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*Analysis*

# Investing in the Indian Securitisation Market: A Legal Primer for Foreign Investors

## Key Takeaways

- India's securitisation market is growing, offering attractive opportunities for not just lenders but also non-financial entities like SaaS companies
- Investment opportunities are also now open to FPIs, outside the RBI Framework
- Currently SEBI and RBI have their own securitisation frameworks. We examine –
  - What assets can be securitised?
  - SEBI is considering expanding the scope of what can be securitised – Will this catalyse dealmaking?
  - What are the differences between the RBI and SEBI frameworks, and what is a true sale?

Securitisation in India, though still a relatively new concept, is rapidly evolving beyond its traditional forms, with discussions underway regarding innovative structures and new approaches. As the market grows, it presents an increasingly attractive opportunity, particularly for foreign investors seeking stable yet significant returns in a fast-growing economy.

India's favourable demographics, characterised by a large middle class, coupled with the strong demand for credit, could make securitised products a promising destination for foreign investment.

This paper explores securitisation in India, covering the following topics –

- Why securitise?
- How is securitisation regulated in the Indian context?
- Use cases –
  - Can a foreign investor buy the loan portfolio of an NBFC?
  - Can a SaaS company securitise and sell its receivables to a foreign investor?
- What are the other considerations to be kept in mind?

## Why securitise?

Benefits for originators:

- *Quick cash flow for otherwise illiquid assets*. A dollar today is more valuable than it is tomorrow. Originators can convert illiquid loans into liquid cash, improving liquidity.

- *Balance sheet relief*. Banks are required to hold capital in proportion to their risk-weighted assets – essentially, the higher the risk of the assets on their balance sheets, the more capital they must hold. Securitisation removes these assets from banks' balance sheets, freeing up capital to be used for other purposes.

- *Addresses asset-liability mismatch*. When assets and liabilities have different maturities, the bank risks facing cash flow issues – especially if short-term obligations arise before long-term assets mature. By converting illiquid assets into immediate cash through securitisation, banks can effectively prevent these mismatches.

- *Risk transfer*. Securitisation enables the transfer of the risk of non-payment or defaults from the originator to investors. If borrowers fail to repay the underlying debt, the loss is borne by investors holding the securities, rather than the originator.

Benefits for foreign investors:

- Relatively low risk, fixed-income securities with regular coupons

- Portfolio diversification

- Attractive risk-adjusted returns – For example, Grip Invest, a high-yield investment platform regulated by SEBI, claims to have launched India's first credit-rated Securitised Debt Instrument ("**SDI**"), offering returns of 12-14% on its SDI products.

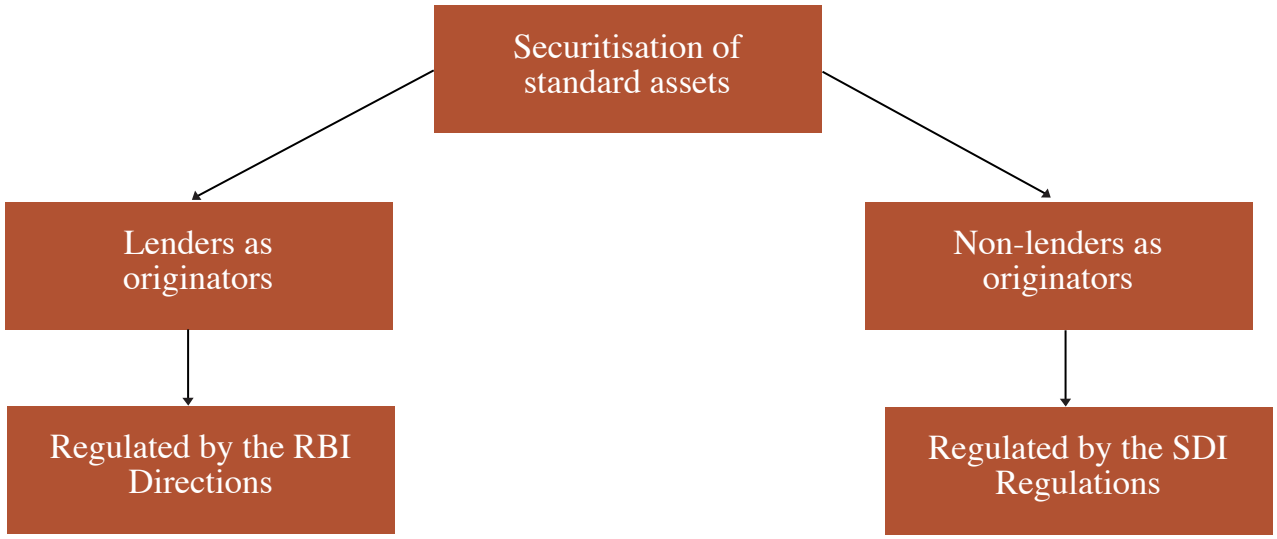
## How is the securitisation market in India regulated?

Dual Supervision by RBI and SEBI – Mutually exclusive?

Securitisations fall into two broad categories, based on the nature of the underlying assets – (a) securitisation of standard assets, and (b) securitisation of sub-standard assets. The focus of this paper is the former, and standard assets are securitised under the supervision of –

a. the Reserve Bank of India (**RBI Directions**[1]) and
b. the Securities and Exchange Board of India (**SDI Regulations**[2]).

The RBI regulates securitisation by banks and non-banking financial companies (NBFCs), while SEBI primarily supervises securitisation by non-lenders when securities are offered to the public or listed. Securities issued under the SEBI framework are termed 'Securitised Debt Instruments[3]' and can be issued by non-lenders through private placements or public offers. The two frameworks intersect when securities issued under the RBI Directions are subsequently listed under the SDI Regulations. The illustration below depicts how the securitisation of standard assets is regulated –




## Can foreign investors participate in securitisation transactions?

Yes, they can. Foreign Portfolio Investors (FPIs) have been permitted to invest in Securitised Debt Instruments since 2017, although the SDI Regulations were enacted in 2008.

This change began with amendments to the FPI Regulations, followed by the inclusion of SDIs as a permitted security in the FEMA Debt Regulations[4]. When this change was initially introduced, non-lender SDIs had to be listed for FPIs to be able to invest in them. However, this requirement has since been removed, permitting FPIs to invest in unlisted SDIs.

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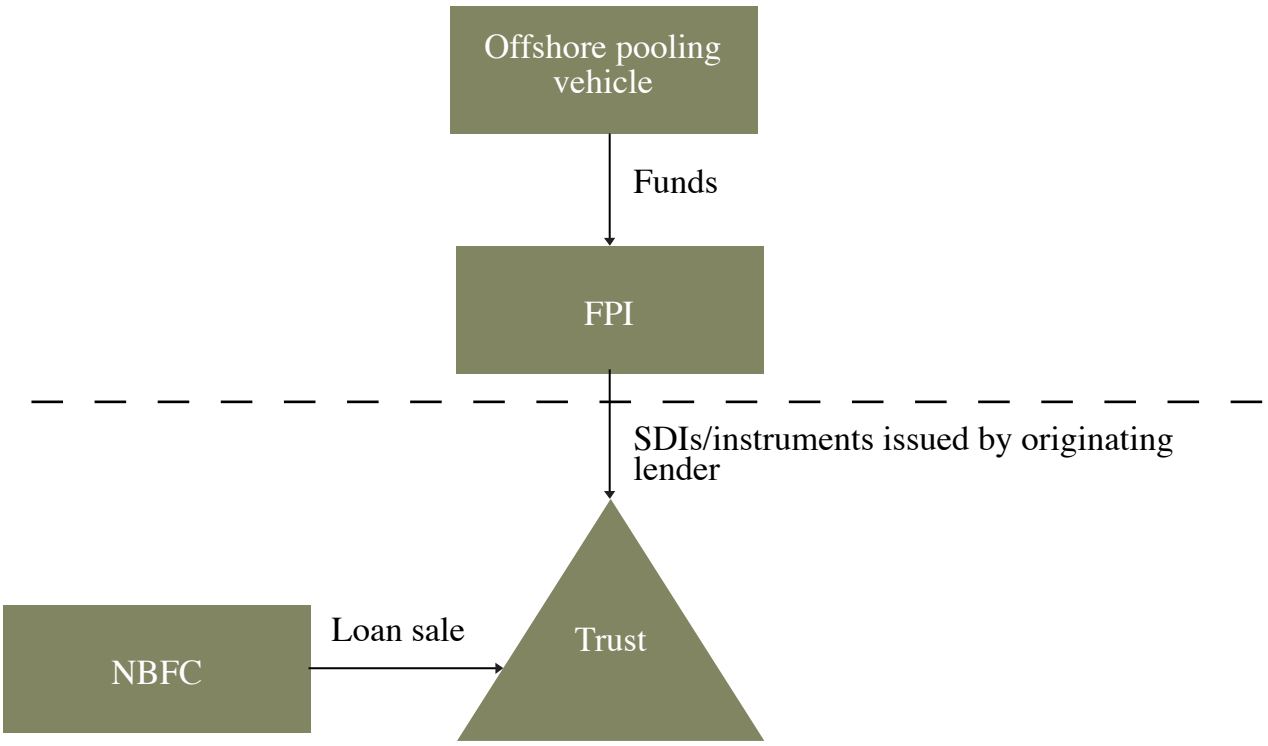
[1] *https://www.rbi.org.in/scripts/bs_viewmasdirections.aspx?id=12165*.
[2] *https://www.sebi.gov.in/legal/regulations/aug-2023/sebi-issue-and-listing-of-securitised-debt-instruments-and-security-receipts-regulations-2008-last-amended-on-august-18-2023-_76336.html*.
[3] Annexure I – Key definitions.
[4] FPIs are permitted to purchase "*Securitised debt instruments, including (i) any certificate or instrument issued by a special purpose vehicle (SPV) set up for securitisation of asset/s with banks, Financial Institutions or NBFCs as originators*".

It is important to note that foreign exchange laws are subject to a strict interpretation, meaning only explicitly permitted investments are allowed. So, for an FPI to invest in an SDI, the security must qualify as one under the definition provided in the SDI Regulations.[5]

It may also be helpful to consider a few examples of how such an investment could play out –

**1. RBI Directions – Can a foreign investor purchase the loan book of an NBFC?**

Yes, an FPI can invest in the loan portfolio of an NBFC or bank through SDIs




The NBFC would first securitise the underlying assets in compliance with the RBI Directions, before issuing securities to foreign investors through an SPE (which may be set up as a trust).

This framework could allow foreign pooled funds, through a registered FPI entity, to access segments of the Indian financial market that would otherwise be off-limits. The combination of high transaction volumes, favourable interest rates on retail credit, and relatively low default risk on small-scale lending could offer attractive returns to investors.

[5] Annexure I – Key definitions.

## 2. SDI Regulations – Could a SaaS company securitise and sell its receivables to foreign investors?

As discussed above, FPIs are permitted to invest in SDIs. The key question that follows is: What can be securitised to create an SDI?

Reg. 2(1)(g) of the SDI Regulations defines 'debt' or 'receivables' that can be securitised as follows –

*"debt" or "receivables" means any right that generates or results into a cash flow and includes*

*i. mortgage debt;*

*ii. such receivables arising out of securities as may be specified by the Board;*

*iii. any financial asset within the meaning of clause (l) of sub-section (1) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (54 of 2002).*

While the term "includes" suggests an illustrative and non-exhaustive definition, SEBI's approach in this regard remains unclear[6]. Additionally, with reference to *(iii)* above, the SARFAESI Act's definition of a 'financial asset' is also broad, and one could argue that this should allow most non-lenders to securitise their receivables[7].

In any case, the working group reviewing the SDI Regulations has recommended expanding and clarifying the scope of this definition. Their proposal seeks to explicitly include rental, equipment leasing, warehouse, and invoice receivables under the SDI Regulations, while also incorporating the definition of "receivables[8]" from the Factoring Regulation Act.

Building on this recommendation, SEBI's December 2024 Board Meeting, and Memorandum to this effect, indicate a willingness to refine this definition and clarify any ambiguities. If the forthcoming amendments explicitly include trade and invoice receivables within the scope of the SDI framework, this could provide much-needed clarity and encourage participation from a broader range of originators, including SaaS or rental/leasing companies.

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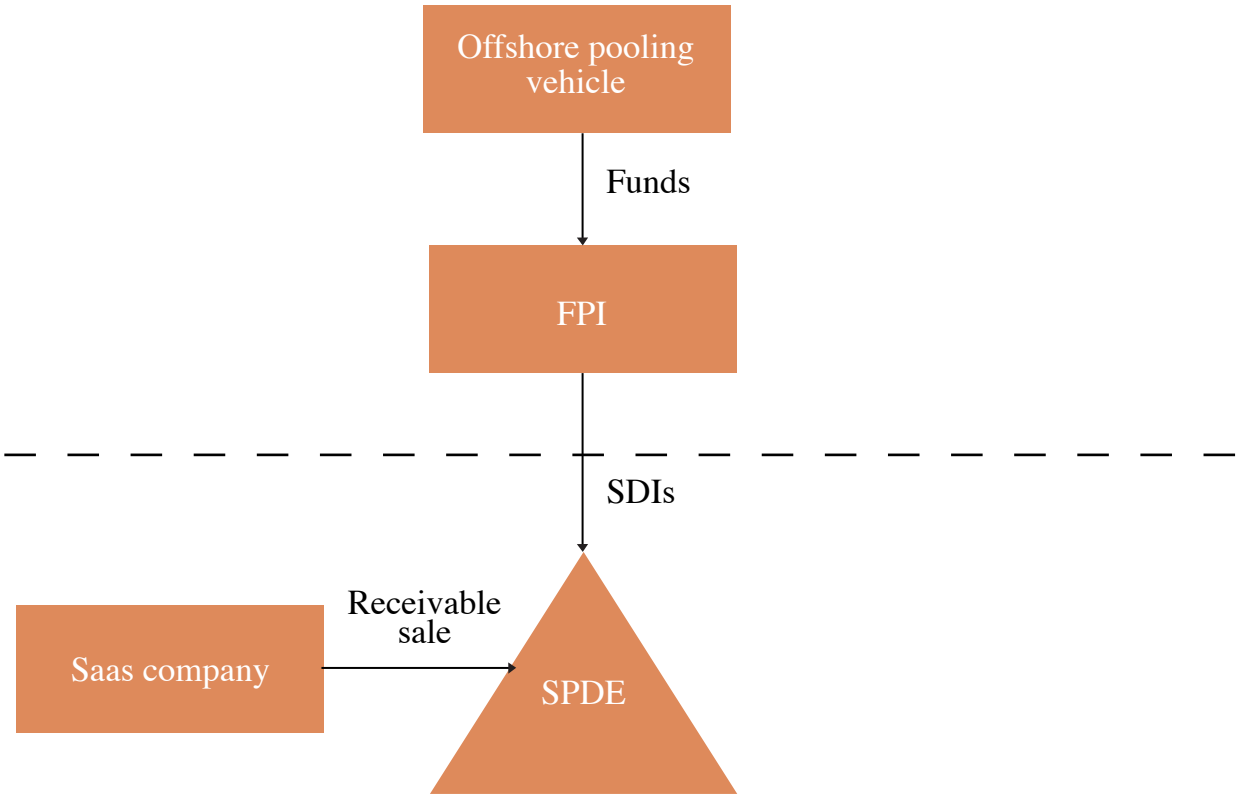
[6] The Report of the Working Group on the Review of SDI Regulations (October 2024) suggested that the definition under Regulation 2(1)(g) is exhaustive and covers only the three categories mentioned in the provision. The report also highlights that the regulations do not explicitly include other types of receivables.

[7] While the SARFAESI Act primarily applies to sub-standard assets, the standalone definition of a financial asset (Annexure-I) is not restricted by such qualifiers.

[8] Receivable means the money owed by a debtor and not yet paid to the assignor for goods or services and includes payment of any sum, by whatever name called, required to be paid for tolls or the use of any infrastructure facility or services."

[9] Annexure I – Key Definitions – definition of an SPDE.

A SaaS company, or an entity with steady cash flows, could securitise receivables through the following structure[9] –




**3. Are there any other differences between the two frameworks?**

The RBI Directions and SDI Regulations not only distinguish between securitisation by lenders and non-lenders but also differ in other aspects. For instance, the RBI Directions mandate a Minimum Retention Requirement (MRR) and a Minimum Holding Period (MHP) for securitised assets. These restrictions ensure that lenders do not 'originate to sell' and lend prudently. The SDI Regulations impose no such requirements.

Common element – True Sale

Despite their differences, both regulatory frameworks[10] incorporate the principle of a 'true sale' detailed below. A true sale is an essential component of securitisation across jurisdictions.

[10] Annexure-II

### What is a True Sale?

A true sale means a complete transfer of ownership and interest in the originated assets to the buyer i.e. the SPE. It results in the immediate legal seperation of the originator from the assets being sold.

By achieving a true sale, the loans or receivables are isolated from the originating party. This protects the transferred assets from the originator's creditors if the originator goes bankrupt.

The RBI broadly prescribes the following guidelines to achieve a true sale[11] —

- Sale between originator and SPE at arm's length for cash consideration
- Transfer of all risks / rewards and rights / obligations pertaining to the asset
- No obligation for the originator to repurchase or fund the repayment of the assets except those arising from breach of warranties or representations

While there are regulatory guidelines in place for achieving a true sale, results have been mixed, particularly due to the challenge of achieving bankruptcy remoteness in practice. Market participants have also highlighted practical difficulties in loan documentation, and servicing challenges surrounding the transfer of the ownership of a loan to an SPE, as being deterrents to achieving a true sale.

## Conclusion

Securitisation is a powerful financial tool that converts assets into liquid securities, enabling businesses to efficiently leverage receivables and raise capital. For investors, it offers diversification opportunities, access to niche markets, and the potential for attractive returns.

However, despite its potential, regulatory uncertainty appears to be a key challenge to broader adoption of the SDI Regulations by non-lenders. Anticipated amendments to the SDI Regulations, including an expanded scope, could unlock significant opportunities in the sector. A clearer and more inclusive regulatory framework may pave the way for greater foreign investor participation in securitised assets. Importantly, a broader range of non-lenders could begin securitising and selling assets to offshore investors, fostering a more dynamic and globally integrated securitisation market.

[11] Master Circulars - Miscellaneous Instructions to all Non-Banking Financial Companies.

## Annexure I – Key definitions

Master Direction – Reserve Bank of India (Securitisation of Standard Assets) Directions, 2021

1. *Special Purpose Entity* – means a company, trust or other entity organised for a specific purpose, the activities of which are limited to those appropriate to accomplish the purpose of the SPE, and the structure of which is intended to isolate the SPE from the credit risk of an originator.

SEBI (Issue and Listing of Securitised Debt Instruments and Security Receipts) Regulations, 2008

1. *Securitisation* – means acquisition of debt or receivables by any special purpose distinct entity from any originator or originators for the purpose of issuance of securitised debt instruments to investors based on such debt or receivables and such issuance.

2. *Securitised Debt Instrument (vide the Securities Contract Regulations Act)* – any certificate or instrument (by whatever name called), issued to an investor by any issuer being a special purpose distinct entity which possesses any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receivable, including mortgage debt, as the case may be.

3. *Special Purpose Distinct Entity (SPDE)* – means a trust which acquires debt or receivables out of funds mobilized by it by issuance securitised debt instruments through one or more schemes.

Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest (SARFAESI) Act, 2002

1. *Financial asset* – means debt or receivables and includes—

i. a claim to any debt or receivables or part thereof, whether secured or unsecured; or
ii. any debt or receivables secured by, mortgage of, or charge on, immovable property; or
iii. a mortgage, charge, hypothecation or pledge of movable property; or
iv. any right or interest in the security, whether full or part underlying such debt or receivables; or
v. any beneficial interest in property, whether movable or immovable, or in such debt, receivables, whether such interest is existing, future, accruing, conditional or contingent; or
vi. any beneficial right, title or interest in any tangible asset given on hire or financial lease or conditional sale or under any other contract which secures the obligation to pay any unpaid portion of the purchase price of such asset or an obligation incurred or credit otherwise provided to enable the borrower to acquire such tangible asset; or
vii. any right, title or interest on any intangible asset or licence or assignment of such intangible asset, which secures the obligation to pay any unpaid portion of the purchase price of such intangible asset or an obligation incurred or credit otherwise extended to enable the borrower to acquire such intangible asset or obtain licence of the intangible asset; or
viii. any financial assistance

## Annexure II – Regulation 10, SEBI (Issue and Listing of Securitised Debt Instruments and Security Receipts) Regulations, 2008

Assignment of debt or receivables

(1) The originator and the trustee shall ensure in respect of the debt or receivables assigned to the special purpose distinct entity that the following conditions are fulfilled:

(a) the debt or receivables generates or is reasonably expected to generate identifiable cash flows for the purpose of servicing the securitised debt instruments in accordance with the scheme;

(b) the originator has a valid enforceable interest in the assets and in the cash flow of the assets prior to the securitisation;

(c) the debt or receivables is free from any encumbrances or impediments to their free transfer or the transfer of the rights attaching thereto and their transfer does not constitute an event of default or acceleration trigger under any agreement;

(d) the necessary regulatory or contractual permissions or consents have been obtained in order to effect the transfer of such debt or receivables from the originator to the special purpose distinct entity;

(e) the originator has not done or omitted to do anything which enables any of his debtors to exercise the right of set-off in relation to such assets;

(f) the debt or receivables is transferred at a price arrived at through an arms' length transaction and solely on commercial considerations; and

(g) any representations and warranties made by the originator regarding the debt or receivables are duly adhered to.

(2) The special purpose distinct entity and the originator shall take all necessary steps to ensure that the debt or receivables acquired by the special purpose distinct entity are duly assigned in its name and are legally realizable by it.

(3) No special purpose distinct entity shall acquire any debt or receivables from any originator which is part of the same group or which is under the same management as the trustee.

(4) The securitisation transaction shall be structured in such a manner so as to minimise the risk of the asset pool being consolidated with the assets of the originator or the sponsor, in the event of insolvency or winding up of either of them.

(5) The special purpose distinct entity and its trustees shall ensure that the debt and receivables assigned to it are through a genuine transaction amounting to a true sale and are legally realizable by it and the special purpose distinct entity shall be remote from the risk of bankruptcy, insolvency and winding up of the originator, sponsor and any other entity.

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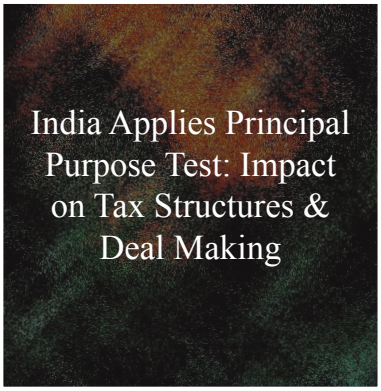





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