Banking in GIFT IFSC

April 2024

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Foreword

India's economy has grown to USD 3.73 trillion.[1] The first trillion was achieved 60 years after independence, and a consistent growth rate has been maintained thereafter. In today's interconnected and dynamic global economy, the role of the financial services sector has become increasingly vital.

As a pioneering initiative in India's financial landscape, the Government of India launched the Gujarat International Finance Tec-City (GIFT City) project in 2007, with an endeavour to develop a smart city that would host an International Financial Services Centre (IFSC) to provide a comprehensive platform for various financial activities, such as banking, insurance, capital markets, asset and wealth management, FinTech, and access to global markets and currencies.

Representing the nation's vision to become a global hub for international finance and commerce, GIFT IFSC offers world-class infrastructure and a regulatory framework to attract leading financial institutions, businesses and investors from around the globe.

This report aims to provide readers with a comprehensive understanding of the unique attributes and business opportunities inherent in this dynamic environment. We invite readers to envision the potential that GIFT City holds, as well as the opportunities it presents for the future.

I extend my sincere gratitude to all the contributors, whose expertise and insights have enriched this publication. I also commend the editorial team for their dedication and diligence in bringing this project to fruition.

May this publication foster continued collaboration, innovation, growth and prosperity of GIFT City and GIFT IFSC.

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Global Financial Services Technology Leader
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1. https://www.zeebiz.com/economy-infra/news-india-to-become-3rd-largest-economy-with-gdp-of-usd-5-trillion-in-3-years-finmin-273873#:~:text=Today%2C%20it%20is%20the%205th,2024%20review%20of%20the%20economy.

GIFT City – an introduction

GIFT City, the Government of India's flagship project, aims to boost India's stature on the world map of international finance by fostering a favourable regulatory environment, promoting talent and facilitating capital flow in the Indian economy.

Recognising India's financial prowess, Finance Minister Mr. Arun Jaitley announced the establishment of GIFT City as India's inaugural International Financial Services Centre (IFSC) during the Union Budget for 2015-16.

GIFT City, often labelled the 'smart city of the future', is located in Gujarat, nestled between Ahmedabad and Gandhinagar. This tri-city ecosystem fosters an environment supporting business, industry, international finance, and foreign investment, symbolising both a nostalgic era and a promising future.

Conceived as a vertical city, GIFT City boasts modern infrastructure such as a fully automated district cooling system (DCS), automated waste collection system (AWCS) and underground utility tunnels.

This top-tier infrastructure has played a vital role in establishing GIFT City as a global leader among smart cities.[2] The urban centre is complemented by contemporary social amenities, such as an international school, healthcare facilities, a five-star hotel, an international exhibition complex, the GIFT City Business Club with both indoor and outdoor sports facilities, diverse dining options, and well-planned residential projects. Collectively, these offerings make GIFT City a truly 'walk-to-work' city.

Government of India operationalised GIFT City as an IFSC in 2015

A greenfield smart city developed on 886 acres of land

Divided into two zones that include a Domestic Tariff Area (DTA) and Special Economic Zone (SEZ)

The financial gateway of India for inbound and outbound investment

1. Along National Highway 48 (Delhi-Mumbai Industrial Corridor)
2. 25 mins from Ahmedabad International Airport
3. 15 mins from nearest railway station and upcoming high-speed rail

2. https://www.thehindubusinessline.com/news/national/gifts-ifsc-amongst-the-fastest-growing-globally/article24935538.ece

GIFT City journey so far…

2007

GIFT City project announced by Gujarat Government

2011

The foundation stone for the GIFT project was laid. Brick and mortar development of GIFT City commenced

2014

GIFT City notified as SEZ for international financial services

2015

Ministry of Finance notifies India's first IFSC

2016

Union Budget provided a competitive tax regime for units in IFSC

2018

RBI notifies IFSC as non-resident zone

2020

IFSC Authority (IFSCA) was established

2021-2022

IFSCA notified key regulations, circulars, notifications

2023

SGX Nifty begins trading as GIFT Nifty from GIFT City

2024

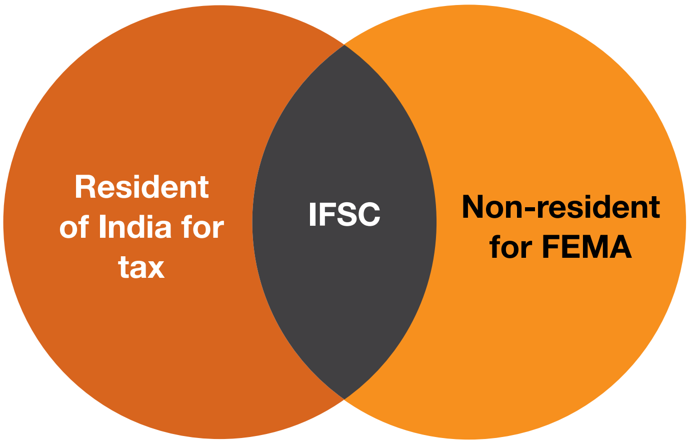
Key announcements:

- Area expansion from 886 acres to over 3,300 acres
- Development of social infrastructure including entertainment, recreational and retail zone
- Operationalisation of metro network in GIFT City by July 2024
- 9-km riverfront along the banks of the Sabarmati River near Gift City to be developed

IFSC

The Government of India launched India's first IFSC in 2015 to accomplish the vision of becoming a significant economic power by fostering the robust growth of international financial services within the nation.

The IFSC is envisioned as a world-class zone dedicated to offering financial services to non-residents and certain residents in a foreign currency (other than the Indian rupee [INR]).

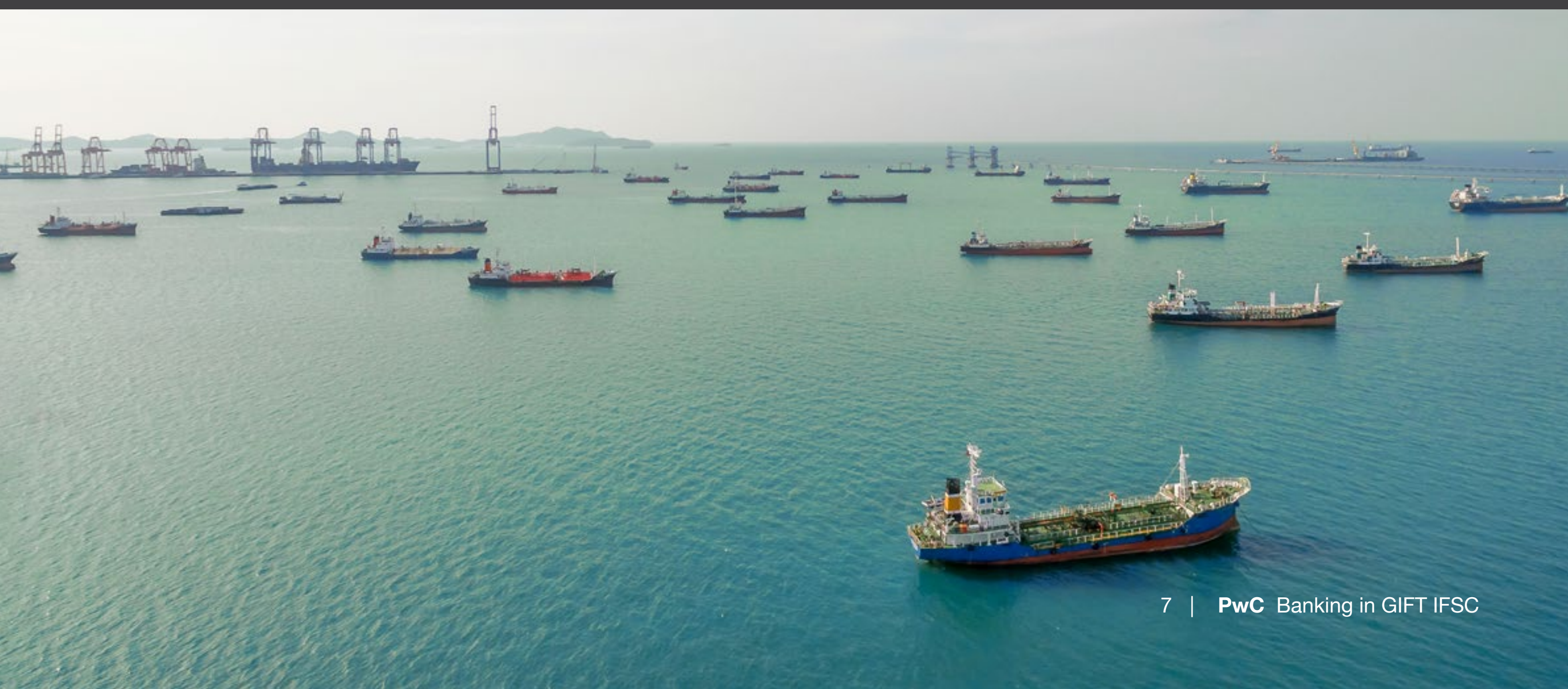


Governing regulator - IFSCA

Established in 2020, the IFSCA plays a role as a statutory body, providing a forward-looking regulatory environment for financial market participants and facilitating ease of doing business. It functions as a unified regulator, combining the powers of the Reserve Bank of India (RBI), Securities and Exchange Board of India (SEBI), Insurance Regulatory and Development Authority of India (IRDAI), and Pension Fund Regulatory and Development Authority (PFRDA) related to financial services, products and institutions within the IFSC.

In addition to securing approvals from the IFSCA for establishing a unit in IFSC, it is also necessary to obtain approvals from the Development Commissioner, SEZ. With effect from 28 February 2024, certain powers and functions of the Development Commissioner, SEZ are now vested with IFSCA.[3]

3. Ministry of Finance (Department of Economic Affairs) Notification S.O. 940(E) dated 28th February 2024



GIFT IFSC: In numbers[4]

580+
registered entities as on 31 December 2023

23
banks registered as on 31 December 2023

USD **51.98** billion
total banking asset size as on 31 December 2023

USD **148** billion
outstanding **derivative transactions** booked by banks till December 2023

2
stock exchanges as on 31 December 2023

USD **66.73** billion
turnover on IFSC **international stock exchanges** in December 2023

USD **52.97** billion
cumulative **debt listing** on IFSC exchanges as on 31 December 2023

USD **10.43** billion
green/ESG/sustainable debt listing as on 31 December 2023

72
broker dealers registered as on 31 December 2023

95
alternative investment funds registered as on 31 December 2023

USD **7.08** billion
total commitments raised as on 31 December 2023

128
aviation assets leased from the IFSC till December 2023

7
ship leasing entities registered as on December 2023

29
IFSC insurance offices and intermediary offices as on 31 December 2023

47
FinTech entities registered as on 31 December 2023

4. IFSCA Bulletin Oct-Dec 2023

Key benefits: GIFT IFSC

Strategic location	Single window clearance	Unified regulator
World-class infrastructure	Availability of talent pool	Progressive regulations
Competitive tax regime	State subsidies	International arbitration centre

Existing business opportunities

- Banking
- Capital markets
- Aircraft leasing
- Asset and wealth management
- Ship leasing
- Bullion
- Insurance
- FinTech

Emerging business segments

- Global in-house centres
- Payment service providers
- Foreign universities
- Global and regional treasury centres

Proposed business segments in GIFT IFSC

- Remote broker dealers in IFSC
- Book-keeping, accounting, taxation and financial crime compliance services from the IFSC

Banking sector – global relevance

Globally, the banking sector plays an important and multifaceted role in economic development. It is integral to the functioning of the economy, supporting economic activities, financial stability and overall growth. In India, the sector's adaptability to evolving market dynamics and its role in promoting financial inclusion contribute significantly to the nation's economic development.

The banking sector plays a crucial role in the growth of international financial centres. The sector's active participation is vital for these centres to achieve their objectives of becoming competitive international hubs thriving with financial activity. Its ability to provide a wide range of financial services, embrace technological advancements and foster global connectivity contributes significantly to the success and attractiveness of such centres.

Background – banking in the IFSC

In 2015, the Reserve Bank of India (RBI) issued guidelines (RBI IFSC Banking Unit [IBU] Guidelines)[5] for establishing banking units in the International Financial Services Centre (IFSC), prescribing the regulatory framework for setting up an IBU by Indian and foreign banks.

Subsequently, in 2019, the Government of India established the International Financial Services Centres Authority (IFSCA) under the IFSCA Act, 2019 enacted by the Indian Parliament. On 1 October 2020, the IFSCA assumed regulatory powers from the RBI, Securities and Exchange Board of India, Insurance Regulatory and Development Authority of India, and Pension Fund Regulatory and Development Authority to develop and regulate financial products, financial services and financial institutions permitted in the IFSC.

On 18 November 2020, the IFSCA (Banking) Regulations, 2020, were notified for banking and investment activities in the IFSC, specifying the regulatory framework for the banking operations of an IBU and superseding the earlier RBI IBU Guidelines.

In 2021, the IFSCA issued the IFSCA Banking Handbook (Handbook),[6] a compendium of detailed directions to the IBUs operating in the IFSC. The handbook is organised into the following three components, providing extensive guidance on banking operations within the IFSC:

General directions	Conduct of business directions	Prudential directions
Deals with licensing of IBUs, lays out the broad principles for banking business, and provides information about the IFSCA's supervisory powers, functions and approach	Aims at ensuring that IBUs meet the minimum standards of conduct expected, particularly concerning the treatment of their clients, their dealings with counterparties and other market participants	Prescribes the non-qualitative prudential requirements applicable on an IBU

5. RBI Notification RBI/2014-15/533 DOR.IBD.BC.14570/23.13.004/2014-15 dated 1 April 2015
6. IFSCA circular F.No. 110/IFSCA/banking Regulation/2021-22/ 6 dated 13 August 2021

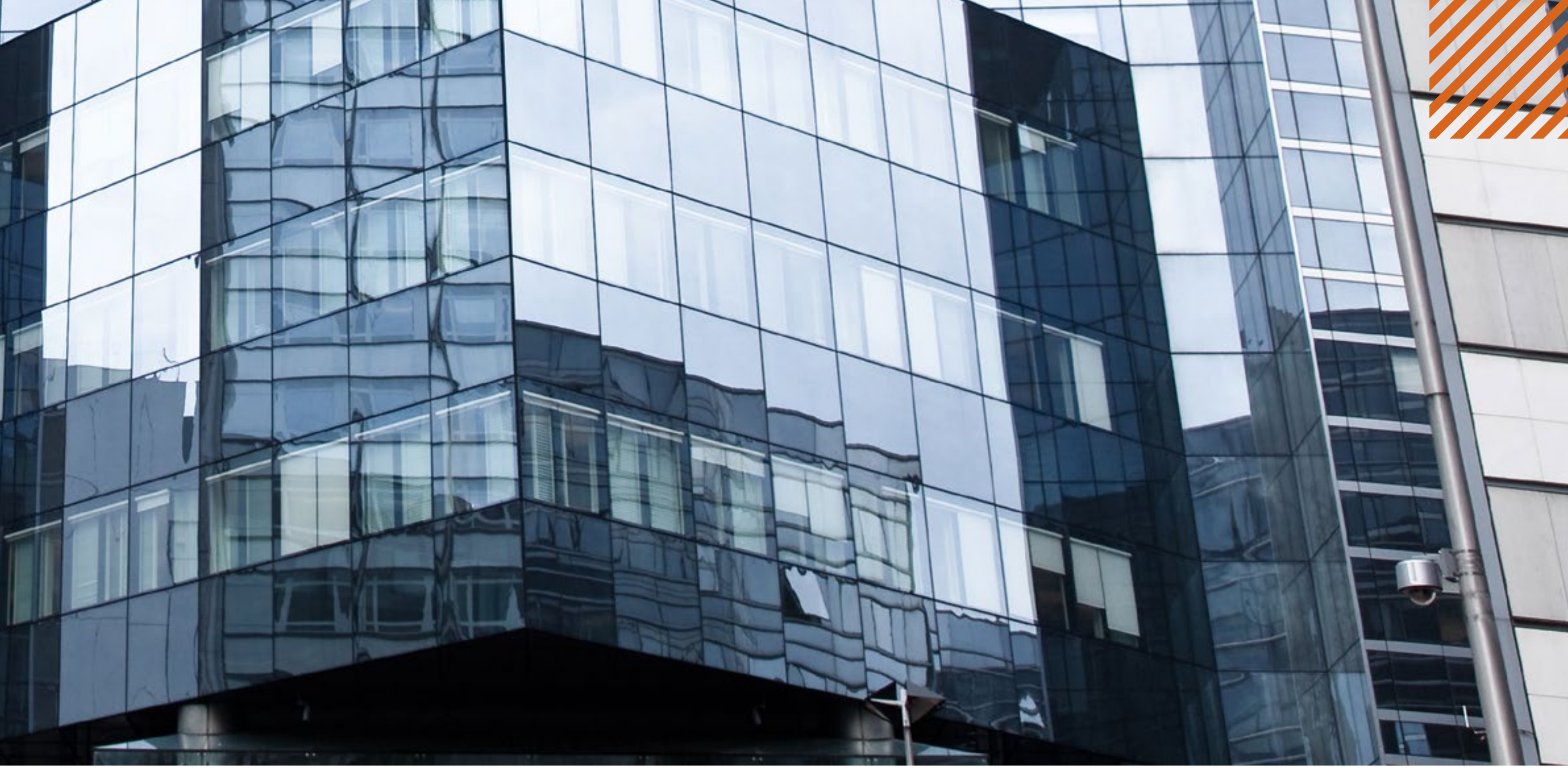
Regulatory framework

Eligibility criteria

- Any Indian or foreign bank (whether having any presence in India or not) can set up an IBU in the IFSC in the form of a branch.
- The parent bank must obtain the following registrations to set up an IBU in the IFSC:
  - licence from the IFSCA and
  - approval from the Special Economic Zone (SEZ) Authority.
- The parent bank must fulfil the following key requirements to establish an IBU in the IFSC:
  - Obtain a 'no-objection' certificate from the home country regulator.
  - Submit an undertaking to the IFSCA regarding the following:
    - ensuring that the IBU has access to liquid assets or financial resources adequate to the nature, size and complexity of its business, thus eliminating any significant risk that liabilities cannot be met.
    - complying with the prudential requirements of its home regulator.
    - sharing reports on capital adequacy, liquidity risk and leverage ratio with the IFSCA, which it submits to its home regulator.
    - notifying the IFSCA in case of any anticipated or actual breach of prudential requirements set by its home regulator.

Minimum capital requirement

The IBU must maintain a minimum capital of USD 20 million from the date of commencement of operations, which can be maintained at the parent level.



Permitted activities

The IBU is permitted to undertake activities:

- mentioned under section 3(1)(e) of the IFSC Act, 2019; or
- mentioned under section 6 of the Banking Regulations Act, 1949, except those expressly prohibited by the IFSCA.

Thus, an IBU is permitted to undertake a wide array of activities permitted for a commercial bank in India and those specifically permitted by the IFSCA. It cannot undertake activities expressly prohibited by the IFSCA, i.e. effecting contracts of insurance and any other activity that the IFSCA has expressly prohibited.

The IFSCA Banking Handbook provides the following indicative list of permissible activities (non-exhaustive):

- Lending to individuals and corporates
- Factoring and forfaiting services
- Undertaking over-the-counter derivative contracts
- Operating as a foreign portfolio investor or eligible foreign investor
- Borrowing and lending to other IBUs
- Accepting deposits
- Trust services
- Credit enhancement
- Equipment leasing and hire purchase
- Referral services
- Underwriting
- Portfolio management services
- Investment advisory services
- Negotiating letters of credit for its constituents
- Distributing capital market products
- Participating in an authorised payment system

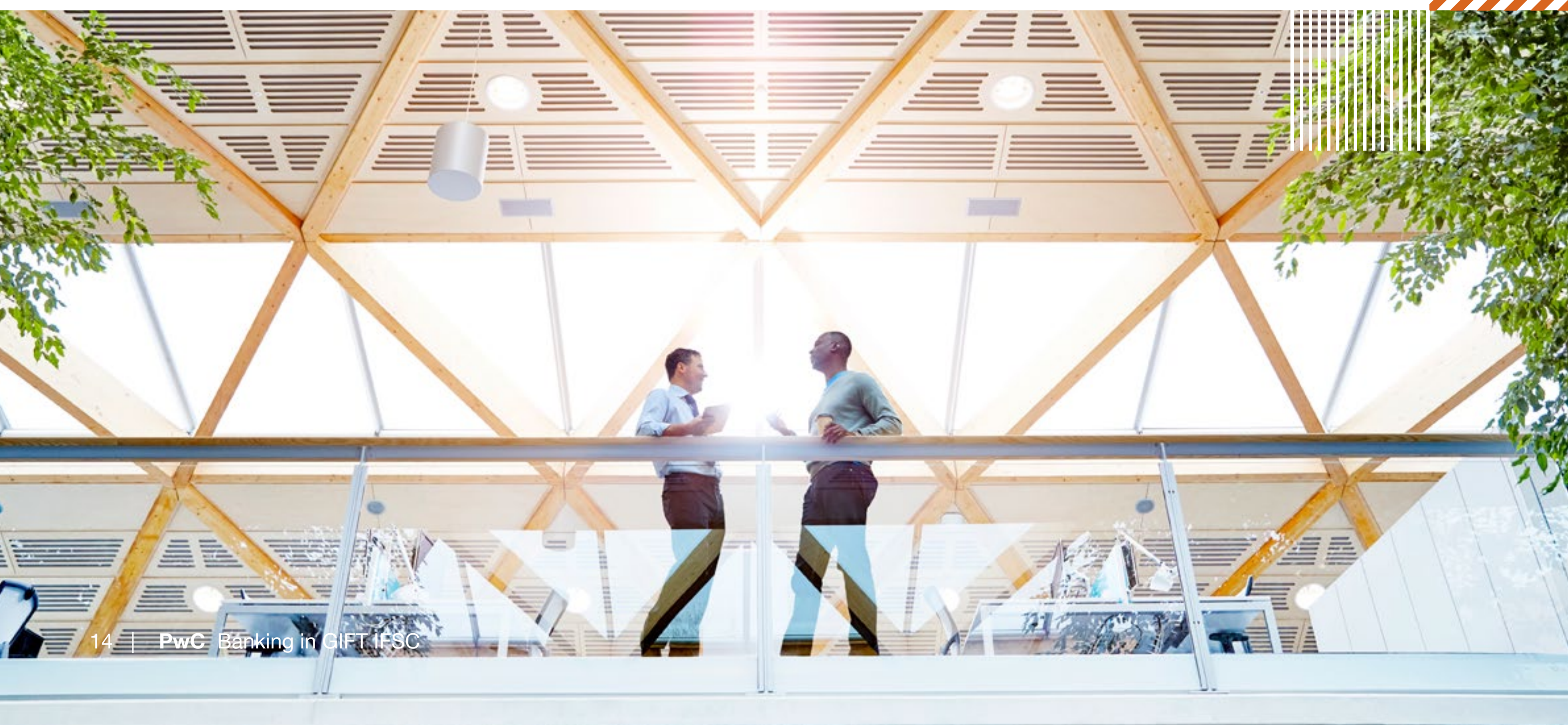
- Trading and clearing member of a stock exchange
- Undertaking transfer of loan assets
- Bullion trading members and clearing members in the IFSC
- Acting as a custodian of assets or securities
- Acting as foreign exchange prime brokerage
- Undertaking remittances and foreign exchange transactions
- Maintaining a global administrative office
- Trading and clearing in precious metals spot and OTC derivatives contract
- Investing in securities issued outside the IFSC (other than Indian securities)
- Operating as an investment banker
- Operating unallocated accounts in bullion
- Offering payment services

Key activities

Lend to Indian borrowers (external commercial borrowings)	Derivatives (including non-deliverable derivative contract, foreign currency interest rate swap, Indian rupee interest rate swap)	Trade finance (including factoring, forfaiting, supply chain financing)	Invest in Indian public markets as FPI	Distribute capital market products and services

Key governance aspects of an IBU

- The parent bank must appoint the governing body of the IBU before commencing its operations and inform the IFSCA. The governing body is responsible for overseeing the business of the IBU and approving its business strategy and business plan.
- The governing body should have at least three members who can be:
  - part of the board of directors or management committee of the parent bank, responsible for overseeing the IBU's business
  - individuals designated by the board of directors, managing committee or any other body of the parent bank responsible for overseeing the IBU's business.
- The governing body should convene at least once per quarter and a minimum of six times per financial year.
- The parent bank should designate a senior officer engaged in the compliance function at the head office as the 'HO compliance contact' of the IBU, responsible for providing information about the parent bank's operations to the IFSCA when requested.
- Furthermore, an IBU must have a chief executive officer (CEO) and compliance officer (see details under the discussion on 'controlled function' below) who should not hold any other responsibilities.



Employee requirements in the IFSC

- An IBU must employ staff commensurate with the size and nature of its business operations.
- The appointments mentioned below are mandatory for the IBU operations, with appointed individuals based out of the IFSC and performing the following functions:
  - **Controlled functions**
    - **CEO –** responsible for day-to-day management, supervision and control of the IBU's activities
    - **Compliance officer –** responsible for all compliance matters on the IBU's activities
    - **Non-executive governance function –** should be a member of the bank's governing body but not be responsible for the day-to-day directions of the IBU's affairs
- The parent bank must apply to the IFSCA for its employees undertaking controlled functions to be granted the 'Approved individual' status. The IFSCA should grant this status to such individuals if it is satisfied that the individual is fit and proper.
- **Designated functions**
    - **Senior manager function –** responsible either alone or jointly with other individuals for the management, supervision or control of one or more parts of IBU's activities
    - In the case of employees undertaking designated functions, the IBU should adopt reasonable steps to satisfy itself that the individual is fit and proper.

Prudential requirements

The following prudential requirements apply to an IBU:

Sr. no.	Particulars	Prudential requirements
1	Liquidity coverage ratio (LCR)	• Higher of – the LCR prescribed by the home country regulator – the LCR prescribed by the IFSCA (presently 100%) • For the IBU, the LCR can be maintained at the parent level, subject to IFSCA approval.
2	Net stable funding ratio (NSFR)	• Higher of – the NSFR prescribed by the home country regulator – the NSFR prescribed by the IFSCA • Currently, the IFSCA has not implemented the NSFR requirement for IBUs.
3	Leverage ratio (LR)	• The LR should be maintained by the parent bank, as applicable under the home country's regulations.
4	Retail deposit reserve ratio (RDRR)	• The RDRR must be maintained daily at 3% of the deposits that are raised from individuals and are outstanding as on the end of the previous working day. • The RDRR must be maintained in specified foreign currency in the form of: – a nostro account of the IBU; or – holdings of sovereign debt securities (including T-bills) rated investment grade or above by at least two rating agencies of international standing.
5	Reserve requirements	• Liabilities of an IBU (other than deposits raised from individuals) should be exempted from the cash reserve ratio or other requirements specified by the IFSCA. • Deposits raised by an IBU from individuals should be subject to such reserve ratios as specified by the IFSCA.

Other key requirements

Currency for conducting business

An IBU should conduct business in specified foreign currencies only, i.e. USD, EUR, JPY, GBP, CAD, AUD, CHF, HKD, SGD, AED and RUB. An IBU may be permitted to conduct such business in INR as may be specified by the IFSCA, subject to settlement in specified foreign currencies. An IBU is permitted to have an INR account to defray its administrative and statutory expenses.

Sustainable linked lending

- An IBU should have a minimum of 5% of gross loans and advances directed toward green, social, sustainable or sustainability-linked sectors or facilities.
- The 5% target must be computed on incremental loans and advances in a financial year.
- An IBU must develop a board-approved policy on green, social or sustainability-linked lending.

Subsidiary model

Presently, all Indian and foreign banks have set up IBUs in the form of branches. However, IBUs can be established in the form of subsidiaries as well.

Tax framework

Tax framework – IBU

Particulars	Branch
Tax holiday	Tax holiday available for 10 consecutive years out of the first 15 years
Minimum alternative tax (MAT)	The MAT applicability must be checked on consolidated India profits. If applicable, MAT is payable at the rate of 15% (plus applicable surcharge and cess) on book profits.
Distribution of profit	Distribution of profit by branch to head office is not taxable, i.e. income to self.
Goods and services tax (GST)	• No input GST on services received from Indian or non-resident vendors • No GST must be charged for services provided to other IFSC or SEZ units • GST applicable on services provided by an IBU to resident parties

Tax framework – non-resident clients

- Interest received by a non-resident on deposits made with an IBU is exempt from tax.
- Interest received by a non-resident on monies borrowed by an IBU is exempt from tax.
- Any income accrued or arisen to or received by a non-resident as a result of transfer of non-deliverable forward contracts or over-the-counter derivatives entered with an IBU is exempt from tax.
- Any income accrued or arisen to or received by a non-resident as a result of:
  - transfer of offshore derivative instruments entered with an IBU is exempt from tax; and
  - distribution of income on offshore derivative instruments is exempt from tax.

Notes

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