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Articles

Trading in Virtual Currencies: An analysis under foreign exchange laws of India

By **Sudish Sharma and Anantha Desikan**

The cryptocurrencies or virtual currencies ("VC")[1] can be defined as a type of digital currency in which encryption techniques are used to regulate the generation of units of currency and verify the transfer of funds, operating independently of a central bank. There are many forms of VC such as bitcoins, ethereum, ripple, NEM and litecoin. The VC are based on blockchain technology. Blockchain may be described as a tamper-evident ledger shared within a network of entities, where the ledger holds a record of transactions between the entities. To achieve tamper-evidence in the ledger, blockchain exploits cryptographic hash functions.[2]

The VC are traded through online exchanges or platforms and the value of VC depends upon the demand and supply of VC traded in such online exchanges or platforms. Such online platforms facilitate exchange of VC for another currency including a fiat currency such as USD.

In order to determine the applicability of foreign exchange laws of India for trading in VC, it is important to understand the classification of VC.

Classification of VC as 'currency' under Foreign Exchange Management Act:

The FEMA[3] provides an inclusive definition of the term 'currency' to include all currency notes, postal notes, postal orders, money orders, cheques, drafts, travellers cheques, letter of credit, bills of exchange and promissory notes, credit cards or such other similar instruments, as may be notified by the Reserve Bank of India. Further, the term 'currency notes' means and includes cash in the form of coins and bank notes[4]. It be noted that RBI has not notified VC as 'currency'.

The term 'coin' is defined under the Coinage Act, 2011 ("Coinage Act") to mean any coin which is made of any metal or any other material stamped by the Central Government or any other authority empowered by the Central Government in this behalf and which is a legal tender including commemorative coin and Government of India one rupee note. Since the VC are not issued by the Central Government or any other authority empowered by the Central Government, VC are not coins under the Coinage Act. Section 22 of the Reserve Bank of India Act, 1934 ("RBI Act") states that the RBI shall have the exclusive rights to issue bank notes in India. Since the bitcoins are not issued by the RBI in India, bitcoins are not 'bank notes'.

Therefore, VC do not fall under the purview of the term 'currency' under the FEMA and the RBI Act as it is not (i) covered under any types of currencies enumerated under Section 2(h) of the FEMA and (ii) notified by the RBI as currency.

Classification of VC as 'foreign exchange' under FEMA:

The FEMA defines a foreign exchange as a

[1] Oxford Dictionary of English, 3rd Edition.
[2] White Paper on Blockchain Technology released on January 05, 2017 by the Institute for Development and Research in Banking Technology (an Institute established by the RBI).
[3] Section 2(h) of the FEMA.
[4] Section 2(i) of the FEMA.

foreign currency[5]. A foreign currency is defined as a currency other than an Indian currency[6]. The VC are not currencies under the FEMA, therefore, the VC are not foreign currencies and thereby, not a 'foreign exchange' under the FEMA.

Classification of VC as 'foreign security' under the FEMA:

The FEMA defines the term 'foreign security' as any security, in the form of shares, stocks, bonds, debentures or any other instrument denominated or expressed in foreign currency and includes securities expressed in foreign currency, but where redemption or any form of return such as interest or dividends is payable in Indian currency[7].

Section 2(za) of the FEMA defines the term 'security' as shares, stocks, bonds and debentures, Government securities as defined in the Public Debt Act, 1944, savings certificates to which the Government Savings Certificates Act, 1959 applies, deposit receipts in respect of deposits of securities and units of the Unit Trust of India established under Section 3(3) of the Unit Trust of India Act, 1963 or of any mutual fund and includes certificates of title to securities, but does not include bills of exchange or promissory notes other than Government promissory notes or any other instruments which may be notified by the RBI as security.

VC do not fall under any of the aforesaid items and therefore, it is not covered under the term 'securities' and thereby are not covered under 'foreign security'.

Classification of VC as "prepaid payment instruments" under the Payment and Settlement Systems Act, 2007:

Section 2(1) (i) of the Payment Systems Act defines the term 'payment system' as a system that enables payment to be effected between a payer and a beneficiary, involving clearing, payment or settlement service or all of them, but does not include a stock exchange and includes the systems enabling credit card operations, debit card operations, smart card operations, money transfer operations or similar operations.

Section 18 empowers the RBI to regulate issuance of payment system instruments and accordingly, the RBI has issued 'Master Direction on Issuance and Operation of Prepaid Payment Instruments' dated October 11, 2017. It defines the term 'prepaid payment instruments' as payment instruments that facilitate purchase of goods and services, including funds transfer, against the value stored on such instruments.

The value of the VC depends upon the value as provided under the VC exchanges and such values are dynamic depending upon the demand and supply in the VC market. However, in case of a prepaid payment instrument, the value stored on such instruments are constant and is equal to the amount of money paid to the payment system providers. Therefore, VC cannot be termed as a 'prepaid payment instrument' under the Payment Systems Act.

Classification of VC as 'property':

In terms of Section 29(c) of Benami Transactions (Prohibitions) Act, 1988, property means property of any kind, whether movable or immovable, tangible or intangible, and includes any right or interest in such property. This is an inclusive definition of property, where both movable and immovable properties are included. VC is movable and intangible and accordingly, it can be called a property as per the aforesaid definition.

In this regard reliance can be made on a case[8] where the Supreme Court held that the term 'property' includes everything that has an

[5] Section 2(n) of the FEMA.
[6] Section 2(m) of the FEMA.
[7] Section 2(o) of the FEMA.

[8] *Vikas Sales Corporation and Anr.* v. *Commissioner of Commercial Taxes & Anr.* [MANU/SC/0519/1996].

extendable value. It includes the item in question and all rights and liabilities associated with it. An element which is material to the expression is 'ownership'. While the property has all interests in it, it is the ownership that lets the owner exercise such interest, where the interest extends to doing everything, an owner is capable of doing to exercise his right in the property.

Further, it be noted that VC are in non-physical form i.e. intangible. Therefore, VC can be classified as rights in intangible movable property.

Jurisprudence in Australia:

The Australian Government published a public ruling[9] on determination of tax in case of a bitcoin, which is a VC ("Public Ruling"). In terms of the Public Ruling, it was held that *Bitcoin holding rights involve an inherent excludability because the Bitcoin software restricts control of a Bitcoin holding to the person in possession of the relevant private key. As the Bitcoin software prescribes how the transfer and trade of bitcoin can occur and transactions are verified through the Bitcoin mining process, Bitcoin holding rights are definable, identifiable by third parties, capable of assumption by third parties, and sufficiently stable as per the Ainsworth test. In weighing all these factors, it is considered that Bitcoin holding rights amount to property within the meaning of paragraph 108-5(1)(a).*

In terms of the Public Ruling, property refers not only to a thing but also to legal relationship with a thing. Accordingly, in Australia, the bitcoin, is a form of VC, is classified as property.

Classification of VC as 'goods' under the Sale of Goods Act, 1930:

Section 2(7) of the Sale of Goods Act defines the term 'goods' to mean every kind of movable property other than actionable claims and money; and includes stock and shares, growing crops, grass, and things attached to or forming part of the land which are agreed to be severed before sale or under the contract of sale. Section 3(36) of the General Clauses Act, 1897 ("Clauses Act") defines the term 'movable property' to mean property of every description, except immovable property. Further, Section 3(26) of the Clause Act defines the term 'immovable property' to include land, benefits to arise out of land, and things attached to the earth, or permanently fastened to anything attached to the earth.

VC are not covered under the definition of term 'immovable property' under the Clauses Act. Therefore, VC are rights in movable property and thereby are intangible 'goods' under Section 2(7) of the Sale of Goods Act.

Implications under foreign exchange laws for trading in VC from a person resident outside India:

VC are classified as rights in intangible movable property. Therefore, if a person resident in India[10] enters into transactions i.e. purchase and sale of bitcoins, with a person resident outside India, such transactions will be considered as import and export transactions, respectively and the provisions of FEMA will be attracted. Under FEMA, all the transactions with a person resident outside India are categorised as capital account transactions and current account transactions.

Classification of transaction in VC as capital account transactions:

Section 2(e) of the FEMA defines capital account transactions as a transaction which alters the assets or liabilities, including contingent liabilities, outside India of persons resident in

[9] Taxation Determination TD 2014/26 issued by the Australian Taxation Office, Australian Government.

[10] Section 2(v) of the FEMA defines 'a person resident in India' as (i) a person residing in India for more than 182 (one hundred and eighty-two) days during the course of the preceding financial year, (ii) any person or body corporate registered or incorporated in India, (iii) an office, branch or agency in India owned or controlled by a person resident outside India and (iv) an office, branch or agency outside India owned or controlled by a person resident in India.

India or assets or liabilities in India of persons resident outside India, and includes transactions referred to in Section 6(3) of the FEMA.

In case of purchase of VC by the buyer from a person resident outside India, the VC gets transferred into the wallet of the buyer and the buyer will have exclusive rights over such VC. In such a case, the situs i.e. the location of assets (i.e. VC) for legal purposes, will be India. Therefore, the purchase of VC does not alter the assets or liabilities outside India of the buyer and accordingly, purchase of VC by the buyer who is a person resident in India do not fall under the category of capital account transactions.

In case of sale of VC by the seller to a person resident outside India, the VC gets transferred to such person resident outside India and the seller will not have any rights over such VC. In such a case, the assets (i.e. VC) will no longer be assets of the seller. Therefore, sale of VC to a person resident outside India does not alter the assets or liabilities outside India of the seller and accordingly, sale of VC by the seller who is a person resident in India to a person resident outside India, do not fall under the category of capital account transactions.

Classification of transactions in VC as 'current account transaction' under the FEMA:

Section 2(j) of the FEMA defines current account transactions as a transaction other than a capital account transaction and includes (a) payments due in connection with foreign trade, other current business, services, and short-term banking and credit facilities in the ordinary course of business, (b) payments due as interest on loans and as net income from investments, (c) remittances for living expenses of parents, spouse and children residing abroad and (d) expenses in connection with foreign travel, education and medical care of parents, spouse and children. It be noted that bitcoins are classified as rights attached to intangible movable property which are used for the purpose of foreign trade. The aforesaid foreign trade may be in the following manner:

(a) Purchase of VC from person resident outside India through foreign exchanges on payment in fiat currencies such as USD to person resident outside India ("**Category 1**"); or
(b) Payments by VC to person resident outside India for purchasing goods or procuring services from person resident outside India ("**Category 2**"); or
(c) Payment by VC to person resident outside India in consideration of acquiring other cryptocurrencies from person resident outside India ("**Category 3**").

Therefore, any payment made or received in connection with purchase or sale transactions of bitcoins by an Indian resident with a person resident outside India under Category 1, Category 2 or Category 3, will be considered as payment made or received in lieu of foreign trade and thereby, come under the purview of 'current account transaction' under the FEMA.

VC are not legal tender in India:

The VC are not considered to be legal tender in India and accordingly, it will not be treated as recognized mechanism for making any payment and receiving any payment, in India. In this regard, reference can be made to the following:

(a) Caution notices issued by the Reserve Bank of India stating the potential financial, operational, legal, customer protection and security related risks associated with dealing with cryptocurrencies;
(b) Press Release issued by the Ministry of Finance stating that dealing in cryptocurrencies may be considered as ponzi schemes. In case the Government or Reserve Bank of India, going forward declares cryptocurrencies including

bitcoins as ponzi schemes, then dealing with cryptocurrencies shall be completely banned and consequently, the person dealing with cryptocurrencies shall be punishable in terms of the Prize Chits and Money Circulation Schemes (Banning) Act, 1978;

(c) In the forty-sixth report of standing committee on finance (2016-2017) on March 17, 2017, on being asked about the legality of bitcoin, a representative of 'Ministry of Finance' submitted while deposing that bitcoin is illegal; **and**

(d) The statement of Hon'ble Finance Minister of India in budget speech for the year 2018, wherein he has stated that the Government of India does not consider cryptocurrencies as legal tender or coin and will take all measures to eliminate use of these crypto assets in financing illegitimate activities or as part of the payment system.

Further, the implications under the FEMA for trading in VC can be analysed herein below:

Implications for purchase of VC from person resident outside India:

Import or export of goods and services is being allowed into India in terms of Section 5 of the FEMA read with FEMA (Current Account Transaction) Rules, 2000 ("**Current Account Transaction Rules**"). With respect to import of goods and services, RBI has issued Master Direction on Import[11]. Further, the Foreign Exchange Management (Manner of Receipt and Payment) Regulations, 2016 ("**Payment Regulations**") prescribes the mode of payment for import transactions. The acceptable mode of payment of imports are (a) payment made in a currency appropriate to the country of shipment of goods; or (b) payment made in foreign exchange through an international card held by him / in rupees from international credit card / debit card through the credit / debit card servicing bank in India against the charge slip signed by the importer or as prescribed by RBI from time to time, provided that the transaction is in conformity with the extant provisions including the Foreign Trade Policy.

The VC are not covered under the term 'foreign exchange'. Therefore, it can be inferred that in case of any imports made by person resident in India under Category 1, the payment cannot be made in VC under the Payment Regulations. For making payment in any other mode other than those prescribed in the Payment Regulations, prior approval of the RBI is required and it is unlikely that RBI will grant such prior approval since VC have not yet been recognised under the Indian laws and are not considered to be legal tender in India.

Further, the Master Direction on LRS[12] was issued by RBI as a liberalization measure to facilitate resident individuals to remit funds abroad for permitted current or capital account transactions or combination of both. The remittance by individual under Category 1 is not a permitted current account transaction under the Master Direction on LRS and prior approval of the RBI is required for remittances not permitted under the Master Direction on LRS. It is unlikely that RBI will grant such prior approval since VC are not considered to be legal tender in India. Additionally, form A2 is required to be submitted to the authorised dealer bank for any remittance under the Master Direction on LRS. However, form A2 does not cover remittances for the purpose for acquisition of VC.

Implications for sale of VC to person resident outside India through Indian or foreign exchanges:

Sale of VC to a person resident outside India

[11] RBI Master Direction No. 17/2016-17 on import of goods and services dated January 01, 2016

[12] Master Direction No. 7/2015-16 on liberalised remittance facilities dated January 01, 2016

under Category 2 or Category 3 will constitute as export of rights in intangible movable property and accordingly, the provisions under the foreign exchange and RBI regulations will be applicable for such transactions.

Regulation 2(2) of the Payment Regulations provides that for export transactions, receipt shall be made in (i) currency appropriate to the place of final destination as mentioned in the declaration form irrespective of the country of the residence of the buyer or (ii) any other mode of receipt of export proceeds as prescribed by the RBI from time to time. The VC are not recognised as legal tender in India by the RBI and the RBI has not recognised VC as a mode of receipt of export proceeds. Therefore, in case of sale of VC under Category 2 or Category 3, the Indian resident seller cannot receive VC as export proceeds.

Conclusion:

In a nutshell, VC are not considered to be legal tender in India. In recent times, the Enforcement Directorate have also raided many VC exchanges operating in India for violations of foreign exchange laws. Therefore, a person resident in India entering into transaction with person resident outside India for trading in VC shall be doing so in violation of the foreign exchange laws of India. While in many jurisdictions, the VC are recognized as legal tender and proper regulations are in place, in India, the regulators are yet to formulate a law or to provide classification to regulate VC transactions both in the domestic as well as international market.

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Cross-border Mergers – Analysis of FEMA provisions

By **Mallika Shekhar and Neeraj Dubey**

Introduction

On 13th April 2017, the Ministry of Corporate Affairs (MCA) notified Section 234 of the Companies Act, 2013 and inserted a new Rule 25A (merger or amalgamation of a Foreign Company with Indian company and vice-versa) in the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 (Compromises Rules), paving way for merger and amalgamation of a Foreign Company with an Indian company and vice-versa. Since Rule 25A required prior approval of the Reserve Bank of India (RBI) for cross-border merger, without corresponding procedural aspects in place, cross-border merger could not take-off. Now, with the RBI notifying the Foreign Exchange Management (Cross Border Merger) Regulations, 2018 (FEMA Regulations/Regulations) for mergers amalgamation and arrangement between Indian and foreign companies on 20th March 2018, this gap has been bridged.

Crucial definitions

The FEMA Regulations cover both inbound and outbound investments. The term “Inbound Merger” means a Cross Border Merger where the Resultant Company is an Indian company whereas “Outbound Merger” means a Cross Border Merger where the Resultant Company is a Foreign Company. The “Resultant Company” means an Indian company or a Foreign Company which takes over the assets and liabilities of the companies involved in the cross-border merger. FEMA Regulations define “Cross Border Merger” as any merger, amalgamation or arrangement

between an Indian company and a Foreign Company in accordance with the Compromises Rules. The term "Foreign Company" has been defined as any company or body corporate incorporated outside India in a jurisdiction specified in Annexure B to Compromises Rules whether having a place of business in India or not.

Cross-border merger: Procedural aspects

Inbound Mergers

When the Resultant Company is an Indian Company, the following procedure becomes applicable:

i. **Issue/Transfer of securities**: The issue or transfer of any security and/or a foreign security, to a person resident outside India should be made in accordance with the pricing guidelines, entry routes, sectoral caps, attendant conditions and reporting requirements for foreign investment as laid down in Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2017 (TISPRO). However, this is subject to the following conditions:
   a. where the Foreign Company is a joint venture (JV) or a wholly owned subsidiary (WOS) of the Indian company, it shall comply with the conditions prescribed for transfer of shares of such JV/ WOS by the Indian party as laid down in Foreign Exchange Management (Transfer or issue of any foreign security) Regulations, 2004 (TIFS);
   b. where the Inbound Merger of the JV/WOS result into acquisition of the Step-down subsidiary of JV/ WOS of the Indian party by the Resultant Company, then such acquisition should be in compliance with Regulation 6 and 7 of TIFS which provide for permission for direct investment in certain cases and investment by Indian party engaged in financial services sector respectively.

ii. **Borrowings**: Any borrowing of the Foreign Company from overseas sources that becomes the borrowing of the Resultant Company shall conform within a period of two years, to Foreign Exchange Management (Borrowing or Lending in Foreign Exchange) Regulations, 2000 or Foreign Exchange Management (Guarantee) Regulations, 2000, as applicable.

iii. **Assets**: The Resultant Company may acquire and hold any asset outside India which an Indian company is permitted to acquire under the provisions of FEMA. Such assets can be transferred in any manner for undertaking a transaction permissible under FEMA.

iv. **Sale of assets**: Where the asset or security is not permitted to be acquired/ held by the Resultant Company under the FEMA provisions, the Resultant Company should sell such asset/ security within a period of two years from the date of sanction of the Scheme of the cross-border merger and repatriate the sale proceeds to India immediately.

v. **Offices:** An office outside India of the Foreign Company, pursuant to the sanction of the Scheme of Cross Border Merger shall be deemed to be the branch/office outside India of the Resultant Company in accordance with the Foreign Exchange Management (Foreign Currency Account by a person resident in India) Regulations, 2015. Accordingly, the Resultant Company may undertake any transaction as permitted to a branch/office under the aforesaid Regulations.

Outbound Mergers

When the Resultant Company is a Foreign Company, the following procedure becomes applicable:

i. **Eligibility:** A person resident in India may acquire or hold securities of the Resultant Company in accordance with TIFS.

ii. **Fair Market Value**: A resident individual may acquire securities outside India provided that the fair market value of such securities is within the limits prescribed under the Liberalized Remittance Scheme laid down under FEMA.

iii. **Repayment**: The guarantees or outstanding borrowings of the Indian Company, which become the liabilities of the Resultant Company shall be repaid as per the Scheme sanctioned by the NCLT in terms of the Compromises Rules. However, this is subject to the following conditions: (a) The Resultant Company shall not acquire any liability payable towards a lender in India in Rupees which is not in conformity with FEMA. (b) A no-objection certificate to this effect should be obtained from the lenders in India of the Indian company.

iv. **Assets**: The Resultant Company may acquire and hold any asset in India which a Foreign Company is permitted to acquire under the provisions of FEMA. Such assets can be transferred in any manner for undertaking a transaction permissible thereunder. In cases where the asset or security in India cannot be acquired or held by the Resultant Company under FEMA, the Resultant Company shall sell such asset or security within a period of two years from the date of sanction of the Scheme by NCLT and the sale proceeds shall be repatriated outside India immediately through banking channels. The Resultant Company may open a Special Non-Resident Rupee Account (SNRR Account) in accordance with the Foreign Exchange Management (Deposit) Regulations, 2016 for putting through transactions under these Regulations and such account shall run for a maximum period of two years from the date of sanction of the Scheme by NCLT.

v. **Offices**: An office in India of the Indian company, after sanction of Scheme of Cross Border Merger, may be deemed to be a branch office in India of the Resultant Company in accordance with the Foreign Exchange Management (Establishment in India of a branch office or a liaison office or a project office or any other place of business) Regulations, 2016. The Resultant Company may undertake any transaction as permitted to a branch office under the aforesaid Regulations.

Compliance related aspects

The FEMA Regulations provide that the valuation of the Indian Company and the Foreign Company shall be done in accordance with Rule 25A of the Compromises Rules. Compensation by the Resultant Company to a holder of a security of the Indian Company or the Foreign Company, may be paid, in accordance with the Scheme sanctioned by the NCLT. The companies involved in the cross-border merger must ensure that any regulatory actions, prior to merger, regarding non-compliance, contravention, violation under FEMA shall be completed. The Resultant Company and/or the companies involved in the cross-border merger are required to furnish reports prescribed by the RBI periodically. Any transaction, because a cross-border merger is undertaken in accordance with the FEMA Regulations, is deemed to have prior approval of the RBI required under Rule 25A of the Compromises Rules. Additionally, a certificate ensuring compliance to the FEMA Regulations from the Managing Director/Whole

Time Director and Company Secretary of the company(ies) concerned shall be furnished along with the application made to the NCLT under the Compromises Rules.

Conclusion

While the FEMA Regulations are a welcome step in providing clarity to the extant regulatory regime and enabling corporate houses abroad to plan their businesses more effectively thereby giving an impetus to the M&A activity in the country, a crucial aspect to take note of is the definition of a "Foreign Company" in these FEMA Regulations which act as a double-edged sword resulting in dual applicability of permitted jurisdictions under Rule 25A as well as these Regulations. Additionally, these Regulations will also have a bearing on pending as well as the future insolvency and bankruptcy proceedings since foreign bidders will now turn towards buying Indian assets. Keeping in mind these factors, the interplay of these Regulations with the existing regime is yet to be seen, going forward.

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Bills, Notifications and Circulars

Fugitive Economic Offenders Bill, 2017 approved by Union Cabinet: This Bill provides for measures to deter economic offenders from evading the process of Indian law by remaining outside the jurisdiction of Indian courts and empowers the Government to confiscate the properties of such offenders in India.

The term "**Fugitive Economic Offender**" has been defined as an individual against whom a warrant for arrest in relation to a scheduled offence has been issued by any court in India, who: (i) leaves or has left India so as to avoid criminal prosecution; or (ii) refuses to return to India to face criminal prosecution.

The term "**Proceeds of crime**" refers to any property derived or obtained, directly or indirectly, by any person from any criminal activity relating to a scheduled offence or the value of such property or where such property is outside the country, then the property equivalent in value held within the country. The term "**Scheduled offence**" as used in the aforesaid definition of "proceeds of crime" refers to offences mentioned in the Schedule, if the total value involved in such offences is one hundred crore rupees or more.

The proposed Bill, lays down the following steps –

1. A director or any other officer as authorized by such director shall file an application to a special court for declaring an individual as fugitive economic offender. Such application shall consist of reasons thereof, any information on whereabouts of such person, value of properties made from proceeds of crime and confiscation sought for, list of related persons who may have interest in such properties as mentioned above.
2. Under Section 7, the director or an officer authorized by such director not below the rank of Deputy Director may attach any property as mentioned in application filed *vide* an order under Section 6. However, an order for **Preservation of Property** can be made in writing if there is reason to believe that the property is proceeds of crime or is owned by such fugitive individual and is being/likely dealt in a manner in which such property shall

become unavailable for confiscation. Such preservation scenario shall not exceed a period of 180 days. The burden of proof for establishing that an individual is a fugitive economic offender lies on the Director/such authorized person. Also, the burden of proof that the property in application is from proceeds of crime shall be on the Director/such authorized person.

3. On receipt of application, the special court would issue a **notice** to the individual and to any other person who has any interest in such property as provided in application. Additionally, the notice shall provide that in case of failure to appear the individual shall be declared as fugitive economic offender.
4. After hearing the application if the court concludes that the individual concerned is a fugitive economic offender, reasons for the same are to be recorded in writing. On such **declaration**, the court shall order the properties to stand confiscated. If any person is aggrieved by order of the special court then he may file an appeal in the High Court within a period of 30 days.
5. In case a person is declared as fugitive economic offender, any court in India in any civil proceedings before it, may in its discretion, **disentitle** such individual from putting forward or defending any civil claim. Such condition also applies to a company wherein such fugitive economic offender is a promoter, key managerial personnel, majority shareholder or representative of the company in such civil proceedings.
6. After passing an order for confiscation, the court shall **appoint an administrator** (insolvency professional as per IBC 2016) to manage and deal with such properties. Such administrator shall hear all claims in relation to such properties and duly prepare a final creditor list wherein the confiscated properties shall be used to satisfy claims in final list. The Administrator shall be responsible for **disposal of such properties**.

Arbitration and Conciliation (Amendment) Bill, 2018: The Union Cabinet has approved the Arbitration and Conciliation (Amendment) Bill 2018 on 7th of March 2018 for introduction in the ongoing session of the Parliament. The Bill is meant to encourage institutional arbitration and provide for a robust Alternative Dispute Resolution (ADR) mechanism in India. This Bill comes in furtherance of the J. Srikrishna High Level Committee Report ("HLC") and the Arbitration and Conciliation (Amendment) Act, 2015 ("2015 Amendment").

The salient features of the aforesaid Bill, *inter alia*, are,

1. To change the present system of appointment of arbitrators by the Supreme Court or High Court, to a system where the arbitrators shall be appointed by arbitral institutions designated by the Supreme Court or High Court;
2. In case where no graded arbitral institutions are available, the Chief Justice of the concerned High Court may maintain a panel of arbitrators for discharging the functions and duties of arbitral institutions;
3. To insert a new Part 1A to the Act for the establishment and incorporation of an independent body namely, the **Arbitration Council of India** ("ACI") for the purpose of grading of arbitral institutions and accreditation of arbitrators, etc.;
4. To provide that the arbitrator, arbitral institutions and the parties shall maintain confidentiality of information relating to arbitral proceedings and also protect the arbitrator or arbitrators from any suit or other legal proceedings for any action or omission done in good faith in the course of arbitration proceedings; and

5. To clarify that Section 26 of the Arbitration and Conciliation (Amendment) Act, 2015, is applicable only to the arbitral proceedings which commenced on or after 23rd October 2015 and to such court proceedings which emanate from such arbitral proceedings, to address the divergent views given by various Courts.

Notably, post introduction of this Bill, the Supreme Court, in the matter of *Board of Cricket in India v. Kochi Cricket Pvt. Ltd. And Ors.* [SLP (C) Nos. 19545-19546 of 2016] pronounced its judgement on 15th March 2018 wherein it held *inter alia* that the Amendment Act prospectively applied to (i) arbitral proceedings that have commenced on or after commencement of Amendment Act and (ii) court proceedings which have begun after commencement of the Amendment Act. The Court has also found that certain individual provisions in the Amendment Act may effectively have retrospective operation, depending on the nature and effect of the provision in question.

Companies Commercial Courts, Commercial Division and Commercial Division of High Courts (Amendment) Bill, 2018: On March 7, 2018, the Companies Commercial Courts, Commercial Division and Commercial Division of High Courts (Amendment) Bill, 2018 was approved for introduction in the Parliament. To aid faster resolution of commercial disputes, the Commercial Courts, Commercial Division and Commercial Appellate Division of High Courts Act, 2015 was enacted and commercial courts were established at District Levels in all jurisdictions, except in the territories over which High Courts have original ordinary civil jurisdiction, for which Commercial Divisions have been constituted in each of these High Courts. Presently, the value of such commercial disputes to be adjudicated by the Commercial Courts or the Commercial Division of High Courts is affixed at INR 1 Crore.

The Bill has been formulated to reduce the specified value of a commercial dispute from INR 1 Crore to INR 3 Lakhs so that commercial disputes of a reasonable value can be decided by commercial courts. This reduction in threshold value would aid in quicker resolution of commercial disputes of lesser value and thus further improve ease of doing business.

The said Bill also provides for establishment of Commercial Courts at district Judge level for the territories over which respective High Courts have ordinary original civil jurisdiction i.e in the cities of Chennai, Delhi, Kolkata, Mumbai and State of Himachal Pradesh. State Governments in the said territories may notify the pecuniary value of commercial disputes to be adjudicated at the district level, which shall be a minimum of INR 3 Lakhs and a maximum of the pecuniary jurisdiction of the courts. For High Courts without ordinary original jurisdiction, a forum of appeal is being provided in the form of Commercial Appellate Courts to be at district judge level, in commercial disputes decided by commercial courts below the level of District judge.

The Bill also proposes the introduction of a pre-institution mediation process in cases where no urgent, interim relief is sought, to provide an opportunity to parties to resolve commercial disputes without Courts' interference, through authorities constituted under the Legal Services Authorities Act, 1987.

The proposed amendments are to be given only prospective effect so as not to disturb the authority of the judicial forum presently adjudicating commercial disputes.

Ratio Decidendi

Incorporating of arbitration clause in a contract from another document - Reference to other document should clearly indicate such intention

Key Points:

1. There is distinction between reference to another document and incorporation of another document in a contract by reference.
2. An arbitration clause contained in an independent document can also be imported and engrafted in the contract between the parties, by reference to such independent document in the contract, even if there is no specific provision for arbitration.

Brief Facts:

In this case, the National Highway Authority of India ("NHAI") entered into a concession agreement with M/s. T.K. Toll Road Pvt. Ltd. for construction of a road. The latter awarded, vide EPC agreement, the work to M/s. Utility Energytech and Engineers Pvt. Ltd. The EPC Contractor, in turn, entered into a construction agreement with M/s. Techtrans Construction Indian Pvt. Ltd. ("Respondent"), which, in turn, sub-contracted their work to Elite Engineering's ("Appellant"). A sub-contract was signed. Some disputes arose over payment between the sub-contractors at the end of the chain, and the Appellant filed Original Petition under Section 9 of the Arbitration and Conciliation Act, 1996 ("Act"). The Respondent denied all the allegations raised by the appellant and also submitted that since there was no arbitration agreement between the parties, the petition under Section 9 of the Act was not maintainable. While this was pending, the appellant moved an application under Section 11(3) and (5) of the Act for appointment of an arbitrator. The High Court maintained there was no arbitration clause in the contract between sub-contracting Parties. On the other hand, the Appellant argued that its sub-contract had adopted the main contract with an arbitration clause. This contention was rejected by the High Court and the Hon'ble Supreme Court.

Points for Consideration:

Whether the Arbitration clause in the EPC agreement was incorporated in the agreement between sub-contracting Parties?

Held:

The High Court maintained that there was no arbitration clause in the contract between sub-contracting Parties. Appellant argued that its sub-contract had adopted the main contract with an arbitration clause. This contention was rejected by the High Court and the Hon'ble Supreme Court. The Apex Court in its judgment emphasised that the sub-contract referred only to technical details and not to arbitration and stated that if the arbitration clause is incorporated in another contract, it should contain a clear reference to the documents containing the arbitration clause and the intention to incorporate it.

Order:

The Appeal was dismissed. [*Elite Engineering and Construction (Hyd.) Private Limited* v. *Techtrans Construction India Private Limited,* Civil Appeal No. 2439 of 2018, decided on 23-2-2018, Supreme Court]

Moratorium under Section 14 of Insolvency and Bankruptcy Code, 2016 will not only be applicable to property of 'Corporate Debtor', but also on 'Personal Guarantor'

Brief Facts:

Mr. V. Ramakrishnan ("1st Respondent"), Director of M/s Veesons Energy Systems Pvt. Ltd. ("2nd Respondent/Corporate Debtor") furnished a personal guarantee of his assets to State Bank of India ("Appellant/Financial Creditor"). Thus, as per definition of "Personal Guarantor" under the Insolvency & Bankruptcy Code ("Code"), Mr. V. Ramakrishnan was the Personal Guarantor for the Corporate Debtor. The Financial Creditor invoked its rights under the SARFAESI Act, 2002 against the Personal Guarantor for recovery from the 1st Respondent. This notice was challenged by the Corporate Debtor before the High Court of Madras and the same was dismissed. The Financial Creditor issued a Possession Notice and took symbolic possession of the secured assets. The Corporate Debtor invoked Section 10 of the Code and subsequently, an order of Moratorium was passed and an Interim Resolution Professional was appointed. Despite the moratorium, the Financial Creditor moved under the SARFAESI Act and proceeded against the assets of the Personal Guarantor, issuing a notice of Sale dated 12th July 2017. The Personal Guarantor, aggrieved from this action, approached the NCLT, Chennai ("Adjudicating Authority") for stay of proceedings under SARFAESI Act, which was granted till the moratorium was over, vide order dated 18th September 2017 ("Impugned Order"). The Financial Creditor filed an appeal before the NCLAT against this order of the Adjudicating Authority.

Points for consideration:

Whether Financial creditor is barred from proceeding against the assets of a Personal Guarantor while a Moratorium applies to the Corporate Debtor.

Held:

Interpreting Section 60 of the Code (Adjudicating Authority for corporate persons), the Appellate Tribunal stated that,"*…in a case where proceeding has been initiated against the Corporate Debtor, if simultaneous proceeding is to be initiated against the Personal Guarantor for bankruptcy proceedings, an application relating to the Insolvency Resolution or Bankruptcy of a Personal Guarantor of such Corporate Debtor is to be filed before the same Adjudicating Authority (National Company Law Tribunal) hearing the 'Insolvency Resolution Process' or 'Liquidation Proceedings' of a 'Corporate Debtor'.*

***…**Therefore, a 'Financial Creditor', including Appellant-State Bank of India, if intends to proceed against the 'Personal Guarantor' of the 'Corporate Debtor', may file an application relating to 'Bankruptcy' of the 'Personal Guarantor' before the same Adjudicating Authority ('Division Bench, Chennai' herein).*"

Interpreting Section 14 of the Code (**Moratorium**), NCLAT observed that it was clear that not only institution of suits or continuation of pending suits or proceedings against the 'Corporate Debtor' are prohibited from proceedings, any transfer, encumbrance, alienation or disposal of any of assets of the 'Corporate Debtor' and/ or any legal right or beneficial interest therein are also prohibited.

Interpreting Section 31(1) of the Code (**Approval of resolution plan**), it was held that *a 'Resolution Plan' if approved by the Committee of Creditors and once approved by the Adjudicating Authority is not only binding on the Corporate Debtor, but also on its employees, members, creditors, guarantors and other stakeholders involved in the Resolution Plan, including the Personal Guarantor.*

Order:

'Moratorium' will not only be applicable to the property of the 'Corporate Debtor' but also on its 'Personal Guarantor'. [*SBI* v. *Ramakrishnan and Ors.* - Company Appeal (AT) (Insolvency) No. 213 of 2017, decided on 28-2-2018, National Company Law Appellate Tribunal]

Adjudicating authority cannot rely on extraneous factors unrelated to resolution process to dismiss an application filed under the Insolvency and Bankruptcy Code

Key Point:

For imposition of penalty under Section 65 of IBC, the Adjudicating Authority has to form a *prima facie* opinion that the financial creditor/corporate applicant has filed a petition under IBC 'fraudulently' or 'with malicious intent' for a purpose other than the resolution of insolvency or liquidation or with the intent to defraud any person.

Brief Facts:

Neeta Chemicals (I) Private Limited (Appellant) had filed an application under Section 10 of the IBC, which was dismissed by National Company Law Tribunal (NCLT), Hyderabad on grounds that the Corporate Debtor had been classified as a non-performing asset as early as 2013 and that the financial creditor, namely State Bank of India (Respondent) had made sufficient efforts to recover the debt from the Appellant, and that the Appellant had filed the application with a *mala fide* intention.

The Appellant challenged the above Order before the National Company Law Appellate Tribunal (NCLAT), contending that the above order was passed on frivolous grounds even though the Appellant had fulfilled all the conditions stipulated in Section 10 of IBC. The Respondent contended that there was significant suppression of liability in the application filed by the Appellant under Section 10 of IBC, therefore, the said application was incomplete and liable to be rejected. The Respondent also contended that the Appellant had grossly misstated the outstanding amount in the said application, which showed its *mala fide* intent.

Held:

NCLAT, by relying on the case of *Unigreen Global Private Limited* v. *Punjab National Bank & Ors., Company Appeal (AT) (Insolvency) No. 81 of 2017*, held that a 'Corporate Applicant' is eligible to file application under Section 10 of IBC if there is a debt and default. It was also held that there was nothing on record to suggest that the Appellant indulged in suppression of facts or approached the Tribunal with unclean hands. Finally, it was held that the NCLT had not held that the application was filed by the Appellant 'fraudulently' or with 'malicious intent' for any purpose other than for insolvency resolution process or liquidation or that the voluntary liquidation proceedings have been initiated with the intent to defraud any person. Accordingly, NCLAT remitted the matter back to NCLT for admission of application under Section 10 of IBC. [*Neeta Chemicals (I) Pvt. Ltd.* v. *State Bank of India,* Company Appeal (AT) (Insolvency) No. 174 of 2017, decided on 22-3-2018, National Company Law Appellate Tribunal]

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