Legal Framework for Social Success Notes in India
Agenda

1. An Overview of Social Success Notes
2. Key Funding Instruments for Investors
3. Indian Regulatory Regime
4. Negotiating and Structuring Transaction Documentation
5. Q&A

Takeaways: An understanding of the Indian legal regime on foreign lending and investments, and key contractual and legal aspects to take note of to implement Social Success Notes
What are Social Success Notes?

1. Loan
2. Provides goods & services
3. Repayment
4a. Outcome payment
4b. Outcome payment

Social Enterprise
Investor
Outcome Payer
M&E Partner
SSNs help align all stakeholders on a common mission to scale impact

- Affordable mission-aligned debt funding for social businesses
- Sustainable impact reaching vulnerable populations at scale
- Making investing for real impact attractive for commercial investors
- Effective use of philanthropic donor capital
Structure of a Social Success Note - Legal Aspects

1. Legal Due Diligence on Social Enterprise
2. Partnership & Services Agreement

Risk Investor

Loan Agreement

Social Enterprise

Outcome Payer

Foundation/Philanthropic Organization

Tripartite Agreement

Social Enterprise, Outcome Payer and Investor

M&E Partner

Services Agreement
Social Success Notes

The Indian Legal Framework
## Fundraising Options

How Indian Entities can access Funds

<table>
<thead>
<tr>
<th>Equity</th>
<th>Debt</th>
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</thead>
<tbody>
<tr>
<td>• Equity shares</td>
<td>• Loans</td>
</tr>
<tr>
<td>• Compulsorily Convertible Preference Shares</td>
<td>• Non-Convertible Debentures</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>Donations and Grants</th>
<th>Hybrid Instruments</th>
</tr>
</thead>
<tbody>
<tr>
<td>FCRA relevant when donor is</td>
<td>• Convertible Notes</td>
</tr>
<tr>
<td>outside India</td>
<td>• Compulsorily Convertible Debt</td>
</tr>
</tbody>
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Process Flow for SSNs in India

Start

Intermediary identifies target SGB, project, risk investor and outcome payer
Due Diligence is performed

M&E Partner performs evaluation
Timelines and evaluation metrics to be recorded in Service Agreement between M&E Partner and Outcome Payer

Investor disburses loan to SGB
In accordance with terms captured in sanction letter (if any) and loan agreement

Outcome Payments
SGB makes repayments to Risk Investor
Funder pays incentives to SGB and Risk Investor

End
Process Flow for SSNs – Foreign Counterparties

Start

Intermediary identifies target SGB, project, risk investor and outcome payer
Due Diligence is performed

Subject to ECB Guidelines

M&E Partner performs evaluation
Timelines and evaluation metrics to be recorded in Service Agreement between M&E Partner and Outcome Payer

Export of Services

Investor disburses loan to SGB
In accordance with terms captured in sanction letter (if any) and loan agreement

Outcome Payments
SGB makes repayments to Risk Investor
Funder pays incentives to SGB and Risk Investor

End
RBI External Commercial Borrowings (ECB) Master Directions

Either Foreign Currency Denominated or Rupee-Denominated

- Any Indian entity borrowing from a non resident entity must comply with ECB Guidelines
  Up to USD 750 Million per year under the automatic route
- All entities eligible to receive FDI are eligible borrowers under ECB Guidelines - Private Limited Companies, LLPs etc
- Filing of Form ECB with Authorised Dealer bank
- Minimum average maturity period for ECBs - 3 years
- Reporting requirements include procuring a loan registration number from Bank prior to drawing down, reporting of any change in repayment terms (crucial for an SSN structure), and filing monthly returns
Foreign Contributions (Regulation) Act

Any donations made to an Indian entity from a foreign source

- Requires registration with the Ministry of Home Affairs through the filing of Form FC3A
- Any person receiving foreign contributions must have an 'educational, cultural, economic, religious, or social' objective
- Eligible 'persons' are an individual, an HUF, a society, a trust or a Sec. 8 Company.
- To ensure that a transaction does not have FCRA implications, payment must be in lieu of goods or services (Explanation 3 to Sec 2(h) of the FCRA)
Pre-transaction Procedures and Timelines

- **Financial and Commercial Due Diligence**
- **Legal Due Diligence (1-2 Months)**
  - Legal Counsel of the Intermediary, or of the Investor
  - Coordinated by in-house functions of all Parties
- **Finalization of commercial terms (1-2 weeks)**
- **Execution and Investment**
- **Negotiation of Commercial Documents (1-2 Months)**
  - Legal counsel and in-house legal teams of all counterparties
Legal Due Diligence

Indicative Pre-transaction Checklist

1. Corporate Governance
   - Constitutional documents, governance structure, details of Board

2. Audit Processes
   - Risk Management and Compliance, Business Continuity Protocols

3. Statutory Registers, Meetings, Returns

4. Details of Shareholding Structure and Debt, if any

5. Business Plan and Key Licenses & Contracts

6. Human Resource Details
Key contractual aspects in structuring SSN Documentation

- **Loan Agreement**
  - Recording of loan size, interest rate, and outcome payments
    - Size of loan, tranches, coupon rate - circumstances in which these clauses vary
  - Tripartite Agreement
    - Size of outcome payment: fixed, or varies with level of outcomes?

- **M&E Services Agreement**
  - Outlining project evaluator roles
    - Project design to ensure that target recipients, geographies, goals are feasible and measurable
    - Documentation to address stage of the project at which they get involved, and their specific deliverables
      (Outcome evaluation or ongoing evaluation?)

- **All Documents**
  - Termination and consequences
    - Events of default
    - Parties' rights to terminate
    - Consequence of force majeure (How would an event like COVID19 affect the contract?)

- **All Documents**
  - Standardized Terms across Documentation
    - Governing law and Dispute Resolution mechanism to be common across contracts
    - Co-terminous nature of contracts
Key contractual aspects in structuring SSN Documentation

Consequences of failure to meet targets
Capital protection such as an investment guarantee, if applicable, to be recorded
Early termination triggers in the event of incapacity to meet outcomes on an ongoing basis

Covenants on SGB
Documents must place:
- Reporting requirements
- Requirements to retain human resources assigned to the project, addressing key man risk
- Covenants against mission drift
- Cure periods

If Government is the Outcome Payer
In India, Govt partnerships effected through: bidding (tendering process)/negotiation in response to a call for proposals from the Govt., or MoU based partnerships
Standard-form contracts likely, with limited negotiation over certain clauses. Eg. sovereign immunity
State-wise differences in public procurement of goods and services
Clauses of relevance to each Stakeholder

**Negotiation of Legal Documentation**

**SGB**
- Alignment of repayment schedule with loan servicing capabilities
- Events of default and consequences of default
- Rights available to Lender (prior consent for management changes)
- Reporting Obligations

**Investor/Lender**
- Payment schedule for SGB as well as outcome payer
- Permissible assignment
- Reporting and oversight rights
- If applicable, rights to revise commercial terms such as coupon rate

**Outcome Payer**
- Payment triggers and timelines
- Measurable definition of outcomes
- Independent measurement of outcomes, if required

**M&E Partner**
- Outlining of roles and responsibilities
- Frequency and mode of deliverables
- Ongoing evaluation or outcome evaluation?
- Payment mechanics, and consequences of termination of other docs.
## A Comparative View of Funding Instruments

<table>
<thead>
<tr>
<th></th>
<th>SSN</th>
<th>Other Results Financing Models (DIB/SIBs)</th>
<th>GRANTS</th>
<th>LOAN</th>
<th>EQUITY</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Regulation in India</strong></td>
<td>ECB Guidelines</td>
<td>Depending on instrument</td>
<td>FCRA</td>
<td>ECB</td>
<td>FDI and FEMA</td>
</tr>
<tr>
<td><strong>Outcome Measurement</strong></td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td><strong>Legal Cost</strong></td>
<td>High</td>
<td>High</td>
<td>Relatively low</td>
<td>Relatively low</td>
<td>Relatively low</td>
</tr>
<tr>
<td><strong>Time</strong></td>
<td>6 months to 1 year</td>
<td>6 months to 1 year</td>
<td>1-2 months</td>
<td>~ 1 month</td>
<td>1-3 months</td>
</tr>
<tr>
<td><strong>Players Involved</strong></td>
<td>Intermediary, SGB, M&amp;E Partner, Investor and Outcome Payer</td>
<td>Intermediary, NGO/NonProfit, M&amp;E Partner, Outcome Payer and Investor</td>
<td>Donor and Recipient</td>
<td>Lender and Borrower</td>
<td>Investor and Investee</td>
</tr>
<tr>
<td><strong>Access</strong></td>
<td>Any entity eligible to receive FDI</td>
<td>Depending on instrument</td>
<td>Trust, societies, S8 Cos.</td>
<td>Companies, LLPs, etc</td>
<td>Any Company</td>
</tr>
</tbody>
</table>
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