CHAPTER IV
GOVERNMENT POLICIES AND FOREIGN CAPITAL IN INDIA

The Industrial Policy Resolution of 1948 and 1956 were the basis of the Government’s policy on foreign capital till 1991. The Indian Government recognised foreign capital as important supplement to domestic saving for the development of the country and for securing scientific, technical and industrial know-how. Although as a matter of policy the major ownership and effective control of undertaking was to be in Indian hands, the government permitted, in a few cases, foreign capital to have major control of an enterprise.

Foreign Investment Policy

Foreign investment in India has been the direct outcome of the liberal trade policies undertaken and implemented by successive governments. The liberalisation program of the government aims at rapid and substantial growth of the country's economy and besides a harmonious integration with global economy. Foreign investment in India has created some wonderful opportunities in the country in terms of creating employment and improving the basic infrastructure of the country.
Since 1990-91, the Government of India embarked on liberalisation and economic reforms with a view to bring about rapid and substantial economic growth and move towards globalisation of the economy. As a part of the reforms process, the government under its New Industrial Policy revamped its foreign investment policy, recognising the growing importance of foreign investment as an instrument of technology transfer, augmentation of foreign exchange reserves and globalisation of the Indian economy.

**Foreign Direct Investment Policy**

The foreign direct investment provides for investment in Indian companies setting up wholly owned subsidiaries in areas which are not reserved exclusively for the public sector or which are not under the prohibited categories such as real estate, insurance, agriculture and plantation.

The approval mechanism for the foreign direct investment has a two-tier system, the automatic route and the approval route. Under automatic route investment in areas are identified and up to the limits of foreign equity prescribed, companies can issue shares and receive inward remittance with a reporting requirement within a period of 30 days. No reference to the government is required. In approval route, the proposals are considered by the Foreign
Investment Promotion Board (FIPB) serviced by the Department of Industrial Policy and Promotion (DIPP). Under a recent measure for simplifying the procedure, the RBI has dispensed with the need for obtaining RBI’s ‘in principle’ permission before receiving overseas investment or at a last stage for issuing shares to the foreign investors. The company however, has to make report to the RBI within 30 days after issue of shares to the foreign investors.¹

**Foreign Direct Investment Policy Till 1991²**

At the time of independence, the attitude of the Indian Government towards foreign direct investment was one of fear and suspicion. This was natural on account of the previous exploitative role played by the British in ‘draining away’ resources from India. This suspicion and hostility found expression in the Industrial Policy of 1948 which, though recognising the role of private foreign investment in the country, emphasised that its regulation was necessary in the national interest. Because of this attitude expressed in the 1948 Resolution, foreign capitalists were dissatisfied and as a result, the flow of capital goods into India was obstructed. The then Indian Prime Minister has some assurances to foreign investors in 1949. They are

1. The Government of India will not differentiate between foreign and Indian capital, the implication being that the government
would not place any restriction or impose any condition on foreign enterprises which were not applicable to similar Indian enterprises.

2. Foreign exchange position permitting, reasonable facilities would be given to foreign investors for remittances of profits and repatriation of capital.

3. In case of nationalisation of the undertaking fair and equitable compensation would be paid to foreign investors.

By a declaration issued on June 2, 1950, the government assured foreign capitalists that they could remit the returns from investments made by them in the country after January 1, 1950. In addition, they were also allowed to have reinvestment of profit.

In the Industrial Policy Resolution of 1956, a more open attitude towards foreign direct investment was declared. But the response evinced was only moderate because foreign capital was allowed only in those industries where Indian capital was scarce.

In 1968, the government issued an illustrative list whereby only some categories of industries were allowed to have inflows of foreign direct investments. In 1973 this list was narrowed down to 19 industries.
There was some let-up in the 1980s, with controls being eased if not dismantled. But it was with the New Economic Policy launched amidst much fanfare in July 1991, that steps to revamp the industrial and trade policy structure got into full swing, and foreign direct investment was assigned a critical role to refurbish a sagging Indian economy.

The New Industrial Policy declared by the government in July 1991 opened the doors of several industries to foreign direct investment. Prior to this policy, foreign capital was generally permitted only in those industries where Indian capital was scarce. It was normally not permitted in trading activities, plantations, banking and financial institutions. The declared policy of the government was also to discourage foreign capital in certain non essential consumer goods and service industries.

**Foreign Direct Investment Policy in Post - 1991**

As a first step the government announced in 1991 a list of industries in which foreign direct investment would be automatically allowed up to 51 per cent. These industries ranged from the capital goods and metallurgical sector to the entertainment, electronic, food processing and service sectors with significant export potential. Hotels and tourist related areas were also allowed foreign equity
holdings by international trading companies up to 51 per cent. In order to accelerate the progress of the power sector, 100 per cent foreign equity participation was allowed for the setting up of power plants.

During 1992-93, several additional measures were taken to encourage foreign direct investment inflows. Foreign direct investment was allowed in exploration, production and refining of oil and marketing of gas. The Foreign Exchange Regulation Act (FERA), 1973, was substantially liberalised in 1991. In 1998-99, more measures were announced to encourage foreign direct investment. The Government decided to permit foreign direct investment up to 49 per cent of the total equity, subject to license, in company providing Global Mobile Personal Communication by Satellite (GMPCS) services.

In August 1999, Foreign Investment Implementation Authority (FIIA) was established within the Ministry of Industry in order to ensure approvals for foreign direct investment. In February 2000, the government took a major decision to place all items under the automatic route for foreign direct investment except a small negative list. To give effect to this decision, the RBI issued a notification on April 5, 2000 which said that all items excluding specific sectors will
be eligible for foreign direct investment under the automatic route up to even 100 per cent.

In 2000-2001, further steps were taken, FDI up to 100 per cent was permitted in e-commerce subject to specific conditions. The dividend balancing condition for foreign direct investment in 22 consumer goods industries was removed. The upper limit of Rs.1,500 crore for FDI in projects involving electricity generation, transmission and distribution (other than atomic reactor plants) was dispensed with. For facilitating greater inflow of foreign funds in the crucial oil-refining sector, ceiling for FDI under the automatic route in oil refining was increased to 100 per cent from the existing 49 per cent. FDI under the automatic route was permitted up to 100 per cent for all manufacturing activities in Special Economic Zones (SEZs) except for certain activities. 100 per cent FDI was also allowed (with certain conditions) in telecommunication sector, for internet service providers, infrastructure providers providing dark fiber, electronic mail and voice mail.

Then in May 2001, some more concessions and fresh proposals were announced. As per a cabinet decision, the manufacture of the ammunition and other defence related products was permitted by the private sector. The private industry can
establish wholly-owned units for the production of defence items, with even an FDI up to 26 per cent, essentially to facilitate technology transfers. In the banking sector, FDI was allowed up to 49 per cent, inclusive of all FDI sources. Earlier 20 per cent was permitted for FDI. In the drug and pharmaceutical sector, 100 per cent FDI was allowed. 10 per cent FDI funding will be allowed in airport projects, but this will be subject to clearance by the Foreign Investment Promotion Board (FIPB). But for FDI up to 74 per cent in airport, no FIPB approval is required and the investment can come through the automatic route. The hotel and tourism industry will be allowed to have 100 per cent FDI. There will be no disinvestments stipulation. Courier services have also been allowed 100 per cent FDI. In the telecom sector, the FDI cap has increased from 49 per cent to 74 per cent for internet service providers with gateways, radio pagers and end-to-end bandwidth. But all investment above 49 per cent would need FIPB approval and be subject to licence and security requirements.

In 2002-2003, the Government of India allowed 100 per cent FDI in the tea sector including plantations. In June 2002, limited FDI was allowed in print media up to 26 per cent in publications of news/current affairs and up to 74 per cent in other publications, especially of a technical nature. In March 2003, the union cabinet decided to set cap of 26 per cent on foreign direct investment in news
channels that seek to uplink from India, putting television news and the print media on par. Until now, there is no separate up linking policy for news and current event channels.

In India, currently after the policy changes in February 2009, many sectors in manufacturing are open to 100 per cent FDI under the automatic route. FDI is allowed up to 100 per cent in all these industries except defence production where it is capped at 26 per cent. FDI is not allowed in a few services including retail trading (except single brand), lottery business and gambling. In the permitted services, foreign equity is allowed below 50 per cent. FDI is currently allowed only up to 49 per cent in scheduled air transport services or domestic passenger airlines. Broadcasting services also have similar rules. Up linking of non-news television channels is the only broadcasting service permitted to have 100 per cent FDI after clearance by the FIPB. The foreign equity is not allowed in cable television networks and Direct-To-Home (DTH) operations. FDI is allowed only up to 26 per cent in print media. It is allowed up to 74 per cent in financial services such as private banks. Insurance, however, can attract FDI only up to 26 per cent. Foreign equity up to 49 per cent is permitted in Asset Reconstruction Companies (ARCs) and in Stock Exchanges and Depositories Clearing Corporations. Except for ARCs, the FDI is capped at 26 per cent. In
telecommunication services-both basic and cellular-although FDI up to 74 per cent is allowed, only 49 per cent is allowed under automatic route with the rest requiring approval from FIPB.

**Investment by Way of Acquisition of Shares**

Foreign investors looking at acquiring equity in an existing Indian company through stock acquisitions can do so without obtaining approvals except in financial services sector, provided (i) such investments do not trigger off the takeover provisions under SEBI’s (Substantial Acquisition of Shares and Takeover) Regulations, 1997 and (ii) the non-resident shareholding after transfer complies with sectoral limits under FDI policy.

As per RBI valuation norms, acquisition price should not be lower than

- Prevailing market price, in case of listed companies.
- Fair market value as per Controller of Capital Issues (CCI) valuation guidelines, in case of unlisted companies.

Acquisitions may be made from an existing Indian company which is either a privately held company or a company in which public is interested i.e., a company listed on stock exchange, provided a resolution to this effect has been passed by the Board of Directors of
the Indian Company. Acquisition of shares of a public listed company is subject to SEBI guidelines and requires prior approval from FIPB. SEBI’s Take-Over Code Regulations require that any person acquiring 15 per cent or more of the voting capital in a public listed company should make a public offer to acquire a minimum 20 per cent stake from the public.

**Foreign Investment Promotion Board and Foreign Direct Investment**

Foreign Investment Promotion Board (FIPB) has been set up by the Government of India in order to increase the flow of foreign direct investments into the country. By doing this, Foreign Investment Promotion Board (FIPB) has been able to give a major boost to the Indian economy.\(^4\)

**Objective of Foreign Investment Promotion Board (FIPB)**

The main objectives of Foreign Investment Promotion Board (FIPB) are:

a) undertaking investment promotion activities,

b) facilitating investment in the country by international companies, Non – Resident Indians and other foreign investors,

c) accelerating growth in the industrial sector and increasing inflows of foreign investment into the country and
d) providing appropriate institutional arrangements, transparent procedures and guidelines for investment promotion and to consider and recommend proposals for foreign investment.

Functions of FIPB

FIPB is assigned some important functions such as:

- approving the foreign investment proposals quickly,
- reviewing the foreign direct investment policies and to communicate with other agencies such as the Administrative Ministries in order to set up guidelines that are transparent and which encourage FDI into the various sectors of the country,
- looking after the implementation of the various proposals that have been approved by it,
- taking up of the activities that encourage FDI into the country such as establishing contact with international companies and also inviting them to invest in India,
- communicating with government, non-government, and industry bodies in order to increase the flow of foreign direct investment into the country,
- communicating with the Foreign Investment Promotion Council that has been set up in the Industry Ministry,
identifying the various sectors that require foreign direct investment and

taking up of all other activities that help in increasing the flow of foreign direct investment into the country.

Foreign Investment Implementation Authority (FIIA)

Government has set up Foreign Investment Implementation Authority (FIIA) to facilitate quick translation of foreign direct investment approvals into implementation by providing a pro-active service to foreign investors and to help them obtain necessary approvals by sorting their operational problems. FIIA is assisted by Fast Track Committee (FTC), which have been established in 30 Ministries/Departments of Government of India for monitoring and solving the difficulties of sector specific projects.  

Functions of FIIA

FIIA has been constituted with the basic objectives of:

- Expediting various approvals/permissions;
- Fostering partnership between investors and government agencies concerned;
- Resolving difference in perceptions;
- Enhancing overall credibility;
- Reviewing policy framework; and
Having liaison with the Ministry of External Affairs for keeping India’s diplomatic missions abroad informed about translation of FDI approvals into actual investment and implementation.

**Foreign Investment Promotion Council (FIPC)**

Apart from making the policy framework investor-friendly and transparent, promotional measures are also taken to attract foreign direct investment into the country. The Government has constituted a Foreign Investment Promotion Council (FIPC) in the Ministry of Industry. This comprises professionals from industry and commerce. It has been set up to have a more target oriented approach towards foreign direct investment promotion. The basic function of the Council is to identify specific sectors/projects within the country that require foreign direct investment and target specific regions/countries of the world for its mobilisation.\(^7\)

**Secretariat for Industrial Assistance (SIA)**

The SIA, functioning with the Department of Industrial Policy and Promotion, Ministry of Commerce and Industry, acts as a gateway to industrial investment in India. It provides a single window clearance for entrepreneurial assistance and facilitates the processing of investors’ applications requiring government approval. Broadly, the objectives of SIA are:
- Assist entrepreneurs and investors in setting up projects and monitors the implementation of these projects;
- Notify all government policy relating to investment and technology.

**Foreign Portfolio Investment Policy**

Portfolio investments in India include investments in American Depository Receipts (ADRs)/Global Depository Receipts (GDRs), Foreign Institutional Investments and investments in offshore funds. Before 1992, only Non-Resident Indians (NRIs) and Overseas Corporate Bodies (OCBs) were allowed to undertake portfolio investments in India. From September 14, 1992 with suitable restrictions, Foreign Institutional Investors (FIIs) were permitted to invest in all the securities traded on the primary and secondary markets, including shares, debentures and warrants issued by companies which were listed or were to be listed on the stock exchanges in India. The entry of FIIs seems to be a follow up of the recommendation of the Narsimhan Committee Report on Financial System. While recommending their entry, the Committee, however did not elaborate on the objectives of the suggested policy. The Committee only suggested that the capital market should be gradually opened up to foreign portfolio investments.
Regulations Regarding Portfolio Investments by Foreign Institutional Investors (FIIs)

- FIIs include asset management companies, mutual funds, and investment trusts as nominee companies, incorporated/institutional portfolio managers or their Power of Attorney holders, University funds, endowment foundations, charitable trusts and charitable societies.

- SEBI acts as the nodal point in the registration of FIIs. RBI has granted general permission to SEBI registered FIIs to invest in India under the portfolio investment scheme.

- All FIIs and their sub-accounts taken together cannot acquire more than 24 per cent of the paid-up capital of an Indian company. Indian companies can raise the above mentioned 24 per cent ceiling to the sectoral cap/statutory ceiling as applicable by passing a resolution by its Board of Directors followed by passing a special resolution to that effect by its general body.

Enhancement in the Limits on Investments by Foreign Institutional Investors (FIIs).

1. Foreign institutional investors registered with SEBI are permitted to invest subject to an aggregate investment limit of
24 per cent of the issued and paid-up capital of an Indian company. In terms of the RBI Notification No.41/2001-RB dated March 2, 2001 and Press Note dated March 8, 2001, the Indian companies were permitted to enhance the normal aggregate portfolio investment limit from 24 per cent to 49 per cent under specified special procedure.

2. It has since been decided to increase the portfolio investment ceiling applicable to Foreign Institutional Investors (FIIs). Pursuant to this decision, Indian companies would henceforth be permitted to raise the aggregate ceiling for FII portfolio investments through the secondary market from the normal level of 24 per cent, up to the applicable sectoral cap levels, of the issued and paid-up capital of the company subject to compliance with the special procedure viz.:

- approval by the Board of Directors of the Company to the enhanced limit beyond 24 per cent; and
- a special resolution passed by the general body of the company approving the enhanced limit beyond 24 per cent.

3. All other requirements governing FII portfolio investments would continue to be operative as before.
Regulations Pertaining to Issue of ADRs/GDRs by Indian Companies

- Indian companies can raise foreign currency resources abroad through the issue of ADRs/GDRs, in accordance with the scheme for issue of Foreign Currency Convertible Bonds (FCCBs) and ordinary shares (through depository receipt mechanism) scheme, 1993 and guidelines issued by the Government of India there under from time to time.

- A company can issue ADRs / GDRs, if it is eligible to issue shares to persons resident outside India. However, an Indian listed company, which is not eligible to raise funds from the Indian capital market including a company which has been restrained from accessing the securities market by the Securities and Exchange Board of India (SEBI) will not be eligible to issue ADRs/GDRs.

- Unlisted companies, which have not yet accessed the ADR/GDR route for raising capital in the international market, would require prior or simultaneous listing in the domestic market, while seeking to issue such overseas instruments. Unlisted companies, which have already issued ADRs/GDRs in the international market, have to list
in the domestic market on making profit or within three years of such issue of ADRs/GDRs, whichever is earlier.

- After the issue of ADRs/GDRs, the company has to file a return in Form DR as indicated in the RBI Notification No. FEMA.20/ 2000-RB dated 3 May 2000, as amended from time to time. The company is also required to file a quarterly return in Form DR- Quarterly as indicated in the RBI Notification.

- There are no end-use restrictions on GDR/ADR issue proceeds, except for an express ban on investment in real estate and stock markets.

- Erstwhile OCBs which are not eligible to invest in India and entities prohibited to buy, sell or deal in securities by SEBI will not be eligible to subscribe to ADRs/GDRs issued by Indian companies.

- The pricing of ADR/GDR issues including sponsored ADRs/ GDRs should be made at a price determined under the provisions of the scheme of issue of Foreign Currency Convertible Bonds and ordinary shares (Through Depository Receipt Mechanism) Scheme, 1993 and guidelines issued
by the Government of India and directions issued by the Reserve Bank, from time to time.

**Regulations Regarding Portfolio Investments by NRIs/PIOs**

- Non Resident Indians (NRIs) and Persons of Indian Origin (PIOs) can purchase/sell shares/convertible debentures of Indian companies on Stock Exchanges under portfolio investment scheme. For this purpose, the NRI/PIO has to apply to a designated branch of a Bank which deals in portfolio investment. All sale/purchase transaction is to be routed through the designated branch.

- An NRI or a PIO can purchase shares up to 5 per cent of the paid-up capital of an Indian company. All NRIs/PIOs taken together cannot purchase more than 10 per cent of the paid-up value of the company. (This limit can be increased by the Indian company to 24 per cent by passing a general body resolution).

- The sale proceeds of the repatriable investments can be credited to the NRE/NRO etc. accounts of the NRI/PIO whereas the sale proceeds of non-repatriable investment can be credited only to NRO accounts.
The sale of shares will be subject to payment of applicable taxes.

**Repatriation of Capital**

Repatriation of capital is permitted at the time of disinvestment of equity by foreign investors. It has been allowed at market rates on stock exchanges from September 15, 1992.\(^8\)

**Payment of Royalty**

The norm for royalty payment is 5 per cent and the over-all norm is 8 per cent inclusive of lump sum payment for technical know-how. These norms are not rigid and are relax able in suitable cases.\(^9\)

**Remittances**

Once investment is permitted, technical know-how fees, royalty and dividend can be freely remitted, provided they are in accordance with the original approval. The payments of dividend would be monitored by the RBI. In the wake of recent liberalisation measures, foreign investment policy has become an open door policy.

**Foreign Brand Name**

Foreign companies have been allowed to use their brand name or trade marks on goods sold in the domestic market with effect from May 14, 1992.\(^10\)
**Prohibitions on Portfolio Investments**

Foreign Institutional Investors (FIIs) are not permitted to invest in equity issued by an Asset Reconstruction Company. They are also not allowed to invest in any company which is engaged or proposes to engage in the activities such as:

- Business of chit fund
- Nidhi Company
- Agricultural or plantation activities
- Real estate business or construction of farm houses (real estate business does not include development of townships, construction of residential/commercial premises, roads or bridges).
- Trading in Transferable Development Rights (TDRs).

**Non – Resident Indian ( NRI ) Policy**

A non-resident Indian (NRI) is an Indian citizen who has migrated to another country. For tax and other official purposes the Government of India considers any Indian national away from India for more than 180 days in a year as a NRI. In common usage, this often includes Indian born individuals who have taken the citizenship of other countries.
NRIs can invest in all avenues open to resident Indians. Persons of Indian origin are restricted to invest in non-agricultural businesses in the country.

NRIs are allowed to invest in shares and stocks in India, either directly by subscribing to shares and debentures of Indian companies on a repatriable or non-repatriable basis, or through the portfolio investment scheme, or in government securities, certificates and units of UTI through remittances from their domestic accounts or remittances from abroad.

NRIs can establish a company or run a business in India.

NRIs can sell the stocks and shares they hold to resident individuals or though the stock exchange. Securities can also be gifted by NRIs.

Income earned on NRI deposits and investments from 1994-95 can be repatriated, subject to certain limits.

The procedure followed for repatriating income from non-repatriable assets in India is that they have to apply to a designated branch of an authorised dealer. It has to be
submitted along with a certificate from a Chartered Accountant. The dealer would then credit the amount repatriable, after due deduction of tax, to the applicant’s NRE/FCNR account.

- The 24 per cent scheme allows Indian companies, except those engaged in agricultural activities, to issue up to 24 per cent of their shares and debentures to NRIs with repatriation benefits.

- The 40 per cent scheme allows for purchase of equity, preference shares and convertible debentures not exceeding 51 per cent of the face value of each issue. Repatriation of up to 40 per cent of the new issue is allowed. Under this scheme, NRIs can invest in new projects or in expansion and diversification projects of existing companies.

- NRIs are allowed 100 per cent repatriation if they invest in Indian companies engaged in priority industries and those involved in export and trading activity. No prior approval of the RBI is required.

- NRIs are allowed to invest in companies dealing in real estate.

- 100 per cent equity participation is allowed in accordance with the RBI's guidelines, though repatriation is permitted after 5
years of the operations, and only from the accumulated foreign exchange earnings, after due taxes are paid.

- General permission of the RBI exists for sale of units of mutual funds to NRIs and FIIs provided the investment is being made through inward remittance through normal banking channels or by debit to the NRIs’ NRE/FCNR account. The returns are accordingly paid into the investor’s NRE/FCNR account.

- In the case of public sector undertakings, NRI holding should not exceed 1 per cent of the paid-up capital. The investment must come from inward remittance through the authorised dealer or through the NRE/FCNR account. Applications are made through the designated SBI branch.

- Funds in fixed deposits are permitted with full repatriation benefits after three years to NRIs.

**External Commercial Borrowing Policy**

**ECB Policy**

1. External Commercial Borrowings (ECBs) include commercial bank loans, buyers’ credit, suppliers’ credit, securitised instruments such as floating rate notes and fixed rate bonds etc., credit from official export credit agencies and commercial
borrowings from the private sector window of Multilateral Financial Institutions such as International Finance Corporations, ADB, AFIC, CDC, etc.

2. ECBs are being permitted by the government to function as a source of finance for Indian Corporate for expansion of existing capacity as well as for fresh investment.

3. The policy seeks to keep an annual cap or ceiling on access to ECB, consistent with prudent debt management.

4. The policy also seeks to give greater priority for projects in the infrastructure and core sectors such as power, oil exploration, telecom, railways, roads and bridges, ports, industrial parks and urban infrastructure etc., and the export sector. Development of financial institutions, through their sub-lending against the ECB approvals are also expected to give priority to the needs of medium and small scale units.

5. Applicants will be free to raise ECB from any internationally recognised source such as banks, export credit agencies, suppliers of equipment, foreign collaborators, foreign equity-holders, international capital markets etc. Offers from unrecognised sources will not be entertained.
Procedure for Seeking ECB Approval

Applications may be submitted by the borrowers in the prescribed format to the Joint Secretary, Department of Economic Affairs, Ministry of Finance, North Block, New Delhi-10001.

The application should contain the following information

✓ An offer letter from the lender giving the detailed terms and conditions

✓ Copy of project appraisal report from a recognised Financial Institution/Bank, if applicable

✓ Copies of relevant documents and approvals from Central/State Governments, wherever applicable, such as FIPB, CCEA, and SIA clearances, environmental clearance, techno-economic clearance from Central Electricity Authority, valid licences from competent authorities, no objection certificate from Ministry of Surface Transport, evidence of export/foreign exchange earnings from the statutory auditor based on the bankers’ realisation certificate, registration with RBI in case of NBFCs, approval for overseas investment from RBI etc. 12
**Approval Under FERA**

After receiving the approval from ECB division, Department of Economic Affairs, Ministry of Finance, the applicant is required to obtain approval from the Reserve Bank of India under the Foreign Exchange Regulation Act, 1973, and to submit an executed copy of the loan agreement to this department for taking the same on record, before obtaining the clearance from RBI for drawing the loan. Monitoring of end-use of ECB will be done by RBI.¹³

**Short-Term Loan from RBI**

While ECB for minimum maturity of three years and above will be sanctioned by Department of Economic Affairs, Ministry of Finance, approvals of short term foreign currency loans with a maturity of less than three years will be sanctioned by RBI, according to RBI guidelines.¹⁴

**Validity of Approval**

Approvals are valid for a period of six months, i.e. the executed copy of the loan agreement is required to be submitted within this period. In the case of FRNs, Bonds etc., the same are required to be launched within this period. In case of power projects, the validity of the approval will be for a period of one year. Extension will not be granted beyond the validity period. However, borrowers are free to
submit fresh application, after a gap of six months, which will be evaluated in the light of the ECB guidelines applicable at that time. In case of infrastructure projects, however, because financial closure may get delayed for reasons beyond the investor's control, extension of validity may be considered on merits.¹⁵

**External Assistance**

The initial periods of development in India were marked by balance of payments difficulties and the shortage of foreign exchange resources. Planners have to rely on external assistance to make available adequate supplies of foreign exchange for supplementing the existing investible resources in the country. External assistance was received from various countries and international institutions in the form of equipments and commodities and technical assistance in the form of the services of experts and training facilities. Assistance came as loans, grants, debt service payment and aid. However, most of the assistance in the initial periods of planning was in the form of interest-bearing loans, while only a fraction was in the form of outright grants. Another characteristic feature of external assistance in the initial years of planning was the reliance on bilateral sources of funding. In fact, up to the third plan period (ending on 31.3.66), loans from multilateral sources (IBRD and IDA) accounted for only 19 per cent of the authorisations, while bilateral assistance accounted for the
remaining 81 per cent. It was only after the 1970s that the multilateral sources of funding began to gain predominance.

**Major Donors**

External assistance made available by various multilateral and bilateral agencies to India comprises of loans and grants. The World Bank extends assistance through its concessional lending window, the IDA, and market based lending through the IBRD. The assistance from the Asian Development Bank (ADB) is also market based. These form the principal sources of multilateral external assistance to India. The significant bilateral sources offering external assistance include Japan, Russia, Germany and United Kingdom.¹⁶

**Major Multilateral Donors**

**Asian Development Bank (ADB)**

The ADB is a major regional financial institution and India’s subscription to the Bank’s capital stock is the fourth largest of all member countries after Japan, the USA and the People’s Republic of China. Although eligible to borrow under the criteria laid down by the ADB, India voluntarily refrained from borrowing initially. However, in order to broad base its resources, it was decided to commence borrowing from ADB in 1986.
Transport & communications, energy, multi-sector projects, industry and non-fuel minerals, social infrastructure, and irrigation are the areas for which Bank lends.

The ADB also provides technical assistance in the form of grants or loans or a combination to facilitate the transfer of resources and technology to developing member countries.\textsuperscript{17}

**International Bank for Reconstruction and Development (IBRD)**

IBRD loans though non-concessional, are available on terms that are relatively more favourable compared to commercial loans. The commitments by IBRD are against projects in various sectors like transport, energy, urban infrastructure (including water & sanitation) etc. The repayment period for IBRD loans is presently 20 years, inclusive of a grace period of five years. The commitment fee on the un-disbursed balance is presently 0.75 per cent.\textsuperscript{18}

**International Development Association (IDA)**

IDA, the soft loan affiliate of the World Bank, depends largely on contributions made from time to time by the wealthier member countries for its financial resources and on repayments received from earlier credits. IDA assistance to India began in June 1961 and has since then been an important component of external assistance programme. IDA commitments, which are known as “Credits”,
presently have a 10 years grace period and are to be repaid over 35 years. The credits to India approved up to 30.06.1987 are repayable in 50 years, inclusive of a grace period of 10 years, and those approved after 01.07.1987 are repayable in 35 years inclusive of a grace period of 10 years. IDA credits carry no interest charge but a service charge of 0.75 per cent per annum is levied on the amount disbursed. Further, there is an annual commitment charge of up to 0.5 per cent per annum on the un-disbursed balance.\textsuperscript{19}

**International Fund for Agricultural Development (IFAD)**

The International Fund for Agricultural Development (IFAD) was set up in 1977 to finance agricultural development projects primarily for the expansion of food production in developing countries. 163 countries are members of IFAD and they are grouped in three lists. List A comprises developed countries, List B are oil producing countries and List C are developing countries. India has been re-elected to the Executive Board of IFAD for the period 2006-2008. IFAD loans are repayable over a period of 40 years including a grace period of 10 years and carry no interest charges. However, a service charge at the rate of 0.75 per cent per annum is levied on the loan amount withdrawn and outstanding.\textsuperscript{20}
Policy Announcements on Bilateral Co-Operation

Subsequent to the budget announcement made in 2003-04, the Government of India reviewed its policy of bilateral development co-operation in September 2004 to affirm the liberalisation and reform orientation in India’s economic policy. Revised guidelines were issued in January 2005 that superseded all earlier guidelines in this regard.

Bilateral development assistance (including grants) is not being availed by the government and its subordinate and attached agencies (societies, trusts, boards, companies, corporations, etc) where the government has substantial control. Bilateral development assistance is being accepted from all G-8 countries, namely, U.S.A., UK, Japan, Germany, France, Italy, Canada and the Russian Federation as well as from the European Commission. European Union countries outside the G-8 can provide bilateral development assistance to India provided that they commit a minimum annual development assistance of US $ 25 million to India. Despite the change in policy, funding of all the ongoing programs and projects was continued as per earlier provisions until their completion. Bilateral assistance is welcomed if it is in the form of technical assistance programmes that aim at enhancement of knowledge/skills of Indian nationals. A
component for provision of equipment/hardware is allowed, if the expenditure on these is insignificant compared to the total project cost. However, the main emphasis is on enhancement of the knowledge and skills of Indians. Bilateral development assistance can also be received by the government, if the assistance is routed through or co-financed with a multilateral agency and the proposed programme/project is to be implemented by the multilateral agency under its own rules and procedures. Such arrangements should be evolved between the participating multilateral and bilateral agencies as part of their policies. Such co-financed programmes or projects would be governed by the procedures applicable to the multilateral agency spearheading the programme/project.²¹

**Revised Guidelines for External Assistance**

External assistance today plays more of a supportive role in financing major infrastructure projects, social sector projects and in building up the institutional capacity. Accordingly, the policy on external assistance has been recast to affirm this changing role of external assistance and to emphasise the reform orientation in India’s economic policy. The revised guidelines as issued in January 2006 emphasise the country’s reduced reliance on external assistance. Multilateral assistance today accounts for nearly 70 per cent of the total assistance to India. Of this, 64 per cent comprises non-
concessional IBRD and ADB loans which are at market rate. The grant component in both these portfolios is negligible. It is felt that though IBRD and ADB loans are market related and therefore costly, the cost of these external loans is still below that of domestic borrowing. This is for the simple reason that domestic interest rates are ruling higher than the international interest rates. Too much reliance on any one source of bilateral funding can also be dangerous.22

Policy on Grant Assistance to Non-Governmental Organisations (NGOs), Autonomous Institutions and Other Such Bodies

All countries can provide bilateral development assistance directly to autonomous institutions, Universities, NGOs, etc. External development partners may consider directing such bilateral assistance towards projects of economic and social importance only. A simplified policy to facilitate the flow of bilateral development assistance to Non Governmental Organisations and autonomous institutions has also been put in place. Bilateral development assistance to these organisations is governed by the Foreign Contribution (Regulation) Act, 1976 and only such organisations that are registered under the said Act, may receive bilateral assistance. Organisations that are not registered under Foreign Contribution (Regulation) Act should obtain prior permission from the appropriate
authority under the said Act. The recipient NGOs, autonomous organisations etc. are required to fill a prescribed proforma and submit it through the concerned external development partner along with their proposals. Department of Economic Affairs does not entertain any direct proposals from NGOs, autonomous organisations, etc. Department of Economic Affairs receives project proposals for funding of NGOs throughout the year so that the process does not suffer delays. The bilateral development partner sends project proposals to the concerned credit division in Department of Economic Affairs when the project concept paper is ready, accompanied by the proforma check-list. Department of Economic Affairs processes the project proposals expeditiously in a time-bound manner. The bilateral development partner country provides information in proforma-II to Department of Economic Affairs in April and October every year on the extent of funding to various organisations and the status of the project. The bilateral partner may transfer funds directly to the accounts of the recipient organisations, after the proposals are approved by Department of Economic Affairs. They may also make their own arrangements for monitoring the physical and financial progress of these projects.²³
Procedure for Disbursement and Release of External Assistance

All external assistance disbursed by the external agencies to Government of India is first received by the central government in the Ministry of Finance, Department of Economic Affairs, Controller of Aid Accounts and Audit (CAA&A).\textsuperscript{24}

Foreign Aid

Foreign aid policy refers to the guidelines which govern the foreign aid strategies of a particular nation. Foreign aid policy helps in the formation of effective procedures with respect to the disbursement of foreign funds between nations.

Objectives of Foreign Aid Policy

Normally, the formulation of policies regarding foreign aid activities are guided by a planned fundamental objectives, some of which are:\textsuperscript{25}

Promotion of Transformational Developments

The aim of such promotional activity is to offer support to the basic changes which govern transformational developments of a country in different spheres, as well as the organizations, manpower and economic frameworks involved with such developments. This, in turn, will bring about progress in the economic and social spheres of a country, without depending on financial aid from foreign nations.
Adherence to this policy leads to sound and stable economic conditions in developing countries.

**Strengthening the Economic Conditions of Weak States**

Following this policy, economically weak nations may lay foundation of a strong economy through introduction of activities like reforms, security, development of competences and stabilisation of the economy.

**Disbursement of Funds for Offering Humanitarian Relief**

Through this policy foreign financial aid can be released on humanitarian grounds such as meeting human requirements during emergencies. Such activity includes helping people to combat natural calamities and man-made disasters (poverty, wars, etc.) and find out ways to minimise suffering.
REFERENCES


4. www.business.mapsofindia.com

5. www.dipp.nic.in

6. www.siadipp.nic.in

7. www.siadipp.nic.in


10. Ibid


12. www.oocities.com