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Article

RoC's recent adjudication order against a global corporate – A regulatory oversight on Significant Beneficial Ownership

By **Noorul Hassan and Aman Gupta**

Recently, the Registrar of Companies, NCT of Delhi & Haryana imposed penalties against a global corporate and its Directors along with its Global CEO, including CEO of the holding company, for violating the provisions related to non-disclosure of Significant Beneficial Ownership ('SBO') under Section 90 of the Companies Act, 2013. The article in this issue of Corporate Amicus analyses the jurisprudence behind the SBO and the RoC's approach towards the Order. The article notes that the RoC has outlined the parameters such as control over the Board of Directors, financial control with the upstream entities, control through contractual agreements, Directors of the subject company holding top positions in the upstream entities, and power of the top managerial personnel through bylaws of the upstream entities as criteria to determine control through 'significant influence'. According to the authors, companies with global corporate structures, need to relook at the requirement of reporting the SBO in the companies.

RoC's recent adjudication order against a global corporate – A regulatory oversight on Significant Beneficial Ownership

By Noorul Hassan and Aman Gupta

Recently, the Registrar of Companies, NCT of Delhi & Haryana, in its extensive 63-page adjudication order[1] ('**Order**'), imposed penalties against LinkedIn India Information Private Limited ('**LinkedIn India**'/'**Company**') and its Directors along with Mr. Ryan Roslansky (Global CEO of LinkedIn) and Mr. Satya Nadella (CEO of Microsoft Corporation) for violating the provisions related to non-disclosure of Significant Beneficial Ownership ('**SBO**') under Section 90 of the Companies Act, 2013 ('**Act**').

Following its unique interpretation of the term '*control*' other than by shareholding in Metec Electronics Private Limited[2] and Leixir Resources Private Limited[3], the Registrar of Companies ('**RoC**') has been investigating the SBO of companies, particularly those having holding companies. While interpreting the applicability, RoC has delved deep into the 'corporate structure' and definition of '*control*', especially for those companies having a global presence with structural layers and top managerial personnel in control.

In this article, we have analyzed the jurisprudence behind the SBO and the RoC's approach towards the Order.

Jurisprudence behind SBO

Firstly, the recommendations of the Financial Action Task Force ('**FATF**') in 2012[4] set out the essential measures that countries should have in place *inter-alia* on reporting transparency and beneficial ownership of legal persons. It sets out that the countries must ensure that their laws mandate the registered companies to procure adequate, accurate, and up-to-date information to identify the natural persons who are the beneficial owners and maintain a register to document the same. Following the FATF recommendations, the Report of the Companies Law Committee released in February 2016[5]

[1] Order is here.
[2] Order is here.
[3] Order is here.
[4] Recommendations of FATF are here.
[5] Report of the Companies Law Committee is here.

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recommended that a definition must be provided for beneficial ownership, the obligation of companies to obtain information on beneficial ownership from its members, and maintenance of a register of beneficial owners.

The Companies (Amendment) Act, 2017, was notified[6] wherein through Section 90 of the Act the concept of 'significant beneficial ownership' was introduced to mean an individual with an indirect shareholding of not less than 10% in the reporting company or exercises 'significant influence' other than by shareholding. The Companies (Significant Beneficial Ownership) Rules, 2018, clarifies that 'significant influence' shall mean the power to participate in the financial and operating policy decisions of the company either directly or indirectly.

In common parlance, 'control' is identified by shareholding. However, there are other aspects to measure such control. The Guidance on Beneficial Ownership for Legal Persons released by FATF in 2023[7] deals with beneficial ownership beyond 'control through shareholding' such as differential voting rights to certain shareholders, power to appoint a majority of senior management lying with an individual, control through debt instruments owing to the terms of a lending agreement, control held by natural persons through positions within an entity, control through informal means (such as personal connections, relatives, etc.).

Indian company law has incorporated the aforementioned by terming it as a 'significant influence' to a certain extent. However, it is practically difficult to identify an SBO wherein the control is not through direct holdings. It is for this reason that the ROC has adopted an approach by digging deeper into the overall shareholding and management structure of the companies with global presence to identify the natural persons in the position of control. This approach is mainly adopted to prevent the misuse of legal personality for criminal purposes and to implement transparency measures.

RoC's Order

The RoC's Order penalized LinkedIn India and its directors along with Mr. Ryan Roslansky and Mr. Satya Nadella, with a cumulative amount of INR 21.5 lakhs on the grounds that they failed to declare their SBO in LinkedIn India.

While adjudicating the penalty in the above matter, the RoC adopted the subjective route to understand whether any 'control' is being exercised by any natural person through

[6] Companies (Amendment) Act, 2017 is available here.

[7] Guidance on Beneficial Ownership for Legal Persons released by FATF is available here.

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'significant influence'. A detailed questionnaire was sent to the Company to examine the same. It was noted by the RoC that prior to LinkedIn's acquisition by Microsoft, LinkedIn Corporation was reported as the ultimate holding company of LinkedIn India. Post-acquisition, this position was taken over by Microsoft Corporation however the same was not recognized in the financial statements of LinkedIn India. Further, in this regard, the Company failed to identify its SBO by sending notices in Form BEN-4, which is a violation of Section 90(4A) of the Act.

To analyze the subjective route, the RoC focussed on three factors/tests to identify the concerns of SBO:

A. SBO through holding subsidiary relationships

LinkedIn India has reflected in its financial statements that LinkedIn Corporation, USA, is its holding company despite its presence in the upstream entities. As understood, 'control' can be exercised even otherwise through shareholding, and in the present case, significant influence was exercised over the board of directors of LinkedIn India. It was noted that the same directors are in both LinkedIn Corporation and LinkedIn India hence the same set of persons cannot control themselves therefore the control has to be seen elsewhere. RoC proceeded to understand the role of Mr. Ryan Roslansky, CEO of LinkedIn Corporation, USA, in exercising significant influence over the Company. It is noted that his role is subject to review and oversight of the Board of Directors of LinkedIn Corporation, USA, and Microsoft Corporation, USA. However, certain incidents were observed to evidence the exercise of control by Mr. Ryan Roslansky such as announcing the global layoff of employees, involvement in R&D activities in LinkedIn India, and enjoying overall leadership roles of which LinkedIn India is a part. Accordingly, in the absence of directors, Mr. Ryan Roslansky has been regarded as the leader of the LinkedIn Corporation, USA, and therefore a Significant Beneficial Owner of LinkedIn India.

It was noted that Mr. Ryan worked under the senior leadership of Mr. Satya Nadella and reports to him. The bylaws of Microsoft Corporation, USA provide that the CEO of Microsoft Corporation has general charge and supervision of business and the designation of duties by the CEO to the Directors would remain in full flow. Thus, Mr. Satya Nadella was also considered as an SBO of LinkedIn India.

B. SBO through Reporting Channel tests

RoC noted that the employees in Microsoft Corporation, USA, holding significant positions have also taken the position of Directors in LinkedIn India, and Microsoft Corporation, USA

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enjoys a 'right to reject' the directorship of its employees in LinkedIn India. This gave rise to the argument that such employees can act as nominees of Microsoft, USA in LinkedIn India to represent its interests and exercise significant influence. It was noted that the Directors of the Company were appointed with no remuneration as they were remunerated from Microsoft, and the same Directors were appointed at most of the other entities of Microsoft globally, and the Directors of LinkedIn Corporation and LinkedIn India were the same after LinkedIn's acquisition, etc. These would infer that the reporting channels in the entire structure run up to Mr. Ryan Roslansky or Mr. Satya Nadella who has the right to exercise significant influence unless decided otherwise through their Board.

C. SBO through Financial Control tests

The treasurers of LinkedIn India including operating signatories and bank guarantee signatories are employees of Microsoft Corporation, USA. The Company adopted a resolution that any decision of its Board of Directors shall not override the decisions of the Treasurer of Microsoft Corporation in relation to financial control. This clearly demonstrated the financial control in the hands of Microsoft, USA. Further, the treasurers are not subject to the supervision of LinkedIn India hence it is evident that the control is being exercised by Microsoft, USA.

Our analysis

The RoC in the present Order has examined the extreme end of the reporting structure of LinkedIn India by questioning the minutest gaps possible. In the present case, the SBO could not be identified through shareholding hence the RoC tried the subjective route to investigate the authority of Mr. Ryan Roslansky and Mr. Satya Nadella over the Company. In doing so, the RoC challenged the very nature of the responsibility of global CEOs towards their group. It examined the acts of providing direction for the future vision and leadership, announcements for global layoffs, and overviewing the operations as a whole for LinkedIn Corporation, as acts of exercising significant influence over LinkedIn India.

The RoC has outlined the parameters such as control over the Board of Directors, financial control with the upstream entities, control through contractual agreements, Directors of the subject company holding top positions in the upstream entities, and power of the top managerial personnel through bylaws of the upstream entities as criteria to determine control through 'significant influence'.

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Conclusion

The views of the RoC in the Order as also in the other adjudication orders issued prior to this Order and that followed it under Section 90 of the Act would now determine the responsibility of such individuals who actually or rather beneficially own the company to disclose their interest. Recently, the RoC in its adjudication order dated 12 June 2024 penalised Samsung SDI India Private Limited along with its directors and KMP on the grounds that proxy control was being exercised over the subject company. In light of the above, companies with global corporate structures, need to relook at the requirement of reporting the SBO in the companies.

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Notifications & Circulars

- Foreign Exchange Management (Overseas Investment) Directions, 2022 revised to clarify on investments in foreign funds
- International trade settlement in Indian Rupees (INR) – Opening of additional Current Account for settlement of import transactions as well
- Insolvency Professionals to act as Interim Resolution Professionals, Liquidators, Resolution Professionals and Bankruptcy Trustees (Recommendation) Guidelines, 2024 issued
- Lending to Micro, Small & Medium Enterprises (MSME) Sector – Master Direction revised
- Priority Sector Lending – Master Direction revised
- Foreign Portfolio Investors – SEBI updates disclosure requirements
- Foreign Portfolio Investors allowed flexibility in managing securities post registration expiry
- Offer for sale of shares to employees via stock exchange mechanism – SEBI modifies framework

Foreign Exchange Management (Overseas Investment) Directions, 2022 revised to clarify on investments in foreign funds

The RBI *vide* A.P. (DIR Series) Circular No. 9 dated 7 June 2024 has issued amendments to the Foreign Exchange Management (Overseas Investment) Directions, 2022 ('**Directions**') to address the varied regulatory frameworks governing investment funds globally and provide clarity to allay the confusion faced by the industry with respect to investments permitted in foreign funds.

The following amendments are introduced in the Foreign Exchange Management (Overseas Investment) Directions, 2022:

(a) Paragraph 1(ix)(e) of the Directions provides that the investment (including sponsor contribution) in units of any investment fund overseas which are duly regulated by the regulator for the financial sector in the host jurisdiction, shall be considered as OPI. The Circular has included the words '*units or any other instrument (by whatever name called)*' in this paragraph to remove the ambiguity with respect to investment in overseas funds which are not structured as investment funds issuing units. Accordingly, it is now permissible to invest overseas in those funds that have issued any other instrument other than units (and will include funds formed as corporate entities, limited partnerships, etc.).

(b) An explanation is added to Paragraph 1(ix)(e) which provides that "'*investment fund overseas, duly regulated' for the purpose of this para shall also include funds whose activities are regulated by financial sector regulator of host country or jurisdiction through a fund manager*". Through this addition, the RBI has clarified that investment in those overseas funds will be permitted where the fund manager is regulated (and the fund is not directly regulated) by the regulator of the host country or jurisdiction. This will open avenues for Indian investors to invest in jurisdictions where the fund manager is regulated but the fund itself is not regulated.

(c) Paragraph 24(1) of the Directions provides that the person resident in India making an overseas investment in the units of an investment fund or vehicle set up in an International Financial Services Centre (IFSC) shall be considered as OPI. The Circular has introduced the same amendment as in Paragraph

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1(ix)(e) of the Directions. Accordingly, all the benefits extended in the host jurisdiction as per Paragraph 1(ix)(e) shall also be available in an IFSC.

International trade settlement in Indian Rupees (INR) – Opening of additional Current Account for settlement of import transactions as well

The RBI *vide* A.P. (DIR Series) Circular No.10 dated 11 July 2022 provided for an additional arrangement for invoicing, payment, and settlement of exports/imports in INR through Special Rupee Vostro Accounts of the correspondent bank/s of the partner trading country maintained with AD Category-I banks in India. Subsequently *vide* FED Circular No. 8 dated 17 November 2023, AD Category-I banks were permitted to open an additional special current account for its exporter constituent exclusively for the settlement of their export transactions thereby enhancing operational flexibility for exporters and aiming to boost India's export sector growth. In this relation, now RBI *vide* FED Circular No. 18 dated 11 June 2024 has stated that on a review, and to provide operational flexibility, the facility of opening an additional special current account by the AD Category-I banks (maintaining Special Rupee Vostro Account in terms of the RBI circular dated 11 July 2022, referred above) for its constituents may also be extended for settlement of their import transactions as well along with the exports.

Insolvency Professionals to act as Interim Resolution Professionals, Liquidators, Resolution Professionals and Bankruptcy Trustees (Recommendation) Guidelines, 2024 issued

The Insolvency and Bankruptcy Board of India ('**Board**') is mandated to recommend Insolvency Professionals (IPs) for appointment as Interim Resolution Professionals (IRPs), Resolution Professionals (RPs), Liquidators, and Bankruptcy Trustees (BTs) under relevant sections of the Insolvency and Bankruptcy Code, 2016, upon referral from the National Company Law Tribunal (NCLT) and Debt Recovery Tribunal (DRT). The Board has now issued Insolvency Professionals to act as Interim Resolution Professionals, Liquidators, Resolution Professionals and Bankruptcy Trustees (Recommendation) Guidelines, 2024 ('**Guidelines**') to provide the procedure for preparing a panel of IPs to act as IRPs, RPs, Liquidators, and BTs.

These Guidelines aim to pre-empt administrative delays by proactively preparing and sharing a panel of IPs with the Adjudicating Authority. Effective from 1 July 2024, to 31 December 2024, the Guidelines specify eligibility criteria for IPs;

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the procedure for submission of Expression of Interest (in Form A) to act as IRPs, RPs, BTs, and Liquidators; preparation of panel of IPs and the criteria for inclusion in the panel based on experience and registration date of the IPs. IPs included in the panel are deemed as willing to act unless permitted otherwise by the AA, ensuring continuity and efficiency in insolvency proceedings. These Guidelines replace the earlier guidelines issued in December 2023 and are intended to streamline the appointment process while ensuring adherence to legal and regulatory standards. However, all actions taken under the repealed guidelines are saved.

Lending to Micro, Small & Medium Enterprises (MSME) Sector – Master Direction revised

The RBI has, *vide* Master Direction FIDD.MSME & NFS.12/06.02.31/2017-18 dated 11 June 2024, notified the updated Master Direction - Lending to Micro, Small & Medium Enterprises (MSME) Sector ('**Master Directions**') applicable to all Scheduled Commercial Banks (excluding RRBs).

RBI has issued three amendments to the Master Directions, which are as follows:

(a) Chapter IV deals with Common guidelines/Instructions for lending to the MSME sector – Paragraph 4.4 provides for Streamlining flow of credit to Micro and Small Enterprises (MSEs) for facilitating timely and adequate credit flow during their 'Life Cycle'. The Master Directions introduced that the banks shall review and tune their lending policies to the MSE sector to ensure that the credit decisions for loans up to INR 25 lakhs to MSEs should be made within 14 working days. Further, for loans exceeding INR 25 lakhs, the timelines must align with Board of Directors approved sanction norms. Additionally, banks are required to prominently display all relevant credit-related information, including decision timelines and document checklists for MSMEs, on a dedicated section of their websites.

(b) Paragraph 4.7 provides for a Structured Mechanism for monitoring the credit growth to the MSE sector. The Master Directions introduced a new set of mechanism to monitor the entire gamut of credit-related issues pertaining to the MSE sector which are: (i) implementation of a Credit Proposal Tracking System (CPTS) or equivalent for centralized registration and e-tracking of all MSME loan applications; (ii) serving indicative checklist of documents to MSEs to apply for loan; (iii) monitoring

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the loan application disposal process and displaying the same on the website of the banks; (iv) providing reasons for rejecting loan applications; and (v) implementation of a system-driven comprehensive performance management information system (MIS) at branches and supervisory levels. These measures aim to enhance transparency, efficiency, and accessibility of credit for MSMEs.

(c) Chapter V deals with Institutional Arrangements wherein Paragraph 5.5 deals with the Cluster Approach. It provides that 'Clusters', as identified by the Ministry of Micro, Small and Medium Enterprises, Government of India, or respective State/UT Governments, will be listed and updated semi-annually by SLBC/UTLBC Convenor banks on their portals. The Ministry's clusters list is accessible on its official website, while State/UT recognized clusters information is obtained directly from local authorities. The lead bank of each district must facilitate credit linkage within all clusters, assess MSE unit credit needs, raise awareness about formal credit, integrate units into skill development, and improve financial services in underserved areas. Banks must include cluster credit needs in branch/block-level plans, which are aggregated into District Credit Plans by lead banks and further into Annual Credit Plans by SLBC/UTLBC Convenor banks. Quarterly, SLBC/UTLBC Convenor banks are required to disclose credit extended to clusters in their State/UT on their portals in a specified format.

Priority Sector Lending – Master Direction revised

The RBI has, *vide* Circular FIDD.CO.PSD.BC.No.7/04.09.01/2024-25, dated 21 June 2024, issued a significant update to the Master Directions on Priority Sector Lending (PSL). These amendments introduce key changes affecting all Commercial Banks, including Regional Rural Banks, Small Finance Banks, Local Area Banks, and Primary (Urban) Co-operative Banks (excluding Salary Earners' Banks). The updates are part of the RBI's ongoing efforts to enhance credit flow to priority sectors and promote balanced economic development across India's districts.

The latest amendments focus on the following areas:

1. ***Adjustment of Weight Assignments in PSL Achievement (Paragraph 7):*** RBI has revised the weight assignments for incremental priority sector credit based on recent district-level credit reviews. Effective until FY 2026-27, districts with lower per

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capita Priority Sector Lending (PSL) (below ₹9,000) will receive higher weight (125%), while districts with higher per capita PSL (above ₹42,000) will receive lower weight (90%). These adjustments aim to incentivize banks to increase credit deployment in underserved regions, fostering equitable economic growth.

2. ***Definition of MSMEs (Paragraph 9):*** The definition of Micro, Small, and Medium Enterprises (MSMEs) shall be applicable as referenced to the Master Direction on Lending to MSME Sector, for clarity and ensuring consistency across RBI guidelines regarding MSME classification and treatment.

3. ***Monitoring of Priority Sector Lending Targets (Paragraph 27):*** Urban Co-operative Banks (UCBs) are now required to report PSL data using the format specified in Sl. No. 61 of Annex III of the Master Direction on Filing of Supervisory Returns (MD on FSR), replacing previous reporting requirements. This change integrates reporting processes within the broader supervisory framework, enhancing efficiency.

These updates reflect the RBI's proactive approach to refining PSL guidelines, aiming to optimize credit distribution to priority sectors and support comprehensive economic development across India.

Foreign Portfolio Investors – SEBI updates disclosure requirements

The SEBI has, *vide* Circular No. SEBI/HO/AFD/AFD-POD-2/P/CIR/2024/76 dated 5 June 2024, updated its guidelines for Foreign Portfolio Investors (FPIs), relaxing timelines for the disclosure of material changes and other obligations. The Circular aims to streamline the disclosure process, ensuring timely and accurate reporting while reducing administrative burdens on FPIs and protecting the interests of investors in the securities market. This update follows the recent amendments to the SEBI (Foreign Portfolio Investors) Regulations, 2019, notified on 3 June 2024.

The key amendments include:

(a) ***Type I Material Changes:*** These significantly affect the FPI's eligibility or operational status and must be reported within 7 working days, with supporting documents submitted within 30 days. These include changes such as jurisdiction, name changes due to mergers or acquisitions, cessation of existence,

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restructuring, regulatory status changes, and breaches of eligibility criteria.

(b) ***Type II Material Changes:*** These are less critical and must be reported within 30 days. This category includes all other material changes that are not classified as Type I. For instance, the deletion of sub-fund or share classes investing in India is now categorized as a Type II change.

Designated Depository Participants (DDPs) reassess the FPI's eligibility based on reported changes, requiring fresh registration for Type I changes. In case of delays in reporting material changes, DDPs are required to inform SEBI within two working days, providing reasons for the delay.

Foreign Portfolio Investors allowed flexibility in managing securities post registration expiry

SEBI has, *vide* Circular No. SEBI/HO/AFD/AFD-PoD-2/P/CIR/2024/77 dated 5 June 2024, issued new regulations to provide Foreign Portfolio Investors (FPIs) with greater flexibility in dealing with the securities post-expiry of their registration. This update comes as part of the SEBI (Foreign Portfolio Investors) (Amendment) Regulations, 2024, which modifies the FPI Master Circular to address the evolving needs of the securities market.

Under the revised guidelines, FPIs must now submit the required fees and any additional information at least 15 days before the current registration expires. If FPIs fail to renew their registration on time, they can re-activate it within 30 days by paying a late fee, provided they comply with all KYC and AML/CFT requirements. During this period, FPIs are allowed to dispose of their existing securities but cannot make fresh purchases. In case of failure to reactivate within this window, SEBI allows a 180-day window for the disposal of its securities. If FPIs do not sell their securities within this period, an additional 180 days is granted, *albeit* with a financial disincentive of 5% of the sale proceeds, which will be transferred to SEBI's Investor Protection and Education Fund ('**IPEF**').

Moreover, SEBI has outlined provisions for dealing with securities held by FPIs under specific regulatory constraints, such as those imposed by courts or enforcement agencies. The new framework also includes mechanisms for handling securities written off by FPIs, mandating their transfer to an escrow account managed by exchange-impanelled brokers for sale, with proceeds going to the IPEF.

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Offer for sale of shares to employees via stock exchange mechanism – SEBI modifies framework

The SEBI has issued Circular No. SEBI/HO/MRD/MRD-PoD-3/P/CIR/2024/82 dated 14 June 2024, amending the framework for the Offer for Sale (OFS) of shares to employees through the stock exchange mechanism.

Previously, employees participating in OFS were required to place bids on T+1 day, based on feedback from stakeholders and recommendations from the Secondary Market Advisory Committee (SMAC). Now, the revised procedure mandates employees to place their bids on T+1 day at the cut-off price of T Day. The allotment price will still be based on the T-day cut-off, with any applicable discounts. All other provisions of the original circular remain unchanged, and these modifications will be effective from the 30th day of issuance of the Circular. Market Infrastructure Institutions (MIIs) are instructed to implement the necessary systems and amendments to their bylaws, rules, and regulations to facilitate this update.

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Ratio Decidendi

- MSME Promoters are exempt from net worth criteria for submitting a Resolution Plan under IBC if they provide security deposit and earnest money deposit – NCLT Kolkata
- Application under Section 9 of IBC by Operational Creditor must be supported by strict proof of debt and default – NCLT, Mumbai
- Acceptance of partial payments by Financial Creditor does not invalidate default or legitimacy of insolvency proceedings – NCLAT
- Arbitration award passed in disregard of evidence on record makes it liable to be set aside as being irrational and patently illegal – Delhi High Court
- Corporate Debtor can pursue remedies under IBC even if it had initiated Arbitration proceedings – Delhi High Court

MSME Promoters are exempt from net worth criteria for submitting a Resolution Plan under IBC if they provide security deposit and earnest money deposit

On 8 April 2022 Wearit Global Ltd. (‘**Corporate Debtor/Company**’), a Micro, Small and Medium Enterprise (‘**MSME**’) was admitted into Corporate Insolvency Resolution Process (‘**CIRP**’). The Resolution Professional (‘**RP**’) invited the Expression of Interest (‘**EoI**’) for submission of Resolution Plans. However, the Company’s suspended director, Mr. Manish Kumar, (‘**Applicant**’) appealed to the RP for a waiver of the INR 15 Crore minimum net worth condition for submitting the resolution plan.

During a meeting of the Committee of Creditors (‘**CoC**’), the request for exemption based on the MSME status of the Applicant was rejected, since he failed to pay the Earnest Money Deposit (‘**EMD**’). As a result, the Applicant was removed from the provisional list of potential Resolution Applicants. The Applicant filed an application before the National Company Law Tribunal, Kolkata (‘**NCLT**’) seeking the setting aside of the minimum tangible net worth criteria of INR 15 crores for being the Applicant of the Corporate Debtor.

The NCLT allowed the application and held that MSME promoters may be exempted from the net worth criteria for submitting Resolution Plans, however, they are required to submit both a Security Deposit as well as EMD. The Tribunal observed that IBC is designed to expedite the reorganization and resolution of insolvency for corporate entities, partnerships, and individuals. Its goals are to optimize asset values, foster entrepreneurship, secure credit availability, and equitably consider the interests of all parties involved.

The NCLT noted that the existing exemptions for MSMEs, particularly under Section 240A of the IBC, make it necessary for resolution applicants to provide an EMD and a Security Deposit, which is refundable if the resolution plan is not accepted. The Tribunal further held that an MSME promoter, who is in default and whose company is undergoing CIRP as a result, may be relieved from meeting the net worth requirement for submitting their resolution plan. However, this relief does not apply to the obligations of submitting the Security Deposit with their EoI and the EMD with their Resolution Plan.

Thereby, the Hon’ble NCLT instructed the RP to accept the Applicant’s EoI and Resolution Plan, waiving the net worth requirement, if Security Deposit and EMD is provided by the Applicant.

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[*Manish Kumar, suspended Director of Wearit Global Ltd.* v. *Rachna Jhunjunwala, RP and Anr.* – Judgement dated 5 June 2024 in I.A. (IB) No. 53/KB/2024 in Company Petition (IB) No. 100/KB/2019, NCLT, Kolkata]

Application under Section 9 of IBC by Operational Creditor must be supported by strict proof of debt and default

The Mumbai Bench of the National Company Law Tribunal ('**NCLT**') has rejected an application filed by Mittal Polymers ('**Applicant / Operational Creditor**') under Section 9 of the IBC for lack of substantial evidence to prove the debt and default against Suvarna Additives Limited ('**Corporate Debtor**').

The NCLT held that substantial evidence is a stringent requirement for initiation of the Corporate Insolvency Resolution Process ('**CIRP**') to prevent unwarranted insolvency proceedings which can have severe implications on the corporate entity involved.

The Applicant is a manufacturer and supplier of chemicals and chemical products. The Applicant raised several invoices between 2015 to 2019 amounting to INR 2,33,10,961/-, for the supply of raw materials payable by the Corporate Debtor. A demand notice dated 15 November 2019 was sent to the Corporate Debtor, but no reply was received, and the payment remained unsettled. Consequently, the Applicant initiated Insolvency Proceeding against the Corporate Debtor, claiming an outstanding amount of INR 1,12,17,578/-.

The Applicant also sought interest on the unpaid invoices under Sections 15 and 16 of the Micro Small Medium Enterprises Development Act, 2006 ('**MSMED Act**'). The Applicant submitted a bank statement to substantiate that no payments were received from 3 December 2019 to 19 December 2019. However, no Ledger or Annual Financial Statement was produced to corroborate the alleged debt or default. The only documents provided to substantiate Applicant's claim were the claim computation table and the Demand Notice issued to the Corporate Debtor. The NCLT highlighted that the crucial documents, such as invoices, and annual statements that are required to support the claims were not provided by the Applicant and there was no evidence indicating that the Corporate Debtor had accepted the alleged debt.

The NCLT relied on the case of *SFO Technologies Pvt. Ltd.* v. *Vanu India Pvt. Ltd.* [IA No. 1106/2022 in Company Appeal (AT) (CH) (Ins.) No. 436/2022], wherein it was held that an application under Section 9 of IBC is not maintainable without strict proof of debt and default. The Hon'ble NCLT further observed that the

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Operational Creditor failed to prove the existence of any operational debt due and payable by the Corporate Debtor, and thereby rejected the application filed by the Operational Creditor.

[*Mittal Polymers* v. *Suvarna Additives Private Limited* – Order dated 12 June 2024 in CP (IB) No. 95/MB/2022, NCLT, Mumbai]

Acceptance of partial payments by Financial Creditor does not invalidate default or legitimacy of insolvency proceedings

The Appellant, a former director of the Corporate Debtor, a company specializing in developing Special Economic Zones ('**SEZs**'), approached the Financial Creditor in 2017, seeking funds for development purposes. It secured loans to the tune of INR 60 crores through an offer letter and subsequent loan agreement, followed by an additional loan of INR 6 crores in 2019.

Owing to several challenges, including a lack of buyers for SEZ units, and economic slowdown that severely affected cash flow and fund availability, the Corporate Debtor failed to meet its repayment obligations, which caused the Financial Creditor to issue a demand notice. Subsequently, the Financial Creditor filed a petition under Section 7 of the Insolvency and Bankruptcy Code, 2016 to initiate Corporate Insolvency Resolution Proceedings ('**CIRP**') against the Corporate Debtor.

While the Company Petition was pending, the parties entered into a One-Time Settlement ('**OTS**') agreement twice. However, the Corporate Debtor failed to honour the terms of the OTS.

The Corporate Debtor then filed an application to record the OTS Agreement and to dismiss the company petition, but the Financial Creditor opposed the same. In the meanwhile, the Company Petition was admitted against the Corporate Debtor by the National Company Law Tribunal, Mumbai Bench ('**NCLT**'). Aggrieved by the same, the Corporate Debtor filed an appeal under Section 61 of the IBC, before the National Company Law Appellate Tribunal ('**NCLAT**').

The NCLAT upheld the NCLT Order and upheld the Demand Notice and subsequent Company Petition as valid documents for initiating CIRP. The loan agreements substantiated the Financial Creditor's claim of INR 58.3 crores. The NCLAT further noted while the OTS agreement shows the Corporate Debtor's intent to settle the dues, the failure to adhere to its terms, cannot nullify the Financial Creditor's right to pursue insolvency proceedings. The NCLAT further held that debt and default were corroborated by various documents, including

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CIBIL reports, statements of loan accounts, and the Corporate Debtor's balance sheet for the fiscal year 2017-2018.

The NCLAT finally opined held the Financial Creditor had acted within its rights by accepting the initial OTS payment and subsequently pursuing CIRP after the Corporate Debtor defaulted on adhering to the terms of the OTS.

[*Jayesh Dani* v. *SREI Equipment Finance Ltd. and Anr.* – Judgement dated 31 May 2024 in Company Appeal (AT) (Insolvency) No. 161 of 2024, NCLAT]

Arbitration award passed in disregard of evidence on record makes it liable to be set aside as being irrational and patently illegal

The Delhi High Court has observed that where an arbitrator has passed an arbitral award without considering the evidence on record, the award is liable to be set aside as being perverse and patently illegal.

Disputes arose from a Memorandum of Understanding ('**MoU**') dated 20 February 2006, where the Petitioner was to build a Mall named 'R-3 Mall' in Ahmedabad, Gujarat, and provide the Respondent with leased space for the mall. The Respondent alleged that the Petitioner breached the MoU by signing a contract with a third party on 9 March 2006, effectively terminating the agreement. The Respondent claimed that the termination was invalid and illegal, prompting them to seek arbitration. Subsequently, an arbitration proceeding was initiated, and the arbitral tribunal granted an award directing the Petitioner to pay the Respondent INR 24,54,458.33 /- with 12% annual interest, wherein INR 20 lakhs was for loss of profit. The Petitioner challenged the Award before the Delhi High Court.

The High Court observed that the Arbitrator's reasoning for awarding INR 20 lakhs for the loss of profit was sparse and unclear. The Court further noted that the Arbitrator himself concluded that it was speculative whether the Respondent would have made any profit, yet the Arbitrator proceeded to grant INR 20 lakhs as a 'reasonable loss of profit' only with a rationale that the Petitioner breached the contract. Thereby, the High Court opined that the Award lacked clear reasoning regarding the evidence presented.

Considering the aforesaid observations the Hon'ble High Court allowed the petition, stating that the award of INR 20 lakhs to the Respondent for loss of profit lacked evidentiary support. Further, it was held that the Arbitrator's failure to ascertain whether the Respondent had actually incurred or would have

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incurred any loss of profit further underscored the inadequacy of the award.

[*Divyam Real Estate Pvt. Ltd.* v. *M2k Entertainment Pvt Ltd.* – Judgement dated 22 May 2024 in O.M.P. (COMM) 162/2020 & I.A. 14331/2012, I.A. 10655/2022, Delhi High Court]

Corporate Debtor can pursue remedies under IBC even if it had initiated Arbitration proceedings

The Delhi High Court while hearing a petition under Section 11(6) of the Arbitration & Conciliation Act, 1996 ('**Arbitration Act**'), seeking the appointment of an Arbitrator, has observed that mere commencement of arbitration proceedings does not bar the Corporate Debtor from pursuing his other remedies including those available under IBC.

The Petitioner No.1 was engaged in the business of manufacturing edible oils and its by-products, was effectively owned and controlled by Petitioner No. 2 and the Respondents were the founders/promoters of Petitioner No. 1.

The Respondents approached OFB Tech Pvt. Ltd. and Petitioner No. 2 with the intent of selling 100% of the Respondents' shares in Petitioner No. 1 to Petitioner No. 2. After discussing, the Respondents executed a Term Sheet, wherein the Respondents projected the average Earning Before Taxes ('**EBITDA**') to be around INR 17.92 crore for FY 2021-22, whereas the actual EBITDA as per the books of accounts was around INR 4.5 crores. Based on these representations, two separate agreements i.e., share purchase agreement & credit facility agreements were executed.

The Petitioner No. 2 upon discovering that the figures were misleading initiated arbitration proceedings against the Respondents. When no Arbitrator was appointed, Petitioner No. 2 filed a petition under Section 11(6) for the Court to appoint an arbitrator.

The Respondents opposed the petition on the ground that there were two independent Agreements i.e. Share Purchase Agreement and Credit Facility Agreement and different parties were signatories to the two Agreements. They claimed that this misjoinder of causes of action makes the petition invalid and further submitted that there is no actual dispute between the parties. Rather, the amounts due from the Petitioners were admitted, consequent to which a petition under Section 7 IBC was filed by the Respondent before the National Company Law Tribunal, Jaipur.

Regarding the Respondent's objection that two separate agreements have been combined into one, the Court stated that the appointed arbitrator is free to conduct separate arbitrations

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for each agreement if it is determined that the agreements cannot be combined into a single arbitration.

The Court also acknowledged that disputes had arisen and that the legal notice issued by the Petitioner No. 2 predated the petition filed under Section 7 of the IBC by the Respondent. As a result, the Respondent's claim that the petition was not maintainable was deemed invalid. The Court ruled that simply initiating arbitration proceedings would not prevent a Corporate Debtor from pursuing other remedies under law. Therefore, the Court allowed the petition and appointed an arbitrator to resolve disputes between the parties, with the condition that the arbitrator complies with disclosure requirements under Section 12(1) of the Arbitration Act.

[*Pitambar Solvex Pvt. Ltd. and Anr.* v. *Manju Sharma and Ors.* – Judgement dated 22 May 2024, 2024: DHC:4450]

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News Nuggets

- Start-ups – DPIIT to focus on early-stage funding, other relaxations, in 100-day action plan
- MSME – Micro, Small and Medium Enterprises Development Act, 2006 set to be revamped
- Donations through Social Security Exchanges recommended to be included for CSR
- Food Business Operators not to claim '100% fruit juice' on their labels: FSSAI
- Entities listed on Social Security Exchanges to submit impact reports for FY 2024
- ESG disclosure norms for listed entities may be eased

Start-ups – DPIIT to focus on early-stage funding, other relaxations, in 100-day action plan

As per a report, the Department for Promotion of Industry and Internal Trade ('**DPIIT**') is looking to focus on the aspects of easing early-stage funding for start-ups, reducing the compliance burden on businesses and overall logistics costs in its 100-day action plan. Further, the DPIIT is also considering reforms to simplify the ease of doing business and introduce a public private partnership governance model for start-ups.

[*Source:* Economic Times, published on 17 June 2024]

MSME – Micro, Small and Medium Enterprises Development Act, 2006 set to be revamped

The Government of India is undertaking a comprehensive review of the Micro, Small and Medium Enterprises Development Act, 2006 ('**MSMED Act**'). The review of the MSMED Act is likely to include reworking the definitions and criteria of MSMEs, measures for development and promotion for the businesses of such enterprises as well as provisions around delayed payments ensuring faster relief in case of delayed payments.

[Source: Business Today, published on 18 June 2024]

Donations through Social Security Exchanges recommended to be included for CSR

The Securities and Exchange Board of India has proposed to the Central Government to consider allowing donations made through Social Security Exchanges (**SSEs**) as valid Corporate Social Responsibility (**CSR**) and accordingly make the amendments to the Companies Act, 2013 (**Act**) and the rules thereunder. Currently, while the CSR activities listed under the Act are the same activities that are undertaken by the entities listed on the SSEs, contributing to organizations through these SSEs, is still not considered as CSR. The proposal made by SEBI will allow companies to utilize the funds allocated for CSR to support organizations through SSE.

[Source: The CSR Journal, published on 17 June 2024]

Food Business Operators not to claim '100% fruit juice' on their labels: FSSAI

The Food Safety and Standards Authority of India ('**FSSAI**') has issued a directive mandating all Food Business Operators ('**FBOs**') to remove any claim of '100% fruit juice' from the labels and advertisements of reconstituted fruit juices with an immediate effect. Further, all FBOs having pre-printed packaging materials stating such claims must exhaust such

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packages before 1 September 2024. The FSSAI reasoned in its directive that since there is no provision for making any 100% claim under the Food Safety and Standards (Advertising and Claims) Regulations, 2018, any such claim would be misleading more so when the main ingredient in the fruit juice is water and only limited fruit concentrates or pulp.

[Source: Press Information Bureau, published on 3 June 2024]

Entities listed on Social Security Exchanges to submit impact reports for FY 2024

Extending the previously issued deadline of filing within 90 days from the end of Financial Year 2024 (**FY 2024**), SEBI has now mandated the entities registered on or those that have raised funds through SSEs to submit to the exchange, an annual impact report by 31 October 2024. Notably, the Report will contain qualitative and quantitative details of past social impacts by the entity, covering aspects such as strategic intent, planning, approach, and an impact scorecard amongst other things.

[*Source:* Financial Express, published on 28 May 2024]

ESG disclosure norms for listed entities may be eased

SEBI is seeking to ease the Environmental, Social and Governance ('**ESG**') related disclosures required to be made by listed companies and their value chain partners. In its consultation paper, SEBI has proposed to mandate disclosures on ESG metrics only for those value chain partners who individually comprise 2 percent or more of an entity's purchase or sales by value. Further, the consultation paper also proposes to make the disclosures by value chain partners, voluntary for the first year instead of the current comply or explain basis.

[*Source:* Financial Express, published on 24 May 2024]

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