A.R.A LAW

Advocates & Solicitors

Strictly for private circulation only

LEGAL EYE

YOUR PEEK INTO THE INDIAN LEGAL SCENE

Volume 5, Issue 5 August, 2001

Attn:

Thought for the month

Nothing worthwhile is ever achieved without deep thought and hard work

INSIDE THIS ISSUE

Privatisation of Airports – The Global Options & Experience 2

Privatisation of Airports –Indian Options 5

Project Finance 9

LEGAL SNAPSHOTS 12

Meet the A.R.A. LAW Team 17

Note from the Editor

Dear Readers,

The last issue of Legal Eye was dedicated to NRIs.

India needs to fly and not merely trot ahead to achieve the goals which the current political establishment has set for itself. The need for reforms has become more acute then ever before. The current issue of *Legal Eye* brings you an update on the privatisation of '*Airports*' in India. The air transport system is an important contributor to the quality of life of the people and an essential part of the world business globalization. Increasing passenger and cargo traffic places further demands on airports to provide adequate facilities and services to ensure safety, regularity and efficiency of air-craft operations. Bearing this in mind, the Government of India has proposed to privatise certain important Airports in the country.

Legal Eye attempts to identify various options of privatisation of Airports in India. Privatisation of Airports to be successful requires vibrant regulatory regime to be in place before the privatisation process, establishment of an independent regulator and more importantly it should be economically viable to the investor.

It remains to be seen as to how the draft policy of Government of India on Aviation reinvigorates the Airport Industry involving private sector.

We trust you will find this issue of the Legal Eye interesting as usual.

- Rajesh N. Begur, Editor, Legal Eye

Privatisation of Airports – The Global Options & Experience

I. Introduction

In the last decade Private Sector Participation (PSP) in Airports has received immense impetus, focus and there has been a sharp increase in private management of the services associated with airports. The private investment was fuelled by the development of new forms of PSP including varying forms of public/private partnerships BOT, BOOT, LOM, LDO and full/partial concessions. In each case, successful privatisation requires the appropriate and efficient regulatory and legal framework that can satisfy customer and investor alike, with the scrutinization of insurance techniques and financial arrangements.

II. Issues

The policy of privatisaion and private participation should invoke all the best practices including competition, transparent tendering, effective regulation and efficient concessions. In order to achieve these objectives are fulfilled, the Government and private parties are required to undertake several specialised focussed activities, hitherto operated or managed by the other party. Some of them are enlisted hereinbelow:

1. Government should specialize in planning, structuring and regulation while the private sector should specialize in management, investment, construction and financing.

2. Transfer of responsibility to the private sector should be accomplished through deregulation and open competition or well-established contractual arrangements including management contracts, capital leases, concessions, sale of assets and rights to operate.

3. Economic regulation should be applied, where there is insufficient competition but it should be transparent and predictable while still accommodating the concerns of the affected parties. In India, this is a fundamental requirement under the tendering process which is normally adopted by the Government.

4. Long-term domestic financing sources must be developed together with a broader and efficient external lending facilities.

5. Commercial risks should be assigned to the private sector but other risks should be assigned according to which party is able to mitigate the risks.

6. Privatization embodying the above can be achieved through legislation or documentation invoking any of the following models, namely, BOL (Build, Operate, Lease), or BOO (Build, Own, Operate), or BOOT (Build, Own, Operate, Transfer) law or similar,

signaling the Government's recognition of the need for private sector participation in infrastructure provision.

III. Models

The privatisation process is normally achieved through several models and extents of private participation. A few typical models are analysed below

1 Full Privatisation
2 Partial Privatisation
   (i) Concessions
   (ii) Strategic Partnerships
   (iii) Management Contracts

1. Full Privatisation

The process involves the transfer of ownership of the entire assets from the Government to private investors through an assignment, flotation or through a trade sale. However, the Government's reluctance to cede control over what is widely regarded as a vital national interest, symbol of pride and the lack of appropriate framework of economic regulation may be an impediment in some countries.

2. Partial Privatisation:

As an effective alternative partial privatization has long been consistently adopted as an effective tool for global privatisation. Partial Privatisation has several layers or modes, including:

(a) *Concessions*: Under this some or all core airport assets are transferred to a private investor who is responsible for financing investment and operating the airport for the term of concession. Concession could range between operations, commercial activities, non-aeronautical activites and non-commercial activities. (Abidjan Hophouet-Boigny Airport, Ivory Coast; Ninoy Aquino International Airport, Bogota El Dorado International Airport)

The majority of concession agreements cover specific issues like exclusivity (monopoly), the term of the concession agreement, third party recognition of concession agreement, commitment of Government support, financial terms such as tax benefits, foreign exchange, landing fee, ICAO standards, non-interference of Government, consequences of forced nationalisation or early termination, obligations and rights of the parties, commercial support by Government, title to property, governing law and dispute resolution among other things. On a much larger scale is the recently concluded 30 year concession agreement covering the transfer of 33 of Argentina's 59 civil airports to a private sector led consortium which includes finance and under taking a US $ 2 billion upgrading and modernization program covering the principal international and principal

international and regional airports. It also has to pay the Government an annual concession fee of US $ 171 million.

(b) *Strategic Partnerships*:

In this form a private sector firm or consortium acquires a stake in a state owned airports. It provides a vehicle for introducing private sector finance and operational expertise in order to directly relieve public financing constraints and to improve operational and financial performance. (Vienna Airport, Austria and Copenhagen Airport , Denmark).

(c) *Management Contracts*:

A private sector contractor is retained to manage airport assets, usually passenger terminal facilities or retailing activities within passenger terminals. This form has been used only in developed countries to improve the quality of service. In developing countries, the stimulus to engage the private sector is more frequently related to securing additional funding for investment projects and for gaining the benefit of private sector skills in project management. In some instances, this is the first step towards a greater privatisation of the airports. (India – ground handling has been privatised on a minimal level)

Every privatisation initiative is a combination of one or more of the options and modes listed above. Globally these models have been implemented in the recent past, important and noteworthy ones are:

Australia	Strategic Partner	49% - Foreign Ownership 15% - Cross Ownership 05% - Airline Ownership
China	Strategic Partner/ Partial Privatisation	49% - Strategic Partner 25% - Public Stock Offering
Germany	Strategic Partner/ Partial Privatisation	25% - Individual Shareholders 51% - Strategic Partner
Greece	Management Contract	55% - Government 45% - Private Consortium
Oman	Strategic Partner/ Partial Privatisation	75% - Strategic Partner 20% - Government 05% - Oman Aviation
South Africa	Partial Privatisation	10% - Black Investors 10% - National Empowerment Fund 09% - Staff
Thailand	Strategic Partner	49% - Strategic Partner 51% - Government

The global experiences especially in regimes similar to India afford a rich and enriching data to assist India in adopting a local need based sui generis system for implementing the privatisation process for

airports. The Indian initiative and the needs of the country have been detailed out in the article **Privatisation of Airports – Indian Options** elsewhere in this publication. ❖

S R Arun & Vachan B

Privatisation of Airports –Indian Options

India has recognised the need to integrate itself into a global economy and has come out with a policy on Airports which has paved way for the involvement and investment by domestic, foreign and private sector.

The Indian Government realises that modernisation and expansion programs infrastructure relating to aviation are to be tailored to the needs of emerging India, by calling for participation by the Private Sector without compromising on safety or security of operations. Simultaneously, the policy of the Indian Government is geared towards a framework for commercialisation of non-profit making airports through profitable land utilisation and setting up of utilities which will generate non-aeronautical revenues and also employment opportunities in the country.

Unlike other areas, aviation has an internationally well defined institutional role where Governments are obliged to follow certain operational patterns based on safety and efficiency norms. The task that remains is the system of effective management of airports and related infrastructure in respect of regulatory and financial norms.

The objective of privatisation in India should be towards creating airports as individual profit centres, independent entities with decision making powers and having its own revenues with the management and as a consequence being more responsive and efficient. Viewed thus, Indian privatisation process could devise its own strategy as a local solution and not contrived by world majors who tend to be overbearing without understanding the relevance of Indian experience.

The Airport Policy of the Indian Government should be implemented in such a manner so as to focus on the operations, maintenance and efficiency parameters of the airports coupled with competition governed by an independent regulatory authority. Also, the policy on Airport infrastructure should always be read alongwith the National Policy on Civil Aviation.

With this background as regards the need of a sui generis policy for India, let us consider the features and possibilities as laid down by the Government of India.

Airport Policy

As per the new Airport Policy, Airports could be on Build-Operate-Transfer (BOT), a joint venture between a private party and Airports Authority Of India (AAI), Build-Own-Operate (BOO) or even Lease-Develop-Operate (LDO). The policy also allows various forms of ownership like wholly private, joint sector (private parties in joint venture with the Central or State Government) or

with public sector units. Airports may also be owned by Central, State Government, Urban local bodies, private companies or even by individuals. What makes the move significant now is that until now, the practice has been to build and operate airports as Governmental structures with both operation and regulation under the purview of the AAI. This meant compromising on operational and efficiency standards, coupled with huge investment backlog. However, with the new policy on Airport infrastructure in place, within the evaluation period, the necessary changes required in the AAI statutes will also be made if so required.

The Plan

According to the policy, what is needed now is a strategy that permits utmost latitude in the patterns of ownership and management of airports in view of the world wide thrust towards corporatization and privatization of airports. Foreign equity participation in airport projects may be permitted up to 74% with automatic approvals, and up to 100% with special permission. The new thinking is that participation of private parties in airport projects is mandatory because of the huge sums involved and also to promote greater efficiency in their management.

Concessions and Incentives

In order to encourage and attract leading and efficient airport managers and development agencies and corporates, the Government of India has offered several sops to the investors in the privatisation process.

Fiscal incentives will be provided to those involved in infrastructure projects as may be decided by the Government from time to time. At present, the following incentives are available:

a. Hundred percent deduction in profits for purposes of Income Tax for the first five years.

b. Thirty percent deduction in profits for the same purpose for the next five years.

c. Full deduction to run for continuos 10 out of 20 fiscal years of the assessee's choice.

d. Forty percent of the profit from infrastructure is also deductible for financial institutions providing long-term finance for infrastructure projects. According to the draft policy, such incentives should be made available not only to new companies investing in airports infrastructure but also to the AAI and existing agencies investing in existing airport infrastructure.

A competitive regulatory framework with minimal controls will be created to encourage the entry and operation of private airports. Private sector investment in the construction, upgrading and operation of new and existing airports including cargo-related infrastructure will be encouraged. The Government will gradually reduce its equity stake in the civil aviation sector.

It will also promote investment in non-aeronautical activities like shopping complexes, golf courses, entertainment parks, and aero-sports near airports to increase revenue, improve the viability of airports, ensure world class airport infrastructure and also promote tourism.

The policy envisages a statutory autonomous Civil Aviation Authority to be constituted to facilitate regulation and monitoring of the privatisation process and its operations. The basic objectives of setting up the Authority will be to ensure aviation safety, security and effective regulation of air transport in the country within a liberalised environment.

Objectives of Private Sector Participation:

Under the objectives of the private participation in airports is sought to be achieved in the following manner:

(i) The private sector will be free to undertake :

a. Construction and operation of new airports.

b. The upgrading and operation of existing airports in consultation with the existing operator including cargo complexes, express cargo terminals, cargo satellite cities and cargo handling facilities.

(ii) Private sector participation will include participation of state Governments, urban local bodies, private companies, individuals and joint ventures on a Build Own Operate (BOO) basis or any other pattern of ownership and management depending on the circumstances.

(iii) Restructuring of major airports belonging to the Airports Authority of India will be undertaken through a long-term lease to private investors for efficient management, an improvement of standards of services/facilities and attracting private investment.

(iv) At privately managed airports, Air Traffic Control (ATC) and aviation security will continue to be provided by the Airports Authority of India (AAI) and customs and immigration facilities by respective Government departments.

(v) The equipment needed for any service would normally be provided by the agency responsible for the service and an equitable system will be established to share revenue between different agencies in keeping with their respective investments and responsibilities.

(vi) Airport operators will follow International Civil Aviation Organization (ICAO) guidelines for levying charges based on cost recovery principle. The Civil Aviation Authority will put in place a regulatory mechanism to prevent the abuse of the monopolistic nature of such infrastructure.

(vii) An objective and well-defined transparent mechanism for allocating slots at airports will be ensured at all times.

(viii) More International gateways shall be provided. It will be ensured that there is atleast one international airport in every region of the country in order to give boost to trade and tourism and adequate capacity on all routes.

(ix) A major thrust will be given to increase the share of commercial revenue from non-aeronautical sources by giving total freedom to airport, operators in the matter of raising non-aeronautical revenue.

(x) At airports managed by AAI, new private investors have been allowed to undertake ground handling alongside national carriers and self-handling by carriers which will increase competition resulting in an improvement in services and a reduction in costs. As part of its commitment towards the privatisation process, the Government has already ensured the privatisation of ground handling facilities in several Indian airports.

(xi) At private airports, at least limited competition will be mandatory.

In order that any privatisation is successful, the Government is required to ensure that objectives of the policy are coupled with the right tools to facilitate efficient and precise implementations. In order to achieve this the Government is expected to provide the adequate and conducive regulatory and legal framework for the process of the implementing the policy. This would include the relevant issues being captured in the legal relationship between the Government and the private parties. The Concession Agreement is one of the most effective and important documents governing the process of privatisation, especially in projects like Airports.

Concession Agreements – Issues to be dealt with

A concession agreement must state clearly the exclusivity of the Concession, in other words, if the economics of the transaction depends upon monopoly, the owner must be contractually bound to an exclusive concession. The Concession Agreement should clearly mention as to what is required of the private party, the extent of independence given to the party, and most importantly, the operation period of the concession. It should also provide for the rights and obligations of the party.

A concession agreement should also provide for a strong and lasting commitment and support from the Government. A concession agreement should guarantee and provide for tax benefits, foreign exchange and repatriation, and concession fee, if any, payable by the Government. Under the present policy the Government has not laid out any policy relating to the concession fee payment. However, the revenue generation and sharing pattern is relative to each individual project and its feasibility.

Consequences of termination of the project, or breach by the Government should also be built in a concession agreement. The issues of guarantees and assurances by the Government, has raised several issues recently in view of the present dispute between Maharashtra State Electricity Board (MSEB), Dabhol Power and the conduct of the Government of India in the entire matter.

The policy in respect of guarantees, concessions and expropriation should be clearly spelt out clearly and expressly, to encourage and provide greater transparency to the private parties intending to undertake the activity.

Other Agreements and Contracts:-

The other documents that would concretise the relationship between the Government and the private party towards Privatisation of Airports would include:

- Joint venture/ Shareholders Agreement – which shall provide for formation of the special purpose vehicle or the airport operating company, capital contribution, share transfer restrictions, operation and management decisions and control, dividends, consequences of termination and dispute resolution.
- Construction contract (EPC)
- Loan Agreements (Financial Documents)
- Supply contracts
- Offtake Agreements
- Operation and Maintenance Agreement. (O& M)

With the preliminary step of having expressed its intent to privatise airports in India, the Government has been sincere in its effort to provide world class infrastructure in the country. However, the microscopic and troublesome issues relating to implementation and documentation needs to have a liberalised and open minded approach to accommodate and facilitate the private parties to make their venture profitable, lucrative and efficient. ❖

S R Arun and Radhika

Project Finance

Infrastructure is, beyond doubt, a necessity for any economy to attract investment. One of the most important aspects of infrastructure is transport. The transport sector has some unique characteristics that make financing a transport project a unique study in itself. One method of financing projects that has become very popular over the past few years has been project finance.

"*Project finance*" is a technique of financing by which income generated from projects are applied to repayment of the loan and the assets employed in the project are used as collateral for the loan.

The most characteristic feature of this technique of practice is that the promoter is not responsible for the financing or the repayment. This is what is referred to as limited recourse or non-

recourse financing. Limited recourse is a variation of the concept of non-recourse financing, where there is recourse against the promoter only to a mutually agreed upon extent. Here, the nature of the exposure of the promoter is normally as an additional comfort on the credit of the promoter. Though there may eventually not be any recourse, there may be some obligation upon the promoter over and above the initial participation.

There are many risks associated with a project, which are hereinbelow dealt with. Some of these risks are:

1. *Traffic risk-*

   This is a feature that is common to all transport projects. It is very important that proper studies of traffic patterns be undertaken because the revenue model would be affected.

2. *Sovereign risk-*

   This is the risk that is associated with the government. One needs to keep in mind the different policies, permissions and compliance. Also, things like change in government and the nature and the value of the currency are issues that need to be kept in mind. With the experience of the Indian government in the power sector, it must be kept in mind that the government may not give any guarantees. It is important to have clarity before hand on any issues relating to the government.

3. *Legal risk-*

   Over and above the sovereign risk, most countries have laws governing airports and the authorities that govern them. Also, there are international norms that need to be complied with. The policy on aviation should clearly lay down what the law is going to be like.

4. *Supply risk-*

   When one has to keep deadlines, there could be a problem with the supply of material or some other ingredient vital to the completion of the project.

5. *Corporate risk-*

   This would be something that most financial institutions would adequately deal with in the agreements.

6. *Force majeure risk-*

   Where there is some force majeure event that occurs, then there ought to be adequate clarity about what happens in the event of a force majeure event.

7. *Commercial risk-*

The viability of the project may change half way through the project. Also, there is a risk of the revenue model not meeting the expectations because of some change in the circumstances of the project. The policy of the government in the realm of airports should be investor friendly.

8. *Credit risk-*

This is a risk that the financial institution takes. This would be adequately dealt with by way of security provisions and guarantees.

The airport sector is one of the fastest growing sectors within the realm of transport. Concession agreements, Airport landing-fee agreements and BOOT (build-own-operate-transfer) contracts are prime examples of work that could be financed in the airport sector. Concession agreements create the right and obligation to build, own, and eventually transfer back to the grantor, an airport. An important aspect of a concession agreement is the legal authority for the grant of the concession. The loan agreement should adequately capture the manner in which the amount would be transferred and the schedule of payments. The collateral that is taken against the finance normally would be subject to due diligence as regards any previous indebtedness and its credit worth.

One of the most critical aspects of project finance is the Special Purpose Vehicle (SPV). This entity is what distances the promoter from the liability. The SPV, by definition, is incorporated for the project alone and normally would not have the power to do much else. The SPV would have the limited purpose of owning the project assets, entering into the project documents, the financing documents and transacting the restrictively defined project business and other activities reasonably incidental thereto.

One of the requirements of a project finance SPV would restrict it from issuing any subsequent debts rated lower than its existing debt, unless such debt is subordinated in payment and security to the existing debt and does not constitute a claim on the project. Also, it is important that the SPV be clear of any litigation or claim due to its previous businesses. This is important in order that the project and the schedule of payments and repayments remain as contemplated at the time of the agreements. It is also important for the SPV not to merge with an entity that has a higher risk exposure. It is also important that the SPV be insulated from the parent and vice versa. Such insulation would negate the effect of any winding up petition or bankruptcy petitions filed by either the parent or the SPV on the other.

Another aspect that needs to be kept in mind in the case of foreign participation is the choice of law. It is critical that the parties understand the implications of all the clauses under the law of the country whose laws are made applicable to the project. This could be done with the help of a local counsel or by an appropriate undertaking from the other party. Where the financial institution is a foreign entity, it is likely that the law governing the financial documents is the law of country of the

financial institution. The concession agreement and the documents relating to the property and the collateral are likely to be those of the country in which the project is being implemented.

Project finance for airports can thus be a powerful tool for a country to improve its infrastructure and attract investment. This tool is most effective when combined with the privitisation initiative of the government in India. The policy of the government in airports should be geared towards using this tool as a way of attracting investment. It would therefore be appropriate to say that the potential in this area is immense. ❖

C. K. Nandakumar

LEGAL SNAPSHOTS

Postal Ballot Norms Effective From 15 June 2001

Confusion over various provisions of the rules on postal ballot, including the effective date of enforcement has finally been resolved. The Department of Company Affairs (DCA) has clarified that the provisions of the postal ballot, notified by the Government in May this year, would be applicable to notices for shareholders meeting or annual general meetings approved after June 15, 2001. The Department has further clarified that the Company would have to hold Annual General Meetings as it is mandatory under Section 156 of the Companies Act, 1956, even if most of the Resolutions proposed to be considered at the meeting are conducted through postal ballot. Companies would be required to announce the results of the postal ballot at the AGM. The date of AGM would be considered as the date of passing of the resolution by postal ballot. ❖

Government of India Announces ESOP Guidelines

The Government has announced detailed draft guidelines under Sec. 17 of the Income Tax Act to consolidate the manner in which the employees' stock options would be controlled, by introducing the Stock Option Guidelines 2000.

These guidelines would cover all types of ESOPs, stock purchase and stock appreciation schemes, the rules of which are still in its final draft stages. According to the guidelines, the shares in these stock option schemes may be those of a subsidiary or a holding company of the qualifying company in India or abroad. Conditions laid down include the following:

- The shares should be listed on a recognised Indian or Foreign stock exchange.
- Every company issuing shares under this plan is required to file complete particulars in a specified format with the Chief Commissioner of Income Tax within six months of the issue of guidelines.
- The stock option plans of the companies need to specify details such as the limit of share issue, the class of employees entitled to take part in the plan, pricing formula and the number of options to be issued to each employee.

- Other conditions include the manner of obtaining approval of shareholders and those relating to restriction on non-transferability of such shares.

- The valuation of unlisted shares will have to be submitted to the Chief Commissioner of Income Tax.❖

RBI Transfers FERA Cases to ED

The Enforcement Directorate has to take on a fresh heavy workload to add to its already cumbersome and heavy backlog of more than 2000 cases. As many as 7500 new cases were forwarded to the agency for investigation and disposal under FERA. The ED Director said that more cases were soon expected to follow. Mumbai and New Delhi account for the 7500 cases required to be investigated.

The surge of cases is attributed to the urgency in disposing of all FERA cases before May 31, 2002, failing which all cases will de deemed to have lapsed, due to the replacement of the draconian FERA with the friendlier FEMA. The ED is however taking solace in the fact that most of these cases refer to delays by importers in confirming with foreign exchange stipulations rather than serious offences, though the agency will have to investigate and rule out instances of deliberate non-compliance. Some of the high profile cases being investigated include the NFL Urea scam, the Lily George case and the Jain Hawala case, as well as corporates such as Seagrams, Essar, ITC and the UB Group.

The RBI has further referred 25,000 FERA cases to the ED relating to the investigation into companies that have sent money abroad, but have allegedly not imported anything. Most of the cases pertain to the companies which have made payments abroad but have not furnished proof of imports to the concerned authorities. It is mandatory on the part of the importers to provide proof of their imports, like Bill of Entry, to their respective bankers.❖

Speed is the Key Word in FDI Policy

On 21 June 2001 the Government revealed a proactive strategy that would focus on speedier implementation of foreign investment projects and establishment of a greater level of interaction with foreign investors, along with refocusing the role of the Secretariat for Industrial Assistance.

The strategy aims at the acceleration of the realisation rate of FDI proposals from the current 47%, with the creation of a mechanism to ensure greater level of coordination with the various Government bodies and departments.

An official statement issued by the Commerce and Industry Ministry said that the SIA would soon contact all foreign investors who have obtained the FIPB approvals to ascertain the progress of implementation of projects and extend any required support.

The SIA would also assume the responsibility of liasoning with the ministries to take up the problems faced by foreign investors, both at individual as well as sectoral level. If required the problem would be taken up by the fast track committee of the Foreign Investment Implementation Authority (FIIA).❖

CBDT Rejects OECD suggestion on Transfer Pricing.

The Central Board of Direct Taxes (CBDT) has turned down a number of suggestions of the Organization of Economic Co-operation and Development (OECD) on changes in India's draft transfer pricing rules. The OECD has suggested incorporating the "range concept" in the transfer pricing norms under which the price claimed by a company is accepted by the tax authority if the difference between the prices arrived at by the Company and the tax authority fall within the range of 10 to 15%. This has not been accepted.

The range concept is an internationally accepted norms under the transfer pricing rules of various countries. The practice was recommended by Indian tax authorities with a view that it would help avoid litigation and paper work to a great extent. Incorporating such a provision in India's rules is however not technically feasible since such a provision would need to be passed by the Parliament.

Another OECD recommendation for allowing MNCs to evolve a transfer pricing method other than what has been prescribed in the relevant rules provided this method is in tune with the established arms length principle, which has also been turned down by the CBDT.

The transfer pricing rules are currently pending before the law ministry for clearance.❖

Mutual Fund to Gain Most From Badla Ban

The SEBI order imposing a ban on Badla trading has had an adverse impact on the stockbrokers. The other market players, especially mutual funds have however benefited from the SEBI order. The funds available to Badla financiers are now available for investments in other areas. Mutual Funds have been able to cash in on this opportunity to persuade stockbrokers to market their products, both equity and debt funds – to the Badla financiers.

SEBI has also decided to ban all deferral products used on the stock exchanges from July 2001. ❖

Investments Abroad

The high level Committee on capital markets has approved overseas investments by Indian partnership firms and companies providing professional services. This indicates that the Government is gradually opening up outward remittances by residents.

Currently, domestic public and private limited companies are permitted to make investments abroad so long as these investments are funded by dollar earnings. The only exceptions are FIs who have been permitted to invest upto a total of $500m annually by buying dollars from the RBI. ❖

Cabinet clears diluted competition bill

The cabinet has cleared the diluted bill on competition law and policies named "Trade Related Competition Bill 2000" to replace the existing Monopolies and Restrictive Trade Practices Act of 1956 (MRTP Act). The bill based on the recommendations of the SVS Raghavan Committee, appointed by the Department of Companies Affairs seeks to regulate anti-competitive practices and the abuse of dominance by corporate entities. It also proposes to set up a 10-member multidisciplinary Trade Related Competition Commission of India (TRCCI) to replace the existing Monopolies and Restrictive Trade Practices Commission (MRTPC).

The dilution comes from making pre merger notifications optional. Under the proposed bill, entities entering into mergers and acquisition (M&A) deals, irrespective of the value of their assets and turnover, need not inform the Commission of the planned deal. However they have the option to seek advance ruling on whether the proposed merger could have appreciable adverse impact on competition.

The new bill vests wide powers on the Commissioner to scrutinize as well as break up a M & A, post deal, if it is felt that M & A has had an appreciable adverse impact on competition or if it is found to be indulging in anti-competitive practices or distorting to fair play in the market. The post merger scrutiny which would be taken up by the Commission on the basis of complaints received by it or suo motu.would be subject to the merging entities crossing a prescribed threshold limit which is a combined turnover of Rs 3000 crore for the merging entities and/or assets base valued at Rs 1,000 crore. The bill has also stipulated stiff penalties, as much as Rs 1 crore for failure on the part of the corporate to comply with the provisions of the legislation.

The Central Government reserves the powers to remove /suspend the members from office.

Present Position:

The bill was introduced in the Lok Sabha on 7th August 01.The bill will be taken up for discussion after the select committee submits its report. The discussion is now expected to come up only in the winter session of the parliament. The law would be taken up for implementation after a year of its becoming an Act so as to give corporates time to understand the new legislation. ❖

Depositors Can’t Open Accounts Online: RBI

According to the RBI guidelines on Internet banking the Regulator has barred banks from extending the facility of opening online accounts. The specific circular issued to commercial banks stated that though the request to open an account can be accepted over the net, accounts should be opened only after a proper introduction and physical verification of the customer’s identity.

According to RBI, only institutions who are members of the cheque-clearing system in the country will be permitted to participate in inter-bank payment gateways for internet payment. Each gateway must nominate a bank as the clearing bank to settle all the transactions.

RBI has said that the payments arising out of cross border e-commerce transactions and all intra-bank payment should be excluded for settlement through an inter-bank payment gateway. ❖

Counter Bids To Open Offer Disallowed for PSU Buyers

SEBI has decided to relax some sections of the Takeover Code in order to help the privatisation process. It has decided to disallow counter offers to the mandatory open offer which the strategic partner has to make, once he buys an equity stake in a PSU.

It has also allowed companies to take management control of the PSU before the completion of the open offer. SEBI has however reiterated that the public offer by the strategic partner after it purchases a stake in the PSU will continue to be mandatory.

While maintaining that the public offer will continue to be applicable to PSUs, SEBI has stipulated that the competitive bidding process will not be followed by a counter offer.

The open offer to be made must be done by the strategic partner within four working days of the signing of the agreement with the Government. The pricing of the open offer will continue to be based on the average price of 26 weeks form the date on which the strategic partner is selected by the Government. The negotiated price will also be a factor in determining the offer price.

Another area where SEBI has relaxed norms is in allowing the successful bidder to transfer shares received through the disinvestment in their names even before the open offer is completed. ❖

Supreme Court Stays HC Proceedings on Bidding for Cellular Slots

The Supreme Court stayed the proceedings on petitions filed before the Madras and the Delhi High Court concerning the bidding process for induction of new operators for cellular slot and issued notices to the parties before the High Courts. This order was passed on a transfer petition filed by the Centre and a notice was also issued to the Telecom Regulatory Authority of India.

The Telecom Dispute settlement Appellate Tribunal (TDSAT) had refused to grant stay on issuing basic telecom licences for operating WLL services in Tamil Nadu. As a consequence, the Department of Telecommunications (DOT) could issue basic telecom licences for Tamil Nadu as Chennai High Courts stay was only valid till the 9th of August, 2001

The Chennai High Court had granted stay on the grant of basic telecom licences by the DOT following a petition by BPL. ❖

SEBI To Announce Futures Trading

SEBI is likely to start trading of futures in about a dozen high profile stocks soon. The decision to allow individual investors to trade in futures is likely to be taken by the market regulator with senior executives of top stock exchanges. The board will also discuss the corporatisation of the stock exchanges. It is learnt that SEBI is pushing for demutualisation very seriously.

SEBI will also discuss ways to insulate the market functioning from the volatility.

With this instrument, an investor can trade in individual stocks three months in advance by paying just 10 per cent margin money. The introduction of tradings in futures in liquid stocks will probably pep the market sentiment. After the banning of Badla, trading volume in the stock markets has gone down drastically. ❖

SEBI To Lay Down Norms To Control MF Investments

The SEBI has decided to prescribe norms for mutual funds to usher in greater transparency in their functioning. SEBI seeks to make it mandatory for a fund categorised as debt or equity to invest atleast 70% of their assets in that class of investment. Thus an equity fund must invest atleast 70% of its net assets at market value in equity instruments, while the balance can be put in cash or money market. Funds would have to maintain this level for 30 out of 52 weeks in a year.

The SEBI norms are based on recommendations made by the Association of Mutual Funds in India, the Apex Body. ❖

SEBI Wants MFs To Disclose Results On Quarterly Basis

SEBI has decided to make it mandatory for mutual funds to disclose their results on a quarterly basis on their websites, as opposed to the half-yearly disclosure of results in newspapers. It was also decided that the fund will have to benchmark the performance of schemes by comparing it with the standard indices. When disclosing, the Fund should also compare with the performance of benchmark indices like the BSE Sensex, BSE 100 or NIFTY during the same period. AMFI (Association of Mutual Funds in India) the Apex Body, has apparently welcomed the move saying this would put Indian mutual funds at par with international standards on disclosure standards.

SEBI will also ask the funds to disclose their portfolio in the SEBI prescribed format on their websites on a continuous basis. Under the standard SEBI format, MFs are required to disclose NPAs, provision for doubtful debt, specify listed and unlisted securities and also give details of rated and unrated debt. ❖

AMFI to Standardise Disclosure Format For Equity, Debt Funds

In order to make it easier to compare different mutual funds, the Association of Mutual Funds in India has prescribed a standard disclosure format for equity and debt funds. This follows the SEBI directing the industry's apex body to outline the guidelines of best practices for portfolio disclosure and industry classification.

Suggestions for equity funds:

- Mutual funds disclose their equity investment in descending order of the scrip's weightage to net assets of the scheme.
- Along with the above should be a note indicating the industry to which the company belongs.
- MFs should disclose the percentage exposure to thinly traded and unlisted stocks for each scheme in the portfolio disclosure statement.

Suggestions for debt funds:

- The portfolio of securities should be categorised into corporate debt, government securities, money market investments and PSU or FI bonds separately.
- Within these categories individual holdings should be disclosed in descending order of their weightage to net assets.

In order to make it easy for investors, a portfolio classification by way of ratings and a pie chart representation of the debt holdings maturity profile has been recommended.

The guidelines were finalised and approved by the AMFI board recently.

Meet the A.R.A. LAW Team

In each issue, we will be profiling one person who is a part of A.R.A. LAW. They will also be sharing their experience of working at A.R.A. LAW.

R

adhika obtained her Law Degree from the University Law College, Bangalore in 2000. She has taken part in debates and Moot Courts at inter-college on topics ranging from constitutional law to personal law. At college, Radhika specialised in the law of company law, commercial law and intellectual property. Radhika is also pursuing her Corporate Secretaryship from the Institute of Company Secretaries, Bangalore.

Working with A.R.A.LAW is an exciting and enriching learning experience. A.R.A.LAW is an excellent example of a young, dynamic and creative law firm which provides its associates with a high quality work environment, challenging opportunities, meaningful career growth and scope for learning and professional development. It has given me the opportunity to work on various assignments evolving the new vistas of corporate law, thereby enabling me to develop my skills and legal acumen. I am very happy to be a part of the A.R.A LAW team. ❖

EDITOR IN CHIEF
Rajesh N. Begur
EDITORIAL TEAM
Krishna Patel
CIRCULATION
M.P. Madhusoodanan
Melanie D'souza

LEGAL EYE is published by A.R.A. LAW for private circulation only.

This newsletter is intended to provide an informational summary of the breaking legal developments in India as they happen. It is not intended to provide definitive legal advice in connection with any particular article, and counsel should be consulted with respect to any of the articles.

Should you require any clarifications or additional updates, please feel free to write to the Editor at:

A.R.A. LAW
Agra Building, 1st Floor
121 M.G. Road
Fort, Mumbai 400023
India
Tel: +91 22 2631700
Fax: +91 22 2631800
e-mail: rajesh@aralaw.com & aralaw@vsnl.com