

Capital Markets Hotline

February 01, 2024

A DEEP DIVE INTO RBI'S MASTER DIRECTION ON COMMERCIAL PAPER AND NON-CONVERTIBLE DEBENTURES DIRECTIONS, 2024

BACKGROUND

The Reserve Bank of India ("RBI") on January 3, 2024 issued the Master Direction – RBI (Commercial Paper and Non-Convertible Debentures) Directions, 2024¹ ("Master Directions"). These Master Directions shall be applicable to all persons/agencies dealing in short term money market instruments, primarily commercial paper ("CPs") and non-convertible debentures ("NCDs"), with an original or initial maturity period of 1 (one) year.

The Master Directions will come into force from April 1, 2024 and shall supersede the existing Reserve Bank Commercial Paper Directions, 2017² and Master Direction - Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 2016³. All issuances undertaken before the date of enforcement of the Master Directions shall be governed by the earlier regulations until their maturity period.

ELIGIBILITY CRITERIA FOR ISSUANCE

a. For issuers

Under the Master Directions, the entities which are permitted to issue CPs and NCDs are as follows:

- Companies as defined under the Companies Act, 2013;
- Non-Banking Financial Institutions ("NBFCs"), including Housing Finance Companies ("HFCs") as defined by the RBI;
- InvITs and REITs as defined under the Income-tax Act, 1961;
- All India Financial Institution ("AIF")⁴;
- Any body corporate with a minimum net worth of INR 100 crores which is not barred from incurring debt or issuing debt instruments in India under law;
- Any other entity permitted specifically by RBI for such issuance;
- Co-operative societies and limited liability partnerships with a minimum net worth of INR 100 crores.

In order to be an eligible issuer, the Master Directions have continued to have a criteria that all fund-based facilities from banks, AIFs or NBFCs availed by the issuer should be classified as a standard asset at the time of issue of CPs / NCDs.

The inclusion of InvITs as an eligible issuer can be seen as a big step towards broadening the issuer base for primary and secondary issuances with Securities and Exchange Board of India ("SEBI").

b. For investors

The Master Directions permit (i) all residents to invest in CPs and NCDs issued in India, and (ii) non-residents to invest in CPs and NCDs to the extent permitted under the Foreign Exchange Management Act, 1999 ("FEMA") and the related regulations and rules.

No investor can invest in CPs or NCDs issued by any related party⁵ in the primary or secondary market.

GENERAL GUIDELINES

The RBI has brought in several key amendments to the existing regulatory framework for the primary issuance of CPs and NCDs.

In the primary market, the issuance is mandated to be in dematerialized form and held with a depository registered with SEBI having a minimum denomination of INR 5 lakhs and in multiples of INR 5 lakhs thereafter.

The CPs are required to be issued at a discount to the face value. Likewise, NCDs are required to be issued at a discount to the face value or with a fixed or floating rate coupon. Such coupon rate for NCDs is linked to either (i) a benchmark published by a Financial Benchmark Administrator; or (ii) RBI's policy rates; or (iii) approved by the Fixed Income Money Market and Derivatives Association of India ("FIMMDA") in order to ensure transparency and an arms' length transaction structure. The coupon amount is also included in the repayment of the CPs and NCDs through the relevant intermediary.

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Other key guidelines prescribed under the Master Directions are as follows:

- 1) The Master Directions have prescribed for a tenor of not less than 7 (seven) days and not more than 1 (one) year in case of CPs, and not less than 90 (ninety) days and not more than 1 (one) year in case of NCDs. Further, within the prescribed tenor, settlement has to be completed within 4 (four) days from the date of agreement of the terms of issuance between the issuer and the investor(s) for the payment of funds to the issuer. In the case of a secondary issuance, the settlement shall be completed in latest 1 (one) day from the date of agreement of the terms of issuance between the issuer and the investor(s).
- 2) There is an express prohibition on any primary issuance to include a call/put option in the terms of both CPs and NCDs.
- 3) The primary issuances cannot be underwritten or co-accepted.
- 4) The issuer is required to disclose the end use of the amount raised through CPs and NCDs in the offer document (whether it is to finance current assets and operating expenses or otherwise).
- 5) The Master Directions prescribe the appointment of an Issuing and Payment Agent (“**IPA**”) for the primary issuance of both CPs and NCDs respectively. Additionally, a Debenture Trustee (“**DT**”) shall be appointed in case of a primary issuance of NCDs.
- 6) The Master Directions have also laid down a requirement of a minimum credit rating of ‘A3’ (as per rating symbol prescribed by SEBI) as assigned by a credit rating agency (“**CRA**”).
- 7) Upon the occurrence of any default in case of CPs or NCDs with regards to the payment of coupon / repayment, the issuer shall be restricted to issue any instrument till the earlier of either the entire obligation being repaid, or 6 (six) months having elapsed from the date of such default.
- 8) Under the Master Directions, a buyback offer can be made after 7 (seven) days of the issuance coming into force, in the case of CPs. However, in the case of NCDs, the timeline extends to a period of 90 (ninety) days from the date of issuance. The procedure for such buyback shall be initiated through the IPA and/ or the DT, as the case may be.

REPORTING REQUIREMENTS

The Master Directions set out reporting requirements in case of primary issuance / secondary market transactions / buy-backs / defaults. Further, the Master Directions also prescribe for the IPA, Depositories and DTs to be obligated as per the periodic intervals and in the format prescribed in the Master Directions.

ROLES & RESPONSIBILITIES

The Master Directions outline the duties and obligations of the IPA, Debenture Trustee, and CRA concerning activities in the CPs and NCDs markets. The IPA is responsible for ensuring the issuer's adherence to the prescribed conditions under the Master Directions for issuance of CPs / NCDs., verifying documents and issuing certificates. DTs shall comply with the applicable SEBI regulations, ensure reporting obligations, and are subject to consequences in case of violations. Similarly, CRAs shall be responsible to assess the rating of the CPs/NCDs based on applicable SEBI guidelines.

The RBI may call for any information or seek any clarification from any agency involved in the CP and NCD markets, including but not limited to, issuers, investors, IPAs, debenture trustees, CRAs, depositories, the clearing corporations and the stock exchanges, which in the opinion of the RBI is relevant and the agency shall furnish such additional information and clarification within the time frame specified.

CONCLUSION

The Master Directions have come as a welcome measure in ensuring transparency, compliance, and investor protection in India's financial markets. The regulatory amendments under the Master Directions could be designed to align with the RBI's vision and recommendations outlined in the statement published on June 6, 2019⁶. The short-term money market instruments such as NCDs and CPs being governed by the Master Directions in one place will lead to further clarity on the reporting requirements to ensure that the market functions in a manner RBI prescribes and envisions. Further, the amendments in relation to buyback and related party investment prohibition fall in line with the need for transparency and investor protection. The requirement for the issuance to be in dematerialized form shall result in an additional layer of monitoring by the regulators as well as an ease of investment for the investors.

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You can direct your queries or comments to the authors.

¹Master Direction – Reserve Bank Of India (Commercial Paper And Non-Convertible Debentures) Directions, 2024, January 3, 2024, available at [https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12592#:~:text=CPs%20and%20NCDs%20shall%20be,%2Fput\)%20is%20not%20permitted.](https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12592#:~:text=CPs%20and%20NCDs%20shall%20be,%2Fput)%20is%20not%20permitted.)

²Reserve Bank Commercial Paper Directions, 2017, August 10, 2017, available at <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11089&Mode=0>.

³Master Direction - Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 2016, available at https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=10563.

⁴AIPI shall include: (a) Export Import Bank of India, (b) National Bank for Agriculture and Rural Development, (c) National Housing Bank, (d) Small Industries Development Bank of India and (e) National Bank for Financing Infrastructure and Development.

⁵Related parties shall have the same meaning as assigned to it under Indian Accounting Standard (Ind AS) 24 – Related Party Disclosures or International Accounting Standard (IAS) 24 – Related Party Disclosures or any other equivalent accounting standards.

⁶Second Bi-monthly Monetary Policy Statement, 2019-20 Resolution of the Monetary Policy Committee (MPC) Reserve Bank of India, June 6, 2019, available at https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=47225.

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