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Contents

Article
All funds under one umbrella 2

Circulars & Notifications 4

News nuggets 5

Ratio decidendi 6

Article

All funds under one umbrella

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The Securities Exchange Board of India (SEBI) has introduced regulations from time to time for protection of investor rights. The objective of the SEBI (Alternative Investment Funds) Regulations, 2012 (AIF Regulations), effective 21-5-2012, [after repealing the SEBI Venture Capital Funds Regulation, 1996 (VCF Regulations)] is to bring all funds established or to be established in India under one omnibus statutory regime.

Scope and applicability

The ambit of AIF Regulations is far reaching as it covers under it, *any fund established in India, for pooling money from investors,* whether Indian or foreign, for investing it in accordance with a defined investment policy for the benefit of its investors. The fund in question may be established in the form of a trust or a company or a limited liability partnership (LLP) or a body corporate. The AIF Regulations exempt the following from its applicability: (i) mutual funds (ii) ESOP and other employee welfare trusts (iii) family trusts (iv) collective investment schemes (v) special purpose vehicles (vi) funds managed by securitization or reconstruction companies, as these would be regulated by their respective extant regulations/ rules.

It is pertinent to note that the existing funds which were governed by the VCF Regulations would continue to be governed by the same; however, once a fund intends to launch a new scheme or increase its targeted corpus, it would require registration as per the AIF Regulations. Such funds have an option of re-registering under the AIF regime, with approval from their investors (two-thirds majority). All other unregistered funds would need registration under the AIF Regulations with SEBI within six months from the date of notification of these regulations. In special cases the fund in question can apply to the SEBI for extension up to twelve months.

Categories of AIFs

The AIF Regulations have classified the funds under its applicability into three broad groups:

- Category I – This category includes venture capital funds, SME funds, social venture funds, infrastructure funds or such other funds which have a positive spillover effects on economy.
- Category II – Funds that do not fall under category I or category III are included in this category. Also included are such funds which do not undertake leverage or borrowing other than to meet day-to-day operational requirements and as permitted under the AIF Regulations.
- Category III – Hedge funds or other funds which trade with a view to make short term returns and for which no specific incentives or concessions are given by the government or any other regulator belong to the third category.

Pertinent conditions for AIFs

All AIFs shall be required to state their investment strategy and purpose in the memorandum submitted to investors. As per the regulations, all AIFs shall have a minimum corpus of Rs. 20 crores. Further, each investor has a minimum limit of Rs. 1 crore to be met for investment into the AIF units. SEBI has capped the number of investors

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for a scheme of every AIF to one thousand investors. It is pertinent to note that the AIF Regulations provide for an exemption mechanism, whereby an existing fund which is unable to meet the requisite conditions can apply to the SEBI for exemption from strict compliance with the AIF Regulations. A cumulative reading indicates that the intent of SEBI is to regulate all AIFs in contrast to its erstwhile view towards regulation of funds.

Categories I and II AIFs shall be close-ended and have a minimum tenure of three years, whereas category III AIFs can be either close or open-ended. The term of AIFs can be extended by a period of two years subject to prior approval of the investors.

SEBI has permitted the listing of all close-ended units of AIFs on stock exchanges which shall be subject to a minimum tradable lot of Rs. 1 crore. AIFs may invest in securities issued by companies outside India, subject to conditions. Further, categories I and II AIFs shall not invest more than 25% of the corpus in one investee-company on the other and category III AIFs may not invest more than 10% in one investee-company. Other compliance requirements include filing an information memorandum 30 days before launching a new scheme submission of annual books of accounts to SEBI and specific conditions stipulated for each category of AIFs. The new regime requires detailed filings and compliances for an effective regulatory control over all funds established and operating in India.

In its Board meeting on 16 August 2012, SEBI has also approved regulations for investment advisors, to be notified as the SEBI (Investment Advisors) Regulation, 2012 (Advisors Regulations), The Advisors Regulations, (like the AIF Regulations) has far reaching consequences as it requires all individuals, body corporate and partnership firms engaged in the business of providing investment advice to investors for consideration to be registered and consequently regulated by the SEBI. Thus, unless specifically excluded by the Advisors Regulations, an entity or an individual providing investment advice would be under the SEBI scanner in addition to the existing regulatory regimes that might govern such investment advisory business. Investment advice not given for consideration or given via media to the public at large are not covered by the Advisors Regulations. It is further proposed that the banks may be permitted to offer investment advisory services only through a subsidiary or a Separately Identifiable Department or Division (SIDD). Such SIDD or a subsidiary would be distinct and require specific approval from the RBI.

The responsibilities of the advisors have been specifically enumerated in the Advisors Regulations such as following a code of conduct, maintaining of capital adequacy ratios, client confidentiality, ensure that the investment advice is suitable and appropriate to the risk profile of the client, conducting yearly audit, etc. The prescribed regulatory requirements present an extensive compliance regime which the potential advisors would have to adhere to.

The AIF regime coupled with the Advisors Regulations is a bold step by SEBI towards mature/futuristic regulation of the Indian financial markets. The corpus requirements, minimum investment limits for AIF's may be difficult to small size funds/investors; on the other hand a sense of over regulation is felt with the Advisors Regula-

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tions coming into the picture, as private entities such as investment advisors were never under the ambit of such governmental control. These regulations entail immense (potential) practical implications on the Indian financial sector, encompassing specific regulation of the majority of entities involved therein. The actual market impact in terms of investment numbers and entities in this field remains to be seen, some consolidation for the smaller funds to remain viable and compliant is expected.

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Circulars & Notifications

Export proceeds – Relaxation for realization & repatriation extended up to 31st March, 2013: Relaxation to realize and repatriate amount representing value of goods or software exported, within 12 months instead of 6 months, has been extended upto 31-3-2013. This relaxation which was earlier available upto 30-9-2012 has been extended with effect from 1st October, 2012 by RBI A.P. (DIR Series) Circular No. 52, dated 20-11-2012. The relaxation has been in force since June, 2008 now.

Liaison Office (LO)/Branch Office (BO) of foreign entities in India – Reporting to Income Tax Authorities: Reserve bank of India has clarified that copies of the Annual Activity Certificate (AACs) submitted to the DGIT (International Taxation) by LOs and BOs should be accompanied by audited financial statements including receipt and payment account. A.P. (DIR Series) Circular No. 55, dated 26th November, 2012 issued in this regard also states that the AD banks shall endorse a copy of the renewal of permission of LOs to the DGIT (International Taxation).

CDS and Corporate Debt Securities - Participation of Mutual Funds: SEBI has allowed mutual funds to participate as users in Credit Default Swaps (CDS) market for eligible securities as reference obligations constituting from within the portfolio of only Fixed Maturity Plans (FMP) schemes, having tenure exceeding one year. Mutual funds are permitted to buy credit protection only to hedge credit risk on corporate bonds they hold and not to sell protection and cannot enter into short positions. Such participation shall be subject to other conditions provided in the Circular CIR/IMD/DF/23/2012, dated 15th November, 2012 issued in this regard. The base of eligible securities for in repo participation of mutual funds in corporate debt securities has also been widened from AAA rated to AA and above rated corporate debt securities.

Requirement of filing using XBRL taxonomy: Specified class of companies required to file the Balance Sheet and Profit and Loss Accounts and other documents under Section 220, Companies Act, 1956 with the Registrar of Companies shall now be required to file them in Extensible Business Reporting Language (XBRL) taxonomy, for the financial year commencing on or after 1st April, 2011. The latest amendment by Companies (Filing of Documents and Forms in Extensible Business Reporting Language) Second Amendment Rules, 2012, dated 30-11-2012 and effective from 2-12-2012 also provide for filing of cost audit report under Section 233B(4) with Central Government and filing of compliance report under clause (d) of Section 209(1), also using the XBRL taxonomy.

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NEWS NUGGETS

Banking mergers to face scrutiny of two regulators

Bank M&As may have to obtain clearance both from the Competition Commission of India (CCI) and Reserve Bank of India (RBI) according to recent reports. As per reports, banks have strongly advocated that they should be exempt from the scrutiny of CCI since they are already regulated by RBI. The same was also reflected in the Banking Laws (Amendment) Bill, 2011. However, this demand from the banking sector spurred regulators of other sectors such as telecommunication, insurance and shipping to make similar demands. There was speculation earlier that only involuntary M&As directed by RBI would require approval from both RBI and CCI. However, all M&As of banking sector shall require approval of CCI for the competition portion of the deal and of RBI for the prudential aspects as per banking norms if this policy is enforced. Proposed amendments to the Competition Act envisage no exemption for any sector in general with the Ministry of Corporate Affairs having the sole authority to grant exemptions on a case to case basis.

Govt. to press 'CTRL' button on foreign investment

The Finance Ministry had recently suggested the Department of Industrial Policy and Promotion (DIPP), the nodal agency for foreign direct investment in India to amend the definition of 'control'. The present definition of control covers only those situations where there is a power to appoint majority of the directors of the company. However the government opines that the definition of control does not bring within its ambit other indirect ways of control such as lien over voting rights, quasi equity instruments and terms of share purchase agreements. DIPP has also been suggested to consult the Ministry of Corporate Affairs so that the amended definition is aligned with the Companies Bill, 2011 presently pending in Parliament. In response to this, DIPP is presently in consultation to provide definition of control on the lines similar to the one under SEBI (Substantial Acquisition of Shares and Takeover) Regulations, 2011.

Scope of ECBs set to widen

The Government is all set to widen the scope of External Commercial Borrowings (ECB) by changing the definition of 'infrastructure', as approved by the Cabinet committee on infrastructure. The Committee has identified five main sectors (transport, energy, water sanitation, communication, social and commercial infrastructure) and 29 infra sub-sectors for inclusion in the definition. The move will enable Indian companies to access foreign markets for funds at lower costs. If announced, companies in the education, health and other notified sectors will be eligible to tap funds through ECBs.

Suspension and de-recognition of sports federations

The International Olympic Council (IOC) has recently suspended the Indian Olympic Associa-

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tion for not complying with the Olympic Charter, failing to take adequate measures to reduce government interference, failure to take action against tainted official and failure to conduct free, fair and transparent elections. Adopting a similar stand, the International Boxing Federation (AIBA) suspended the Indian Boxing Federation (IBF) for failing to conduct free and fair elections. The IBF's recognition was subsequently cancelled by the Ministry of Youth Affairs and Sports. The Archery Association of India (AAI) has also been derecognized by the Ministry of Youth Affairs and Sports. However the World Archery Federation (FITA) has given its backing to the AAI stating that following the National Sports Code is not a requirement of the FITA, therefore it would not suspend the AAI.

Service providers to meet quality of service benchmarks for wireless data services

The Telecom Regulatory Authority of India (TRAI) has released "The Standards of Quality of Service for Wireless Data Services Regulations, 2012". The regulations mandate every Cellular Mobile Telephone Service provider or Unified Access Services provider to set up a test set up comprising of servers and test probes to cover the entire geographical area of coverage of different data services in the licensed service area. The service providers are required to meet the quality of service benchmarks for wireless data services in respect of parameters like provision or activation of data services, successful data transmission download/upload attempts from a test server and minimum download speed from a test server covering all tariff plans. Service providers have to publish on their websites, the details of all data services offered, along with their tariff, clearly indicating the cities and towns where such data services and tariff plans are applicable. The service providers shall not offer new data services or modify the existing data services or tariff (s) without such prior publication.

RATIO DECIDENDI

Industrial disputes non-arbitrable

The Bombay High Court, in its order dated 20-11-2012, has held that industrial disputes or a dispute relating to enforcement of a right or an obligation created under the Industrial Disputes Act, 1947 (the Act) is non-arbitrable. The respondent-employees of the petitioner-company had filed applications under Section 33(C)(2) of the Act in the Labour Court for recovery of their earned wages. On the other hand, the petitioner filed applications under Section 8 of the Arbitration & Conciliation Act, 1996 (the Arbitration Act) which was rejected by Labour Court. While delivering its decision, the High Court observed as follows:

- The existence of a valid arbitration agreement and whether a subject matter can be subject to arbitration should be decided by the Court before which the judicial proceedings are pending as the judicial authority is not expected to

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act mechanically while deciding application under Section 8 of the Arbitration Act. Thus the Labour Court had correctly gone into the issue of arbitrability of the dispute and not left it to the decision of the arbitrator.

- The test in the present case to decide whether the dispute can be referred to arbitration is not whether the action therein is in-rem or in-personam, but whether adjudication of such disputes is reserved by the legislature exclusively for public fora as a matter of public policy.

On examination of the intent of the Act, the High Court held that it is a beneficial legislation and has vast applicability, as the decisions under the Act may not only affect one employee, but the industry as a whole. Further, the reliefs and remedies that can be granted by a Labour Court are different from reliefs that can be granted by an arbitrator. Moreover, the Act itself provides for arbitration under Section 10A, wherein the dispute is not treated merely as an individual dispute but is always approached from the context of the larger picture of the industry as a whole and the status of the arbitrator is also not the same. Further, Section 10A(5) of the Act, specifically excludes application of the Arbitration Act to the arbitrations under Section 10A.

It is thus seen that, adjudication of industrial disputes is reserved by the legislature exclusively for the authorities established under the Act, as a matter of public policy. Therefore, by necessary implication the same stands excluded from the purview of the private fora of the arbitrator. [*Kingfisher Airlines Limited* v. *Capt. Prithvi Malhotra & Ors.* - Bombay High Court Order in *Writ Petition Nos. 2585, 2586, 2587 of 2012*].

Existence of name in trade document not creates binding contract

The Delhi High Court (Division Bench) in its judgment dated 30-11-2012 rejected an appeal for enforcement of a foreign arbitration award on the ground that the existence of a valid arbitration agreement between the parties was not proved. The appellant company filed an appeal before the Single Judge under Sections 47 and 48 of the Arbitration and Conciliation Act, 1996 (the Act) to seek enforcement of a Foreign First Tier Arbitration Award, an Arbitration Appeal Award and a Final Foreign Arbitration Award, to realise the amount awarded in its favour against the respondent.

The objection raised by the respondent before the Single Judge was that there was no arbitration agreement between the parties as the respondent is not a party to the purported agreement. Section 47(1)(b) of the Act requires the person seeking enforcement of a foreign award to produce the arbitration agreement. The learned Single Judge observed that no document was placed on record to show an exchange of correspondence between the appellant and the respondent, wherein respondent accepted the existence of an agreement between it and the appellant. As per the Single Judge's order, both the first tier arbitral tribunal and the appellate board did not advert to the fundamental question as to existence of an arbitration agreement between the parties. Accordingly, the Single Judge concluded that there was no valid arbitration agreement between the appellant and the respondent within the meaning of Section 7 read with Section 47(1)(b) of the Act.

The Division Bench held that until the default

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notice was served upon the respondent by the appellant, there was no correspondence at all between the appellant and the respondent. Thus the contention of the appellant that the trade confirmations/ communications were within the knowledge of the respondent and entered on behalf of the respondent, had no basis and the contention on existence of MOU between respondent and of the appellant that there was an MOU between the respondent and another person which entitled latter to execute agreements on behalf of the respondent was also rejected by the Court. Thus, mere existence of the name of the respondent on the trade document did not create a binding contract between the respondent and the appellant. [*Cinergy Corporation PTE. Ltd.* v. *National Agricultural Co-operative Marketing Federation of India Ltd.* – Delhi High Court Order in FAO(OS) 572/2012].

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