

May 2014

Highlights

- DIPP releases Consolidated FDI Policy, 2014.
- RBI permits FDI in Limited Liability Partnerships.
- SEBI amends Clauses 35B and 49 of Listing Agreement.
- SEBI sets Foreign Portfolio Investor limit of 10% equity.
- SEBI to frame regulatory norms for Foreign Account Tax Compliance Act.
- Deposit Regulations notified under Companies Act, 2013.
- Delhi High Court: Mere co-operation between consortium members does not result in an 'Association of Persons'.
- SC: Stay on Demolition of two Supertech towers in Noida.
- SC: Tenants under lawful possession in terms of TPA cannot be forcefully dispossessed by secured creditor acting under SARFAESI Act.

Corporate Brief

➤ *DIPP releases Consolidated FDI Policy, 2014.*

The Department of Industrial Policy and Promotion (DIPP) has released the Consolidated Foreign Direct Investment (FDI) Policy for 2014, which is effective from April 17, 2014, and supersedes the Consolidated FDI Policy, 2013. The new Policy reflects various policy changes already effected viz. definition of 'control', 'group company', non-compete clauses in pharma sector, issuance of shares against royalty due for payment, increase in foreign investment limits for various sectors, etc. The new Policy clarifies that non-residents (including NRIs) having acquired and continuing to hold control in accordance with SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011, can acquire more shares of Indian listed entities through registered brokers, subject to compliance under Foreign Exchange Management Act, 1999.

[See D/o IPP F. No. 5(1)/2014-FC.I dated April 17, 2014]

➤ *RBI permits FDI in Limited Liability Partnerships (LLP).*

Under the extant Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, only a Company incorporated under Companies Act, 1956 or a Venture Capital Fund was eligible to accept FDI. Reserve Bank of India has amended the said Regulation specifying the norms and conditions for receiving foreign investment in LLP. Any form of foreign investment in an LLP, direct or indirect (regardless of nature of 'ownership' or 'control' of an Indian company) shall require prior government/FIPB approval. An Indian company having foreign investment (direct or indirect, irrespective of percentage of such foreign investment), will be permitted to make downstream investment in an LLP only if both company and LLP are operating in sectors where 100% FDI is allowed under the automatic route and there are no FDI-linked performance related conditions. While instructions issued in the Circular shall be effective from May 20, 2011, the reporting requirements shall come into force from the date of issue of instructions by RBI. [See RBI/2013-14/566 A.P. (DIR Series) Circular No.123 dated April 16, 2014]

➤ *SEBI amends Clauses 35B and 49 of Listing Agreement.*

Amendments to Clause 49 (Corporate Governance) of the Listing Agreement have put in place stricter disclosures for protection of investors and norms to ensure equitable treatment of all shareholders including minority and foreign shareholders. Important changes include disclosures on pay packages, implementation of an effective whistle blower mechanism, and existing material related-party contracts or arrangements which are likely to continue beyond March 31, 2015 shall be required to be placed for approval of shareholders in first general meeting subsequent to October 1, 2014 (i.e. date from which revised Clause 49 would come into effect). SEBI has also introduced a new Clause 35B, stipulating that listed entities would have to mandatorily provide e-voting facility to shareholders on resolutions proposed to be passed at general meetings.

[See CIR/CFD/POLICY CELL/2/2014 dated April 17, 2014]

➤ *SEBI sets Foreign Portfolio Investor limit of 10% equity.*

With effect from 1st June, 2014, a Foreign Portfolio Investor (FPI) would be allowed to hold a maximum of 10% of equity shares per company, while existing overseas investors viz. Foreign Institutional Investors (FIIs) and Qualified Foreign Investors (QFIs) would be required to convert to this new regime. Where an FPI already holds 10% of equity shares in an Indian company, no fresh purchases would be allowed in that company till its holdings fall below this threshold limit of 10%. If an FII or its sub-accounts already holds in excess of 10% in a company, it would not need to divest any shares even after conversion to FPI.

➤ *SEBI to frame regulatory norms for FATCA.*

India has concluded an "in substance" Inter-Governmental Agreement with USA under Foreign Account Tax Compliance Act (FATCA), to combat possible tax evasion by Americans through Indian financial entities, to be implemented from July 1, 2014. Under FATCA, USA can seek information available with Indian financial institutions on offshore accounts of its citizens/entities. Regulatory norms for market intermediaries in this regard are awaited from SEBI.

➤ *Companies (Acceptance of Deposits) Rules, 2014 ('Deposit Rules') notified under Companies Act, 2013 ('CA 2013').*

CA 2013 lays down stricter rules for acceptance of deposits. Securities application money retained for more than 60 days without issuance of securities shall be deemed to be a deposit. Any advance amount received for business purposes would be deemed to be deposit on expiry of 15 days from the date they are due for refund. 'Deposit' includes any receipt of money by way of deposit, loan or in any other form, subject to exceptions provided in the Deposit Rules. Small public companies may be unable to accept deposits due to stringent requirements (should have net worth not less than INR 1 billion or turnover not less than INR 5 billion). Further, companies that accepted deposits prior to CA 2013 will be required to comply with requirements under CA 2013.

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Litigation Brief

➔ *Delhi High Court: Mere co-operation between consortium members does not result in an 'Association of Persons' (AOP)*

In *Linde AG, Linde Engineering Division & Another v. DDIT*, Delhi High Court has ruled that where there is an independent and distinct scope of work for each consortium member as well as, no risk sharing, mere cooperation amongst consortium members would not result in the formation of an AOP in India. Linde and Samsung had jointly submitted a bid for execution of an EPC (Engineering, Procurement and Construction) project as a Consortium, which was issued in their favor.

The Delhi High Court, in this case, was confronted with the question whether the consortium constitutes an AOP under Section 2(31) of the Income-Tax Act, 1961 ("ITA"), and, hence, was liable to be taxed as a separate taxable entity. The Delhi High Court held that in order for a consortium to be taxable as an AOP/ separate taxable entity, the following essential elements should be present: (i) It must be constituted by 2 or more persons having a common purpose, (b) It must move by common action and have some scheme of common management, (c) Cooperation amongst members must be real and substantial. Based on the findings that Linde and Samsung had independent scope of work, had not entered into any arrangement for profit/loss sharing and had received separate payments from the Project Owner, the Delhi High Court held that their Consortium did not constitute an AOP.

Another key issue was whether income of Linde arising out of offshore supply of equipment and preparation of related designs is taxable in India under the ITA or under the current Double Taxation Avoidance Agreement between India and Germany ("DTAA"). On this issue, the matter was remanded back to Authority for Advance Rulings for determining whether Linde has a 'permanent establishment' in India, in light of Article 12 of DTAA between India and Germany, which stipulates that fees for technical services (not linked inextricably with offshore supplies of equipment) are liable to be taxed where these services arise i.e. in Germany. However, if the fees are attributable to a 'permanent establishment' in India, taxation shall be according to Article 7 of this DTAA. [See (W.P.(C) NO.3914/2012 & CM No.8187/2012)]

➔ *SC: Stay on Allahabad High Court Order for Demolition of two Supertech towers in Noida.*

Last month, on a petition filed by the concerned Resident Welfare Association (RWA), Allahabad High Court had ordered demolition of two 40-storey towers in the Emerald Court project in NOIDA. The RWA claimed that NOIDA Authority permitted the Developer to raise the height of both towers from 66 mtr. to 121 mtr. without maintaining the mandatory distance from an adjoining building for fire safety and increasing pressure on civic amenities. The High Court ruled that approval and construction of both structures violated Uttar Pradesh Apartment (Promotion of Construction, Ownership and Maintenance) Act", and

accordingly ordered demolition of the offending towers. It directed prosecution of officials of the Developer and NOIDA Authority and directed the Developer to refund moneys to investors along with 14% interest compounded annually. Now, as a welcome relief to buyers, the Hon'ble Supreme Court of India in *Dhirender Sharma & Others v. Emerald Court Owner Resident Welfare Association & Ors.* stayed the demolition order passed by the Allahabad High Court but restrained the Developer from alienating any part of these buildings or creating any third party rights therein and directed status quo until further directions. [See PC No. 6754/2014]

➔ *SC: Tenants under lawful possession in terms of TPA cannot be forcefully dispossessed by secured creditor acting under SARFAESI Act.*

In *Harshad Govardhan Sondagar v. International Assets Reconstruction Company Ltd. and Others*, the Supreme Court of India has held that a lease in respect of a secured asset, which has been validly created under the Transfer of Property Act ("TPA") does not automatically stand determined when the secured creditor takes recourse to Section 13 of Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act ("SARFAESI Act"). The Court held that without the expiry/determination of a valid lease, the possession of the lessee is lawful and such lawful possession has to be protected by all courts and tribunals.

While the Supreme Court clarified that the provisions of the SARFAESI Act will override the TPA to the extent of any inconsistency, on an interpretation of Section 13 of the SARFAESI Act, it held that any lease, validly made prior to creation of the mortgage by the borrower or made in accordance with Section 65A of the TPA prior to receipt of a notice under Section 13(2) of the SARFAESI Act, will continue to subsist, notwithstanding any action under Section 13(4) of SARFAESI Act by the secured creditor. The secured creditor does not have the right to dispossess such tenants during the tenure of the lease. The SC further held that when assistance is sought by the secured creditor under Section 14, the Chief Metropolitan Magistrate or District Magistrate, as the case maybe, will have to give adequate opportunity to the tenant in order to determine whether the lease is valid in terms of the TPA. The SC clarified that though Section 14 of the SARFAESI Act attached finality to the decision of the CMM / DM, the same would be open to judicial review by the High Courts / Supreme Court. [See Criminal Appeal No. 736/2014]

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