FRANKLIN
SOCIÉTÉ D'AVOCATS

NEWSLETTER – MARCH 2007

India Desk

SUMMARY

EDITOR'S NOTE

Bridging Gaps

It is my pleasure to present the first edition of the *India Desk Newsletter*. The newsletter is a service of the recently launched India Practice of the Firm. This initiative stems from the increasingly international focus of the Firm's Outsourcing and New Technologies practices, which has led us to travel frequently to India and work with Indian attorneys. Seeing the potential for rapid growth in business between France and India and the need for an integrated approach to this market, the Firm started the India Desk. Our goal is to serve as a bridge for business between France and India. As part of our service offering to French clients, the India Desk calls upon the experience of an Indian attorney, Prashant Mara, who has joined our Paris office and has on-point experience in Indian laws and markets. The India Desk will be able to act as a first point of contact and support, in France, for all legal queries relating to Indian laws and regulations. Through our extensive network of contacts in the legal and business sectors in India, we can also help clients to choose and work with the right legal and commercial partners in India.

We recognize that the first step to building an effective entry and operations strategy in a country such as India with its diverse and sometimes complicated legal structure is to be aware of the laws that may affect the planned undertaking. In order help our clients and friends to achieve this objective, we intend this newsletter to be a quarterly publication with articles covering important areas of law relevant to French companies planning to enter and operate in India. The newsletter will also contain snippets of major business news from the Indian market and updates on the legal environment in India. It will be our endeavour to make the information as practical and relevant as possible to the readers. Having said this, I would also add a note of caution here that the articles are intended to provide only a brief overview of the laws and are not intended to constitute legal advice applicable to a specific situation. Indeed, to cover all issues and facets in a newsletter would be impractical and counter productive. The newsletter aims to be informative and perhaps just as importantly, we hope that it will encourage you to let us know what more we can do to cover areas and issues of concern to you as you plan your entry into India or deal with the challenges that arise with your existing operations in India.

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Indian Business

'06 Trends

The Indian economy continued to grow in 2006 at a rate unmatched since the independence of India in 1947. Last year also saw a second round of liberalization by the Government allowing private sector participation in almost all sectors of the economy and further opening up of the Indian market to FDI. In this section, we take a look at some of the major trends in Indian business in 2006..

Consistent Growth

At the end of 2005 many analysts predicted that the 8 % growth that the economy saw in 2004 and 2005 could not be sustained in 2006. Contrary to such expectations the economy maintained the trend and investors grew more confident. Growth was not limited to certain sectors such as the IT-BPO sector which have traditionally recorded 30% figures. Sectors such as manufacturing/industrial production and agriculture also grew at a good pace which increased market confidence to an even greater extent.

Mergers and Acquisitions

Mergers & Acquisitions dominated the business environment in India. Cash rich Indian companies went abroad to acquire foreign companies in order to establish a presence in new markets. The Indian IT sector was very active in foreign acquisitions with "Near Shore Delivery" as a concept finding support from offshore services providers and customers alike. Other industries such as power and automobile companies also cautiously started to look at inorganic growth outside India. Multinationals already present in India consolidated their presence by acquiring other Indian companies, while other multinationals entered India through acquisitions and joint ventures.

Influx of VC

The burgeoning growth of the Indian economy became a big draw for Venture Capital firms from across the globe. During the year, there was a significant move by these firms to invest in Indian start-ups, particularly players in the telecom, IT, and BPO segments. A study conducted by Evalueserve showed that VC and private equity investments had begun picking up in India in 2004, with the gradual recovery of the global technology markets. The investments had risen from around US$ 1.65 billion in 2004 to US$ 2.2 billion in 2005 and had touched US$ 3.48 billion by the end of June 2006. According to Evalueserve, in August alone, at least five India-specific funds—totaling more than US$ 600 million, were announced by VCs in the US, Switzerland and Japan, that included telecom among their target markets..

India INC.

India INC. is a term used to refer to a new breed of homegrown companies who are on their way to becoming global players. 2006 saw India INC performing well by consolidating their presence in India and establishing footprints across the globe. India INC. comprises of a growing number of professionally run Indian companies which are listed on stock exchanges around the world and have corporate governance at the top of their agenda. India INC also realized the importance of marketing "Brand India" and combined efforts to showcase India to the world with great success.

Employment Market

While India does have a large talent pool (annually 167,000 engineering students and 1.54 million graduates pass out of the country's educational institutions), not all are 'industry-ready' or equipped with the necessary skill sets to become useful to the companies. This means that while there is plenty of supply at the entry level of operations, there are huge gaps in the middle management and senior management levels. This has resulted in increased levels of poaching and attrition over the past five years, and the same continued in 2006. Further, due to the shortage of personnel for middle and senior management positions, costs of hiring for these posts also went up in 2006 to the extent that some pay packages were comparable to those being paid in US and European companies.

Data Security

2006 also saw renewed attention on the issue of data protection and security in India, especially in the IT and BPO industry. Cases of theft of data and credit card fraud by BPO employees raised serious concerns about the ability of Indian companies to safeguard data of their customers. As a response to these concerns, the Government of India introduced a Bill in the Parliament, which, if passed, will criminalize data thefts and also provide stricter penalties for companies failing to protect data of customers.

Though these measures are a step in the right direction, experts believe that they may not be sufficient. European companies may still have to rely on contractual provisions and security audits to ensure that data protection principles are complied with by their Indian counterparts.

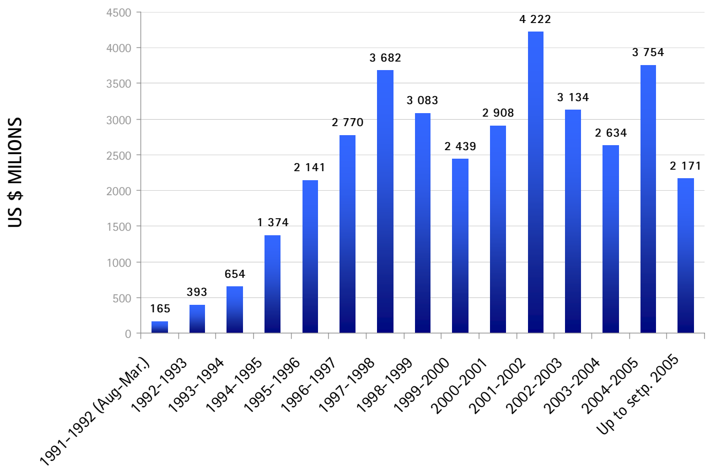
Practice Note: Foreign Investment in India

Favored Destination for FDI

For more than four decades following India's independence in 1947, the economic policies of the Indian government discouraged foreign investment. This state of affairs began to change in 1991 following a critical foreign exchange crunch that pulled the economy down to the extent of defaulting on loans. The Government responded by initiating a slew of domestic and external trade policy measures partly prompted by the ongoing crisis and partly due to the pressure of international organisations and governments. The new policy regime radically pushed forward in favour of a more open and market oriented economy. Theses reforms have been hugely successful, as shown by the FDI inflow chart below[1] and by the unabated and impressive growth of the Indian economy.

India has now displaced the United States of America as the second-most favored destination for FDI in the world after China and is currently ushering in the second generation reforms aimed at further and faster integration of the Indian economy with the global economy. As a result of the various policy initiatives taken, India has been rapidly changing from a restrictive economic regime to a liberal one, and FDI is encouraged in almost all the economic activities under the automatic route which does not need Government approval (explained in detail below). As recently as the last financial quarter, the Central Government has divested some of its own powers of approving foreign investments that it exercised through the Foreign Investment Promotion Board (FIPB) and has handed them over to the automatic approval route under the Reserve Bank of India (RBI). Sectoral caps in hitherto closed sectors such as infrastructure, aviation and retail have been eased to encourage FDI flow into India.

INDIA: YEAR WISE FDI INFLOWS



Investment in Various Sectors

FDI is allowed under the automatic route in all activities/sectors except as outlined below:

- *Prohibited sectors.* No FDI is permitted in the following sectors:
    - retail trading (except single brand retailing),
    - atomic energy,
    - lottery, and
    - gambling and betting.

- *Activities/items that require an industrial license prior to foreign investment.* These sectors are: distillation and brewing of alcoholic drinks, manufacture of tobacco products, industrial explosives, defence equipment, industrial explosives and hazardous chemicals, for which a separate application needs to be made to the Secretariat of Industrial Assistance prior to foreign investment.
- *Technical and Financial Collaboration.* Prior permission of the FIPB is necessary for proposals in which the foreign group has an *existing financial/technical collaboration* in India in the same field. If the foreign group makes additional investment as a follow on to an existing collaboration then subject to the sectoral limits, no permission is required.

[1] Statistics from the Ministry of Commerce, Government of India.

- *FDI Sectoral Caps*. Prior permission of the FIPB is necessary for proposals where the *foreign investment exceeds the notified sectoral policy caps* under the FDI policy. FDI sectoral caps presently are at four levels- 24 percent, 49 percent, 74 percent and 100 percent. Most sectors such as green field airports, IT, construction, wholesale trading, petroleum/natural gas, coffee and tea processing, power, non-banking financial services, mining, agriculture (and related sectors) fall under the 100 percent category and thus do not need prior Government approval.

Procedure under the automatic route

FDI in sectors/activities permitted under the automatic route does not require any prior approval either by the Government or the RBI. Investors are only required to notify the Regional Office of the RBI within 30 days of receipt of inward remittances and file the required documents with that office within 30 days of issue of shares to foreign investors.

Procedure under Government Approval

FDI in activities not covered under the automatic route require prior government approval. Approvals of all such proposals including composite proposals involving foreign investment/foreign technical collaboration is granted on the recommendations of the FIPB, Department of Economic Affairs (DEA), Ministry of Finance. Proposals including financials are submitted to the FIPB for recommendations and the approval process usually takes around 12 to 14 weeks depending on the sector of investment..

Investment in Existing Companies

Les investisseurs étrangers peuvent bénéficier de la procédure automatique dans le cadre de la création d'entreprises, mais aussi de la prise de participation au capital de sociétés indiennes existantes, sous certaines conditions supplémentaires, dont les trois principales sont les suivantes :

- The money to be remitted into India should be in foreign currency;
- The proposed expansion programme should be in the sector(s) under automatic route and within the sectoral caps, failing which the proposal would need Government approval through the FIPB; and
- Compliance with rules governing the issuance of equity and preference shares in an Indian company.

Some Practical Tips

- The FIPB has been set up as a department in the Ministry of Finance to negotiate and clear proposals for FDI where Government approval is necessary and has the flexibility to examine proposals in totality. Unfortunately, at times there is very limited transparency in the way the decisions not granting approval are taken. It is therefore best to follow up with the FIPB and to use experienced intermediaries to increase your chances of success..
- Proposals should be unambiguous with respect to the sector of investment since this will determine the sectoral cap as well as the method of entry (automatic or Government approval). In case of ambiguity, appropriate precedents should be referred to for guidance and advice from legal experts should be sought.
- Irrespective of whether FDI is through the automatic or the Government approval (FIPB) route, the foreign investor will have to ensure that it procures all state level clearances and approvals necessary from the State Government before it can actually start operations. This is a feature necessitated by the Federal form of governance in India, where certain approvals such as environmental clearances, health and safety approvals, and land concessions are handled by various State Government authorities. Sufficient time and resources should be factored into the business plan for these approvals.

News Snippets

Intellectual Property Rights

The shape of goods in India is capable of protection under the Indian law governing industrial designs, but this protection lasts only for five years in most cases without the option to renew the registration. This has caused considerable difficulties to foreign companies having distinctively shaped products since after the end of the five year period of protection; anybody could copy the shape of the product. This situation is changing however, as a recent Delhi High Court decision has held that product shapes may also qualify as trademarks under Indian law. With this decision of the Delhi High Court, any company with a distinctively shaped product can now register the shape as a trademark and hold exclusive trademark rights in perpetuity subject to renewals.

Information Technology

The long awaited bill to amend the Information Technology Act was introduced in the Indian Parliament in December 2006. If passed, the Bill will impose stricter penalties and criminal sanctions against offenders of the Act. The amendment comes in the wake of continued breach of confidential personal information by personnel of Indian companies, especially Business Process Outsourcers. The bill seeks to prevent data theft by prescribing stricter security procedures for Indian companies handling personal data. Further, the act tries to deter individuals from stealing and selling data by imposing criminal sanctions on such offenders.

Business News

On November 5, 2006, the Government of India increased the FDI ceiling for telecom companies from 49% to 74%, subject to certain conditions.

Tata- Corus Deal: Tata Steel Limited acquired Corus Group Plc through a complete share capital buy out, at a price of 608 pence in cash for each share valuing Corus at GBP 6.2 billion. The acquisition was funded through cash resources and loans raised by Tata Steel and its subsidiary companies formed for the purpose of this acquisition. Some analysts said the deal was expensive and could strain Tata finances at least in the short term. However, Tata Steel is confident that it would achieve a number of strategic objectives including providing Tata Steel with access to new, higher end-markets and a more sophisticated customer base.

Hindalco- Novelis Deal: Aditya Birla Group's Hindalco Industries Limited, India's largest non-ferrous metals company, and Novelis Inc., the world's leading producer of aluminum rolled products, announced on 11th February 2007, that they have entered into a definitive agreement for Hindalco to acquire Novelis in an all-cash transaction which values Novelis at approximately US$6 billion, including approximately US $2.40 billion of debt. Under the terms of the agreement, Novelis shareholders will receive US $44.93 in cash for each outstanding common share

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Danone: Economic Times (a leading newspaper in India) reports that Groupe Danone has confirmed that it is on the lookout for "new opportunities" for developing its core businesses in India. The French foods giant said India was a key market for the group even as it sought arbitration with the Wadia Group- its Indian JV partner in Britannia (a leading confectionary and dairy company in India)- on a case pertaining to violation of non-compete clause between them.