



**INDIAN LEGAL AND BUSINESS UPDATE**  
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**1. Foreign Direct Investment beyond 24% in micro units to require Foreign Investment Promotion Board approval.**

Any foreign investment in excess of 24 per cent in an industrial unit, which manufactures items reserved for micro and small enterprises (MSEs), will require prior approval of the Foreign Investment Promotion Board (FIPB). Moreover, any industry which manufactures items reserved for MSEs will require an industrial license subject to some general conditions, including export of at least 50 per cent of new or additional production over a period of three years. This was notified by the government in a new Press Note on September 3, 2009.

Earlier, any unit having more than 24 per cent foreign direct investment (FDI) had to withdraw its registration as a small-scale unit and obtain industrial licence. However, the new Press Note removed this process which will help in attracting more FDI into the cash-starved MSEs. The Act defined micro units in the manufacturing sector as those where investment in plant and machinery does not exceed INR 2.5 million, while small units as those investing between INR 2.5 million and INR 50 million. In the services sector, the investment in equipment up to INR 100,000 is defined as micro enterprises and INR 100,000 to Rs 20 million as small units. The new Press Note is sixth in a series in 2009. The MSE sector in India has around 26 million units which employ about 60 million people.

**2. Foreign Exchange Management Act to be amended to reflect Press Notes 2 & 4.**

The government has sought to put an end to the ambiguities in the implementation of Press Notes 2 and 4, which significantly relaxed foreign direct investment guidelines, with the commerce ministry requesting the Reserve Bank of India (RBI) to make changes in the Foreign Exchange Management Act (FEMA) to operationalise the guidelines. The direction from the government follows a number of references and queries from investors, who have pointed out that the changes have not been incorporated in the FEMA or notified in the annual master circular on foreign direct investment (FDI) issued by the RBI.

The ministry has also requested the RBI to incorporate the changes in FEMA following Press Note 6, which made changes in FDI rules for the small scale and micro scale industrial undertakings. Press Notes 2 and 4 state that FDI routed through an Indian company owned and controlled by resident Indians will not be taken into account while calculating sectoral limits. An

Indian-owned company is defined as one in which resident Indians or Indian companies have more than a 50 per cent beneficial stake. Control has been defined as the power to appoint the majority of directors. The guidelines also include rules for transfer of ownership or control of Indian companies in sectors with FDI limits from resident Indian citizens to non-resident Indian citizens.

### **3. Law ministry clears new Foreign Direct Investment screen test**

The long-pending proposal to enact a new law to screen foreign investment for security reasons has been cleared by the law ministry. Finishing touches are being given to the proposed legislation, and the final draft is expected to be ready by the year-end. The Cabinet secretariat is working on the proposed law, which will be critical for sensitive sectors such as telecom. There will be sectors that would be strategic, in which foreign direct investment (FDI) would not be allowed through the automatic route. In some cases, FDI will not allow. In some, use of the Foreign Investment Promotion Board (FIPB) route to further scrutinise. And in some cases, the automatic route will be allowed, but there will be post-sanction scrutiny.

The new law would outline guidelines by which security screening of FDI on the basis of sensitive locations and sectors would be conducted. Foreign firms with a dubious background would also come under the security lens, irrespective of the country of origin or sector of operation. The earlier discussions on sector-specific or country-specific restrictions have been dropped in favour of an intervention wherever necessary, not guided by the sector of investment or origin of funds. Currently, FDI proposals for certain sectors like telecom, defence and aviation are screened by security agencies. FIPB takes inputs from the home ministry before clearing such proposals. However, proposals going through the automatic route do not face this scrutiny. The proposed legislation would bring proposals under the automatic route, which is handled by Reserve Bank of India, also under the security radar.

### **4. Realty watchdog work in full swing**

A draft bill on the much-awaited real estate regulator is being finalized that will protect the interest of home buyers by ensuring a transparent and healthy real estate sector. According to the draft, a builder will have to register a project with the regulator before he can market the properties. For this, the builder will have to submit a documentary proof of land ownership and the mandatory licenses to the regulator for registration. Once verified, the entire information about the project will be available on the regulator's website that will be accessible to everybody. The regulator will also scrutinize the advertisements and names of brokers. This process will ensure the legitimacy and the viability of the project, ending the current practice of realty firms launching projects without land ownership or mandatory approvals that leads to buyers getting stuck with inappropriate or illegal projects.

If the proposed regulator gets all the proposed powers, a property buyer would know exactly what he is buying. Importantly, the draft bill prohibits a builder from accepting an advance from a home buyer before the sale agreement is signed. At present, builders force buyers to pay 20-30

per cent of the cost of the property before making a sale agreement. To make the builder accountable, the draft suggests that he will have to submit a bank guarantee of 5 per cent of the total cost of the project, which will be encashed by the regulator if the builder does not complete the project on time or violate a condition that has been agreed upon in the agreement. The draft bill also addresses the concern of the home buyer on the cancellation of an allotment. If a builder unilaterally cancels the allotment, he will have to refund the entire amount along with interest. At present, developers generally forfeit a disproportionately-large percentage of the total amount paid by the buyer if the sale deed is cancelled on the buyer failing to make timely payment.

#### **5. Pension Regulatory Fund Development Authority Nod for corporate pension fund proposal**

The board of the Pension Regulatory Fund Development Authority (PRFDA) on September 3, 2009 approved the proposal to manage the pension corpus of companies. The pension regulator has given its in-principle nod to the proposal and it will announce the guidelines for managing such funds in about four weeks. Corpus management of companies will be a new area for PRFDA. Till now it has been managing the corpus of individuals under the New Pension System. The scheme, which was earlier restricted to government employees, was extended to all citizens in May this year.

#### **6. Government mulls leasing sick units under Public Private Partnership**

The government may lease six sick units on a public private partnership (PPP) basis instead of disposing of these units through an outright sale. The department of fertiliser plans to invite bids for the revival of these plants in November and is seeking Cabinet clearance to start the process. The department had earlier also examined the option of a direct equity sale but opted for a PPP model because it offered revenue sharing opportunities. In April 2007, the Cabinet decided to revive eight plants owned by the Fertiliser Corporation of India and Hindustan Fertiliser Corporation. These plants include Barauni, Talcher, Ramagundam, Durgapur, Haldia, Gorakhpur, Korba and Sindri. Each of these has the capacity to produce about 1.15 million tonne of urea a year and their revival is estimated to require investment of INR 45 billion each. The department will initially invite bids for six plants.

The PPP mode will involve an upfront payment by private bidders, along with a revenue share to be paid to the government over the lease. The concession period has not yet been finalised but the department is looking at the possibility of 90 years. Besides, land will also be leased out to the private companies for commercial use. The plan to long-lease sick units is the outcome of discussions by an empowered panel of secretaries that the Cabinet approved in October 2008. Chaired by the fertiliser secretary, its objective was to suggest financial models for the revival of eight units.

#### **7. Deemed export benefits on way out**

The finance ministry is planning to downsize or scrap incentives to the industry that are prone to

abuse. The changes may take effect in budget 2010-11. Schemes that may get downsized or may even be scrapped include deemed export benefits that the commerce ministry gives to exporters, with budgetary support from the finance ministry. This is one of the two duty drawback schemes through which the government compensates an exporter for the duty paid in India on products that are exported. The idea is to ensure that taxes paid here do not make the product less competitive abroad.

This benefit, called deemed export benefits or 'duty draw back and refund of terminal excise duty', is believed to be abused by exporters who make fake claims to demand excess refund of taxes paid in India. For this scheme, the government provides funds to the commerce ministry as a budgetary allocation. This scheme compensates exporters on claims that are not generally entertained under the other larger scheme of duty drawback scheme operated by the Central Board of Excise and Customs, for which more documentary support is required. The larger duty draw back scheme is a statutory benefit unlike the deemed export benefit.

#### **8. Supreme Court: Warrant issued by foreign court cannot be executed in India**

The Supreme Court has held that a warrant issued by a foreign court could not be executed in India without a formal request from the Government concerned for extradition of the accused. A bench of the Supreme Court set aside the Bombay High Court order, whereby it had refused to stay the arrest of a non resident Indian, who is facing allegations of kidnapping his own daughter from the custody of her mother.

A Georgia court in the US had issued an arrest warrant against him and Interpol subsequently issued red corner notice (RCN) for his arrest. Disposing the appeal, the apex court concurred with the stand of Ministry of External Affairs (MEA), which had stated that even violation of an order passed by the court of competent jurisdiction in the US was punishable for six months only and hence, he could not be extradited for the commission of such an offence.

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