COUNTRY COMPARATIVE GUIDES 2023

The Legal 500 Country Comparative Guides

India

PROJECT FINANCE

Contributor

Cyril Amarchand Mangaldas & Herbert Smith Freehills

Santosh Janakiram

Partner | santosh.janakiram@cyrilshroff.com

Manasvini Raj

Partner | manasvini.raj@cyrilshroff.com

Dhananjaya (DJ) Chak

Partner | dhananjaya.chak@hsf.com

Martin Kavanagh

Partner | martin.kavanagh@hsf.com

This country-specific Q&A provides an overview of project finance laws and regulations applicable in India.

For a full list of jurisdictional Q&As visit **legal500.com/guides**

INDIA
PROJECT FINANCE

1. What are the typical ownership structures for project companies in your jurisdiction? Does this vary based on the industry sector?

In India, project companies are incorporated and constituted as special purpose vehicles (SPVs) for undertaking the implementation of a project, which structure is consistent across all industry sectors. The shares in the SPV are held by sponsors, which may be either Indian or offshore investors (subject to foreign exchange regulations).

The ownership structure for project companies does not vary based on the industry sectors of the project, other than in certain limited circumstances such as captive electricity generating plants where the captive user must have minimum ownership of at least 26% of the captive generating plant.

2. Are there are any corporate governance laws or accounting practices that foreign investors in a project company should be aware of?

The Companies Act, 2013 (Companies Act) sets out the various structures for corporate governance for a project company incorporated in India. Any foreign ownership in such company will be further subject to the foreign exchange control laws including the Foreign Exchange Management Act, 1999 (FEMA) and the rules/regulations thereunder (such as the Consolidated Foreign Direct Investment Policy, 2020 read with the FEMA (Non-Debt Instruments) Regulations, 2019)).

While there are no specific taxes on foreign ownership, gains arising or accruing to a foreign investor upon the sale of foreign investments are regarded as either (i) long-term capital gains if unlisted shares in a project company are held for a period in excess of 24 months, or (ii) short-term capital gains if held for a period shorter than 24 months, subject in each case to the benefits of any lower tax rates available under double taxation avoidance agreements (DTAAs). The purchaser must withhold taxes payable by the foreign seller and deposit it to the credit of Indian Government.

When investments are made into Indian entities by a foreign entity through loans/debentures, interest payable to the foreign entity is subject to withholding taxes in India, which amounts are to be deposited to the credit of Indian Government.

3. If applicable, what forms of credit support from sponsors or host governments are typically provided?

Sponsor funding is provided through ordinary equity or structured investments. As part of lending terms, sponsors also provide contractual support such as completion support, cost overrun support and/or guarantees to lenders to mitigate construction risk or credit concerns.

Credit support from the Indian Government varies by sector. For instance, the Government of India (GOI), notified the Scheme for Financial Support to Public Private Partnerships (PPPs) in Infrastructure in 2020, to provide financial support in the form of grants, one time or deferred, to infrastructure projects undertaken through PPPs with a view to making them commercially viable. In 2022, the Department of Economic Affairs, GOI, notified a Scheme for Financial Support for Project Development Expenses of PPP Projects – India Infrastructure Project Development Fund Scheme to fund costs of transaction advisors/consultants engaged in the development of PPP projects. A payment security mechanism is often made available to the developer of certain renewable energy projects, where the offtaker is a government distribution company.

4. What types of security interests are available (and suitable) for a project financing in your jurisdiction?

Indian laws recognise the creation of security interests

 © 2023 Legalease Ltd

over property in the following manner:

a. **Immovable property**– Immovable properties are secured by way of a mortgage. The most common forms of mortgages in India are an English mortgage under a registered deed and an equitable mortgage by deposit of title deeds.
b. **Movable property**– Movable property is usually secured by way of a charge under a deed of hypothecation. Security interest over movable property can also be clubbed with mortgage of land under a registered mortgage deed.
c. **Securities –** Shares of a company are pledged under a pledge agreement together with marking the shares as pledged in the relevant depository in case of dematerialised securities or delivery of share certificates to the trustee in case of physical securities.

Depending on factors such as the nature of the property, ownership or location of assets, approval may be required under different laws before the creation or enforcement of a security interest. For instance, the creation of a security interest over Indian assets in favour of offshore lenders may require the prior approval of the Reserve Bank of India (RBI) or an authorised dealer in India under FEMA.

5. How are the above security interests perfected?

The following requirements apply to the perfection of security interests set out in Paragraph 4 above:

a. A company creating security interest under any security document is required to be registered with the registrar of companies (ROC) of the state in which the registered office of such company is located vide forms prescribed under the Companies Act. The priority of the security interest as regards the holders of the security is determined by the chronological order of filing with the ROC, in the absence of specific contractually agreed security ranking provisions.
b. An English mortgage must be registered with the relevant sub-registrar of assurances of the jurisdiction within which the mortgaged land is situated. Equitable mortgages in some notified states are also required to be registered with or intimated to the relevant sub-registrar.
c. Further, security interests (other than pledges) are also required to be registered (for record purposes only) by the holder of security with the Central Registry of Securitisation Asset Reconstruction and Security Interest of India (CERSAI), constituted under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interests Act 2002 (SARFAESI Act).
d. Any security interest created is also required to be filed by the holder of security with the information utilities (IU) under the Insolvency and Bankruptcy Code 2016 (IBC). The record of default of debt registered with the IU is evidence of default and the same can be used to initiate the corporate insolvency resolution process against the debtor.

Typically, all contractual, regulatory and corporate authorisations required for security creation are obtained prior to execution of the security documents.

Documents executed in India are subject to payment of state specific stamp duty rates in the state of execution of the documents. In case of transfer of debt, modification of the existing charge extends the security to the new lender.

6. Please identify how security is enforced (notably the enforcement options available for secured parties) both pre and post insolvency/bankruptcy of the project company?

Pre-Insolvency: Secured creditors can approach the Debt Recovery Tribunal established under the Recovery of Debts and Bankruptcy Act, 1993, for enforcement of their security or file an ordinary civil suit under the Code of Civil Procedure 1908. The SARFAESI Act further provides special self-help remedies to certain secured creditors. These legal remedies are available primarily only for domestic creditors. The SARFAESI Act allows secured creditors representing not less than 60% of value of the outstanding debt to *inter alia* take over the management of the borrowing company and to take possession and sell the secured assets.

An English mortgage may be enforced through a private sale of property subject to compliance with the conditions prescribed under the Transfer of Property Act, 1882. The intervention of the court would usually be required for enforcement of an equitable mortgage or hypothecation. In the case of a pledge, court intervention is not required and the creditor may sell the pledged securities after giving reasonable notice to the pledgor.

 © 2023 Legalease Ltd

Any sale pursuant to enforcement and repatriation of proceeds by offshore lenders is subject to the Indian foreign exchange regulations.

Post Insolvency: The insolvency resolution process under IBC, which is available to both financial and operational creditors, whether domestic or international, encourages distress resolution. The resolution process starts from the date an application is admitted by the National Company Law Tribunal and is generally required to be concluded within 180 days from the admittance date (with a long stop of 330 days). A moratorium is imposed on all proceedings against the debtor until completion of the resolution process. If the resolution process fails, the debtor's liquidation is commenced. Upon initiation of the liquidation process, a secured creditor may choose to either (i) relinquish its collateral and receive proceeds from the sale of the debtor's assets or (ii) realise its security interest over assets charged exclusively in its favour outside of the liquidation process.

7. What are other important considerations in relation to the security regime in the jurisdiction that secured parties should be aware of?

Other than as set forth above, secured parties should seek to be aware of, any existing encumbrances over the assets over which security is proposed to be created. A creditor typically undertakes physical searches and online searches including with CERSAI.

8. What key project risks should lenders be aware of in project financings in your jurisdiction? This may include, but may not be limited to, the following risks: force majeure, political risk, currency convertibility risk, regulating or permitting risk, construction/completion risk, supply or feed stock risk or legal and regulatory risk).

Project financing involves certain risks which are as follows:

- Delays in procurement of regulatory or contractual approvals.
- Delays in land procurement and right of way.
- Regulatory risks.
- Construction risks.
- Foreign exchange risks.
- Demand risk.
- Fuel or raw material availability risk.
- Force Majeure.
- Terrorism.
- Burglary and theft.
- Machinery breakdown.

Generally, risks are non-insurable in nature, barring only certain categories of risks (terrorism, theft) which are insurable. Most of the above risks are assumed by the SPV. However, the government may assume certain risks in PPP projects (e.g. land procurement). In general, project financing in India runs on the basis of limited recourse structures.

9. Are any governmental / regulatory consents required and are any financing or project documents requirement to be filed with any authority in order to be admissible in evidence in a court of law, valid or enforceable?

Typically, domestic infrastructure lending in India may require only project or concession specific approvals. However, foreign equity and loan investments are regulated by the RBI and FEMA. RBI approval may be required if the financing exceeds the prescribed limits under FEMA regulations or otherwise fall within the restrictions as to end use, tenor etc.

In India, notarisation of documents is used to verify the execution of the documents. In respect of foreign documents, an apostille certificate is usually sufficient to create a presumption under law that the party to the document has signed the document.

Security documents are required to be registered or filed with the government authorities in India as noted above. Documents that are unstamped or inadequately stamped are inadmissible as evidence in courts.

10. Are there are any specific foreign exchange, royalties, export restrictions, subsidies, foreign investment, that are relevant for project financings (particularly in the natural resources sectors)?

All natural resources being property of the state are licensed to private parties according to relevant governmental policies. Royalties and taxes are payable as per the licence granted by or concession entered with the government and prevailing income tax laws. Generally, natural resources are freely exportable subject to sector-specific restrictions.

 © 2023 Legalease Ltd

Generally, any foreign investment in India is required to comply with relevant sectoral caps and applicable conditions of investment, if any. Foreign investments in the infrastructure sector are under the automatic route in most cases and therefore, do not require the prior approval of the Indian government. Further, there are no specific protections for foreign investment from the government's ability to acquire or nationalise assets, except for judicial review of such acquisitions. Certain bilateral investment treaties entered into by India also extend protection to relevant foreign investors.

11. Please set out any specific environmental, social and governance issues that are relevant. For example, are project companies subject to certain ESG laws, reporting requirements or regulations?

Most infrastructure projects require environmental clearance from the Ministry of Environment and Forests. Depending on location of the project, other clearances such as forest clearance, coastal regulation zone clearance, pollution clearances (only an intimation in case of white category industries (such as solar)), disposal of hazardous wastes approvals, etc., prior to the construction phase are required.

With respect to social governance, statutory licenses under the applicable industrial and labour legislations are required for the tenure of the project if the SPV employs labour personnel.

At present, there is no centralised ESG reporting requirement for project companies in India. However, from financial year 2022-2023, the top 1,000 listed companies in India (by market capitalisation) are required to make detailed ESG disclosures.

12. Has any public-private partnership models or laws been enacted in the jurisdiction, and if so, are they specific to certain industry sectors?

In India, the commonly adopted models in projects on a PPP basis include (a) build-operate-transfer (preferred model for national highway projects contracted by National Highways Authority of India); (b) build-own-operate; (c) build-operate-lease-transfer (preferred model in the highways and ports sector); (d) design-build-operate-transfer (preferred model for redevelopment of railway stations); (e) lease-develop-operate (preferred model for concessions for airport operation and maintenance); (f) operate-maintain-transfer; (g) hybrid annuity model (newly introduced model in the roads sector). These models are typically based on level of investment, ownership control, risk sharing, technical collaboration, duration and financing.

Other than the PPP schemes referred to in answer 3 above, there is no consolidated policy in relation to PPPs in India at the central level. Certain states in India such as Andhra Pradesh, Gujarat, Punjab and Karnataka have formulated legislations to invite wider PPP in the infrastructure sectors.

13. Will foreign judgments, arbitration awards and contractual agreements to arbitrate be upheld?

Yes, India has robust legislation to supervise the enforcement of foreign judgments, foreign arbitral awards, and contractual agreements to arbitrate. The Code of Civil Procedure, 1908 (CPC), provides that where a foreign decree (being a money decree) has been rendered by a superior court in a territory which the GOI has by notification recognised to be a "reciprocating territory", it may be enforced in India. In such cases, Indian courts will not re-examine any issue unless on certain grounds such as violation of natural justice or breach of an Indian law.

India is party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958 and the Geneva Convention on the Execution of Foreign Arbitral Awards, 1927. An award made in a signatory country can be enforced in India as long as the award is final in the signatory country and the signatory country has been notified as a convention country by India. For awards that are passed in non-convention states, a fresh civil suit is required to be initiated in India.

Indian courts will endeavour to give effect to an arbitration agreement unless the underlying dispute cannot be under Indian law.

14. Is submission to a foreign jurisdiction and waiver of immunity effective and enforceable?

Indian courts will not ordinarily restrain a contracting party containing a foreign jurisdiction dispute resolution clause from approaching the court of choice, subject to certain exceptions for example if choice of jurisdiction is vexatious or oppressive, or is in a *forum non conveniens*, then Indian courts will intervene.

India has adopted the principle of restrictive sovereign immunity. The general rule is that a person bringing a

 © 2023 Legalease Ltd

"suit" against a foreign sovereign state requires prior written permission from the GOI. However, this is inapplicable in cases of implied waivers, for example in commercial transactions entered into by a foreign government corporation/ entity. No permission is required before bringing enforcement proceedings under the Arbitration and Conciliation Act, 1996against a foreign sovereign.

15. Please identify what you consider to be (a) the key current issues for project financing in your jurisdiction; and (b) any emerging trends or topics which should be considered or focused on by project financing stakeholders.

While project finance in India has traditionally been associated with "core" sectors such as roads, highways, power projects, ports and airports, the increased government focus on urban development and associated infrastructure has recently seen several transactions in the space of health and sanitation, renewable energy, mass transit, data centres, logistics and waste-to-energy.

The project financing sector in India has been affected by stressed assets in the infrastructure sector. To tackle the same, RBI issued RBI (Prudential Framework for Resolution of Stressed Assets) Directions 2019 to require the lenders to implement a resolution plan and enter into an inter-creditor agreement in a time-bound manner, providing for *inter alia*, a standstill on civil action and IBC proceedings during the prescribed standstill period with a few exceptions.

The RBI has also permitted banks and certain financial institutions to lend to Infrastructure Investment Trusts (InvITs) which is giving a boost to infrastructure financing and allowing InvIT platforms to become more competitive.

India's climate goals have also played a role in bolstering transactions in the renewables space resulting in issuance of "green bonds" and "green finance" in the domestic project financing space. The use of listed or unlisted bonds for project finance have also seen an increase.

Indian borrowers are also looking to cross-collateralise and cross-leverage across various assets and changing the traditional outlook of project finance as a limited recourse, single asset finance product.

16. Please identify in your jurisdiction what key legislation or regulations have been implemented (or will / plan to be) for projects in connection with the energy transition?

India has announced its commitment to set up 175 GW of renewable energy capacity by 2022 and 450 GW by 2030. India also announced the target of net-zero emissions by the year 2070 at the 2021 United Nations Climate Change Conference (COP26).

In April 2021, RBI became a member, of the Central Banks and Supervisors Network for Greening the Financial System (NGFS) which is a global network of banks involved in developing best practices towards climate risk management. RBI also recently released a paper on climate risk and sustainable finance for stakeholder comments. The Securities and Exchange Board of India (SEBI) has also issued a Consultation Paper for Green and Blue Bonds as a mode for Sustainable Finance.

Indian Banks' Association has set up a large working group, comprising representatives of key banks, to provide recommendations on sustainability finance. Recently, the committee of experts on sustainable finance submitted their report to the International Financial Services Centers Authority which includes recommendations, amongst others, for developing a voluntary carbon market and setting up of a dedicated MSME platform for sustainable lending.

17. Please identify if there are any material tax considerations which need to be taken into account for a project financing in your jurisdiction, and if so, how such tax issues can be mitigated.

All transactions between an Indian company and its foreign group company must be on an arm's length basis, subject to the specific methodologies under the Indian tax laws. In cases where the transaction is concluded to be not at arm's length , the differential amount is considered as income in the hands of Indian company. Such differential amount is to be reimbursed/repatriated by the foreign group company to the Indian company in whose hands the transfer pricing adjustments were made. If such amount is not reimbursed/repatriated to the Indian company, then it shall be considered as a loan advanced by the Indian company to the foreign group company and accordingly, notional interest income would accrue (and be taxable for) to the account of the Indian company.

 © 2023 Legalease Ltd

Additionally, Indian domestic tax laws contain certain "thin capitalisation" rules i.e. interest expenses claimed by an Indian entity in relation to payments made to its non-resident related parties are restricted to the lower of: (a) 30% of its earnings; or (b) interest paid or payable to such related party.

Under the new Indian GST regime, import of project equipment is subject to applicable customs and import duties and goods and services taxes (GST).

18. What types of funding structures (e.g. debt, equity or alternative financing) are typical for project financing in your jurisdiction. For example, are project bond issuances, Islamic finance and – in the context of mining deals – streams or royalties, seen as attractive (and common) options for stakeholders?

Typically, project finance is provided by banks, foreign portfolio investors and financial institutions in the form of debt, including both onshore and offshore funds. For domestic lenders, rupee loans and rupee denominated bonds remain popular funding structures. For offshore funds, the external commercial borrowing route remains the primary source of funding. A part of the funding requirement is received from the sponsors, domestic funds and international market participants in form of mezzanine financings.

Bonds or other market instruments can be issued in India or offshore by project companies on a private-placement basis or to the public, subject to various eligibility criteria and restrictions on end-use and investment amount (which vary based on the nature of the borrowing or the investor).

In line with the investor and stakeholder demand and growing momentum for business trust structures as a financing vehicle in the Indian market space, SEBI has permitted trust structures operating in infrastructure sector (InvITs) and real estate sectors (REITs) to raise monies and invest in SPVs engaged in the implementing greenfield or brownfield infrastructure projects.

At present, RBI regulations do not recognise Islamic finance products.

19. Please explain if there are any regional development banks or export credit agencies, and if so, what is their role in project financing in your jurisdiction and beyond.

The Indian government has set up National Bank for Financing Infrastructure and Development (India's principal development financial institution for infrastructure financing) and National Investment and Infrastructure Fund (a collaborative investment platform for international and Indian investors, anchored by the GOI), with special focus on financing of long-term and crucial infrastructure sectors. In addition, the domestic government players such as State Bank of India and Indian Renewable Energy Development Agency have historically invested in the infrastructure sectors and have actively funded the renewable sector, transmission and road sectors.

20. Please explain if there are any important insurance law principles or considerations in connection with any project financing in your jurisdiction.

Only Indian insurers registered with the Insurance Regulatory and Development Authority (IRDA) can insure assets in India. Typically, assets situated in India are not permitted to be insured by an insurer whose principal place of business is outside India without permission of IRDA. Reinsurance arrangements are to be approved by the respective insurance company's board in consultation with IRDA.

Any remittance of any claim under any insurance cover by an offshore creditor is subject to foreign exchange control regulations as prescribed by the RBI from time to time.

 © 2023 Legalease Ltd

Contributors

Santosh Janakiram
Partner

santosh.janakiram@cyrilshroff.com

Manasvini Raj
Partner

manasvini.raj@cyrilshroff.com

Dhananjaya (DJ) Chak
Partner

dhananjaya.chak@hsf.com

Martin Kavanagh
Partner

martin.kavanagh@hsf.com

 © 2023 Legalease Ltd