In brief: loan document terms in India

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Loan document terms

Standard forms and documentation

What forms or standardised terms are commonly used to prepare the bank loan documentation?

The Indian Banks Association has circulated standard facility documentation for consortium lending, which is followed by most public sector Indian banks. Usually, lenders follow their own individual formats for bilateral financing transactions; however, the clauses across banks are similar.

Private sector banks usually prefer to follow the documentation as prescribed by the Asia Pacific Loan Market Association for syndicated transactions. Most sizeable corporate financing transactions are negotiated, and the documentation is modified accordingly.

Pricing and interest rate structures

What are the customary pricing or interest rate structures for bank loans? Do the pricing or interest rate structures change if the bank loan is denominated in a currency other than the domestic currency?

The interest is calculated by reference to a bank rate. The Reserve Bank of India provides the formula that a bank must use to calculate its marginal cost of funds-based lending rates (MCLR).

Under the external commercial borrowing (ECB) regulations, the interest rate linked to a foreign loan provided in foreign currency may be linked to the six-month LIBOR rate of different currencies or any other six-month interbank interest rate applicable to the currency of borrowing (eg, EURIBOR) to determine the all-in cost for the loan. The benchmark rate in the case of rupee-denominated ECB should be the prevailing yield of the government securities of corresponding maturity. The lenders charge a spread over and above the benchmark rates in accordance with the thresholds prescribed.

Borrowing in foreign currency is usually cheaper compared to borrowing in Indian rupees. However, the hedging costs and currency value fluctuations may negate the initial price advantage gained.

Have any procedures been adopted in bank loan documentation in your jurisdiction to replace LIBOR as a benchmark interest rate for loans?

At present, the market practice is still unclear, and many banks continue to use the LIBOR interest rate where applicable. Recently, the Indian Banks' Association (IBA) has written to companies and industry bodies asking them to prepare for the phasing out of LIBOR. The IBA also formed a working group on LIBOR transition and is in the process of developing a guidance note for banks.

Other loan yield determinants

What other bank loan yield determinants are commonly used?

The MCLR of banks act as the pricing floor for lending in Indian rupees. The practice of granting original issue discount is generally not prevalent in India.

Yield protection provisions

Describe any yield protection provisions typically included in the bank loan documentation.

Almost all loan documentation in India includes provisions for increased cost, prepayment premiums and withholding tax gross-up provisions.

The increased cost provisions are standard clauses in a loan transaction, wherein an obligation is imposed on the borrower to make good any additional cost incurred by the lender on account of changes in the laws and regulations and compliance thereof.

Prepayment premium clauses are also often included as a measure for the lender to recover costs in the event that the borrower repays the loan prior to the maturity date. However, there are certain restrictions on the collection of prepayment premium for floating rate loans by banks.

Indian corporates are usually not required to withhold tax while paying interest to banks in India. However, Indian banks do not insist on grossing up payments for tax withholding for other fees charged. Adequate tax certificates are provided to the banks in this regard. Where the loan transaction is between parties in different jurisdictions, tax gross-up provisions are included.

Accordion provisions and side-car financings

Do bank loan agreements typically allow additional debt that is secured on a pari passu basis with the senior secured bank loans?

Loan agreements usually restrict the borrower from incurring any additional financial indebtedness without the prior approval of the lender. However, additional loans may be allowed on a pari passu basis with the senior secured lender depending on the purpose of the additional financing and the maintenance of adequate security cover.

Financial maintenance covenants

What types of financial maintenance covenants are commonly included in bank loan documentation, and how are such covenants calculated?

Financial covenants included in bank loan documentation usually provide for maintenance of debt service coverage ratios, regulation of cash burn, maintenance of minimum net worth, maintenance of EBITDA ratios and end-use restrictions on borrowed funds. These covenants are usually stricter in loans that are given to special purpose vehicles, which are very common in project financing transactions. However, the financial covenants are generally more relaxed in general corporate financing in large corporates that have multiple verticals and revenue generating streams.

Other covenants

Describe any other covenants restricting the operation of the debtor's business commonly included in the bank loan documentation.

Some other common covenants included in standard loan documentation pertain to:

- negative pledges;
- the disposal of assets;
- restrictions on mergers and acquisitions;
- changes in business;
- changes in management or ownership;
- changes in constitutional documents;
- the payment of dividends; and
- the maintenance of credit rating.

Mandatory prepayment

What types of events typically trigger mandatory prepayment requirements? May the debtor reinvest asset sale or casualty event proceeds in its business in lieu of prepaying the bank loans? Describe other common exceptions to the mandatory prepayment requirements.

When a borrower under debt has received an influx of money owing to the occurrence of an event – for instance, the sale of a branch of the business, the sale of property owned by the business, or proceeds of insurance – the creditor may seek for mandatory prepayment of the loan from those proceeds. The debtor is mandatorily obliged in such an event to direct the proceeds resulting from those events to the payment of the loan, albeit prior to the maturity date, and is not permitted to reinvest the same into its business. Prepayment premiums are usually not imposed upon the occurrence of a mandatory prepayment event.

In some instances, such prepayment may result in adverse tax consequences, in which case the mandatory prepayment may not be enforced.

Debtor's indemnification and expense reimbursement

Describe generally the debtor's indemnification and expense reimbursement obligations, referencing any common exceptions to these obligations.

Where a creditor incurs expenditure or undertakes a liability on behalf of the borrower, the creditor may require the borrower to repay the expenditure or indemnify it for any loss caused. Those terms are generally included in the loan documentation and may include indemnification for any default and repayment of transaction costs, amendment costs, stamp duty, security agent or trustee fees, the cost of litigation, etc, in relation to the loan transaction. The obligation on the debtor is waived only when the loss or cost is incurred by the creditor owing to its own gross negligence or wilful misconduct.

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Give the date on which the above content is accurate.

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