



INDIAN LEGAL AND BUSINESS UPDATE
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1. Government to have Stricter Rules for FDI Approvals

The Government has finalized far-reaching changes to the country's Foreign Direct Investment (FDI) policy to account for increasing concerns voiced by security agencies. The new guidelines include amending the automatic approval list by significantly expanding the role of the Foreign Investment Promotion Board (FIPB) i.e. the nodal agency for clearing FDI proposals. FIPB will now scrutinize proposals in which funds are routed through tax havens (like Mauritius) and those that fall under a proposed "sensitive list" even if they are under the current automatic approval route.

FIPB, which comprises members from most key ministries, will also consider foreign personnel and the requirement for imported labour in FDI applications before giving approval. The issue of foreign workers has recently been a source of controversy, with the government objecting to Chinese blue collar workers coming into India on tourist visas instead of business visas to work on high tech construction projects. It also plans to put in place a threshold FDI criterion that will be fixed by various administrative ministries as well as the central bank and the stock market regulator, under which any FDI proposal above this level would also trigger scrutiny.

A "dynamic checks" system will also operate after an FDI proposal is approved, if subsequent developments require permission to be blocked. A designated agency will be set up and equipped with a database to scrutinize FDI approval. There are also plans for a Foreign Investments (National Security Concerns) Act which will incorporate all powers for the central government to ensure national security is not affected by inflow of foreign investment.

2. Central Government plans regular monitoring of FII holdings in a company

The Department of Economic Affairs, the Ministry of Commerce and Industry and the Reserve Bank of India have come to a consensus that Foreign Institutional Investment (FII) in a company should be monitored on a monthly or a quarterly basis to ensure there is no breach of sectoral caps under the proposed Foreign Direct Investment (FDI) guidelines. The Commerce and Industry Ministry had mooted a proposal to revisit the existing guidelines a few months ago based on the principle that sectoral caps should be composite, covering all kinds of foreign investments that include FIIs, NRIs, ADRs, GDRs, foreign currency convertible bonds and convertible preference shares, and there should not be any sub-caps for each of them.

Under the current policy, the total holding of FIIs in an Indian company is not permitted to exceed 24 per cent of the paid-up capital. However, this limit can be increased to the sectoral cap limit by passing a resolution at the annual general meeting of the company. The proposal is expected to come up for discussions with the Committee of Secretaries after which it would be referred to the Cabinet Committee on Economic Affairs for final endorsement. Questions were raised on an initial proposal by the Commerce and Industry Ministry that March 31 be fixed as the prescribed date for calculation of foreign investment as it was not feasible to monitor FII investments on a day-to-day basis

3. Dual Tax Structure for Goods & Services

Laying the roadmap for the introduction of a Goods and Service Tax (GST), State Governments proposed a dual GST structure, with two rates for goods and a single rate for services. The tax would be levied both by the Central and the State Government, though there is still no clarity as to when the new tax regime will be implemented. Union Finance Minister had during the budget session set April 1, 2010 as the date for the new tax regime that seeks to re-distribute the burden of taxation equitably between manufacturing and services.

The amendment is required to allow the Union Government to tax beyond the manufacturing stage and allow states to tax services. There will also be separate legislation on central GST and model state GST that would spell out the rates at which the tax would be levied. The rates being discussed are between 8 and 10 per cent for the lower slab and 16 and 18 per cent for the upper slab, as the idea is to have revenue neutrality. The states have proposed that the Union Government should compensate them for loss of revenue if any, during the first five years introduction of GST.

4. EPFO Proposes Salary Cap Rise to Rs. 10,000

The Employee Provident Fund Organisation (EPFO) has sent a proposal to the labour ministry to increase the salary limit for paying employee provident fund (EPF) to Rs. 10,000 from the current Rs. 6,500. It has also proposed covering companies with a minimum of 10 employees under the Employee Provident Fund and Miscellaneous Provisions Act (EPF & MP Act), 1952, against the present norm of a minimum of 20 employees. The organized labour sector comprises 300 million workers, of which only 40 million are covered under EPFO regulations. If the proposal is approved by Parliament, the EPFO is likely to cover 150 million workers in the organized sector, which would be 50 per cent of the organized labour market. This move will help contractual workers. The change in the limit, if approved, could be an important move because of rising salaries over the years.

5. SEBI Allows Auction for QIBS in Follow-On Offers

The Securities and Exchange Board of India (SEBI) has amended the Issue of Capital and

Disclosure Requirements Regulations (ICDR) to allow pure actions for qualified institutional investors (QIBS) in follow-on public offerings. The method may be later extended to initial public offerings. SEBI has introduced the pure auction method of book building in shares sale, where institutional bidders can bid at any price above the floor instead of restricting them to bid in a band fixed by investment bankers. Shares would be allotted to those whose bids are at the top price, starting from the highest bidder.

This would be initially tried with follow-on public offers (FPOs) by companies whose shares are already listed on the stock exchanges. Under the auction method, retail and high net worth investors will surrender their choice to play a part in the price discovery as they would be allotted shares at the floor price discovered in the auction. However, the auction method has not been mandated by SEBI. The company can either choose this method or the book building method, meaning that SEBI has decided that the issuer is free to place a cap either in terms of the number of shares or percentage to issued capital of the company so that a single bidder does not garner all the shares on offer, ensuring a wider distribution of shareholding.

6. Proposed Amendment to Copyright Act to Restrict 'Fair Dealing' Clause

The Copyright Act (Amendment) Bill 2009, which is slated to be taken up by the Union Government shortly, may restrict cover versions of sound recordings by proposing to introduce royalty payments for cover versions, extending the time-period within which these recordings cannot be made and restricting the medium for these recordings. Till date, under the Copyright Act, 1957 certain acts would not constitute an infringement namely those listed under the concept of "fair dealing". Article 52(1)(j) of the Act permits music companies, subject to certain restrictions, to make their own "versions" of an exiting song.

The proposed Bill seeks to introduce Section 31 C, under which companies can no longer automatically get such permission for making version recordings of any songs. They would have to pay royalty for a minimum of 50,000 copies of the version song for each year during which copies are made, regardless of how many copies they eventually sell.

Moreover, the new section proposes to increase the period during which version recordings are not permitted – from two years to five years – from the time the first sound recording of the work is made. In addition, the Bill is believed to contain a clause under which such sound recordings would have to be "in the same medium as the last recording unless the medium of the recording is no longer in current commercial use". This clause ignores the fact that a substantial amount of audio sales are through digital medium these days.

7. Profitable Unlisted PSUs to be Listed in Stock Exchange

The Union Government has announced a bold disinvestment policy that could see unlisted public sector companies with a positive net worth being listed in the stock market and the proceeds from sale of government equity being used entirely for social sector programmes for a three year

period. The decision, which was announced by Home Minister after a meeting of the Cabinet Committee on Economic Affairs, opens the doors for around 50 public sector companies to get listed.

Unlisted public sector companies qualifying for the IPOs should have a positive net worth and should be making a profit for three years. Besides, listed public sector companies that are profitable and have less than 10 per cent floating equity will also be going to the market. Disinvestment proceeds from the sale of government equity during April 2009 to March 2012 will be used to meet capital expenditure for specific social sector schemes. The money from disinvestment will go into the National Investment Fund (NIF) created in 2005.

8. RBI issues new norm to make e-commerce faster

The Reserve Bank of India (RBI) has mandated to make online commerce faster for customers, by stating that all payments for such transactions be credited directly to merchants, instead of getting cleared by intermediaries. Currently, until a payment is authorized and processed by intermediaries, a transaction is not completed. For instance, online retailers such as eBay do not ship goods purchased online unless funds are credited to their account, before being routed through an intermediary. CC Avenue, Bill Desk, Direct Pay, ICIC PaySeal and Paypal are among major payment gateways in India. The new measure will ensure that the e-payments made by customers are remitted to the accounts of the merchants who have supplied the goods and services without undue delay. Under the new system, all payments to merchants shall be effected within a maximum of three days from the date of transaction. Now no payment other than the commissions at the pre-determined rates/frequency shall be payable to the intermediaries. The existing system has some pitfalls like delay in transferring money to the merchant; some times the delay is of more than seven days.
