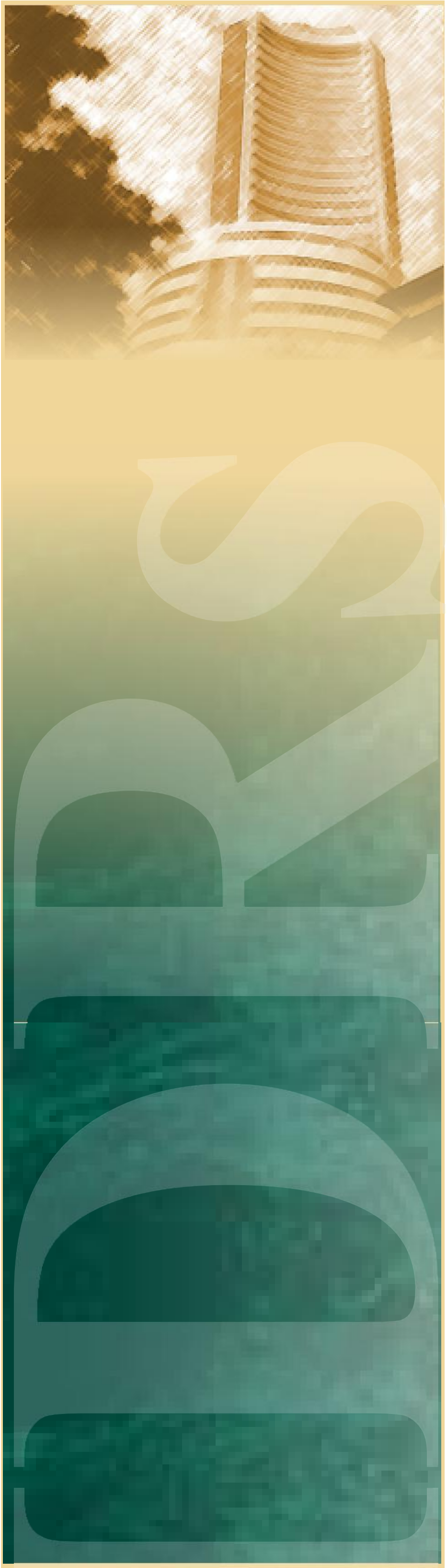
Indian Depository Receipts



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After a two-year gap following the introduction of Section 605-A in the Indian Companies Act, 1956 ("Companies Act") which permitted foreign companies to make a public offer of Indian Depository Receipts (IDRs"), the Department of Company Affairs, Government of India ("DCA") has prepared a draft Companies (Issue of IDRs) Rules, 2002 ("Draft IDR Rules"). News reports have indicated a few salient features of the Draft IDR Rules, which are briefly discussed in this update for your information.

The Draft IDR Rules propose to include certain eligibility criteria for foreign companies, which are looking at listing in India, including a five-year profitability criteria, a dividend record of more than 10% during the said five-year period, a 2:1 debt-equity ratio as well as an existing listing on an international stock exchange. Some good companies which are in the small and mid-size market segment may not be able to meet with all the criteria mentioned above, particularly the dividend criteria as foreign companies typically re-invest their profits into the business as opposed to Indian companies which are used to declaring dividends out of profits. These eligibility criteria may undergo some modifications based on the subsequent discussions that the DCA intends to have with other Indian regulatory authorities. Additionally, the Draft IDR Rules do not seem to require the foreign company to have any business in India, in order to seek an Indian listing. Prior to pursuing a listing in India, the foreign company will be required to seek the approval of the DCA.

The actual process for the issue of IDRs by a foreign company would be similar to the process followed by foreign private issuers looking at listing on American and European stock exchanges. The IDR would be an instrument denominated in Indian Rupees and represented by underlying securities of the foreign company, which are required to be listed on an international stock exchange. Hence, the foreign company would issue the securities underlying the Indian Depositary Receipts to an overseas custodian bank, which will in turn authorize the domestic depositary bank in India to issue IDRs to Indian investors. As part of the IDR process, the foreign company will also be required to appoint a merchant banker and file a due diligence report with the Securities and Exchange Board of India ("SEBI") and the Registrar of Companies. This portion is corresponding to the Indian IPO process where the merchant bankers are required to file a due diligence report in a prescribed format with the SEBI prior to the IPO.

There are also a few restrictions that are imposed by the IDR Rules such as an IDR cannot be redeemed into the underlying securities within a period of one year from the date of the listing of the IDRs on the Indian bourses. This restriction is somewhat unusual and the rationale for imposing such a restriction is also a little unclear. The foreign company is also required to transfer the IDR proceeds into a separate account and provide details of the use of the IDR proceeds and their repatriation. This requirement is similar to the reporting requirements for an Indian company issuing ADRs/GDRs to overseas investors.

The IDR route is attractive for small and mid-cap foreign companies, which are familiar with Indian markets or have promoters of Indian origin. Typically, these companies would be based in the Silicon Valley, U.S.A and South East Asia. With the cost of compliance increasing for

companies that want to be listed in the U.S., a listing in India may be an attractive option for foreign companies that view India as a potential market.

All the provisions of the Draft IDR Rules discussed above are in draft form and are currently being discussed by all the relevant Indian regulatory bodies including the SEBI and the Reserve Bank of India at a meeting convened by the DCA. We will keep you informed of the developments in this regard.

Source: The Economic Times, Mumbai Edition, October 1, 2002 and the Business Standard, Mumbai Edition, October 1, 2002.

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About us

Nishith Desai Associates is a research-based Indian legal and tax counseling firm, with offices in Mumbai and Palo Alto, California. We focus on three core areas of legal practice, namely corporate and securities law, international taxation and information, communication and entertainment laws. As part of our corporate and securities law practice, our team has worked on several overseas listings of Indian companies including the ADR issues of **Infosys Technologies, Satyam Infoway, Rediff.com, Silverline Technologies** and **Wipro** and the GDR issue of **Himachal Futuristic Communications Limited**. Our team has also worked on the recent domestic IPO of **Bharti Tele-Ventures** where we represented **Singapore Telecom's** interest. Our focus on cross-border legal and regulatory issues has given us an in-depth understanding of the various issues that arise when a company seeks to list on a foreign bourse, ranging from the conflicts between the corporate law requirements in the two jurisdictions, the double taxation issues that arise in connection with the returns that international investors get on their investments and other complex issues.