. 	<p>conformity with the Act, rules, or regulations framed thereunder.</p> <ul style="list-style-type: none"> ♦ Obtain a no-objection certificate (NOC) from the lenders in India of the IC.
Acquisition / Holding or transfer of the assets of Transferor Company.	An IC may hold/ acquire or transfer any assets/securities outside India pursuant to the provisions of the Act, rules or regulations framed thereunder.	A FC may hold/ acquire / transfer any assets/securities outside India pursuant to the provisions of the Act, rules or regulations framed thereunder.
Transfer of assets / securities not permitted to be acquired / held	<p>Where the asset or security held outside India is not permitted to be acquired or held by the resultant company IC under the Act, rules or regulations, then the resultant company IC shall;</p> <ul style="list-style-type: none"> ♦ Sell such asset or security within a period of 2 years from the date of sanction of the Scheme by NCLT and immediately repatriated the sale proceeds to India. or ♦ Utilise it for payment of an overseas liability not permitted to be held under FEMA guidelines within the 2 year period. 	<p>Where the asset or security in India cannot be acquired or held by the resultant company (FC) under the Act, rules or regulations, then the resultant FC shall:</p> <ul style="list-style-type: none"> ♦ Sell such asset or security within a period of two years from the date of sanction of the Scheme by NCLT, and immediately repatriated the sale proceeds outside India or ♦ Utilise it for repayment of Indian liabilities within the period of 2 years.
Bank accounts	The resultant IC may open a bank account overseas, in foreign currency for a maximum period of 2 years from the date of sanction of Scheme	The resultant FC may open Special Non-resident Rupee (“SNRR”) account in India in accordance with FEMA Regulations, 2016 for a maximum period of 2 years from the date of sanction of Scheme

Other Common Conditions for Inbound and outbound cross border merger:

- ♦ **Valuation** The valuation of the IC and the FC has to be in accordance with the Rule.
- ♦ **Compensation** to the shareholders by the resultant IC or FC has to be paid in accordance with the Scheme sanctioned by the NCLT;
- ♦ **Regularisation of non-compliances** Companies to ensure completing requisite regulatory actions prior to merger with respect to any non-compliance, contravention, violation under FEMA.
- ♦ A certificate from the Managing Director/Whole Time Director and Company Secretary(if available), of the concerned Companies, ensuring compliance to these Regulations shall be furnished along with the application made to the NCLT under the Rule.

For details refer: <https://rbi.org.in/Scripts/NotificationUser.aspx?Id=11235&Mode=0>

■ Prudential Norms for Classification, Valuation and Operation of Investment Portfolio by Banks – Spreading of MTM losses and creation of Investment Fluctuation Reserve (IFR)

Notification- RBI/2017-18/147 dated 2nd April 2018

In order to address the systemic impact of sharp increase in the yields on Government Securities RBI has decided to grant banks the option to spread provisioning for Mark To Market (MTM) losses on investments held in Available for Sale (AFS) and Held for Trading (HFT) for the quarters ended 31st December 2017 and 31st March 2018. The provisioning for each of these quarters may be spread equally over up to 4 quarters, commencing with the quarter in which the loss is incurred.

Banks that utilise the above option will have to make suitable disclosures in their Notes to Accounts/ quarterly results providing details of-

- ♦ the provisions for depreciation of the investment portfolio for the quarters ended December 2017 and March 2018 made during the quarter/year and
- ♦ the balance required to be made in the remaining quarters.

For details refer: <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11236&Mode=0>

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Circulars

■ Resolution of Stressed Assets – Revised Framework

Circular- RBI/2017-18/131 dated 12th February 2018

The RBI has issued a circular to substitute the existing guidelines with a harmonized and simplified generic framework for resolution of stressed assets. Among other matters, the circular requirements include early identification and reporting of stressed assets, implementation of resolution plan and appropriate **disclosures in the Financial Statements**

For details refer: https://www.rbi.org.in/scripts/BS_CircularIndexDisplay.aspx?Id=11218

■ Hedging of Commodity Price Risk and Freight Risk in Overseas Markets (Reserve Bank) Directions, 2018

Circular- RBI/2017-18/138 dated 12th March 2018

The RBI has issued Hedging of Commodity Price Risk and Freight Risk in Overseas Markets (Reserve Bank) Directions, 2018. Among other matters, the direction requires banks to obtain an annual certificate from the **statutory auditors** of entities confirming that the hedge transactions and the margin remittances are in line with the exposure of the entities. The directions also require **statutory auditors** to comment on the risk management policy of entities for hedging exposure to commodity price risk and freight risk and the appropriateness of the methodology to arrive at the quantum of these exposures.

The relevant instructions on the subject in the following circulars **stand withdrawn as on 1st April 2018:**

- ◆ A. P. (DIR Series) Circular No. 68 dated 17th January 2012 on *Risk Management and Inter-Bank Dealings - Commodity Hedging*.
- ◆ Sections E and F of A. P. (DIR Series) circular no. 32 dated 28th December 2010 on *Comprehensive Guidelines on Foreign Exchange Derivatives and Overseas Hedging of Commodity Price and Freight Risks* and the relevant appendices.
- ◆ A. P. (DIR Series) Circular No.35 dated 10th November 2008 on *Remittance related to Commodity Derivative Contract Issuance of Standby Letter of Credit / Bank Guarantee*

The directions will come into force on 1st April 2018.

For details refer: https://www.rbi.org.in/scripts/BS_CircularIndexDisplay.aspx?Id=11226#EN

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Press Releases

▪ Deferment of Ind AS implementation for Scheduled Commercial Banks

Press Release dated 5th April 2018

RBI vide its circular no RBI/2015-16/315 dated 11th February 2016 (<https://rbi.org.in/Scripts/NotificationUser.aspx?Id=10274&Mode=0>) had mentioned that Scheduled Commercial Banks (SCBs), excluding Regional Rural Banks (RRBs), were required to implement Indian Accounting Standards (**Ind AS**) from 1st April 2018.

However, necessary legislative amendments – to make the format of financial statements, prescribed in the 3rd Schedule to Banking Regulation Act 1949, compatible with accounts under Ind AS – are under consideration of the Government. In view of this, as also the level of preparedness of many banks, it has been decided to **defer implementation of Ind AS by 1 year i.e. 1st April 2019**.

For details refer: https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=43574

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