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Legal Update for the month of August 2009

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EXECUTIVE SUMMARY

It is a pleasure to bring to you the Legal update for the month of August 2009. The various writings herein consisting of Press Release, Notifications, Circulars, Case Laws and Daily News Snippets bring to you the present Indian Legal scenario and the proposed changes in the same.

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- NEWS SNIPPETS

We hope you continue to find this legal update informative and enjoyable.

PRESS RELEASES

CHANGES IN FOREIGN DIRECT INVESTMENT NORMS

PIB Press Release, Dated – 22 July, 2009

Government has put in place a liberal and investor-friendly policy on Foreign Direct Investment (FDI) under which FDI up to 100 per cent is permitted on the automatic route in most sectors/ activities. The policy on FDI is reviewed on a continuing basis through inter-ministerial consultations, with due consideration of relevant issues raised by various stakeholders. During February 2009, Government had issued guidelines on the subject of calculation of total foreign investment, i.e., direct and indirect foreign investment in Indian companies; transfer of ownership or control of Indian companies in sectors with caps from resident Indian citizens to non-resident entities and clarificatory guidelines on downstream investment by Indian companies through Press Notes 2, 3 and 4 of 2009 respectively. The Department of Economic Affairs had requested Department of Industrial Policy & Promotion for examination of certain issues relating to these Press Notes including, inter alia, certain issues mentioned by the Reserve Bank of India, to which Department of Industrial Policy & Promotion had responded. The Policy on Foreign Direct Investment (FDI) is incorporated in the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000, notified under the Foreign Exchange Management Act (FEMA), 1999. Section 13 of the Act provides for imposition of penalty, after adjudication, for contravention of the provisions of the Act or Rules/ Regulations.

UNIQUE TRANSACTION NUMBER

**Press Release No. BSC/BY/GN-276/09, Dated – 24 July, 2009, Issued by
Ministry of Finance**

The Government has decided to make it compulsory to quote Unique Transaction Number (UTN) in the Income-tax return forms to be filed by all the assesseees to whom such number has been allocated by the Income-tax Department. Since the UTN has not been communicated to the taxpayers, therefore, the requirement of quoting UTN in Income-tax return form for assessment year 2009-10 has been kept in abeyance.

Unique Transaction Number would be allotted against each transaction in which tax has been deducted or collected at source. It is proposed to make it compulsory to quote this Number in the Income –tax return forms so as to ensure prompt verification and granting of tax credits to the taxpayers.

This system of allotting Unique Transaction Number is expected to become operational by 1st January, 2010.

NOTIFICATIONS

SECURITIES AND EXCHANGE BOARD OF INDIA (INTERMEDIARIES) (AMENDMENT) REGULATIONS, 2009 – INSERTION OF CHAPTER V-A

**Notification No. LAD-NRO/GN/2009-10/12/169546, Dated- 14 July, 2009,
Issued by SEBI**

In exercise of the powers conferred by section 30 of the Securities and Exchange Board of India Act, 1992 (15 of 1992), the Board hereby makes the following regulations to further amend the Securities and Exchange Board of India (Intermediaries) Regulations, 2008, namely:-

1. These regulations may be called the Securities and Exchange Board of India (Intermediaries) (Amendment) Regulations, 2009.
2. They shall come into force on the date of their publication in the Official Gazette.
3. In the Securities and Exchange Board of India (Intermediaries) Regulations, 2008, after Chapter V, the following chapter shall be inserted, namely:-

“CHAPTER V-A

33A. Situations when summary procedure to be followed – Notwithstanding anything contained in these regulations, any proceedings initiated under chapter III of the erstwhile Securities and Exchange Board of India (Procedure for Holding Enquiry by Enquiry Officer and Imposing Penalty) Regulations, 2002 (repealed vide Notification No. LAD –NRO / GN / 2008 / 11 / 126538, dated May 26, 2008) prior to the coming into force of these regulations, shall be disposed of in accordance with provisions of this Chapter.

33B. Procedure to be followed under this Chapter (1) – The Chairman or member may appoint an officer of the Board, not below the rank of Assistant General Manager or Assistant Legal Advisor for giving his recommendation after following the procedure under this regulation in respect of the proceedings referred to in regulation 33A:

Provided that in respect of the proceedings referred to in regulation 33A, if a representation is received from an intermediary to dispense with the procedure laid down in regulation 33B, the Chairman or the members may not appoint an officer of the Board under this sub-regulation and pass an appropriate order after considering the representation of the intermediary.

- (2) The officer appointed under sub-regulation (1) shall issue to the intermediary, against whom the proceedings are being held, a notice requiring the intermediary to make a written submission in reply to the notice within such time, not exceeding fifteen days after the receipt of the notice, as may be specified in the notice:

Provided that the officer may extend the time mentioned under sub-regulation (2) for sufficient reasons to be recorded in writing.

- (3) If the intermediary fails to make a written submission to the notice within the period specified in the notice, the officer shall, after considering the circumstances and in light of the material on record, submit a report to the Chairman or the member as the case may be, and may recommend taking of

any action under regulation 27 as he considers appropriate in the circumstances of the case and shall give reasons for recommending such action.

- (4) If the intermediary makes submission within the said period, the officer shall, after considering the submission so made, submit a report to the Chairman or the member, as the case may be, and may recommend taking of any action under regulation 27 as he considers appropriate in the circumstances of the case and shall give reasons for recommending such action.
- (5) The Chairman or the member, as the case may be, after receipt of recommendations from the officer under sub-regulation (3) or sub-regulation (4), shall pass such orders as he may deem appropriate.
- (6) The Chairman or the member may pass a common order in respect of a number of intermediaries where the subject-matter in question is substantially the same or similar in nature.

33C. Publication of order – The Board shall issue a press release in respect of an order under this Chapter in at least two newspapers of which at least one shall have nationwide circulation and shall also put the order on the website of the Board”.

**FOREIGN EXCHANGE MANAGEMENT (BORROWING OR LENDING IN
FOREIGN EXCHANGE (SECOND AMENDMENT) REGULATIONS,
2009–AMENDMENT IN SCHEDULE I AND SCHEDULE II**

**Notification No. G.S.R. 547 (E) [NO. FEMA, 194/2009-RB], Dated – 17 June,
2009, Issued by Foreign Exchange Department, RBI**

In exercise of the powers conferred by clause (d) of sub-section (3) of section 6 and sub-section (2) of section 47 of the Foreign Exchange Management Act, 1999 (42 of 1999), the Reserve Bank of India hereby makes the following amendments in the Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 (Notification No. FEMA 3/2000-RB, dated May 3, 2000), namely:-

1. SHORT TITLE AND COMMENCEMENT

- (a) These Regulations may be called the Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) (Second Amendment) Regulations, 2009.
- (b) They shall come into force from the dates specified in these Regulations.*

2. AMENDMENT OF THE REGULATIONS

In the Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 (Notification No. FEMA 3/2000-RB dated May 3, 2000) (hereinafter referred to as ‘the principal regulations’),-

(A) In Schedule I in paragraph (1). -

- (a) in sub-paragraph (iv)
 - (i) for clause (AA), the following shall be substituted and shall be deemed to have been substituted with effect from 29th day of May, 2008, namely :-

“(AA) Borrowings in foreign exchange per borrower company per financial year up to such amounts not exceeding US Dollars 500 million or its equivalent as directed by the Reserve Bank from time to time shall be permitted for such permissible end-uses as indicated by Reserve Bank from time to time.”

- (ii) in sub-paragraph (A), in clause (a), for ‘Explanation’ the following shall be substituted and deemed to have been substituted with effect from the 8th day of October, 2008, namely :-

“Explanation: The following sectors will qualify as infrastructure sectors, namely: (i) Power, (ii) Telecommunication, (iii) Railways, (iv) Road including Bridges, (v) Sea Port and Airport, (vi) Industrial Parks, (vii) Urban Infrastructure (water supply, sanitation and sewage projects) and (viii) Mining, Exploration and Refining”.

- (b) for sub-paragraph (ix) the following shall be substituted and shall be deemed to have been substituted with effect from 22nd day of October, 2008, namely :-

“(ix) Parking of loan amount – The proceeds of borrowings in foreign exchange availed under the schedule may, pending utilisation for permissible end-uses, be parked abroad or in India as directed by the Reserve Bank from time to time.”

(B) In Schedule II, in paragraph (3), in sub-paragraph (iii),

- (i) in sub-paragraph (A) in clause (a) for ‘Explanation’ the following shall be substituted and shall be deemed to have been substituted with effect from the 8th day of October, 2008, namely :-

“Explanation: The following sectors will qualify as infrastructure sectors, namely: (i) Power, (ii) Telecommunication, (iii) Railways, (iv) Road including Bridges, (v) Sea Port and Airport (vi) Industrial Parks, (vii) Urban Infrastructure (water supply, sanitation and sewage projects) and (viii) Mining, Exploration and Refining”.

- (ii) clause (AA) shall be substituted and deemed to have been substituted with effect from the 29th day of May, 2008.

“(AA) Borrowings foreign exchange per borrower Company per financial up to such amounts as directed by the Reserve Bank from time to time shall be permitted for such permissible end-uses as indicated by Reserve Bank from time to time.”

- (iii) for sub-paragraph (viii), the following shall be substituted and shall be deemed to have been substituted with effect from the 22nd day of October, 2008, namely:-

“Parking of loan amount–The proceeds of borrowings in foreign exchange availed under the schedule may, pending utilization for permissible end uses, be parked abroad or in India as directed by the Reserve Bank from time to time.”

CIRCULARS

EXPORTS OF GOODS AND SOFTWARE – REALISATION AND REPATRIATION OF EXPORTS PROCEEDS – LIBERALISATION

A.P. (Dir Series) Circular No. 70, Dated – 30th June, 2009, Issued by Foreign Exchange Department, RBI

1. Attention of Authorized Dealer Category –I (AD Category-I) banks is invited to A.P. (DIR Series) Circular No. 50 dated June 5, 2008, enhancing the period of realization and repatriation to India of the amount representing the full export value of goods or software exported, from six months to twelve months from the date of export, subject to review after one year.
2. The issue has since been reviewed and it has been decided in consultation with Government of India to extended the above relaxation for a further period of one year i.e., up to June 30, 2010, subject to review.
3. The provisions in regard to period of realization repatriation to India of the full export value of goods or software exported by a unit situated in Special Economic Zone (SEZ) as well as exports made to warehouses established outside India remains unchanged.
4. AD Category-I banks may bring the contents of this circular to the notice of their constituents and customers concerned.
5. The Directions contained in this circular have been issued under sections 10(4) and 11(1) of the Foreign Exchange Management Act (FEMA), 1999 (42 of 1999) and are without prejudice to permissions /approvals, if any, required under any other law.

EXTERNAL COMMERCIAL BORROWINGS (ECBs) POLICY

A.P. (DIR Series) No. 71, Dated – 30th June, 2009, Issued by Foreign Exchange Department, RBI

1. Attention of Authorized Dealer Category –I (AD Category-I) banks is invited to the A.P. (DIR Series) circular No. 46, Dated January 2, 2009 relating to External Commercial Borrowings (ECB).
2. On a review, it has been decided to modify some aspects of the ECB policy as indicated below:-
 - (i) ECB for Integrated Township – As per the extant policy, corporates, engaged in the development of integrated township, as defined in Press Note 3 (2002 Series) dated January 4, 2002, issued by DIPP, Ministry of Commerce & Industry, Government of India are permitted to avail of ECB, under the Approval route, until June 2009. On a review of the prevailing conditions, it has been decided to extend the permission up to December 31, 2009, under the Approval route. All other terms and conditions, stipulated in the A.P. (DIR Series) circular referred to above, remain unchanged.
 - (ii) ECB for NBFC sector–As per the current ECB norms, Non-Banking Finance Companies (NBFCs), which are exclusively involved in financing of the infrastructure sector, are permitted to avail of ECBs from multilateral /regional financial institutions and Government

owned development financial institutions for on-lending to the borrowers in the infrastructure sector under the Approval route, subject, inter alia, to the condition that the direct lending portfolio of these lenders vis-à-vis their total ECB lending to NBFCs, at any point of time, should not be less than 3:1. It has now been decided to dispense with this condition with effect from July 1, 2009. The proposals will, however, continue to be examined by the Reserve Bank under the Approval route, as hitherto.

- (iii) ECB for Development of Special Zone – As per the extant guidelines, ECB is permissible for the Infrastructure sector, which is defined as (i) power, (ii) telecommunication, (iii) railways, (iv) road including bridges, (v) sea port and airport, (vi) industrial parks, (vii) urban infrastructure (water supply, sanitation and sewage projects) and (viii) mining, refining and exploration. Further, units in the Special Economic Zone (SEZ) are also permitted to access ECBs for their own requirements. However, ECB is not permissible for the development of SEZ. It has now been decided to allow SEZ developers also to avail of ECB under the Approval route for providing infrastructure facilities, as defined in the ECB policy, within the SEZ. However, ECB shall not be permissible for development of integrated township and commercial real estate within the SEZ.
 - (iv) Corporates under Investigation – Currently, the ECB policy is not explicit about accessing of ECB by the corporates, which have violated the extant ECB policy and are under investigation by the Reserve Bank and/or Directorate of Enforcement. It is clarified that corporates, which have violated the extant ECB policy and are under investigation by Reserve Bank and/or by Directorate of Enforcement, will not be allowed to access the Automatic route for ECB. Any request by such corporates for ECB will be examined under the Approval route.
3. The modifications to the ECB guidelines will come into force with immediate effect. All other aspects of the ECB policy, such as USD 500 million limit per company per financial year under the Automatic route, eligible borrower, recognised lender, end-use, all-in-cost ceiling, average maturity period, prepayment, refinancing of existing ECB and reporting arrangements remain unchanged.
 4. Necessary amendments to the Notification No. FEMA 3/2000-RB dated May 3, 2000, viz. Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 are being issued separately.
 5. AD Category-I banks may bring the contents of this circular to the notice of their constituents and customers concerned.
 6. The Directions contained in this circular have been issued under sections 10(4) and 11(1) of the Foreign Exchange Management Act (FEMA), 1999 (42 of 1999) and are without prejudice to permissions/approvals, if any, required under any other law.

ISSUE OF INDIAN DEPOSITORY RECEIPTS (IDRS)

RBI/2009-10/106 A.P. (DIR Series) Circular No. 05, Dated - July 22, 2009

1. Attention of Authorised Dealer Category-I (AD Category-I) banks is invited to Companies (Issue of Indian Depository Receipts) Rules, 2004 (IDR Rules) notified by the Ministry of Corporate Affairs and subsequent amendments made thereto and Circular No. SEBI / CFD / DIL / DIP / 20 /2006 / 3 / 4 dated April 3, 2006 issued by the Securities and Exchange Board of India (SEBI) regarding issue of Indian Depository Receipts by foreign companies in India and the SEBI (Disclosure and Investor Protection) Guidelines, 2000.
2. In order to facilitate the eligible companies resident outside India to issue Indian Depository Receipts (IDRs) through a Domestic Depository and to permit persons resident in India and outside India to purchase, possess, transfer and redeem IDRs, it has been decided to operationalise the IDR Rules, notified by the Government of India, as amended from time to time, with immediate effect.
3. Accordingly, eligible Companies resident outside India may issue Indian Depository Receipts (IDRs) through a Domestic Depository. The permission has been granted subject to compliance with the Companies (Issue of Depository Receipts) Rules, 2004 and subsequent amendments made thereto and the SEBI (DIP) Guidelines, 2000, as amended from time to time. In case of raising of funds through issuance of IDRs by financial/banking companies having presence in India, either through a branch or subsidiary, the approval of the sectoral regulator(s) should be obtained before the issuance of IDRs.

Investment by Persons resident in India / FIIs / NRIs in IDRs

4. The FEMA Regulations shall not be applicable to persons resident in India as defined under section 2(v) of FEMA, 1999, for investing in IDRs and subsequent transfer arising out of transaction on a recognized Stock Exchange in India. Foreign Institutional Investors (FIIs) including SEBI approved sub-accounts of the FIIs, registered with SEBI and Non-Resident Indians (NRIs) may also invest, purchase, hold and transfer IDRs of eligible companies resident outside India and issued in the Indian capital market, subject to the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 notified vide Notification No. FEMA 20 / 2000-RB dated May 3, 2000, as amended from time to time. Further, NRIs are allowed to invest in the IDRs out of funds held in their NRE / FCNR (B) account, maintained with an Authorised Dealer / Authorised bank.

Fungibility

5. Automatic fungibility of IDRs is not permitted.

Period of redemption

6. IDRs shall not be redeemable into underlying equity shares before the expiry of one year period from the date of issue of the IDRs.

Procedure for transfer and redemption of IDRs

7. At the time of redemption / conversion of IDRs into underlying shares, the Indian holders (persons resident in India) of IDRs shall comply with the provisions of the Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004 notified vide Notification No. FEMA 120

/ RB-2004 dated July 7 2004, as amended from time to time. Accordingly, the following guidelines shall be followed, on redemption of IDRs:

- i. Listed Indian companies may either sell or continue to hold the underlying shares subject to the terms and conditions as per Regulations 6B and 7 of Notification No. FEMA 120/RB-2004 dated July 7, 2004, as amended from time to time.
- ii. Indian Mutual Funds, registered with SEBI may either sell or continue to hold the underlying shares subject to the terms and conditions as per Regulation 6C of Notification No. FEMA 120/RB-2004 dated July 7, 2004, as amended from time to time.
- iii. Other persons resident in India including resident individuals are allowed to hold the underlying shares only for the purpose of sale within a period of 30 days from the date of conversion of the IDRs into underlying shares.
- iv. The FEMA provisions shall not apply to the holding of the underlying shares, on redemption of IDRs by the FIIs including SEBI approved sub-accounts of the FIIs and NRIs.

Others

8. The proceeds of the issue of IDRs shall be immediately repatriated outside India by the eligible companies issuing such IDRs. The IDRs issued shall be denominated in Indian Rupees.
9. AD Category –I banks may bring the contents of this circular to the notice of their constituents and customers.
10. Necessary amendments to the Foreign Exchange Management (Transfer or Issue of Security by a Person Resident Outside India) Regulations, 2000 and Foreign Exchange Management (Transfer or Issue of Any Foreign Security) Regulations, 2004, are being issued separately.
11. The directions contained in this circular have been issued under Sections 10(4) and 11(1) of the Foreign Exchange Management Act, 1999 (42 of 1999) and are without prejudice to permissions / approvals, if any, required under any other law.

**SERVICE TAX ON COMMISSION PAID TO MANAGING DIRECTOR/
DIRECTORS BY THE COMPANY-REG**

**Circular No. 115/09/2009 – ST Dy. No. 324/Comm (ST)/2008,
Dated - 31 July, 2009**

1. Below mentioned issues have been referred to the Board seeking clarifications:-
 - (i) applicability of service tax under 'Business Auxiliary service' on commission paid to Managing Director / Directors (whole time, or Independent) by the company,
 - (ii) applicability of service tax on Independent Directors who are part of the Board of Directors under 'Management Consultant service'.
2. Both the matters have been examined by the Board and the clarifications are as under:-

- (i) Some Companies make payments to Managing Director/Directors (Whole-time or Independent), terming the same as 'Commissions'. The said amount paid by a company to their Managing Director/Directors (Whole-time or Independent) even if termed as commission, is not the 'commission' that is within the scope of business auxiliary service and hence service tax would not be leviable on such amount.
 - (ii) The Managing Director / Directors (Whole-time or Independent) being part of Board of Directors perform management function and they do not perform consultancy or advisory function. The definition of management consultant service makes it clear that what is envisaged from a consultant is advisory service and not the actual performance of the management function. The payments made by Companies, to Directors cannot be termed as payments for providing management consultancy service. Therefore, it is clarified that the amount paid to Directors (Whole-time or Independent) is not chargeable to service tax under the category 'Management Consultancy service'. However, in case such directors provide any advice or consultancy to the company, for which they are being compensated separately, such service would become chargeable to service tax.
3. In view of the above, it is clarified that remunerations paid to Managing Director / Directors of companies whether whole-time or independent when being compensated for their performance as Managing Director/Directors would not be liable to service tax.

Pending issues may be resolved in line with the above.

CASE LAWS

WINDING UP – EXCLUSION OF CERTAIN TIME IN COMPUTING PERIOD OF LIMITATION

Section 458A, read with section 543, of the Companies Act, 1956

**[2009] 93 SCL 166 (SC)
SUPREME COURT OF INDIA**

**Ajay G. Podar
Vs.**

Official Liquidator, Jaipur Spinning and Weaving Mills

FACTS:

An order of winding of the company was passed by the High Court in 1983 and the Official Liquidator was appointed on that day. The period of limitation of five years to file for misfeasance proceedings, referred to in section 543(2), expired in 1988. Misfeasance proceedings were filed by the Official Liquidator against the appellant in 1989. The appellant's case was that the said proceedings stood filed beyond limitation as prescribed under section 543(2). The Company Judge came to conclusion that the total period of limitation provided under the Act is five years from the date of winding up order besides exclusion of one year following the date of winding up order, and, thus, considered that the application was within limitation. The Division Bench of the High Court affirmed the order of the Company Judge. On appeal, the appellant submitted that since limitation is specifically provided for period of five years under section 543(2), it was not open to the Official Liquidator to rely upon and take resort to general limitation provision contemplated by section 458A to extend the period of limitation from five years to six years. The appellant further submitted that section 458A, in any event was not applicable, as

misfeasance proceedings instituted by the Official Liquidator could not be said to be proceedings instituted in the name and on behalf of the company. The Official Liquidator on the hand submitted that section 458A supplements Part III of the Limitation Act and it does not extend the period of limitation of five years, rather it provides for exclusion in the matter of computation of a period of five years limitation under section 543(2).

HELD:

On reading the provisions of section 458A and section 543(2) it is found that, there is a clear dichotomy between the concept of the 'period of limitation' on one hand and the concept of 'computation of that period'. Section 543(2) limits the time after which misfeasance or breach of trust proceedings, retainer proceedings and misapplication proceedings become time-barred. This dichotomy finds place not only in the above provisions of the Act but also under the provisions of the Limitation Act. Under section 2(f) of the Limitation Act, the period of limitation is required to be computed in accordance with the provisions of that Act. Further, the Limitation Act not only prescribes the period of limitation for different types of suits and applications but it also further provides for computation. If any period of limitation is to be excluded from the prescribed period of limitation the party has to satisfy any of the appropriate provisions in section 4 to 24 of the Limitation Act. The law of limitation is a procedural law. It is addressed to the commencement of a proceeding.

Although section 543(1) and (2) provides for locus and forum yet there is no provision for computation of the period of limitation. The Court was proceeding on the basis that section 543(2) provides for a different limitation that the limitation prescribed under article 137 of the Limitation Act. However, section 543(2) does not rule out the applicability of sections 12 to 24 in Part III of the Limitation Act. Part II of the Limitation Act deals with limitation of suits, appeals and applications, whereas Part III deals with the computation of period of limitation. Similarly, section 543(2) deals with limitation for application/claims mentioned in section 543(1) which includes misfeasance proceedings, whereas the computation of the period of five years is contemplated by section 458A.

There was no merit in the contention advanced on behalf of the appellant that by virtue of section 458A the period of limitation was extended by one year. Part III of the Limitation Act excludes certain circumstances mentioned in section 12 to 24 for computation of the period of limitation. Similarly, section 458A provides for an additional circumstance which is required to be taken into account as an item of exclusion in the matter of computation of the period of limitation of five years prescribed by section 543(2). That circumstance is a period spent between the date of commencement of winding up of the company and the date on which the winding up order is passed plus one year therefrom. If this period of limitation is to stand excluded it is only by virtue of section 458A, which circumstance is not contemplated by section 12 to 24 of the Limitation Act. Just as a different period of limitation is prescribed for misfeasance proceedings vide section 543(2) so also vide section 458A a special circumstance is indicated as an item of exclusion of certain time in computing the period of limitation. Therefore, there is no conflict between section 458A and section 543(2). If so read, there was no extension of the period of limitation of five years as was contended by the appellant. Section 458A excludes period between date of commencement of winding up of the company and date on which winding up order is passed plus one year therefrom. Therefore, it is a case of exclusion and not of extension of period of limitation of five years prescribed under section 543(2).

As regards contention of the appellant, that section 458A was not applicable to misfeasance proceedings instituted by the Official Liquidator, as such, proceedings were not in the name and on behalf of a company which was being wound up by the Court; in that connection, reliance was placed on section 458A which prescribes the mode of computation of the period of limitation for any suit or an application in the name and on behalf of a company which is being wound up by the Court. Therefore,

it was sought to be argued that misfeasance proceeding instituted by the Official Liquidator was neither a suit nor an application in the name and on behalf of a company which was being wound up by the Court. There was no merit in that argument. If book-debt is assigned by the company to a bank which fails to file a suit for recovery of money within the time prescribed under the Limitation Act, it would not be open to the Official Liquidator to institute the suit under section 458A because in that event the Official Liquidator is said to have filed a suit not on behalf of the company but on behalf of the bank. It is to such cases that section 458A will not apply. In the instant case, the Official Liquidator was authorised to take steps to recover assets, both financial and other assets by the company court under winding up order. It was pursuant to that authority that the Official Liquidator had instituted the misfeasance proceedings for recovery on 1-12-1989. The said proceedings had been initiated in the name of company and on behalf of the company to be wound up. The name of the applicant indicated in the appeal paper book showed that the Official Liquidator had filed misfeasance proceedings in the name of the company and on behalf of the company. Therefore, section 458A was squarely applicable to misfeasance proceedings instituted by the Official Liquidator in the name of the company and on behalf of the company-in-liquidation. Once an application is made in the name and on behalf of the company, section 458A would become applicable. In the instant case the winding up order indicated that the company court had granted such a sanction and the misfeasance proceedings had been instituted by the Official Liquidator in terms of section 457(1)(a). The claim on behalf of a company (in liquidation) filed by the Official Liquidator is in the form of application, though it is really a plaint and, hence, it cannot be stated that the misfeasance proceedings are proceedings instituted by the Official Liquidator in his own independent right. Once it is held that the said application is in the nature of a plaint then section 457 would apply. Section 458A is intended to extend the limitation period for the benefit of the company (in liquidation) and the Official Liquidator appointed to carry on its winding up process by collecting the assets and distributing the same among those entitled to the same. The underlying object in extending the limitation period is to enable the Official Liquidator to take charge of the affairs of the company; to examine the records, account books; to study the annual statements and, accordingly, proceed to recover and collect the assets. He has also to find resources for conducting the proceedings. The proceedings initiated by him by way of judge's summons or suit for enforcement of the recoveries cannot but be on behalf of the company having regard to his sources of authority, viz., the provisions of the Act and the statutory obligation in discharge of which he has to Act in this behalf. The Act does not contemplate his acting in the matter of recoveries excepting as the Official Liquidator and excepting on behalf of the company.

Therefore, section 458A, dealing with computation of the period of limitation, has to be read with section 543(2).

For the aforesaid reasons, there was no merit in the civil appeal and the same was, accordingly, to be dismissed.

**WINDING UP – CIRCUMSTANCES IN WHICH A COMPANY MAY
BE WOUND UP**

Section 433 of the Companies Act, 1956

**[2009] 93 SCL 134 (ALL)
HIGH COURT OF ALLAHABAD, LUCKNOW BENCH**

**Naresh Chandra Sharma
Vs.
Avadh Rubber Ltd.**

FACTS:

The petitioner was a shareholder and a former director of the respondent company. The petitioner had filed winding up petition against the respondent-company on the ground that the respondent-company had failed to pay his salary/remuneration for period from February, 2003 to April, 2003 along with pending allowances and increments. The respondent denied petitioner's claim stating that since the petitioner ceased to be on rolls of the company after 31-1-2003, there was no question of payment of any salary from February to April, 2003 and thereafter. The respondent-company raised objection against the maintainability of the writ petition on ground that for the payment of arrears of salary, the company might not be wound up under section 433(e) as the arrears of salary is not debt.

HELD:

The employee of the company can file the petition for winding up of the company on its failure to pay the salary to the employees but passing the order for winding up of the company depends upon satisfaction of the Company Judge that there is no other mode to claim the dues and salary and, further, without winding up of the company, the same cannot be paid. Therefore, the instant company petition was to be entertained subject to determination that the petitioner was employee of the opposite party and without the order of winding up of the company, the payment of dues against the salary was not payable.

The petitioner demanded his salary from February, 2003 to April, 2003. However, it was denied by the respondent on the ground that since the petitioner ceased to be on rolls of company after 31-1-2003, there was no question of payment of any salary from February to April, 2003 and thereafter. In view of contrary facts, before passing any order for winding up of the company, it had to be decided that the petitioner was entitled to the salary for the period he claimed and the same had become due for which several disputed facts had to be determined which could be determined only after going through the evidences adduced by the parties. Therefore, civil court would be the best Court to determine the factual aspects involved in the matter for payment of salary and the petitioner could resort to the claim for payment of salary under the term 'debt' by filing the civil suit before the civil court.

Therefore, the company petition was to be dismissed.

NEWS SNIPPETS

GOVERNMENT PLANS TO FREE ROYALTY, TECH FEE IN FOREIGN TIE-UPS

Thousands of companies that have foreign collaborations and many more that will do so in future stand to benefit as the government plans to free payment of royalty for use of trademark or brand and of technology transfer fees.

A draft Cabinet note prepared by the Department of Industrial Policy & Promotion (DIPP), under the commerce ministry, proposes to put such payments on the “automatic route” without restrictions and subject only to the Foreign Exchange Management Act (Current Account Transactions) Rules of 2000. The Cabinet note has gone to the Cabinet Committee on Economic Affairs, which is expected to take it up soon.

DIPP’s move has been endorsed by both the Planning Commission as well as the Department of Economic Affairs, both of which play critical roles in such policy decisions.

At present, if the technology transfer fee exceeds \$2 million, it has to be approved by the Projects Approval Board, under the Ministry of Commerce and Industry. For royalty, the limit is 5 per cent of domestic sales and 8 per cent of exports. If there is no transfer of technology, royalty is capped at 1 per cent of domestic sales and 2 per cent of exports.

According to DIPP, the situation has changed significantly, with the country sitting on foreign exchange reserves of over \$300 billion. Therefore, the department says, there is no justification for any restriction on payment of royalty. It has also argued that in a globalised economy the evaluation of technology and assessment of quality and justification for the knowhow and royalty payment need to be left to commercial considerations of the parties entering the contract. The issue should not be in the domain of the government.

However, such payments involve foreign exchange outflows, which are administered through FEMA rules, that decide which transactions cannot be allowed and which require approval of the Reserve Bank of India.

TAX TREATMENT FOR LLP ON LINES OF PARTNERSHIP FIRMS

A Limited Liability Partnership (LLP) will be taxed on the same lines as partnership firms – this would mean taxation of profit in the hands of the entity; the partners will be exempted. Ending the period of uncertainty on how a LLP will be treated for taxation purposes, the Finance Bill, 2009 states that “it is proposed to incorporate the taxation scheme of LLPs in the Income –tax Act on the same lines as the taxation scheme currently prevalent for general partnerships”. The Bill further proposes to make the amendments effective from April 1, 2010, for assessment year 2010-11. A LLP is an alternative corporate business vehicle that allows professionals such as chartered accountants, lawyers, and enterprises engaged in the information technology sector, science and technology sector, and venture capital business among others to create commercially efficient vehicles for providing business and services of high quality. The LLP Act provides for nomination of ‘designated partners’ who have been given greater responsibility. It has been proposed in the Finance Bill that the designated partner shall sign the Income–tax returns of an LLP, or, where for any unavoidable reason such designated partner is not able to sign the return or where there is no designated partner as such, any partner shall sign the return. In case of liquidation of an LLP, the Finance Bill proposes that every partner will be

jointly and severally liable for payment of tax unless he proves that non-recovery cannot be attributed to any gross neglect, misfeasance or breach of duty on his part. As an LLP and a general partnership are being treated as equivalent (except for recovery purposes) in the Act, the conversion from a general partnership firm to an LLP will have no tax implications if the rights and obligations of the partners remain the same after conversion and if there is no transfer of any asset or liability after conversion. If there is a violation of these conditions, the provisions of section 45 of the Act will apply.

NO STAMP DUTY IN SEZs

Developers of Special Economic Zones (SEZs) will get a blanket exemption from stamp duty on land purchases within the notified area for non-core activities, such as building hotels, housing complexes, shopping malls and golf courses, according to a Government official. The exemption had become a contentious issue with States where these projects are located demanding that it be restricted to core manufacturing areas, which have to cover at least 50 per cent of the total SEZ land. The Government has extended this to cover the whole area within the zone and has issued guidelines detailing the circumstances under which the sop can be availed, said the official asking not to be named. For the developers of the 500-odd SEZs in the country, slated to bring in investments of over Rs. 1,00,000 crore, this ends the uncertainty that has cropped up after some States had voiced their opposition. Orissa had objected to the Centre giving such a tax sop without consulting States and had termed the move *ultra vires*. It had pointed out that while the Centre had powers to legislate on stamp duty, the power to fix the duty rates lay with the States. This had forced the Commerce Department to seek the Law Ministry's opinion the provision in the SEZ Act. The exemption, however, will be available only after formal approval of the zone. For land bought after in-principle approval, the State Government may either give the exemption upfront or collect the duty and refund it after the zone has been set-up. If under some circumstances notification of a zone is cancelled the State Government will be entitled to withdraw the concession and recover the same from the developer.

ECBs FOR SEZs MAY BE ALLOWED

The Government is considering to permit developers and units in the Special Economic Zones (SEZs) to raise external commercial borrowings, a move that could reopen the window for mopping up overseas funds. An announcement to this effect could be made in the Budget scheduled to be unveiled by Finance Minister, Pranab Mukherjee in the Lok Sabha on July 6. The decision, sources said, would promote development of the special economic zones, besides helping the Government in arresting decline in the foreign exchange reserves.
