KIIFB Controversy

Why in News

Recently, the **Enforcement Directorate** (ED) has opened a preliminary inquiry to examine if borrowings by the **Kerala Infrastructure Investment Fund Board** (KIIFB) from overseas markets violated the provisions of the **Foreign Exchange Management Act (FEMA) 1999.**

- KIIFB was established to **manage the Kerala Infrastructure Investment Fund** (KIIF), as per the **KIIF Act 1999.**
- In **2016,** the government **changed the role of KIIFB** from handler of investment bonds to an **entity to mobilise the resources for developmental projects** over and beyond the budget.

Key Points

- The **Comptroller and Auditor General**(CAG) highlighted that the KIIFB had raised Rs. 2,150 crore from the international market without the consent of the Central government in 2019.
    - A **prior consent** of the Government of India is necessary before a State Government raises a loan.
- KIIFB had also overstepped its legal bounds by issuing **masala bonds** to raise money from foreign markets in violation of **Article 293 (1) of the Constitution.**
    - **Article 293 (1):** The executive power of a State extends to borrowing within the territory of India upon the security of the Consolidated Fund of the State within such limits. State governments can give guarantees within such limits as fixed by the legislature of the concerned State.
- The ED has also asked the **Reserve Bank of India** (RBI) about the details of ‘no objection certificate’ it had supposedly extended to the KIIFB, enabling the agency to take sizable loans from the foreign financial market.

- **Implications of Inquiry:**
  - The investigation could potentially **cause a fall in the revenues** of the **KIIFB.**
  - It might **affect the extended loans** being offered to KIIFB by the **International Finance Corporation** (IFC) - a part of the **World Bank group.**
  - With an ongoing investigation, **investors would not be willing to buy its masala bonds,** which will further lead to loss of revenues.
  - The investigation can also **result in an administrative paralysis, halting all the infrastructure development projects** for which the KIIFB had collected the funds.
- **Kerala Government's Stand:**
  - It disagrees with the CAG's finding on the basis that **KIIFB is a corporate entity and not the State government.**
    - As per **FEMA provisions, corporate entities can issue masala bonds** to raise funds from foreign markets.
  - Kerala also criticises the move because CAG has **unilaterally submitted its audit** observations **without giving the State its right of reply.**

Masala Bonds

- They are **rupee-denominated bonds** used by **Indian companies to raise funds** from the **overseas market** in Indian rupees.
- **Eligibility for Issuance:**
  - According to RBI, **any corporate, body corporate and Indian bank is eligible to issue** these bonds overseas.
  - These can be **issued and subscribed** by a resident of such country that is a member of the **financial action task force** (FATF) and whose securities market regulator is a member of the **International Organisation of Securities Commission** (IOSCO). It can also be subscribed by **multilateral and regional financial institutions** where India is a member country.
    - IOSCO is the international body that brings together the world's securities regulators and is recognised as the global standard setter for the securities sector.
- **Limitations:**
  - As per the **RBI guidelines,** the money raised through such bonds **cannot** be used for **real estate activities** other than for development of **integrated township or affordable housing projects.**
  - Also, it cannot be used for investing in capital markets, purchase of land and on-lending to other entities for such activities as stated above.

Source:TH