Foreign Exchange Developments

June 2008

(i) External Commercial Borrowings (ECB) by Services Sector - Liberalisation

Entities in the service sector, *viz.*, hotels, hospitals and software companies have been permitted to avail ECB up to USD 100 million, per financial year, for the purpose of import of capital goods under the Approval Route. All other aspects of ECB policy shall remain unchanged. The facility to companies, including those in the services sector, to avail trade credit up to USD 20 million per import transaction, for a period less than 3 years, for import of capital goods, shall continue.

[A.P. (DIR Series) Circular No. 46 dated June 02, 2008]

(ii) Risk Management and Inter-Bank Dealings - Commodity Hedging Exposures of Domestic Oil Refining and Marketing Companies

Residents in India are permitted to enter into a contract in a commodity exchange or market outside India to hedge price risk in a commodity, subject to terms and conditions. Further, select commercial bank ADs have been delegated the authority to grant permission to companies listed on a recognised stock exchange to hedge commodity price risk in the international commodity exchanges / markets. Also, domestic oil refining and marketing companies have been

permitted to hedge commodity price risk based on the inventory volumes, subject to conditions.

With a view to facilitating domestic crude oil refining companies to hedge their commodity price risk exposure dynamically, it has been decided to extend the following facilities:

A. Hedging of Domestic Purchases of Crude Oil and Sales of Petro-Products

As per the prevailing trade practices, indigenously produced crude oil is purchased at international prices by the refineries. However, hedging of price risk on domestic purchases of crude oil was not permitted. In order to enable domestic crude oil refining companies to hedge their risk exposures, they have been permitted to hedge their commodity price risk on domestic purchase of crude oil and sale of petroleum products on the basis of underlying contracts linked to international prices on overseas exchanges / markets. The hedging is allowed strictly on the basis of underlying contracts.

B. Hedging of Anticipated Imports of Crude Oil

In order to provide greater flexibility, domestic crude oil refining companies have been permitted to hedge their commodity price risk on crude oil imports in overseas exchanges / markets, on the basis of their past performance up to 50 per cent of the volume of actual imports during the previous year or 50 per cent of the average volume of imports during the previous three financial years, whichever is higher. Contracts booked under this facility will have to be regularised by production of supporting import orders during the currency of hedge. An undertaking may be obtained from the companies to this effect.

The hedging has to be undertaken only through AD Category - I banks, who have been specifically authorised by Reserve Bank in this regard, subject to certain conditions and guidelines.

AD Category - I banks should ensure that the domestic crude oil refining companies hedging their exposures comply with the following:

i. to have Board approved policies which define the overall framework within which derivatives activities are undertaken and the risks contained;

ii. sanction of the company's Board has been obtained for the specific activity and also for dealing in OTC markets;

iii. the Board approval must include explicitly the mark-to-market policy, the counterparties permitted for OTC derivatives, etc.; and

iv. domestic crude oil companies should have put up the list of OTC transactions to the Board on a half yearly basis, which must be evidenced

by the AD Category - I bank before permitting continuation of hedging facilities under this scheme.

AD Category - I banks should also ensure "user appropriateness" and "suitability" of the hedging products used by the customer as laid down by the Reserve Bank.

[A.P. (DIR Series) Circular No. 47 dated June 03, 2008]

(iii) Overseas Investments - Liberalisation / Rationalisation

The Regulations governing overseas investments have been further liberalised as under :

Overseas Investment in Energy and Natural Resources Sectors

At present, an Indian Party is allowed to make direct investment in Joint Ventures and / or Wholly Owned Subsidiaries outside India up to 400 per cent of the net worth as on the date of the last audited balance sheet, under the Automatic Route. With a view to provide greater flexibility to Indian parties for investment abroad, it has been decided, in consultation with the Government of India, to allow Indian companies to invest in excess of 400 per cent of their net worth, as on the date of the last audited balance sheet, in the energy and natural resources sectors such as oil, gas, coal and mineral ores, with the prior approval of the Reserve Bank.

Investment in Overseas Unincorporated Entities in Oil Sector

(i) In terms of the existing FEMA provisions, Navaratna Public Sector Undertakings (PSUs) are allowed to invest in overseas unincorporated entities in oil sector (*i.e.* for exploration and drilling for oil and natural gas, *etc.*), which are duly approved by the Government of India, without any limits, under the automatic route. This facility is now extended to ONGC Videsh Ltd (OVL) and Oil India Ltd (OIL).

(ii) With a view to further liberalise the procedure, it has now been decided, in consultation with the Government of India, to allow a similar facility to other Indian entities to invest in overseas unincorporated entities in oil sector up to 400 per cent of the net worth of the Indian company as on the date of the last audited balance sheet after ensuring that the proposal has been approved by the competent authority and is duly supported by a certified copy of the Board Resolution approving such investment.

Capitalisation of Exports

An Indian Party making direct investment outside India by way of capitalisation, in full or part of the amount due to the Indian Party from the foreign entity on account of payment for export of plant, machinery, equipment and other goods / software

to the foreign entity, has to obtain the prior approval of the Reserve Bank where such export proceeds have remained unrealised beyond a period of six months from the date of exports. In order to align this provision with the Foreign Trade Policy, Indian parties may, henceforth, approach the Reserve Bank for capitalisation of export proceeds only in cases where the exports remain outstanding beyond the prescribed period of realisation.

[A.P. (DIR Series) Circular No. 48 dated June 03, 2008]

(iv) Export of Goods and Services - Payments of Claims by Insurance Companies - Write off

AD banks were permitted to write off the export bills and delete them from the XOS statement in respect of outstanding export bills where claims were settled by ECGC.

In order to liberalise the procedures further, AD Category - I banks have been permitted to write off, in addition to the claims settled by ECGC, the outstanding export bills settled by other insurance companies which are regulated by IRDA. The application should be supported by a documentary evidence from ECGC / insurance companies registered with IRDA, confirming that the claim in respect of the outstanding export bills has been settled and that the export incentives, if any, have been surrendered, write-off the relative export bills and delete them from the XOS statement. Such write-off will not be restricted to the limit of 10 per cent. Further, claims settled in Rupees by ECGC / insurance companies should not be construed as export realisation in foreign exchange and claim amount should not be allowed to be credited to Exchange Earners' Foreign Currency Account.

[A.P. (DIR Series) Circular No. 49 dated June 03, 2008]

(v) Export of Goods and Services - Realisation and Repatriation of Export Proceeds - Liberalisation

In terms of the existing FEMA provisions, the amount representing the full export value of goods or software exported should be realised and repatriated to India within six months from the date of export. The present period of realisation and repatriation to India of the amount representing the full export value of goods or software exported has been enhanced from six months to twelve months from the date of export, subject to review after one year. The provisions in regard to period of realisation and repatriation to India of the full export value of goods or software exported by a unit situated in Special Economic Zone (SEZ) as well as exports made to warehouses established outside India with the permission of Reserve Bank remain unchanged.

[A.P. (DIR Series) Circular No. 50 dated June 03, 2008]

(vi) Deferred Payment Protocols dated April 30, 1981 and December 23, 1985 between Government of India and erstwhile USSR

The rupee value of the special currency basket has been fixed at Rs.60.5828 with effect from May 13, 2008.

[A.P. (DIR Series) Circular No. 51 dated June 03, 2008]

(vii) Deferred Payment Protocols dated April 30, 1981 and December 23, 1985 between Government of India and erstwhile USSR

The rupee value of the special currency basket has been fixed at Rs.62.5198 with effect from May 23, 2008.

[A.P. (DIR Series) Circular No. 52 dated June 11, 2008]

(viii) Overseas Direct Investment by Registered Trust / Society

With a view to further liberalising the policy on overseas investments, it has been decided, in consultation with the Government of India, to allow Registered Trusts and Societies engaged in manufacturing / educational sector to make investment in the same sector(s) in a Joint Venture or Wholly Owned Subsidiary outside India, with the prior approval of the Reserve Bank subject to compliance with the prescribed eligibility criteria.

[A.P. (DIR Series) Circular No. 53 dated June 27, 2008]