Inter alia...

AZB & PARTNERS
ADVOCATES & SOLICITORS

SEPTEMBER 2011 • STRICTLY FOR PRIVATE CIRCULATION

Contents

Inter alia… is a legal newsletter published each quarter by AZB & Partners for a select list of clients and colleagues. Each issue aims to provide a snapshot of the recent legal developments in certain critical areas: infrastructure, foreign direct investment, securities law, exchange control regulations, corporate law, media and entertainment, intellectual property and banking. We hope you will find the content informative and useful. If you have any questions or comments, please email us at: editor.interalia@azbpartners.com or call AZB & Partners.

AZB & PARTNERS
ADVOCATES & SOLICITORS

MUMBAI
EXPRESS TOWERS | 23RD FLOOR | NARIMAN POINT | MUMBAI 400021 | INDIA | TEL +91 22 66396880 | FAX +91 22 66396888 | EMAIL mumbai@azbpartners.com

DELHI
AZB HOUSE | PLOT NO. A8 | SECTOR 4 | NOIDA 201301 | INDIA | TEL +91 120 4179999 | FAX +91 120 4179900 | EMAIL delhi@azbpartners.com

BANGALORE
AZB HOUSE | 67-4 4TH CROSS | LAVELLE ROAD | BANGALORE 560001 | INDIA | TEL +91 80 42400500 | FAX +91 80 22213947 | EMAIL bangalore@azbpartners.com

PUNE
ONYX TOWERS | 1101-B | 11TH FLOOR | NORTH MAIN ROAD | KOREGAON PARK | PUNE 411001 | INDIA | TEL +91 20 67256666 | FAX +91 20 67256600 | EMAIL pune@azbpartners.com

AZB & PARTNERS
ADVOCATES & SOLICITORS

Inter alia...

- Waiver of Central Government approval for payment of remuneration to professional managerial personnel
- Guidelines relating to scheme of arrangement/ amalgamation
- Name availability guidelines

Corporate

❖ The Ministry of Corporate Affairs ('**MCA**') has, by its circular dated July 14, 2011, waived the requirement for listed companies or their subsidiaries to seek approval of the Central Government for payment of remuneration to professional managerial personnel ('**Personnel**') of companies having no profits or inadequate profits, provided that such Personnel do not have any direct or indirect interest in the capital of the company or its holding company (during a period of two years prior to the date of appointment of such Personnel by the company) and such Personnel have at least a graduate level qualification with expert and specialised knowledge in their profession.

❖ MCA, by its circular dated July 26, 2011 has issued guidelines ('**MCA Guidelines**') to the Regional Directors ('**RDs**') and Registrar of Companies ('**ROCs**') in relation to a scheme of arrangement/amalgamation ('**Schemes**') under Sections 391-394 of the (Indian) Companies Act, 1956 ('**Companies Act**'). The MCA Guidelines require ROCs to examine/undertake, *inter alia*, matters such as (i) the filing position; (ii) investor grievances; (iii) inspection, investigations, technical scrutiny; and (iv) pending prosecutions against the relevant companies and their directors, and to submit their report to the RD in a time bound manner. Thereafter, RDs are required to examine/undertake various matters including (i) whether notices were served to the concerned regulatory authorities; (ii) obtaining opinion of the Law Ministry on complicated legal/technical issues; (iii) whether share exchange ratio is as per the valuation report and generally accepted accounting principles; (iv) whether consideration is paid in cash or other than in shares; (v) whether there will be a substantial increase in promoters' holding in listed companies; and (vi) whether the Schemes are meant to circumvent the law in garb of obtaining the approval of the relevant High Court under the accepted principle of "Single Window" approval[1].

❖ MCA has issued the Name Availability Guidelines, 2011 on July 8, 2011 (which came into effect from July 24, 2011). Some of the key provisions contained in these guidelines are as follows:

i. the guidelines supersede all previous circulars and instructions issued by MCA regarding name availabillity, thereby, *inter alia*, doing away with the higher minimum authorised share capital criteria for use of certain key words in the corporate names *i.e.* "Corporation", "International", "InterContinental", "Asia", "India", "Industries", "Enterprises", "Business", "Manufacturing" *etc.*;
ii. the proposed name need not necessarily be indicative of the main object, unless the main business is a financial activity *e.g.* finance, housing finance, chit fund *etc.*; and
iii. if the proposed names include words such as "Insurance", "Bank", "Stock Exchange", "Venture Capital", "Asset Management", "Mutual fund" *etc.*, the applicant would need to provide a declaration as regards compliance with requirements prescribed by the respective legislations and regulators regarding such indicative businesses.

Capital Markets & Securities

- Amendment to the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996

❖ The Securities and Exchange Board of India ('**SEBI**') in its board meeting held on July 28, 2011 has reviewed certain policies relating to mutual funds ('**MFs**') and proposed certain amendments to the SEBI (Mutual Funds) Regulations, 1996 ('**MF Regulations**'). Subsequently, on August 30, 2011, SEBI issued the SEBI (Mutual Funds) (Amendment) Regulations, 2011 ('**Amendment Regulations**') incorporating amendments to the MF Regulations. Some of the key amendments are:

i. Regulation 24 of the MF Regulations has been amended to prescribe specific requirements to be complied with by asset management companies ('**AMCs**') to (a) undertake management and advisory services to pooled assets including offshore funds, insurance funds, pension funds, provident funds *etc.*; and (b) undertake portfolio management services and advisory services for non broad based funds. The amended Regulation 24 provides guidance on, *inter alia,* disclosures to be made with respect to conflict of interest (if any), sharing of fund managers and other key personnel for certain activities, and certain other requirements to be complied with by the AMCs to undertake such activities.
ii. Regulation 25 of the MF Regulations has been amended to include a requirement that all the operations of MFs including trading desks, unit holder servicing, and investment operations, if already not based in India, should be brought in India within a period of one year from the notification of the Amendment Regulations.

1 Under Sections 391-394 of the Companies Act.

iii. The Amendment Regulations have included a separate chapter in the MF Regulations on launching infrastructure debt fund schemes by MFs.

❖ SEBI, through a circular dated August 9, 2009[2] ('**SEBI Circular**') has permitted Qualified Foreign Investors ('**QFIs**') to invest in equity and debt schemes of MFs through the following two routes:

i. Direct route: Under this route QFIs can hold MF units in demat accounts in India through a SEBI registered depository participant ('**DP**'). QFIs are required to open a demat account with a qualified DP, and can subscribe and redeem units of MFs through such DP.
ii. Indirect route: Under this route QFIs can hold MF units *via* Unit Confirmation Receipt ('**UCR**'). The MF is required to appoint UCR issuing agents overseas and one SEBI registered custodian in India. Rupee denominated units of the MFs are held as underlying by the custodian in India in demat mode against which the UCR issuer would issue UCR to be held by QFIs. QFIs are permitted to subscribe/redeem units of MFs through the UCR issuer, who acts as an agent to the MF.

The SEBI Circular provides guidance on the operational and other requirements for implementing these investment routes and clarifies that a QFI cannot be a person resident in India or a foreign institutional investor or a sub-account registered with SEBI.

❖ SEBI had prescribed initial listing and disclosure norms with regard to the issue and listing of debt securities in the form of the SEBI (Issue and Listing of Debt Securities) Regulations, 2008 ('**Debt Listing Regulations**'). SEBI has by way of a circular dated September 28, 2011, prescribed additional disclosure and other guidelines with regard to the issue and listing of structured products/market linked debentures ('**Guidelines**'). These will be applicable to structured products/market linked debentures including all such securities that have an underlying principal component in the form of debt securities as defined under Regulation 2(d) of the Debt Listing Regulations, and where the returns are linked to market returns on other underlying securities/indices. However, securities which do not promise to return the principal amount in full at the end of the tenor of the instrument will not be considered as debt securities and, therefore, will not be eligible for issue and listing under the Debt Listing Regulations. The Guidelines will be applicable in relation to all offer documents for which in-principle/final approval is sought from the stock exchanges on or after November 1, 2011. Certain (primary) criteria has been prescribed in the Guidelines for the issue of structured products/market linked debentures. Furthermore, SEBI has prescribed certain additional disclosures (in addition to the Debt Listing Regulations) to be made in all offer documents relating to the issue of such structured products/market linked debentures.

❖ SEBI has, on August 16, 2011, amended Regulation 13 of the SEBI (Prohibition of Insider Trading) Regulations, 1992 to specifically include within its purview disclosures which are to be made by the "promoters" and members of "promoter group" of listed companies, thereby mandating certain disclosures of interest or holding (*i.e.* shares or voting rights) and change in interest by the "promoters" and members of "promoter group" (as per the prescribed thresholds) within the time prescribed.

❖ SEBI on September 23, 2011, has issued the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ('**New Takeover Regulations**') replacing in entirety the existing SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997. The New Takeover Regulations will come into force from October 23, 2011[3].

❖ Pursuant to the notification of the New Takeover Regulations, a consequent amendment has also been made to Clause 35 of the equity listing agreement ('Listing Agreement') which clarifies that the meaning of the term "encumbrance" as used in the Listing Agreement will have the same meaning as under Regulation 28(3) of the New Takeover Regulations, *i.e.* will include, "a pledge, lien or any such transaction, by whatever name called". Going forward therefore, one would need to determine whether arrangements such as non-disposal arrangements, and other transfer restrictions on shares of a listed company would need to be disclosed pursuant to the terms of the Listing Agreement.

❖ On August 1, 2011, SEBI issued a concept paper along with the draft SEBI (Alternative Investment Funds) Regulations, 2011 ('**Draft Regulations**') that seek to introduce a comprehensive regulatory framework for private pools of capital which collect funds from institutional or high net worth investors in India and the manager of such Alternate Investment Fund ('**AIF**') who manages the fund for investments in India. The Draft Regulations seek to subsume the SEBI (Venture Capital Fund) Regulations, 1996 ('**VCF Regulations**'), though existing domestic

2 CIR/IMD/DF/14/2011.

3 For further details, please refer to our Client Update of October 2011.

venture capital funds ('**VCFs**') would continue to be regulated under the VCF Regulations until wound up. However, the SEBI (Foreign Venture Capital Investor) Regulations, 2000 have not been subsumed in the Draft Regulations. Additionally, all portfolio management schemes that "pool" assets for investment in unlisted securities are also proposed to be regulated under the Draft Regulations, and no carve out has been made for existing pooled schemes.

The Draft Regulations provide for the following categories of funds: (i) VCFs; (ii) private investment in public equity ('**PIPE**') funds; (iii) private equity funds; (iv) infrastructure funds; (v) debt funds; (vi) real estate funds; (vii) small and medium enterprise ('**SME**') funds; (viii) social venture funds; and (ix) strategy funds (residual category, including hedge funds). The Draft Regulations have provided investment restrictions applicable to each of the aforesaid categories of funds.

The Draft Regulations provide for AIFs to be registered in the form of trusts, companies, or LLPs. The number of shareholders/partners is restricted to 50 in case the AIF is registered as a company/LLP. If registered as a trust, it is proposed that 1,000 investors could participate in the concerned AIF. The Draft Regulations provide for the minimum size of an AIF as ₹200 million and minimum investment amount by an investor, as greater of ₹10 million or 0.1% of the fund size. The Draft Regulations provide the term of the AIF to be for a minimum period of five years and extendable by up to two years upon approval of at least 75% of the investors. AIFs are required to be close ended and limit redemption rights of investors.

The manager or sponsor or designated partner will need to contribute at least 5% of the total contributions of the AIF, which will be locked in till the redemption by the last investor. Amongst providing limitations for co-investments by the sponsor in underlying portfolio investments, the Draft Regulations also provide for the AIF's sponsor, manager or designated partner to acquire all unliquidated investments at the end of the fund term.

There have been multiple representations made by various associations and VCF associations to delink the highly regimented silor proposed by the Draft Regulations.

❖ On September 26, 2011, SEBI issued a concept paper ('**IA Concept Paper**') that seeks to introduce a comprehensive regulatory framework for regulating investment advisors. SEBI has invited comments on the Concept Paper latest by October 31, 2011. The IA Concept Paper defines investment advisor to mean "any person or entity that provide investment advice directly or indirectly for a consideration, which may be received directly from the investor or who holds himself out as an investment advisor". Further, "investment advice" is defined as an advice whether written, oral or through any other means regarding investment of funds in financial products or products that are traded and settled like financial products for the benefit of the investor (including financial advice, financial planning service or actions which would influence an investment decision and are incidental to making an investment/investment decision).

The IA Concept Paper also sets out the various categories of individuals/non-individuals who would be required to obtain registration in order to provide investment advisory services. It provides specific exemptions for certain classes of individuals and entities who provide investment advice solely incidental to some other business or profession and in the course of other business or profession, and where the advice is general and does not specify particular securities. Further, presently, it is not clear if the proposed framework will also apply where investment advice is being provided by local advisory companies only to persons/entities (including offshore managers and funds) outside India. The IA Concept Paper also sets out the registration requirements for persons seeking registration as an investment advisor including requirements in relation to minimum qualification, capital adequacy, key personnel, adequate infrastructure, fit and proper criteria. The IA Concept Paper stipulates certain other conditions and disclosure requirements to be complied with by investment advisors including in relation to fees and charges, business, disciplinary history, terms and conditions on which it offers advisory services among others. Interestingly the IA Concept Paper limits the civil and criminal liability of investment advisors in respect of advice given by them only to advice that is negligent or *malafide* in nature and any dispute between the investment advisor and his client would be resolved through grievance redressal mechanism or arbitration created by SEBI.

❖ On September 23, 2011, SEBI notified the SEBI (Issue of Capital and Disclosure Requirements) (Second Amendment) Regulations, 2011 ('**ICDR Amendment Regulations**'). Some of the significant changes to the SEBI (Issue of Capital and Disclosure Requirements) Regulations, 2009, as amended ('**ICDR Regulations**') are set out below:

i. Certain of the criteria for undertaking an initial public offer[4], has been amended by way of the ICDR Amendment Regulations *viz.* the limit of 50% of the net tangible assets being held by way of monetary assets is no longer applicable in the case of a public offer undertaken entirely by way of an offer for sale; and the track record of distributable profits for at least three out of the immediately preceding five years is

4 Specified under Regulation 26 of the ICDR Regulations.

now required to be met with by the issuer on both a stand-alone and consolidated basis. An issuer with a subsidiary(ies) for a period of less than five years is required to have net profits on a consolidated basis in at least one year for which consolidated accounts of the issuer are prepared.

ii. The ICDR Amendment Regulations prescribe enclosure of a statement on "Price Information of Past Issues handled by Merchant Bankers (who are responsible for pricing this issue)" with all due diligence certificates to be submitted to SEBI by lead managers in relation to draft red herring prospectuses filed with SEBI, and red herring prospectuses and prospectuses filed with ROCs on or after November 1, 2011. The format for such disclosure has been specified by SEBI by way of a circular dated September 27, 2011[5].

iii. The format and contents of bid-cum-application forms have been rationalised to ensure that materially important information is provided in a structured, logical and user-friendly manner. Furthermore, there would be a single bid-cum-application form for bids *via* both the ASBA route, *i.e.* application supported by blocked amount process, and the non-ASBA route. The abridged prospectus is to now contain company/project specific information and emphasise materially relevant disclosures. Generic information, not specific to an issuer, is to be brought out in the form of a general information document, circulated along with a bid-cum-application form. The contents of bid-cum-application forms and general information documents have been specified by SEBI by way of a circular dated September 27, 2011[6], which is applicable to all red herring prospectuses and prospectuses filed with ROCs on or after November 1, 2011.

iv. The ICDR Amendment Regulations prescribe the conditions applicable in the case of a rights issue of Indian depository receipts ('**IDRs**') and a rights issue of IDRs on a fast track basis. In this regard, an offer document and an addendum are required to be filed with SEBI and the stock exchanges where the IDRs are proposed to be listed. Furthermore, a draft offer document is required to be filed with SEBI on a confidential basis. The disclosures in the draft offer document and offer document are to be in compliance with the home country requirements of the listed issuer and the addendums to each of the draft offer document and the offer document (to be attached to the offer document to be circulated in India) must contain the relevant disclosures prescribed under the ICDR Amendment Regulations.

In order to be eligible for a rights issue of IDRs, the issuer (i) should not be in breach of ongoing material obligations under the IDR Listing Agreement, as applicable, or material obligations under the deposit agreement entered into between the domestic depository and the issuer; and (ii) should have made an application to all the recognised stock exchanges in India, where its IDRs are listed, for listing of the IDRs to be issued by way of the rights issue, and chosen one such stock exchange as the designated stock exchange.

❖ SEBI (Merchant Bankers) Second Amendment Regulations, 2011

❖ SEBI has, on August 16, 2011, amended Regulation 14(1), sub-regulation (1) of the SEBI (Merchant Bankers) Regulations, 1992 by inserting a new clause which states that every merchant banker must keep and maintain records and documents pertaining to due diligence exercised in pre-issue and post-issue activities of issue management and in case of takeovers, buybacks and delisting of securities.

Foreign Investment & Trade

❖ New Consolidated Foreign Direct Investment Policy

❖ Government of India ('**GoI**') has issued the consolidated foreign direct investment ('**FDI**') policy on September 30, 2011 to be effective from October 1, 2011 ('**FDI Policy**'). Some of the significant changes which have been introduced in the FDI Policy include *inter alia*:

i. FDI in construction development activities in the education sector and old-age homes has been exempted from the conditionalities (such as minimum and built up area, capitalisation and lock-in) imposed on FDI in the construction development sector.

ii. FDI in apiculture (bee-keeping) has been permitted upto 100% under the automatic route, under controlled conditions.

iii. Previously, FDI upto 100% under the automatic route was permitted in existing and new industrial parks. This coverage has been now been expanded to specifically include research and development in bio-technology, pharmaceutical and life sciences.

5 Bearing No. CIR/CFD/DIL/5/2011.

6 Bearing No. CIR/CFD/DIL/4/2011.

iv. FDI limit for FM radio has been enhanced to 26% from the earlier 20%.

v. Applications for conversion of imported capital goods/machinery and pre-operative/pre-incorporation expenses to equity instruments are to be made within 180 days from the date of such import of capital goods/machinery. Payments for pre-operative/incorporation expenses can now be made directly by the foreign investor to the company or through a bank account, opened by the foreign investor, as provided under Foreign Exchange Management Act, 1999 regulations.

vi. Apart from the above, the FDI Policy also incorporates a specific clarification stating that only equity shares, fully, compulsorily and mandatorily convertible debentures and fully, compulsorily and mandatorily convertible preference shares, with no in-built options of any type, would qualify as eligible instruments for FDI. As a consequence, any such instruments which are issued or transferred to non-residents which have in-built options or supported by options sold by third parties would lose their equity characteristic and need to adhere to the extant external commercial borrowings ('**ECB**') policy. The exact scope and implications of the condition, including whether its application is prospective or retrospective, is yet to be ascertained and further clarifications are expected shortly.

❖ The Department of Industrial Policy and Promotion ('**DIPP**') had introduced a discussion paper on the rationale and relevance of caps in the FDI Policy, and had invited feedback on related issues by July 15, 2011. As per the discussion paper, the following issues were open for views, suggestions and feedback: (i) whether the equity caps fulfil any purpose other than control? (ii) whether, in the context of the FDI policy, activities that can now be undertaken indirectly, through downstream investments, should be allowed to be done directly? (iii) whether there is any relevance left for equity caps, especially below 49%? (iv) whether the concerns supposed to be addressed by control through equity caps can be addressed through sectoral conditions? (v) whether imposition of caps create an unfair opportunity for arbitrage? (vi) if at all it is better to have caps in certain sectors, whether a better option is to ask multi national corporations to have their securities listed on Indian stock exchanges and then offload equity within a stipulated period? and (vii) as long as sectoral caps exist, whether it should be specified that they are exclusive of foreign institutional investment ('**FII**')?

❖ The Reserve Bank of India ('**RBI**') has issued a series of circulars on September 23, 2011 and September 26, 2011 with respect to liberalisation and rationalisation of ECBs, specifically in the infrastructure sector.

Pursuant to the aforesaid circulars, RBI has, subject to certain prescribed conditions permitted infrastructure companies to (i) utilise 25% of fresh ECB towards refinancing domestic Rupee loans under the approval route; and (ii) import capital goods by availing of short term credit, under the approval route. Further, "Interest During Construction" has been introduced as a permissible end-use for infrastructure companies. RBI has also enhanced the ECB limit for (i) borrowers under the automatic route for the real estate sector, industrial and infrastructure sector by US$250 million per financial year; and (ii) corporates in service sectors by US$100 million per financial year.

RBI has further liberalised the policy relating to structured obligations to permit direct/indirect foreign equity holders as per the ECB guidelines to provide credit enhancement to Indian companies engaged exclusively in the development of infrastructure. In this regard, RBI has issued certain clarifications, including with respect to: (i) the term "debt" in the debt-equity ratio; and (ii) calculation of equity of the foreign equity holder for ECBs of or beyond US$ 5 million.

❖ RBI through a circular dated September 7, 2011 ('**ECB Circular**') has simplified the procedure in relation to request for change of lenders for an existing ECB, which may now be approved by Authorised Dealer Category-I banks ('**AD Banks**') and reported to RBI, provided the original lender is an (i) international bank; (ii) a multilateral financial institution; (iii) a regional financial institution; (iv) an export credit agency; or (v) a supplier of equipment, and the new lender also belongs to any one of the above mentioned categories. In this regard, the AD Bank will have to ensure that certain conditions are fulfilled, including that the new lender is a recognised lender, that there is no change in other terms and conditions of the ECB, and that the ECB is in compliance with the extant ECB guidelines.

❖ RBI, through a circular dated August 23, 2011 has amended the Issuance of Non-Convertible Debentures (Reserve Bank) Directions, 2010 dated June 23, 2010 ('**NCD Directions**') to revise the symbol of minimum rating required for issuance of non-convertible debentures of maturity up to a period of one year. The circular came as a result of the standardisation of rating symbols and definitions for credit rating agencies by SEBI.

❖ RBI, by its circular dated July 15, 2011 has attempted to regularise the establishment of liaison offices ('LOs') and branch offices ('BOs') of foreign entities established in India prior to June 1, 2000 which were functioning without the approval of RBI, by requiring foreign entities who have established an LO or BO in India prior to June 1, 2000, which continue to function without obtaining prior permission from RBI, to approach RBI within a period of 90 days from July 15, 2011 for regularisation of establishment of such offices in India.

❖ RBI, through a circular dated July 21, 2011 ('**Hedging Circular**') has allowed non-resident importers and exporters to hedge their currency risk with respect to exports from and imports to India, invoiced in Indian Rupees with AD Banks in India. The relevant products to which this circular is applicable are forward foreign exchange contracts with Indian Rupees as one of the currencies and foreign currency- Indian Rupee options. The AD Bank can opt for one of the prescribed models to facilitate the abovementioned hedging facilities.

❖ Hedging facilities for non-resident entities

Banking & Finance

❖ Working group report on non banking financial companies

❖ Draft guidelines on licensing of private sector banks

❖ The Report of the Working Group on the Issues and Concerns in the NBFC Sector ('**Report**') has been released by RBI on August 23, 2011. The Report has reviewed the existing regulatory and supervisory framework of Non Banking Financial Companies ('**NBFCs**') and recommended appropriate regulatory and supervisory measures to address these issues faced by the NBFCs. Some of the key recommendations of the working group ('**Working Group**') include:

i. The requirement for registration with RBI for all new NBFCs is to be retained at net owned fund ('**NOF**') of ₹20 million till the RBI Act, 1934 ('**RBI Act**') is amended. However, the minimum asset size necessitating registration is ₹500 million.
ii. NBFCs with asset size below ₹10 billion and not accessing any public funds may be exempted from registration.
iii. All registered NBFCs, regardless of whether or not they accept deposits, may require the prior approval of RBI for a change in control or transfer of shareholding directly or indirectly in excess of 25% of the paid up capital of the company.
iv. The twin criteria of assets and income for determining the principal business of a company may continue. However, the minimum percentage threshold of assets and income may be increased to 75%.
v. Tier I capital for Capital to Risk Weighted Assets Ratio ('**CRAR**') purposes may be specified at 12%.
vi. Liquidity Ratio should be introduced for all registered NBFCs such that cash bank balances and holdings of Government securities fully cover the gaps, if any, between cumulative outflows and cumulative inflows for the first 30 days.
vii. Asset classification and provisioning norms similar to banks to be introduced in a phased manner for NBFCs.
viii. NBFCs may be subject to regulations similar to banks while lending to stock brokers and merchant banks.
ix. Board approved limits for bank's exposure to real estate may be made applicable for the bank group as a whole, where there is an NBFC in the group, with increased risk weights for NBFCs that are not sponsored by banks.
x. NBFCs may be given the benefits available to "secured creditors" under the Securatisation and Reconstruction of Financial Assets and Enforcement of Security Interests Act, 2002.
xi. All NBFCs with assets of ₹10 billion and above, whether listed or not, should be required to comply with Clause 49 of SEBI Listing Agreements including mandatory disclosures.
xii. NBFCs with assets of ₹10 billion and above will be subject to more intensive inspections.

❖ RBI, on August 29, 2011 released draft guidelines on the licensing of private sector banks ('**Draft Guidelines**'). Comments are required to be submitted to RBI on the Draft Guidelines by October 31, 2011. Some of the key features of the Draft Guidelines include:

i. Entities or groups owned and controlled by Indian residents, which have diversified ownership, and a successful track record of at least 10 years will be eligible to promote banks. Any entity/group, whose income or assets or both from real estate, construction and/or broking activities individually or taken together in the last three years is or exceeds 10% of their total income or assets may not promote banks.
ii. The aggregate non-resident shareholding in the new bank must not exceed 49% for the first five years after which it will be as per the extant policy.

iii. RBI has introduced the concept of Non-Operative Holding Company ('**NOHC**') to be registered with RBI as an NBFC through which an entity or groups is required to hold the bank as well as all the other financial companies (including NBFCs) in the promoter group. NOHCs will be governed by prudential guidelines to be separately notified by RBI.
iv. Existing NBFCs, if considered eligible by RBI, may be permitted to either promote a new bank or convert themselves into banks.
v. Minimum capital requirement for newly licensed banks will be ₹5 billion. The NOHC is required to hold at least 40% of the paid-up capital of the bank for a period of five years from the date of receipt of the banking license. Shareholding by NOHC in excess of 40% must be brought down to 20% within 10 years and to 15% within 12 years from the date of licensing of the bank.
vi. The exposure of the bank to any entity in the promoter group cannot exceed 10%, and exposure to all entities in the group cannot exceed 20%, of the paid-up capital and reserves of the bank.
vii. The bank is required to get its shares listed on stock exchanges within two years of licensing.
viii. The bank is required to maintain a minimum capital adequacy ratio of 12% for a minimum period of three years after the commencement of its operations.

Competition

❖ Leading real estate player fined for abuse of dominant position

❖ The Competition Commission of India ('**CCI**'), in the case of **Belaire Owner's Association *v.* DLF Limited and HUDA**[7], dealt with the issue of abuse of dominant position by DLF Limited ('**DLF**'). The dispute between the apartment allottees of a building complex in Gurgaon, constructed by DLF, which was being heard by the CCI, finally resulted in the CCI imposing a penalty of ₹6,300 million on DLF by its order of August 12, 2011.

The CCI limited the definition of "relevant market" as services provided by developers/ builders for construction of high end residential buildings in Gurgaon. The dominance of DLF was established by taking into account factors such as market share, relative strength over nearest competitor, economies of scale and fixed assets. The CCI held that by imposing arbitrary, unfair and unreasonable conditions on the allottees, DLF has abused its dominant position in the relevant market. The CCI directed DLF (i) to cease and desist from formulating and imposing such unfair conditions in its agreements with buyers in Gurgaon; and (ii) to suitably modify unfair conditions imposed on its buyers.

This case made it clear that provisions of an agreement entered into prior to coming into force of the Competition Act, 2002 will not escape CCI scrutiny if implementation of such provisions is now prohibited by the Competition Act, 2002.

Telecom, Media & Technology

❖ The Telecom Commercial Communications Customer Preference (Sixth Amendment) Regulations, 2011

❖ The Telecom Regulatory Authority of India ('**TRAI**'), on September 5, 2011, issued the Telecom Commercial Communications Customer Preference (Sixth Amendment) Regulations, 2011 ('**TCCCP Amendment Regulations**') amending the Telecom Commercial Communications Customer Preference Regulations ('**TCCCP Regulations**'). Some of the key amendments made to the TCCCP Regulations are as follows:

i. The provisions relating to the obligations of access providers, blacklisting of telemarketers *etc.*, which are specifically prescribed under Regulations 12, 18, 19, 20, 21 and 22 of the TCCCP Regulations are to come into force on September 27, 2011.
ii. The definition of the term "Licensee" has been included to mean any person licensed for providing specified public telecommunication services under Section 4(1) of Indian Telegraph Act, 1885.
iii. The scope of the term "transactional message" under the TCCCP Regulations has been broadened. As per the TCCCP Amendment Regulations, (i) a licensee has been included into the list of parties which are entitled to send information to customer(s); and (ii) students have been included as a party entitled to receive information from a registered educational institution (as against to only parents and guardians previously).

7 Case No. 19 of 2010 dated August 12, 2011.

iv. The erstwhile exemption granted to the agencies of the Central and State Government from the scope of unsolicited commercial communication has now been removed. Further, the transmission of messages by or on the directions of bodies established under the Constitution or TRAI ('**Authority**') or any agency authorized by such Authority have also been included in the scope of unsolicited commercial communication.

v. Limits have been prescribed for the number of short service messages ('**SMSs**') that a service provider is permitted to send *i.e.* (i) no more than 100 SMSs per day per user number; (ii) in case of post paid telephone numbers, no more than 3000 SMSs per month per user number and no more than 100 SMSs per day per user number from a date to be notified by TRAI.

❖ Amendment of telecom licenses regarding monitoring of calls

❖ The Department of Telecommunications ('**DoT**') has, by notifications dated July 13, 2011 ('**DoT Notifications**'), amended the license agreements for provision of unified access services and cellular mobile telephone services. The amendment *inter alia* provides the following:

i. The licensee is required to augment its technical systems to facilitate monitoring of at least 480 simultaneous calls with at least 30 simultaneous calls for each of the law enforcement/security agencies designated by the Central/State Government ('**Designated Agencies**'). Presently, there are nine Designated Agencies.

ii. Each MSC of the licensee in a service area is required to have the necessary capacity for providing at least 3000 numbers for monitoring.

iii. The above requirements are to be complied with within three months of the date of the DoT Notifications.

iv. The stipulations regarding the monitoring capacity and the number of Designated Agencies may be amended by the licensor separately by issuing instructions at any time.

❖ FM Radio - Phase III Policy

❖ The Union Cabinet, on July 25, 2011, issued the "Policy Guidelines on Expansion of FM radio broadcasting services through private agencies (phase – III)" ('**Phase III Policy**'), which amends the existing phase-II policy dated July 13, 2005. Some of the key features of the Phase III Policy include (i) detailed qualifications for applicant companies; (ii) the total FDI and FII limit has been increased from 20% to 26% subject to prior FIPB approval; (iii) imposition of restrictions on change of composition of the largest Indian shareholder; (iv) restriction on running of total channels in a city and country; (v) news bulletins of All India Radio is permitted to be carried in exactly the same format (unaltered) on such terms and conditions as may be mutually agreed with Prasar Bharati; and (vi) e-auction process has been introduced for granting permissions for the FM channels (city wise and channel wise).

❖ Clarifications on privacy and data security regulations

❖ GoI issued a press note on August 24, 2011 ('**IT Clarification**') providing certain clarifications on the applicability and scope of the Information Technology (Reasonable Security Practices and Procedures and Sensitive Personal Information) Rules, 2011 ('**Security Practices Rules**'). Some of the key provisions of the IT Clarification are as follows:

i. The Security Practices Rules apply only to bodies corporate or persons located within India;

ii. Rules 5 and 6 of the Security Practices Rules[8] are applicable only to entities which provide services under a direct contractual obligation with the provider of the personal data or information (*i.e.* natural persons and not body corporates that further transmit the information from natural persons), and are not applicable to entities which provide services under a contractual obligation with other bodies corporate; and

iii. The reference in Rule 5 of the Security Practices Rules to obtaining consent from information providers through "letter, fax or email" has been clarified to include any mode of electronic communication.

Insurance, Real Estate & Employment

❖ Approval for registration of transfer of shares

❖ The Insurance Regulatory Development Authority ('**IRDA**') by its circular dated August 11, 2011 has set out the regulatory process to be followed by IRDA whilst granting an approval for registration of transfer of shares under Section 6A(4) of the Insurance Act, 1938 ('**Insurance Act**'). An insurance company cannot register any transfer of shares without prior approval of IRDA, where after the transfer, the total holding of the transferee exceeds 5% of the company's

8 Rules 5 and 6 impose certain obligations on collection and disclosure of information.

❖ Land Acquisition and Rehabilitation and Resettlement Bill, 2011

❖ Treatment of international workers

paid-up capital, or where the transferee is a banking or investment company, 2.5% of the paid-up capital. IRDA is required to carry out the requisite due diligence of the proposed transferee or shareholder prior to grant of approval for registration of transfer of shares under the provisions of Section 6A (4) of the Insurance Act and for issue of shares to the proposed transferee or shareholder. IRDA is also required to examine various issues including the minimum lock-in period that may be imposed on the proposed stake holder before granting approval.

❖ The Ministry of Rural Development has prepared a preliminary draft dated July 27, 2011, of the Land Acquisition and Rehabilitation and Resettlement Bill, 2011 ('**Land Acquisition Bill**'). The objective of the Land Acquisition Bill is to facilitate land acquisition for various public purposes, while addressing the concerns of farmers and those whose livelihoods are dependent on the land being acquired.

The provisions of the Land Acquisition Bill, applies when GoI acquires land (i) for its own use, hold and control; (ii) in order to transfer it to private companies for a public purpose; and (iii) for the immediate and declared use by private companies for a public purpose. The Land Acquisition Bill prescribes the minimum compensation package payable to the person from whom the land is acquired. In addition, the Collector is required to provide rehabilitation and resettlement entitlements to the affected family. The Land Acquisition Bill does not preclude private companies from directly purchasing land from farmers and others, but proposes that in cases where a private company acquires more than the prescribed threshold, a fair rehabilitation or resettlement package be offered.

❖ The Employees' Provident Fund Organisation ('**EPFO**') has issued a circular dated August 30, 2011, to provide clarity regarding the provisions relating to treatment of international workers under the employees' provident fund scheme and the employees pension scheme framed under the Employees Provident Funds and Miscellaneous Provisions Act, 1952. Some of the key aspects of this circular are as follows (i) Indian nationals may be treated as international workers with effect from the date of commencement of the Certificate of Coverage issued by EPFO, Head Office; (ii) all foreign nationals, other than excluded employees, are to be treated as international workers and that each office of the employer may maintain a separate register with regard to such international workers; (iii) the member will continue to be an international worker till the time the final settlement is made in accordance with the provisions of the scheme.

Taxation

❖ Liaison office of foreign company to constitute permanent establishment

❖ Guidelines for prior permission under Section 281 of the Income Tax Act, 1961

❖ Parent company taxed as "real owner" of shares held by subsidiary

❖ The Authority for Advance Rulings (Income-tax) ('**AAR**'), in the case of Columbia Sportswear[9], held that the LO of the foreign company would constitute the foreign company's Permanent Establishment ('**PE**') in India under Article 5 of India-US Tax Treaty on the ground that, the LO was undertaking various activities e.g. identifying a competent manufacturer, negotiating a competitive price, getting the material tested to ensure quality, *etc.* which were beyond the scope of mere purchase of goods and/or collecting information. The AAR further held that even if the activities undertaken by the LO were covered by approval received from RBI, it would not be relevant in determining whether such activities constitute a PE of the foreign company in India under Indian tax law.

❖ Central Board of Direct Taxes ('**CBDT**') has issued Circular No. 4/2011, dated July 19, 2011, prescribing guidelines to be followed by an Assessing Officer ('**AO**') while considering an application for permission to transfer or create a charge on the assets of the taxpayer as contemplated under Section 281 of the Income Tax Act, 1961. The circular *inter alia*, provides (i) circumstances under which permission should be granted by an AO; (ii) the process for applying for permission, including the form for the same; (iii) timelines for grant/refusal of permission; and (iv) validity of permission.

❖ The Bombay High Court ('**Bombay HC**') in the case of Aditya Birla Nuvo & Ors *v.* DDIT & Ors.[10], held that even though the registered shareholder of the shares of the Indian joint venture company ('**JV**') was the Mauritian subsidiary of the US parent, the "real" owner of such shares was the US parent, and the Mauritian subsidiary had merely held such shares as a "permitted transferee" and "no more than a representative" of the US parent. While reaching this conclusion, Bombay HC *inter alia*, relied significantly on the wording of the clauses in the joint venture agreement and shareholders' agreement amongst the US parent and Indian joint venture partners, which, *inter alia*, contemplated that (i) the right to appoint directors to the board of the JV

9 **Columbia Sportswear Co., In re.**, [2011] 12 taxmann.com 349 (AAR - New Delhi), dated August 8, 2011.

10 **Aditya Birla Nuvo & Ors *v.* DDIT & Ors.**, [2011] 12 taxmann.com 141 (Bom.), dated July 14, 2011.

vested with the US parent and not the Mauritian subsidiary (which was the registered shareholder); (ii) veto rights were available to the US parent and not the Mauritian subsidiary; (iii) there was joint and several liability of the US parent and Mauritian subsidiary, even though the US parent was not the registered shareholder; and (iv) in case of offer for sale from a third party, right of first refusal was granted to the US parent and not the Mauritian subsidiary. Accordingly, Bombay HC held that it was a case of the US parent (being the owner of shares of JV) selling the shares of the JV and not the case of Mauritius registered shareholder selling the shares of the JV.

Aditya Birla Nuvo and New Cingular Wireless Services Inc. have filed Special Leave Petitions against this decision, which are currently pending before the Supreme Court ('**SC**'). Separately, New Cingular Wireless Services Inc. has also filed an Intervention Application before SC in the Vodafone case on the ground that Bombay HC in the Aditya Birla Nuvo case has made references to its decision in the Vodafone matter. The hearings in the Vodafone matter are currently ongoing in SC.

AZB & PARTNERS
ADVOCATES & SOLICITORS
Inter alia...

❖ Supply of SIM Cards liable to service tax

❖ SC, in **Idea Mobile Communication Ltd. *v.* Commissioner of Central Excise & Customs, Cochin**[11], delivered an important ruling on the question of whether the value of SIM cards sold by Idea Mobile Communications Ltd. ('**Idea**') to their mobile subscribers should be considered a taxable service or whether it should be taxable as sale of goods. SC held that the amount received by Idea from its subscribers towards SIM cards will attract the levy of service tax as SIM cards are never sold as goods independent from services provided and are considered part and parcel of the services provided. The dominant position of the transaction is to provide services, and not to sell goods, *i.e.* SIM cards, which would hardly have any value on its own, without the service.

Intellectual Property

❖ No safe harbor for intermediaries for copyright infringement in India

❖ Copyright societies and royalties

❖ In the case of **Super Cassettes Industries Ltd. *v.* MySpace Inc. & Another**[12], Delhi High Court ('**Delhi HC**'), for the first time dealt with the issue of intermediary liability for copyright infringement in India.

The Super Cassettes Industries Ltd. ('**SCL**') contended that the defendants were guilty of primary infringement under Section 51(a)(i) and Section 51(a)(ii) of the Copyright Act, 1957 ('**Copyright Act**'), as the defendants were communicating and disseminating copyrighted works of SCL to the public and providing a platform to users for uploading infringing content. SCL also contended that the defendant had knowledge of such infringement, given that they had created specific technological tools to tackle copyright infringement, and were also generating revenue by placing advertisements along with the infringing content. One of the arguments relied upon by the defendant was that the defendant was an "intermediary" under the Information Technology Act, 2000 ('**IT Act**') and, therefore, could not be held liable for copyright infringement committed by third parties, relying on the "safe harbour" provisions under Section 79 of the IT Act.

Delhi HC held the defendant liable for copyright infringement, on the ground that the rights exercised under the Copyright Act (as provided under the proviso to Section 81 of the IT Act) would override *inter alia* the protection provided to intermediaries under the IT Act.

❖ Two recent judgments by the Bombay HC and the Delhi HC have dealt with the contentious issue of payment of royalties for a copyrighted work to collecting societies.

In **Music Broadcast Private Ltd. *v.* Indian Performing Rights Society Ltd.**,[13] Music Broadcast Private Ltd. ('**MBPL**') had sought *inter alia*, a permanent injunction restraining Indian Performing Rights Society Ltd. ('**IPRS**') from demanding or collecting royalties in respect of sound recordings broadcasted by its FM radio station, arguing that MBPL was only required to obtain a license for such broadcast from the Phonographic Performance Ltd. ('**PPL**'), and that IPRS could charge royalties only if there is a "public performance" of such copyrighted work. Bombay HC held in favour of MBPL *inter alia* holding that IPRS was not entitled to receive any royalty, and that IPRS cannot interfere with the MBPL's broadcast of sound recordings. The court held that once the underlying works were incorporated into a sound recording, a new copyrightable work, *i.e.*, the sound recording, comes into existence. Hence, it held that the producer or owner of the sound recording was the owner of the copyrighted work and had exclusive right to it under Section 14(1)(e) of the Copyright Act, 1957. An appeal against the judgment has been admitted by the Division Bench of the Bombay High Court and the operation of the judgment has been stayed pending disposal of the appeal[14].

11 2011-TIOL-71-SC-ST, dated August 4, 2011.

12 IA No. 15781/2008 and IA No. 3085/2009 in CS (OS) No. 2682/2008 (dated July 29, 2011).

13 Suit No. 2401 of 2006, Bombay HC (dated July 18, 2011).

14 APP/615/2011, Division Bench, Bombay HC.

In IPRS **v. Aditya Pandey & Another**[15] and PPL **& Ors v.** CRI **Events Private Limited & Ors**[16], the issue of the eligibility of IPRS to charge royalties for broadcast of sound recordings was discussed. In this case, the Delhi HC discussed *inter alia* in detail, ownership and authorship of a work and the question of ability to exploit a work or exercise exclusive rights over such work being coextensive to the extent of ownership, right, or license granted over such work. The court after examining the definition and scope of copyright under Section 14 of the Copyright Act, 1957, *inter alia* clarified that if the sound recording were to be "performed" in public, a license from IPRS is essential, whereas if the same were to be "played" in public, a license from the PPL would suffice. Appeals against the orders are pending before the Delhi High Court[17].

15 CS (OS) 1185/2006, dated July 18, 2011.

16 CS (OS) 1996/2009, Delhi HC, dated July 18, 2011High Court.

17 FAO (OS) 425/2011 and FAO(OS) 423/2011.