
August 2025

# Reserve Bank of India issues new directions to govern Non-Fund Based credit facilities

With a view to harmonise and consolidate the regulatory framework for extending Non-Fund Based ("**NFB**") facilities (particularly guarantees and co-acceptances), the Reserve Bank of India ("**RBI**"), on August 6, 2025, has issued the Non-Fund Based Credit Facilities Directions, 2025 ("**NFB Directions**"). The NFB Directions also include specific guidelines for Partial Credit Enhancement ("**PCE**") facility, which aim to strengthen the bond market, for, *inter alia*, bonds issued by corporates to fund projects. The NFB Directions will be applicable from April 1, 2026, or at an earlier date as adopted by a regulated entity in accordance with its internal policy.

## Applicability

The NFB Directions are applicable to the following entities (referred to as Regulated Entities "**REs**" under the NFB Directions):

1. the NFB Directions in entirety are applicable to commercial banks (such as Regional Rural Banks ("**RRB**") and local area banks); primary (urban) co-operative banks/state co-operative banks/central co-operative banks; and All India Financial Institutions ("**AIFI**"); and
2. only PCE framework under the NFB Directions are applicable to Non-banking Finance Companies ("**NBFC**") in the middle layer (including Housing Finance Companies ("**HFCs**")) and above.

Further, the NFB Directions are not applicable to derivative exposure of REs, however REs are still required to adhere to the general conditions laid down in Chapter II of the NFB Directions (as also synopsised below) in respect of their derivative exposures.

## General regulatory conditions

The NFB Directions stipulate certain general conditions required to be complied by REs for issuance of an NFB facility (including derivative exposures), which *inter alia* require REs to establish an internal credit policy for issuance of NFB facilities, covering aspects such as limits, credit appraisal, security requirement, fraud prevention, and monitoring.

Further, the NFB Directions have simplified regulations relating to the issuance of NFB facilities by REs for those customers who have not availed a fund-based credit facility from such RE. Generally, issuance of an NFB facility to such customers is prohibited, however, the restriction is not applicable for the following:

 

1. derivative contracts;
2. PCE facility;
3. NFB facility backed by a counter-guarantee from another RE;
4. where the obligor has not availed fund-based facility from any RE;
5. where no objection certificate has been obtained from REs who have extended fund-based facilities to the obligor; or
6. NFB facility which is fully secured by way of eligible financial collateral[1].

Additionally, the NFB Directions restrict REs from issuing NFB facility for assuring redemption/repayment of funds raised by an entity, unless such NFB facility has been specifically permitted by the RBI.

The details of NFB credit facilities extended by REs must be disclosed in the format provided in the NFB Directions.

## Conditions applicable to Guarantees

The NFB Directions require REs to issue irrevocable[2], unconditional[3], incontrovertible guarantees, containing mechanism for honor upon invocation (unless there is a court order restraining such honor), without any demur. Further, REs are required to have an internal policy for issuance of such guarantees, which policy is required to address, *inter alia*, ceilings for issuances generally and for unsecured guarantees, invocation, settlement, claim period, etc.

### Electronic guarantees

The NFB Direction recognises issuance of electronic guarantee by REs, for which, REs are required to frame Standard Operating Procedure ("**SOP**"). The broad guidelines for framing such SOPs have been elucidated in Annex 1 of the Directions.

### Guarantee favouring another RE

The NFB Directions have prohibited REs from issuing guarantee in favour of another RE as security in relation to a fund-based credit facility (other than in respect of trade related transactions) being extended by such other RE. However, this restriction is not applicable where such other RE is extending an NFB facility.

### Guarantees involving overseas transactions

The NFB Directions continue to permit authorised dealer banks to:

1. extend NFB facilities for bonafide current or capital account transactions (including guarantee in respect of liability of an exporter) under Foreign Exchange Management Act, 1999; and
2. issue guarantee to or on behalf of a foreign entity (or its step-down subsidiary controlled by an Indian entity) in relation to its ordinary course of business overseas. However, such guarantee must be backed by a counter-guarantee or collateral from the Indian entity or its group company.[4]

[1] Specified in paragraph 7.3.5 of Master Circular – Basel III Capital Regulations dated April 1, 2025, as amended from time to time.
[2] Implying that there will be no clause in the contract that would allow the guarantor to unilaterally cancel the same.
[3] Implying that there will be no clause in the contract that could prevent the RE from being obliged to pay out in a timely manner in the event that the original counterparty fails to meet its obligation.
[4] Refer the Foreign Exchange Management (Overseas Investment) Directions, 2022 for detailed instructions on issuance of guarantee specified hereunder.

## Guarantees on behalf of stock/commodity brokers

The NFB Directions restrict all REs other than Scheduled Commercial Banks ("**SCBs**") to issue guarantees on behalf of stock/commodity brokers in favour of stock/commodity exchanges, in lieu of the security deposit/margin requirements stipulated by the exchange.

## Conditions applicable to co-acceptances

REs are required to co-accept only genuine trade bills and ensure that the subjected goods are received in the stock account of the borrower. Further, REs are not permitted to co-accept bills which are either drawn by another RE or where the underlying transaction has already been financed by another RE.

## PCE framework

In addition to SCBs (excluding RRBs), the Directions also permit AIFIs and NBFCs in middle layer (including HFCs) and above (collectively the "**PCE Permitted REs**") to issue a PCE facility in relation to bonds issued by: (a) corporates/ special purpose vehicles for funding projects; (b) non-deposit taking NBFCs (registered with the RBI including HFCs) having an asset size of INR 1,000 crore (Indian Rupees one thousand crore) or more for the purpose of refinancing the existing debt of such NBFCs/ HFCs; and (c) municipal corporations subject to paragraph 2.3.7.3(iii) of the Master Circular - Loans and Advances – Statutory and Other Restrictions dated July 1, 2015. The RBI envisages that the PCE facility may assist in enhancing the credit rating of aforementioned bonds, thus enabling access to funds on better terms.

The primary guidelines in relation to a PCE facility are as follows:

1. PCE Permitted REs are required to have credit policies with suitable provisions for issuance of a PCE facility;
2. the PCE facility is required to be a subordinated, irrevocable, contingent line of credit (revolving at the option of an RE) available strictly for repayment of bonds and not for any other purpose, irrespective of the seniority of claims of other creditors *vis-à-vis* the bond holders;
3. any drawdown under the PCE facility is required to be repaid within 30 (thirty) days. In case such drawal remains outstanding for more than 90 (ninety) days, then the relevant PCE Permitted RE will be required to classify the PCE facility along with all other facilities extended by it to the borrower as a non-performing asset;
4. the PCE Permitted RE, bond issuer, the bondholders (acting through the trustee) and all other lenders to the project (as applicable) are required to enter into a legally binding contract, defining the conditions for drawal of the PCE facility;
5. the maximum PCE exposure limit of all PCE Permitted REs, in aggregate, is capped at 50% of bond issue size. This limit may be undertaken by a single PCE Permitted RE or multiple PCE Permitted REs, subject to the aforesaid cap of 50%;
6. the PCE facility cannot be sanctioned by a PCE Permitted RE after the issuance of the bonds or in the form of a guarantee;
7. PCE Permitted REs are restricted from investing in bonds which have been credit enhanced by way of a PCE facility extended by another PCE Permitted RE;
8. PCE facility can only be extended for bonds rated 'BBB-' or higher (pre-enhancement), by 2 (two) accredited credit rating agencies. The obligation to regularly monitor such ratings lies on PCE Permitted REs;
9. the tenor of bonds issued by NBFCs/HFCs which has been credit enhanced by a PCE facility cannot be less than 3 (three) years;
10. the rating of bonds with and without the PCE facility is required to be clearly disclosed in the offer document;

11. an escrow account will be required to be administered in terms of the bond trustee arrangement for ring fencing the project assets created from the proceeds of the bonds, and the related cash flow; and
12. a legally binding document is required to be entered into amongst the lenders of the project, bond holders and PCE Permitted REs extending the PCE facility, prior to issuance of bonds, for determining the security interest sharing mechanism in relation to the project assets.

The NFB Directions also provide that refinancing of project loans by way of a PCE facility backed bonds issuance will not amount to restructuring under the Prudential Framework for Resolution of Stressed Assets.

Guidelines for balance sheet treatment, capital requirements, exposure limits, and asset classification norms related to PCE facilities have also been stipulated in the NFB Directions.

## Key amendments

The key changes introduced by the NFB Directions include the following:

1. extending the applicability of the provisions contained in the NFB Directions to co-operative banks and AIFIs;
2. specific criteria for issuance of an NFB facility to customers who have not availed any fund-based facility from the relevant RE;
3. prohibition from issuance of guarantee by REs in favour of another RE as security in relation to a fund-based credit facility (other than in respect of trade related transactions) being extended by such other RE,
4. waiver of margin requirement (i.e., 50% margin of which 25% should be in cash) for issuance of guarantees on behalf of stock/ commodity brokers;
5. permission to AIFIs and NBFCs including HFCs in middle layer and above for participating in PCE facilities; and
6. increase in the individual exposure limit for PCE Permitted REs extending PCE facility from 20% to 50% of the bond issue size.

## Conclusion

The NFB Directions lay down a harmonious and clear path for issuance of NFB facilities by REs, including co-operative banks and AIFIs. The REs will benefit from the lucid and concise instructions contained in the directions for determining the permissibility of transactions. Further, the NFB Directions will also empower the board of REs to stipulate suitable internal policies for the purpose of extending NFB facilities, within the contours of the broad guidelines suggested by the RBI. By categorically restricting certain transactions, the NFB Directions will result in a decrease in the overall risk exposure of REs, while increasing their accountability and monitoring requirements, for extending an NFB facility.

The RBI has consistently focused on developing the bond market in India by issuing various circulars incentivising and safeguarding the bond market participant. The introduction of a consolidated and comprehensive PCE framework, allowing participation by AIFIs, NBFCs and certain HFCs, will also assist in the growth by providing a reliable fallback mechanism for the investors and paving the way for participation by NBFCs which are expanding at an exponential rate.

## Finance Practice

JSA has a widely recognised market leading banking & finance practice in India. Our practice is partner led and is committed to providing quality professional service combining domain knowledge with a constructive, consistent, comprehensive and commercial approach to issues. Clients trust our banking lawyers to take a practical and business-oriented approach to achieving their objectives. Our lawyers have a clear understanding of the expectations and requirements of both sides to a financing transaction and provide tailored advice to each client's needs. The practice is especially praised for its accessibility and responsiveness and its ability to work well with international firms and clients. We represent a variety of clients including domestic and global banks, non-banking finance companies, institutional lenders, multi-lateral, developmental finance and export credit institutions, asset managers, funds, arrangers and corporate borrowers in different sectors on a wide range of financing transactions.

Our full spectrum of services includes advising clients on corporate debt transactions (including term and working capital debt), acquisition finance, structured finance, project finance, asset finance, real estate finance, trade finance, securitisation, debt capital markets and restructuring and insolvency assignments.

Our practice has been consistently ranked in the top-tier for several years, and several of our partners are regarded highly, by international publications such as Chambers and Partners, IFLR, Asia Law, Legal 500, Asia Legal Business, IBLJ and Leaders League.

**This Prism has been prepared by:**


**Nand Gopal Anand**
Partner

**Harshit Dusad**
Principal Associate

**Vrindesh Patel**
Senior Associate

18 Practices and
41 Ranked Lawyers

7 Ranked Practices,
21 Ranked Lawyers

14 Practices and
12 Ranked Lawyers

12 Practices and 50 Ranked Lawyers

20 Practices and
22 Ranked Lawyers

8 Practices and
10 Ranked Lawyers
Highly Recommended in 5 Cities

Recognised in World's 100 best competition practices of 2025

Among Best Overall
Law Firms in India and
14 Ranked Practices

---------

9 winning Deals in
IBLJ Deals of the Year

---------

11 A List Lawyers in
IBLJ A-List - 2025

Asia M&A Ranking 2024 – Tier 1

----------

Employer of Choice 2024

---------

Energy and Resources Law Firm of the Year 2024

---------

Litigation Law Firm
of the Year 2024

---------

Innovative Technologies Law Firm of the Year 2023

---------

Banking & Financial Services
Law Firm of the Year 2022

Ranked Among Top 5 Law Firms in India for ESG Practice

2022

Ranked #1
Best Law Firms to Work

---------

Top 10 Best Law Firms for Women

For more details, please contact km@jsalaw.com

www.jsalaw.com

Ahmedabad | Bengaluru | Chennai | Gurugram | Hyderabad | Mumbai | New Delhi