

# Perpetual Debentures

*Debt on Paper, Equity in Substance,  
and the Hat It Wears Under Each Law*

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Commercial Drivers | Many Hats | The CRT Lens

## Commercial

Reasons issuers consider for  
perpetual debt

## Hats

Multiple frameworks, Multiple  
identities, one instrument

## Watch-outs

Where the equity classification  
is lost



Swipe →

# 01

## COMMERCIAL USE CASES

# Scenarios in which Perpetual Debentures can be Effective

### Long-Horizon Funding Without Dilution

#### INTRA-GROUP

Promoter intends to fund group companies without dilution of any investors in the target company, yet have a quasi-equity investment, protecting the equity of investors and not triggering any debt covenants

### Balance Sheet Optics for Stressed Subs

#### COVENANT PROTECTION

Funding a stressed subsidiary with plain debt worsens leverage and risks event of default on senior debt. Perpetual debt sits below the line under Ind AS, preserving every debt-to-EBITDA and debt-to-equity covenant in the group (subject to lenders' acceptance of IndAS classification)

### Capital Reduction Consideration

#### LOSS CRYSTALLISATION

Section 66 capital reduction can be discharged in cash, property, instruments, or the creation of a liability. Cancelling eroded preference shares against perpetual debentures crystallises the capital loss on the basis of FMV while preserving repayment capacity by continuing with the original face value

### Repatriation Without Buyback or Cap Reduction Friction

#### EXIT FLEXIBILITY

Promoter retains the ability to repatriate funds without the buyback restrictions on cap on number of shares/ net worth, source of funds/ availability of free reserves, the cooling-off period, or the NCLT route in case of a capital reduction.

**Every Use Case Answers a Commercial Question First**

*Regulatory architecture and tax treatment are downstream consequences of the commercial driver*



# 02

## REGULATORY AND TAX MATRIX

### Maturity and Coupon are Discretionary. Map the Hat Under Each Law.

#### The Structural

#### THE THESIS

No fixed maturity. Coupon and principal repayment discretionary in quantum and timing. Keeping these two features as discretionary in the hands of the borrower, renders an equity-like instrument.

#### Equity in Balance Sheet. Coupon Below the Line.

#### IND AS 32

Equity classification preserves EBITDA and keeps the instrument off the leverage numerator.

#### Debenture. Not Share Capital.

#### COMPANIES ACT/ FEMA

Does not enter the statutory definition of net worth under Section 2(57). The same asymmetry spills over to FEMA ODI for outbound investments. Not permissible under inbound investments as well.

#### Debt. Coupon Deductible.

#### DIRECT TAX

Section 36(1)(iii) deduction available when coupon is actually paid. However, transfer pricing recharacterization risk to be borne in mind.

#### Not a Financial Creditor.

#### IBC

No fixed maturity and no enforceable obligation to repay principal or pay coupon. Holder is not a financial creditor – provides comfort to external lenders of the target, but promoters bear a redemption risk

### Map All Hats Before Choosing the Instrument

*The Ind AS classification does not bind the Companies Act, FEMA, the tax law, or*

IBC



## The Takeaway

Perpetual debentures have versatile use case scenarios. Maturity and mandatory coupon, if made discretionary, can transform the substance, but the legal form is tested under each separate framework.

### Commercial

Long-horizon funding, stressed-sub support, capital reduction consideration, and frictionless repatriation

### Ind AS 32

Equity classification preserves EBITDA and keeps the instrument off the leverage numerator.

### Direct Tax

Coupon deductible under Section 36(1)(iii) when actually paid – TP recharacterization risk to be assessed

### The Watch-out

**Commercial Watch-Out:** Modifying the maturity and coupon changes the character of equity back to debt

**Regulatory Watch-Out:** Debt instrument under Companies Act and FEMA – regulatory net-worth does not increase, and inbound investments under FEMA not permissible; outbound permissible only if control (i.e., more than 10% shareholding established)

