



Scheme

Financing Infrastructure Projects through the India Infrastructure Finance Company Limited (IIFCL)

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Secretariat for the Committee on Infrastructure

Preface

This initiative addresses the need for providing long-term debt for financing infrastructure projects that typically involve long gestation periods. Debt finance for such projects should be of a sufficient tenure that enables cost recovery across the project life. Indian capital markets, however, are deficient in long-term debt instruments. Setting up of the India Infrastructure Finance Company (IIFC) is aimed at bridging the gap.

Underdeveloped pension and long-term debt markets have restricted the tenure of project finance in India. Most of the available debt is of seven to twelve years, maturity whereas infrastructure projects require a longer pay back period. This constraint leads to front loading of tariffs during the initial years of the project cycle with a view to ensuring repayment of debt. Besides affecting the users, this handicap also affects the competitiveness of infrastructure projects.

This scheme was evolved by the Ministry of Finance after extensive deliberations with the Planning Commission, financial institutions, experts and other stakeholders. The scheme thus formulated was considered and approved by the Committee on Infrastructure, chaired by the Prime Minister, and subsequently endorsed by the Union Cabinet.

The India Infrastructure Finance Company (IIFC) has since been corporatised and operationalised. It will provide financial assistance through long term debt; either by way of refinance to banks and financial institutions or by direct lending to project companies. It will lend up to 20% of the capital costs of a project. For project appraisal and lending operations, IIFC would rely on the lead banks associated with the respective projects. Built into this scheme is a preference for Public Private Partnership (PPP) projects that are awarded to private companies selected through a competitive bidding process. Such projects will be eligible for direct lending by IIFC, and will also receive overriding priority.

IIFC will raise funds from both domestic as well as external markets on the strength of government guarantees, which will be extended as necessary. In the first year of its operation, a guarantee limit of Rs.10,000 crore (US\$ 2.2 billion) has been specified by the Government.

IIFC is expected to provide the much needed long-term debt for financing infrastructure projects. In doing so, it will play a catalytic role in building world-class infrastructure in India.

(Gajendra Haldea)
Adviser to Deputy Chairman

Scheme for Financing Infrastructure Projects through the India Infrastructure Finance Company Limited (IIFCL)

The scheme was notified by the Ministry of Finance, Department of Economic Affairs vide O.M. No. 10/12/2005-INF dated 4th January 2006.

1. Introduction

- A. Whereas the Government of India recognizes that there is significant deficit in the availability of physical infrastructure across different sectors and that this is hindering economic development.
- B. Whereas the development of infrastructure requires debt of longer maturity to supplement the debt funds presently available; and
- C. Whereas the Government of India recognizes that such debt is usually not available because of the following constraints:
- (a) Absence of benchmark rates for raising long term debt from the market;
 - (b) Asset-liability mismatch of the tenor of debt in case of most financial institutions; and
 - (c) High cost of long term debt.
- D. Now, therefore, the Government of India has decided to put into effect the following scheme for providing financial support to improve the viability of infrastructure projects.

2. Short Title and Extent

2.1 The Scheme will be called the Scheme for financing Viable Infrastructure Projects. It will be administered by the Ministry of Finance through IIFCL.

2.2 The Scheme will come into force with immediate effect.

3. Definitions

3.1 In this Scheme unless the context otherwise requires:

- (a) **Empowered Committee** means a Committee set up for the purposes of this Scheme under the chairmanship of Secretary (Economic Affairs) and including Secretary, Planning Commission, Secretary (Expenditure) , Secretary (Financial Sector) and in his absence Special Secretary / Additional Secretary (Financial Sector) and Secretary of the line Ministry dealing with the subject;
- (b) **IIFCL** means the India Infrastructure Finance Company Ltd (a company incorporated under the Companies Act, 1956);
- (c) **Lead Bank** means the Financial Institution (FI) that is funding the project and is designated as such by the Inter-Institutional Group or consortium of financial institutions; provided the risk exposure of IIFCL is less than that of the lead bank in a project;

- (d) **Long Term Debt** means the debt provided by the IIFCL to the Project Company where the average maturity for repayment exceeds 10 years;
- (e) **Private Sector Company** means a company in which 51% or more of the subscribed and paid-up equity is owned and controlled by private entities;
- (f) **Project Company** means the company which is implementing the infrastructure project for which assistance is to be given by the IIFCL;
- (g) **Project Term** means the duration of the contract or concession agreement for a PPP project;
- (h) **Public Private Partnership (PPP) Project** means a project based on a contract or concession agreement, between a Government or a statutory entity on the one side and a Private Sector Company on the other-side, for delivering an infrastructure service on payment of user charges;
- (i) **Public Sector Company** means a company in which 51% or more of the subscribed and paid-up equity is owned and controlled by the Central or a State Government, jointly or severally, and includes any undertaking designated as such by the Department of Public Enterprises and companies in which majority stake is held by Public Sector Companies other than financial institutions; and
- (j) **Total Project Cost** means the lower of the total capital cost of the project:
 - (i) as estimated by the government/ statutory entity that owns the project;
 - (ii) as sanctioned by the Lead Bank; and
 - (iii) as actually expended.

But does not include the cost of land incurred by the government/ statutory entity.

4. Funding of IIFCL

4.1 Apart from its equity, the IIFCL shall be funded through long-term debt raised from the open market. This debt can be any or all of the following:

- (a) Rupee debt raised from the market through suitable instruments created for the purpose; the IIFCL would ordinarily raise debt of maturity of 10 years and beyond.
- (b) Debt from bilateral or multilateral institutions such as the World Bank and Asian Development Bank.
- (c) Foreign currency debt, including through external commercial borrowings raised with prior approval of the Government.

4.2 The IIFCL would raise funds as and when required, for on lending, in consultation with the Department of Economic Affairs. The magnitude of funds raised would be determined by demand from viable infrastructure projects. To the extent of any mismatch between the raising of funds and their disbursement, surplus funds would be invested in marketable government securities.

4.3 The borrowings of IIFCL may be guaranteed by the Government of India. The extent of guarantees to be provided shall be set at the beginning of each fiscal year by the Ministry of Finance, within the limits available under the Fiscal Responsibility & Budget Management Act. However, bonds issued by IIFCL, unless otherwise directed by Government of India, will not be included against Statutory Liquidity Ratio requirements. For 2005-06, the extent of guarantee to be provided by Government of India will be Rs.10,000 crore.

4.4 The guarantee fee payable by the IIFCL would be 0.25% per annum on outstanding balances.

4.5 The facility of guarantees including the terms for guarantee will be reviewed after 5 years, and its continuation shall be subject to the outcome of the review.

5. Eligibility

5.1 The IIFCL shall finance only commercially viable projects. Viable projects may also include those projects that will become viable after receiving viability gap funding under a government scheme.

5.2 In order to be eligible for funding under this Scheme, a project shall meet the following criteria:

- (a) The project shall be implemented (i.e. developed, financed and operated for the Project Term) by:
- (i) A Public Sector Company;
 - (ii) A Private Sector Company selected under a PPP initiative; or

(iii) A Private Sector Company

Provided that IIFCL shall assign overriding priority to Private Public Partnership projects that are implemented by Private Sector Companies selected through a competitive bidding process.

Provided further that a Private Sector Company, other than that defined in the first proviso above, would not be eligible for direct lending by IIFCL and may be funded only through the refinance mode. The total lending for such private projects shall not exceed 20% of the lending programme of IIFCL in any accounting year. The eligibility for direct lending and/or raising the limit of 20% will be reviewed at the end of one year having regard to the progress made in funding public sector and PPP infrastructure projects.

Provided also that the IIFCL may lend directly to projects set up by Private Sector Companies subject to the following conditions:

- (i) The service to be provided by the infrastructure project is regulated, or the project is being set up under an MOU arrangement with the Central Government, any State Government or a PSU;
- (ii) the tenor of IIFCL lending should be longer than that of the longest tenor commercial debt by at least two years; and
- (iii) direct lending plus the refinance business, if any, on account of this category of borrowers (Private Sector Companies not selected through a competitive bidding process) should not exceed 20% of the total lending by IIFCL in any accounting year. (This limit is the same as the limit

currently imposed for the refinance window.)

- (b) Provided that in case of Railway projects that are not amenable to operation by a Private Sector Company, the Empowered Committee may relax the eligibility criterion relating to operation by such company.
- (c) The project should be from one of the following sectors:
 - (i) Roads and bridges, railways, seaports, airports, inland waterways and other transportation projects;
 - (ii) Power;
 - (iii) Urban transport, water supply, sewage, solid waste management and other physical infrastructure in urban areas;
 - (iv) Gas pipelines;
 - (v) Infrastructure projects in Special Economic Zones; and
 - (vi) International convention centres and other tourism infrastructure projects.

Provided that the Empowered Committee may, with approval of the Finance Minister, add or delete any sector/sub-sectors from this list.

5.3 Only such projects which are implemented through a Project Company set up on a non-recourse basis shall be eligible for financing by IIFCL.

It is clarified that only such projects, which are implemented by the borrower company directly,

or through a special purpose vehicle, on a non-recourse basis, shall be eligible for financing by IIFCL.

It is further clarified that the aforesaid would be subject to maintaining an escrow account which may be entrusted to any bank involved in financing of the project and the discretion with regard to the bank would be that of the Board of Directors of IIFCL.

5.4 In the event that the IIFCL needs any clarification regarding eligibility of a project, it may refer the case to the Empowered Committee for appropriate directions.

6. Appraisal & Monitoring by Lead Bank

6.1 The Lead Bank shall present its appraisal of the project for the consideration of the IIFCL. Based on such appraisal, the IIFCL may consider and approve funding to the extent indicated in Article 7 below.

6.2 The IIFCL will not normally be required to carry out any independent appraisal of the project.

6.3 The Lead Bank shall be responsible for regular monitoring and periodic evaluation of compliance of the project with agreed milestones and performance levels, particularly for purpose of disbursement of IIFCL funds. It shall send periodic progress reports in such form and at such times, as may be prescribed by IIFCL.

7. Lending Terms

7.1 The IIFCL may fund viable infrastructure projects through the following modes:

- (a) Long Term Debt;
- (b) Refinance to Banks and Financial Institutions for loans, with tenor exceeding 10 years, granted by them; and
- (c) Any other mode approved by Government from time to time.

7.2 The Project Company will have the right to choose any of the modes of lending given above. The terms at which the Project Company can access Long Term Debt shall not be inferior to the terms at which refinanced debt is available to the Project Company.

7.3 The total lending by the IIFCL to any Project Company shall not exceed 20% of the Total Project Cost. Loans will be disbursed in proportion to debt disbursements from financial institutions.

7.4 The rate of interest charged by IIFCL shall be such as to cover all funding costs including administrative costs and guarantee fee, if any.

7.5 The IIFCL will release funds to the Lead Bank as and when due. The Lead Bank/FI consortium will make disbursements on behalf of the IIFCL and seek reimbursement which shall be made within one month of receiving a demand, with necessary particulars, from the Lead Bank.

7.6 Recovery of loans advanced by IIFCL shall be the responsibility of the Lead Bank. Recovery of IIFCL loans shall be *pari passu* with project debt (other than subordinate debt) till 80% of the project debt (other than subordinate debt) of the Lead

Bank and FI consortium (inclusive of interest due) has been recovered. Thereafter the Lead Bank/FI Consortium would assume the payment risk as guarantors of the IIFCL loan from that stage onwards.

Provided, however, that IIFCL may not insist on guarantee by the Lead Bank, but it shall position on its staff, personnel with expertise in risk assessment, and the regulatory norms that should govern IIFCL shall be defined and brought into operation at the earliest.

7.7 The charge on project assets shall be *pari passu* with project debt (other than subordinate debt) and will continue beyond the tenure of project debt (other than subordinate debt) till such time the amounts lent by IIFCL, together with interest and other charges thereon remain outstanding.

7.8 The IIFCL, the Lead Bank and the Project Company shall enter into a Tripartite Agreement for the purposes of this scheme. The format of such Tripartite Agreement shall be prescribed by the Empowered Committee from time to time.

7.9 In the first two years of operation of the Scheme, projects meeting the eligibility criteria could be funded on a first-come, first served basis. In later years, if need arises, funding may be provided based on an appropriate formula, to be determined by the Empowered Committee that balances needs across sectors in a manner that would broad-base sectoral coverage and avoid pre-empting funds by a few large projects.

7.10 Subordinate Debt

IIFCL may provide Debt which ranks lower in security than the project debt carrying a

pari passu charge (the “**Subordinate Debt**”) to finance PPP Projects subject to the following conditions:

- (a) The project should have been awarded through open competitive bidding;
- (b) it should have been approved by the PPPAC (Public Private Partnership Approval Committee) under the Guidelines for Formulation, Appraisal and Approval of PPP projects or by the Empowered Institution under the Guidelines for Financial Support to PPP in infrastructure;
- (c) the concession agreement should provide for an escrow account that would secure the annual repayment of Subordinate Debt before returns on equity are paid;
- (d) in case of termination of concession agreement, the concessioning authority will pay in terms of termination payment at least 80% of the Subordinate Debt on account of a concessionaire default or concessioning authority default, during operation period of the concession, in the escrow account as mentioned in the Model Concession Agreement (MCA). Where MCA is not available, a similar provision should be incorporated;
- (e) Subordinate Debt shall not exceed 10% of the Total Project Cost and shall form part of the maximum limit of 20% as specified in para 7.3 of the SIFTI;
- (f) Subordinate Debt to be borrowed by the Project Company from any or all sources shall not exceed one half of its paid up and subscribed equity;
- (g) interest on Subordinate Debt shall be 2% to 3% higher than the highest interest charged by any bank in the consortium of lenders for the project;
- (h) there may be a moratorium of 4 to 5 years on repayment of principal and interest due in respect of Subordinate Debt. IIFCL may take this aspect into account while assessing the project’s viability;
- (i) repayment of principal shall not commence before 6 to 7 years from the Commercial Operation Date (COD) of the project and shall extend between a period of 12 to 15 years from COD;
- (j) Subordinate Debt lenders shall have second charge on all assets (including receivables) of the Borrower, both present and future, to secure the Subordinate Debt in accordance with the loan agreement. The said second charge to secure Subordinate Debt shall rank *pari passu* with all lenders for their subordinate debts. The aforesaid second charge of subordinate debt lenders shall be subordinate to the first *pari passu* charge of the senior lenders for their senior debts; and
- (k) Subordinate Debt shall not be converted into equity.

8. Lending to PPP Projects

8.1 A project awarded to a Private Sector Company for development, financing, construction, maintenance and operation through Public Private Partnership (as defined in the Scheme for Viability Gap

Funding) shall be accorded priority for lending under this Scheme.

8.2 In case of PPP projects, the private Sector Company shall be selected through a transparent and open competitive bidding process.

8.3 PPP projects based on standardized/ model documents duly approved by the respective government would be preferred. Standalone documents may be subjected to detailed scrutiny by the IIFCL.

8.4 Prior to inviting offers through a open competitive bid, the concerned government or statutory entity may seek 'in principle' approval of the IIFCL for financial assistance under the Scheme. Any indication given by IIFCL at the pre-bid stage shall not be treated as a final commitment. Actual lending by IIFCL shall be governed by the appraisal by the Lead Bank carried out before financial closure of the project.

9. Review of the Scheme

9.1 The Scheme may be reviewed by the Government at the end of 5 years or earlier if required. The continuation of the Scheme, with or without modifications, will be dependent on the outcome of such a review.

9.2 IIFCL would be regulated directly by the Government and a *sui-generis* regulatory regime for IIFCL may be brought into operation at the earliest.

9.3 In order to avoid frequent references to the Cabinet on procedural matters, modifications to the SIFTI may be made at the level of Empowered Committee already set-up under the Scheme subject to the

approval of the Finance Minister and the Prime Minister.

9.4 An Oversight Committee of Secretaries would be constituted for reviewing the working of IIFCL on a bi-annual basis.

9.5 The debt equity ratio in respect of the road sector projects considered for financing may not exceed 4:1.