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Case Study on FEMA - RBI slapped Rs 125 Crore on Reliance Infrastructure



FCS Deepak Pratap Singh, Last updated: 28 February 2023

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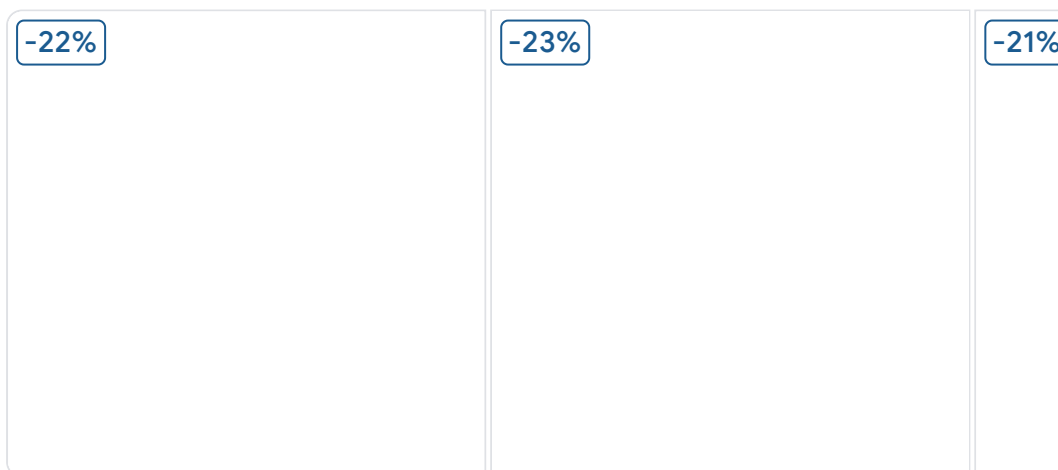
1. The Reserve Bank of India (RBI) has asked the Anil Dhirubhai Ambani Group firm, Reliance Infrastructure (earlier, Reliance Energy), to pay just under Rs 125 crore as compounding fees for parking its foreign loan proceeds worth \$300 million with its mutual fund in India for 315 days, and then repatriating the money abroad to a joint venture company. These actions,

according to an RBI order, violated various provisions of the Foreign Exchange Management Act (FEMA).

2. In its order, RBI said Reliance Energy raised a \$360-million ECB on July 25, 2006, for investment in infrastructure projects in India. The ECB proceeds were drawn down on November 15, 2006, and temporarily parked overseas in liquid assets.



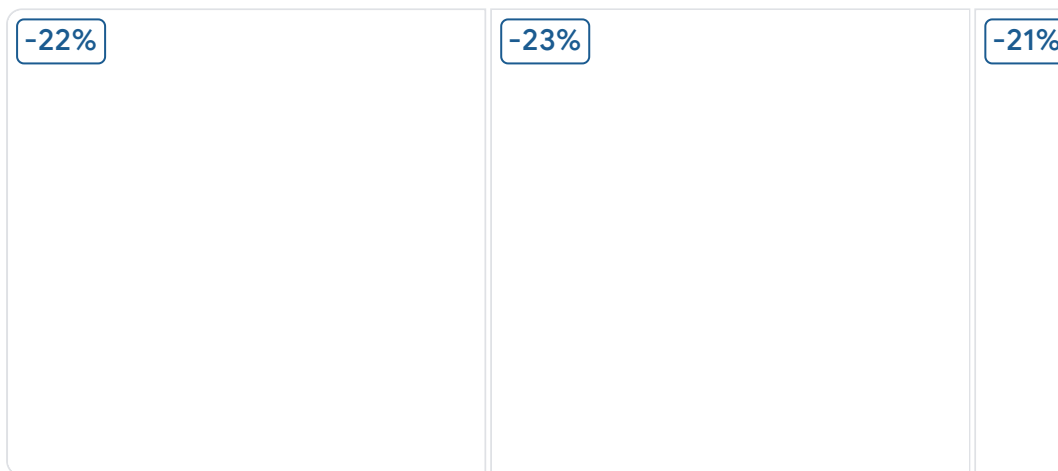
3. On April 26, 2007, Reliance Energy repatriated the ECB proceeds worth \$300 million to India while the balance remained abroad in liquid assets.



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4. It then invested these funds in Reliance Mutual Fund Growth Option and Reliance Floating Rate Fund Growth Option on April 26, 2007.

5. On the following day, i.e., on April 27 2007, the entire money was withdrawn and invested in Reliance Fixed Horizon Fund III Annual Plan series V.
6. On March 5, 2008, Reliance Energy repatriated \$500 million (which included the ECB proceeds repatriated on April 26, 2007, and invested in capital market instruments) for investment in capital of an overseas joint venture called Gourock Ventures based in British Virgin Islands.
7. RBI said, under FEMA guidelines issued in 2000, a borrower is required to keep ECB funds parked abroad till the actual requirement in India. Further, the central bank said a borrower cannot utilise the funds for any other purpose.



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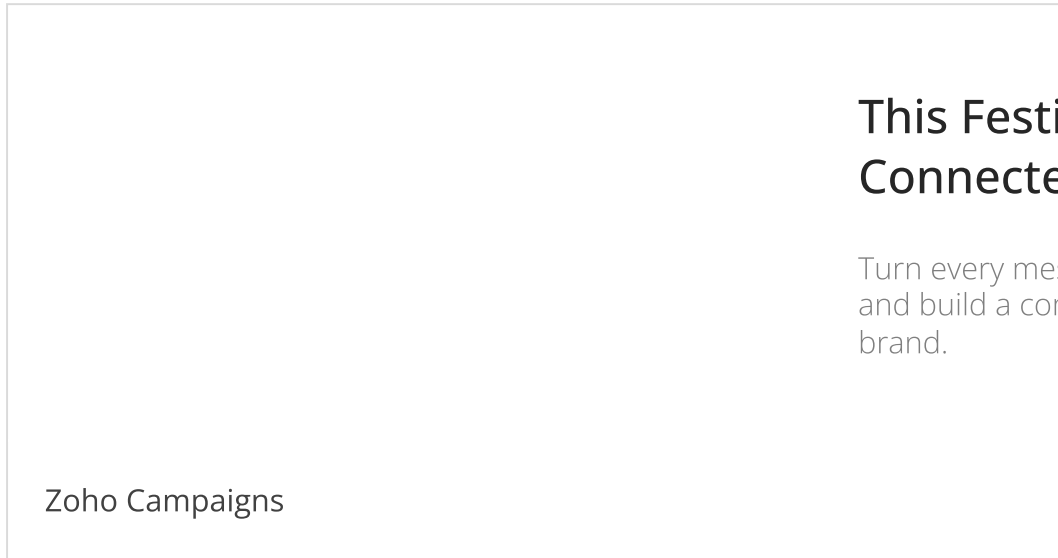
RBI MASTER DIRECTION - EXTERNAL COMMERCIAL BORROWINGS, TRADE CREDITS AND STRUCTURED OBLIGATIONS

4. PARKING OF ECB PROCEEDS

ECB proceeds are permitted to be parked abroad as well as domestically in the manner given below:

4.1. PARKING OF ECB PROCEEDS ABROAD

ECB proceeds meant only for foreign currency expenditure can be parked abroad pending utilisation. Till utilisation, these funds can be invested in the following liquid assets;

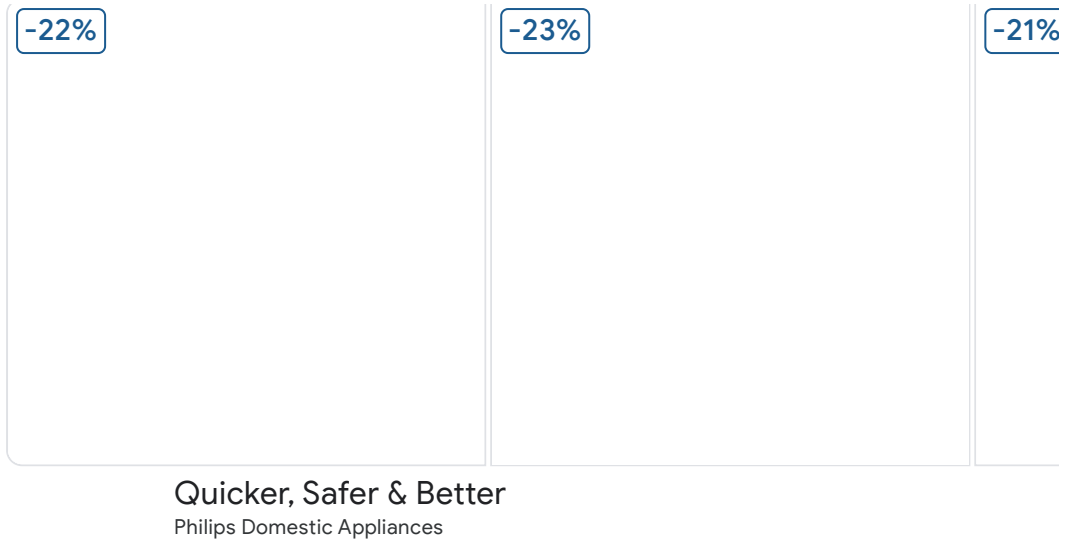


- (a) deposits or Certificate of Deposit or other products offered by banks rated not less than AA (-) by Standard and Poor/Fitch IBCA or Aa3 by Moody's;
- (b) Treasury bills and other monetary instruments of one-year maturity having minimum rating as indicated above and
- (c) deposits with foreign branches/subsidiaries of Indian banks abroad.

4.2. PARKING OF ECB PROCEEDS DOMESTICALLY

ECB proceeds meant for Rupee expenditure should be repatriated immediately for credit to their Rupee accounts with AD Category I banks in India.

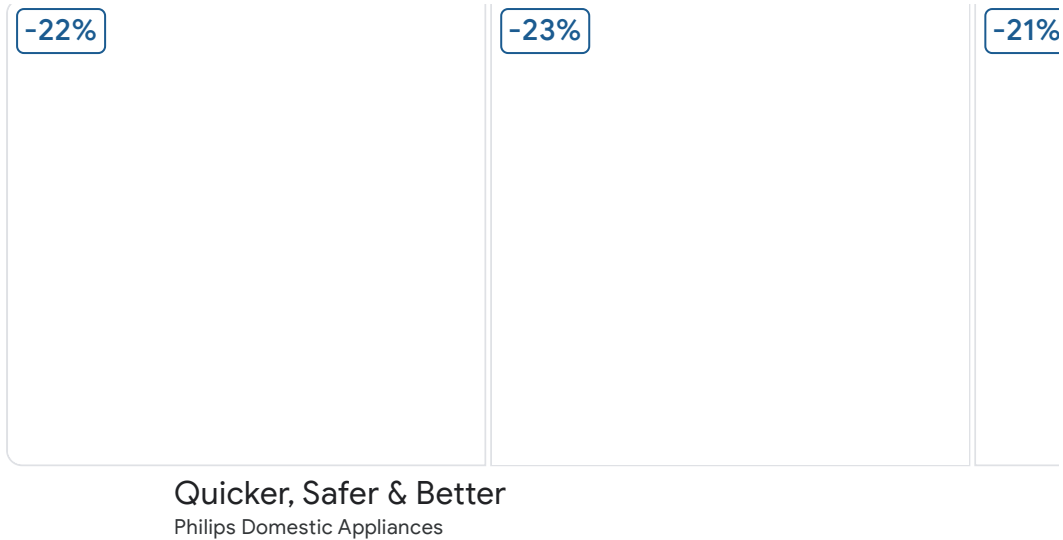
ECB borrowers are also allowed to park ECB proceeds in term deposits with AD Category I banks in India for a maximum period of 12 months cumulatively. These term deposits should be kept in unencumbered position.



8. THE RELIANCE ENERGY ACCEPTED CONTRAVENTION OF PROVISIONS OF FEMA AND ECB NORMS and requested for compounding of offence.

9. During the personal hearing on June 16, 2008, Reliance Energy, represented by group managing director Gautam Doshi and Price waterhouse Coopers executive director Sanjay Kapadia, admitted the contravention and sought compounding. The company said due to unforeseen circumstances, its Dadri power project was delayed. Therefore, the ECB proceeds of \$300 million were brought to India and was parked in liquid debt mutual fund schemes, it added.

10. Rejecting Reliance Energy's contention, RBI said it took the company 315 days to realise that the ECB proceeds are not required for its intended purpose and to repatriate the same for alternate use of investment in an overseas joint venture on March 5, 2008.



11. Reliance also contended that they invested the ECB proceeds in debt mutual fund schemes to ensure immediate availability of funds for utilisation in India.

12. The RBI do not find any merit in this contention also as the applicant has not approached RBI either for utilising the proceeds not provided for in the ECB guidelines, or its repatriation abroad for investment in the capital of the JV.

RBI MASTER DIRECTION - EXTERNAL COMMERCIAL BORROWINGS, TRADE CREDITS AND STRUCTURED OBLIGATIONS

6. Reporting Requirements: Borrowings under ECB Framework are subject to following reporting requirements apart from any other specific reporting required under the framework:

6.1. Loan Registration Number (LRN): Any draw-down in respect of an ECB should happen only after obtaining the LRN from the Reserve Bank. To obtain the LRN, borrowers are required to submit duly certified Form ECB, which also contains terms and conditions of the ECB, in duplicate to the designated AD Category I bank. In turn, the AD Category I bank will forward one

copy to the Director, Reserve Bank of India, Department of Statistics and Information Management, External Commercial Borrowings Division, Bandra-Kurla Complex, Mumbai – 400 051 (Contact numbers 022-26572513 and 022-26573612). Copies of loan agreement for raising ECB are not required to be submitted to the Reserve Bank.

6.2. Changes in terms and conditions of ECB: Changes in ECB parameters in consonance with the ECB norms, including reduced repayment by mutual agreement between the lender and borrower, should be reported to the DSIM through revised Form ECB at the earliest, in any case not later than 7 days from the changes effected. While submitting revised Form ECB the changes should be specifically mentioned in the communication.

6.3. Monthly Reporting of actual transactions: The borrowers are required to report actual ECB transactions through Form ECB 2 Return through the AD Category I bank on monthly basis so as to reach DSIM within seven working days from the close of month to which it relates. Changes, if any, in ECB parameters should also be incorporated in Form ECB 2 Return.

6.4. Late Submission Fee (LSF) for delay in reporting:

6.4.1. Any borrower, who is otherwise in compliance of ECB guidelines, can regularise the delay in reporting of drawdown of ECB proceeds before obtaining LRN or delay in submission of Form ECB/Form ECB 2 returns, by payment of late submission fees in accordance with Part XIII of Master Direction - Reporting under Foreign Exchange Management Act, 1999.¹¹

13. In its defence, the company said the exchange rate gain on account of remittance on March 5 2008, would be a notional interim rate gain as such exchange rate gain is not crystallised.

14. The Reliance has also stated that in terms of accounting standard 11 (AS 11), all foreign exchange loans have to be restated and the difference between current exchange rate and the rate at which the same were remitted to India, has to be shown as foreign exchange loss/gain in profit and loss accounts.



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15. However, in a scenario where the proceeds of the ECB are parked overseas, the exchange rate gains or losses are neutralized as the gains or losses restating of the liability side are offset with corresponding exchange losses or gains in the asset. In this case, the exchange gain had indeed been realised and that too the additional exchange gain had accrued to the company through an unlawful act under FEMA," the order said.

16. It said as the company has made additional income of Rs 124 crore, it is liable to pay a fine of Rs 124.68 crore.

17. On August 2008 , the company submitted another fresh application for compounding and requested for withdrawal of the present application dated April 17, 2008, to include

contravention committed in respect of an another transaction of ECB worth \$150 million.

18. But RBI said the company will have to make separate application for every transaction and two transactions are different and independent and cannot be clubbed together.

Published by

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