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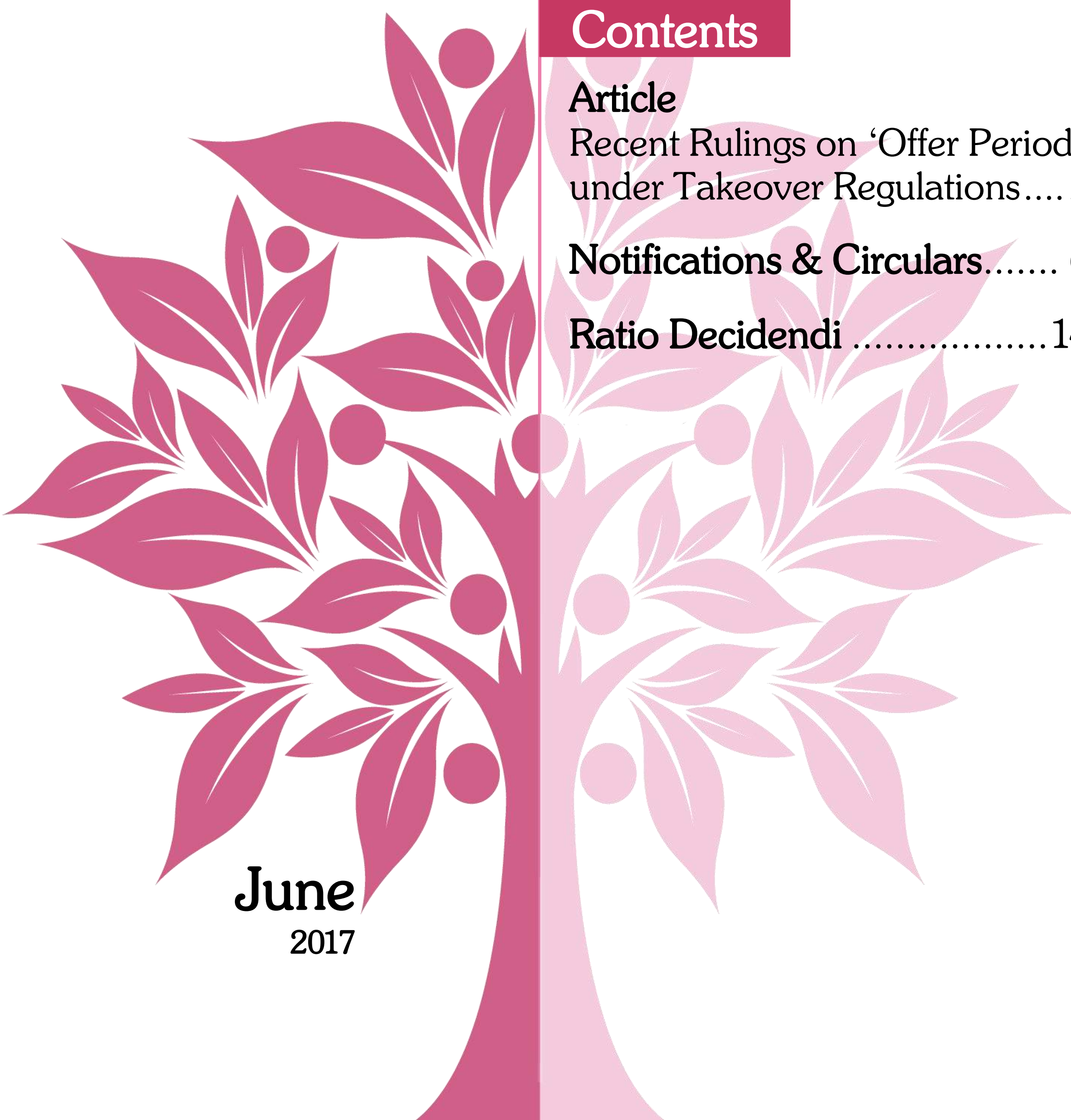

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Article

Recent Rulings on 'Offer Period' under Takeover Regulations

By Anu Chowdhry

Public offers in relation to acquisition of shares and takeover of public companies in India is governed by a self-contained code enshrined in the SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 2011 ('2011 Regulations'), that replaced the erstwhile SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997 ('1997 Regulations').

The legislative intent was best summarized by the Hon'ble Supreme Court in *Nirma Industries Limited* v. *Securities and Exchange Board of India* ((2013) 8 SCC 20), as a Code ''(a) to ensure that the target company is aware of the substantial acquisition; (b) to ensure that in the process of the substantial acquisition or takeover, the security market is not distorted or manipulated; and (c) to ensure that the small investors are given an option to exit, that is, they are offered a choice to either offload their shares at a price as determined in accordance with the Takeover Code or to continue as shareholders under the new dispensation. In other words, the Takeover Code is meant to ensure fair and equal treatment of all shareholders in relation to substantial acquisition of shares and takeovers and that the process does not take place in a clandestine manner without protecting the interest of the shareholders.''

Recent rulings on open offers by the Hon'ble Supreme Court have brought to fore the duties and obligations cast on both a potential acquirer and a target company. The rationale behind placing restrictions on certain actions that may be taken during the subsistence of an offer period is primarily to prevent the target company's assets from being dealt with in a manner that may potentially be detrimental to existing shareholders, or have a bearing on their decision to participate in the open offer.

Commencement of Open Offer

The 2011 Regulations specify the events and thresholds limits that would trigger the requirement for a potential acquirer to make an open offer, except when exempted under the specific circumstances prescribed by the 2011 Regulations.

In *Securities and Exchange Board of India* v. *Burren Energy India Limited* (Civil Appeal No. 361 of 2007), the Hon'ble Supreme Court of India interpreted the nature of an 'Memorandum of Understanding' for the purposes of identifying the date of commencement of an offer period. Burren Energy India Limited ("Burren"), incorporated under the laws of England and Wales in 2004, was formed to acquire the entire share capital of Unocal Bharat Limited ("UBL").

UBL held 26.01% of the issued share capital of Hindustan Oil Exploration Co. Ltd ("Target Company"). The shares of UBL had previously been acquired in 1996 by Unocal International Corporation ("UIC"). Burren, with an intention to acquire UBL, had entered into a Share Purchase Agreement with UIC on February 14, 2005 ("SPA"). By virtue of the SPA, Burren indirectly came to acquire 26.01% shareholding of the

Target Company which were earlier held by UBL. As the proposed acquisition was in excess of the prescribed 15% limit under the Takeover Regulations, Burren made a public announcement for sale/purchase of shares of Target Company on February 15, 2005. However, on the date of execution of SPA (i.e. February 14, 2005), Burren proceeded to appoint two of its directors on the Board of the Target Company.

As per the Takeover Regulations applicable to the present case [i.e. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997, as amended *vide* SEBI (Substantial Acquisition of Shares and Takeovers) (Second Amendment) Regulations, 2002], an acquirer was prohibited from making any appointment on the Board of Directors of the Target Company during the subsistence of the 'offer period'. SEBI contended that the said appointments of the directors on the Board of the Target Company were made during the subsistence of the offer period, and therefore were in violation of the Takeover Regulations.

The interpretation of 'Memorandum of Understanding' was key to resolving this dispute, for it had direct bearing on identifying the commencement date for the purpose of computing the tenure of the offer period. The Takeover Regulations define an 'offer period' as the period between the date of signing of an MoU or making of a public announcement, as the case may be, and the date of completion of offer formalities. According to SAT, the term 'Memorandum of Understanding' referred only to those understandings between parties that fell short of a concluded agreement. Based on this literal interpretation of the term, SAT ruled that given the absence of an MoU between the concerned Parties, the date of public announcement would be the event that would trigger commencement of the offer period. Thus, as the appointments dated February 14, 2005 were made before the public announcement dated February 15, 2005, the directors' appointments had not been made during the offer period.

Rejecting SAT's narrow interpretation, the Hon'ble Supreme Court noted that the term 'Memorandum of Understanding' may also include a concluded agreement in appropriate situations. Even in cases where a concluded agreement is executed subsequently to an MoU, the 'offer period' would still be said to commence from the date of execution of such MoU. The Hon'ble Supreme Court concluded that if the offer period can be triggered by an understanding between the parties that is yet to fructify into a concluded agreement, there is no reason why such offer period could not commence from the date of a concluded agreement, in the absence of an MoU. Therefore, as the offer period was triggered on execution of SPA dated February 14, 2005, and the appointments dated February 14, 2005, had been made during the subsistence of the offer period, such appointments violated the embargo under Regulation 22(7).

Importantly, this ambiguity in the definition of an offer period under the Previous Takeover Regulations does not exist in the Current Regulations. The Current Regulations peg the commencement of the offer period to the date of entering into an agreement – whether formal or informal – to acquire shares/voting rights/control in a target company. Clearly, for the purposes of the Current Regulations, it is immaterial whether such agreement is merely informal or definitive/conclusive in nature leaving little room for imprecise computation of the triggering of an offer period.

Agreement executed between Parties	Commencement of 'Offer Period'
MoU	From date of MoU
MoU followed by definitive agreement(s)	From date of MoU
Definitive agreement in absence of an MoU	From date of definitive agreement

During subsistence of Open Offer

Understanding the nature of an 'Memorandum of Understanding' also has bearing on identifying transactions undertaken by a target company during the subsistence of an offer period, that may fall foul of the embargo under the Takeover Regulations. In *Sanjay Dalmia and Others* v. *Securities and Exchange Board of India* (Appeal Nos. 102 and 101 of 2014), the Securities Appellate Tribunal, Mumbai, interpreted the scope of an 'Memorandum of Understanding' for the purposes of identifying impugned actions of a target company.

In this case, on November 12, 2009, Pramod Jain and two others made a public announcement under the Takeover Regulations, 1997, disclosing their intention to acquire 25% stake of the target company, and accordingly filed a draft letter of offer on November 26, 2009, seeking approval of SEBI for such acquisition. On December 21, 2009, the Board of Directors of the target company passed a resolution to develop a company-owned property situated in Mumbai ("Mumbai Property") subject to approval of shareholders. On the same date, a notice was addressed to the shareholders convening an Extraordinary General Meeting to seek their approval on the same.

However, in the intervening period, the target company had entered into an MoU dated December 26, 2009, with Sheth Developers and Suraksha Realty Ltd. ("Developer") for joint development of a company-owned property situated in Mumbai ("Mumbai Property") for a consideration of INR 542 Crore. After execution of this MoU, on January 18, 2010, the shareholders gave their consent to the company and authorized execution of the Joint Development Agreement in respect of the Mumbai Property.

Clearly, the public offer made by Mr. Pramod Jain and others was subsisting as on the date of execution of the MoU by the Company. As per Regulation 23(1) of the Takeover Regulations applicable to the present case [i.e. SEBI (Substantial Acquisition of Shares and Takeovers) Regulations, 1997], during the subsistence of the offer period, the Board of Directors of a target company is expressly prohibited from selling, transferring, encumbering or otherwise disposing of the assets of the target company as well as expressly prohibited from entering into any agreement for the same, without first obtaining prior approval of the general body of shareholders. Thus, before taking as well as before attempting to take such actions during the subsistence of the offer period, it is mandatory for the Board of Directors of a target company to seek prior approval of the general body of shareholders.

The target Company defended its actions by disputing the nature of the MoU dated December 26, 2009. According to the target Company, the MoU was not a binding contract between the parties, did not seek to create any encumbrance or rights over the company's assets in favour of the Developer, and therefore was not legally enforceable. On the other hand, SEBI contended that the MoU dated December 26, 2009 was in gross violation of the embargo under the Takeover Regulations. The intent of the Company to enter into legally enforceable obligations over its assets with a third party could be ascertained from terms of the MoU. For instance, the target company had received part payment of consideration equivalent to INR 35 Crore from the Developer on execution of the MoU. Further, title deeds of the concerned property were required to be kept by the Company in an escrow, within 48 hours of execution of the MoU, which title deeds would be released only upon execution of the Joint Development Agreement between the parties. Additionally, the MoU also envisioned a remedy in favour of the Developers (refund of partial consideration along with 18% interest) in the event of the target company's shareholders rejecting the joint development proposal.

The SAT held that the Board had indeed sought to encumber the Mumbai Property during the subsistence of the offer period, and had attempted to do so by bypassing the general body of shareholders. Thus, transactions requiring prior shareholder approval necessitate a broad interpretation of the term 'agreement'. To contend that the term 'agreement' used in Regulation 23 would not apply to transactions labelled or perhaps cloaked as MoUs, would amount to defeating the very object of the provision.

Conclusion of Open Offer

Once made, an open offer made by an acquirer may only be withdrawn by it on the limited grounds specified under the 2011 Regulations – namely, if statutory approvals for open offer or for effecting acquisitions attracting the obligation to make an open offer is refused; on death of the acquirer (being a natural person); or if conditions stipulated in the agreement for acquisition attracting the obligation to make an open offer are not met for reasons beyond the control of the acquirer.

In *Pramod Jain* v. *Securities and Exchange Board of India* (Civil Appeal No. 9103 of 2014), the Hon'ble Supreme Court examined the issue of an acquirer's right of withdrawing from a public offer. In this case, the Apex Court held that in the absence of circumstances that prejudice the acquirer to the extent of rendering the carrying out of the public offer impossible, discovery of *mala fide* actions or adverse decisions taken by a target company after announcement of a public offer *per se* would not justify automatic withdrawal of a public offer by an acquirer, especially since an acquirer has recourse to other remedies at appropriate fora against any such mala fide/illegal actions of a target company.

Thus, in the general scheme of the 2011 Regulations as well as numerous decisions of the Apex Court on this issue, public offers once made may not be withdrawn by an acquirer – circumstances under which an acquirer may withdraw its offer are construed strictly. As the Regulations mandate an acquirer to first undertake a due diligence exercise of the target company before filing a draft letter of offer, a potential acquirer is assumed to have undertaken a thorough assessment of the target company's financial health and the feasibility of implementing the proposed acquisition.

[The author is an Associate in Corporate Practice, Lakshmikumaran & Sridharan (UK) LLP, London]

Notifications and Circulars

SEBI Circular on Mutual Funds amended: The Securities Exchange Board of India ("SEBI") vide its Circular dated April 28, 2017 ("Circular"), has partially modified the provisions relating to executive remuneration of a prior SEBI Circular No. SEBI/HO/IMD/DF2/CIR/P/2016/42, dated March 18, 2016, ("Prior Circular") applicable to all Mutual Funds ("MF"), Asset Management Companies ("AMCs"), Trustee Companies and Board of Trustees of Mutual Funds.

Previously, an MF or AMC was required to mandatorily make the following remuneration-related disclosures on their website:

(i) Name, designation and remuneration of the following persons or their corresponding equivalent:

(a) Chief Executive Officer (CEO);

(b) Chief Investment Officer (CIO);

(c) Chief Operations Officer (COO); and

(d) all employees of MF or AMC, whose annual pay was equal to or above rupees sixty lakhs for the year or the monthly remuneration in aggregate was not less than rupees five lakhs per month, if the employee is employed for a part of a particular financial year.

(ii) Ratio of CEO's remuneration to median remuneration of MF/AMC employees.

(iii) MF's total average asset under management ("AAUM"), debt AAUM and equity AAUM and rate of growth over last three years.

Pursuant to the Circular, remuneration disclosures are also required to be made for the following persons:

(i) remuneration drawn by top ten employees in a particular financial year; and

(ii) name, designation and remuneration of every employee of MF or AMC with remuneration equal to or above one crore and two lakh rupees for a particular financial year or monthly remuneration in aggregate was not less than eight lakhs and fifty thousand rupees per month, if the employee is employed for a part of a particular financial year. These monetary limits have been enhanced from the limits of rupees sixty lakhs and rupees five lakhs, respectively, in the Prior Circular.

All disclosures are required to be made within one month from the end of the respective financial year (effective from 2016-17). These disclosure requirements seek to promote transparency in remuneration policies, so that executive remuneration is aligned with the interests of investors.

Online Registration Mechanism for Securities Market Intermediaries: The Securities Exchange Board of India ("SEBI") *vide* its Circular dated May 02, 2017, has issued directions to certain categories of intermediaries (i.e. stock brokers, sub-brokers, merchant bankers, underwriters, Registrar to an issue and share transfer agents (RTA), debenture trustees, bankers to an issue and credit rating agencies) to operationalize the process of registration through a fully online mechanism, in furtherance of the announcement made in the Union Budget speech given by the Minister of Finance, Government of India on February 01, 2017.

The SEBI Intermediary Portal (https://siportal.sebi.gov.in) has now been made operational for the above-mentioned categories of intermediaries who are henceforth required to submit all registration-related applications online (including application for registration, processing of application, grant of final registration, application for surrender or cancellation, submission of periodic reports, etc.).

Securities and Exchange Board of India (SEBI) Board meeting held on April 26, 2017: SEBI Board met on April 26, 2017 to discuss the implementation of an effective regulatory framework and broaden the scope of financial inclusion for the benefit of participant(s) across all market segments. Certain measures decided upon by the SEBI Board are stated below:

Instant Access Facility (IAF) in Mutual Funds and use of e-wallet for investment in Mutual Funds: Pursuant to discussions, a Circular was issued by SEBI on May 8, 2017 wherein IAF was provided to all resident investors in liquid mutual fund schemes offered by Mutual Fund(s) (MFs) and Asset Management Companies (AMCs). IAF facility works in such a manner that redemption proceeds can be credited in the bank account of the investor on the same day as the redemption request. Investment(s) through IAF can be capped to a monetary limit of INR 50,000 or 90% of the latest folio value, whichever is lower. MF(s) and AMC(s) would be required to make disclosures in the offer related documents with respect to the IAF facility and approvals shall be obtained from AMC board and trustees to restrict mis-selling and to ensure effective implementation of the facility.

In line with the objective of digitization, SEBI has introduced the usage of e-wallets to facilitate investments in MFs by a retail investor based on an agreement/arrangement by such MFs/AMCs with pre-paid instrument issuers. AMC/MFs shall ensure that extant regulation(s) with respect to cut-off timings, time stamping, etc., are complied with and the total subscription through e-wallets is restricted to INR 50,000 per AMC/MF in a financial year. Further, the MF/AMC is required to ensure that promotional schemes, cashback, vouchers and other such incentives shall not be issued by e-wallet issuers to investors either directly or indirectly.

Amendment of Securities Contracts (Regulation) (Stock Exchanges and Clearing Corporations) Regulations, 2012: In line with the Union Budget of Financial Year 2016-17, SEBI issued a Circular dated September 28, 2016 introducing "options" in commodity derivative market. Accordingly, a public consultative process was initiated by SEBI vide a consultation paper issued on January 19, 2017 to solicit views on suitable amendments to SECC Regulations that will enable trading in options on commodity derivatives exchanges. SEBI Board based on the aforesaid public consultation process, has now approved a proposal to amend the relevant provisions of SECC Regulations. The guidelines for trading in *"options"* on commodity derivatives exchanges are expected to be issued by SEBI shortly.

Inclusion of systemically important Non-Banking Financial Company(s) (NBFC) in category of Qualified Institutional Buyer(s) (QIB): As announced by the Finance Minister in his Union Budget speech for the financial year 2017-18, systemically important NBFCs registered with the Reserve Bank of India (RBI) that exceed a certain net worth shall be categorized as QIBs. Accordingly, SEBI Board has considered the proposal and has approved necessary amendment(s) in the SEBI (Issue of Capital and Disclosure Requirements) Regulations 2009

(ICDR Regulations) to include NBFCs having net-worth exceeding INR 500 crore under the category of QIBs. The aforesaid measure shall strengthen the market for initial public offering(s) (IPO) and will permit such qualified NBFCs to participate in the qualified institutions placement process.

Scheduled Banks and Financial Institutions to be exempted from ICDR Regulations from provisions relating to preferential allotments: As per Regulation 72(2) of the ICDR Regulations, issuers are prohibited from issuing shares to any person on a preferential basis if such person has sold the equity shares of the issuer in the preceding 6 months. ICDR Regulation 72(6) mandates the lock-in of pre-preferential allotment shareholding of allottees for a period of 6 months from the date of trading approval. However, only MFs and insurance companies were exempted from the said requirements. Now, SEBI Board has approved the extension of such relaxation to Scheduled Banks and public financial institution(s) as well with the objective to ease out restructuring norms for such banking institutions, which are mandated to reduce their non-performing asset(s) and are restricted by the preferential issue provisions provided under the ICDR Regulations.

Monitoring of utilization of issue proceeds: To effectively supervise the utilization of funds raised through IPOs, the ICDR Regulations has mandated the appointment of a *"Monitoring Agency"* in cases where the issue size of the securities exceeds INR 500 crore. To strengthen the monitoring process, SEBI has reduced the threshold limit to where the issue size (excluding offer for sale component) exceeds INR 100 crore along-with the introduction of certain other measures like frequency of submission of Monitoring Agency report (on quarterly basis instead of half yearly basis) and the report is required to be submitted within 45 days from the end of the quarter to the stock exchanges and uploaded on the website of the issuer for wider dissemination to public. The management of the Company concerned has the obligation to study the said report and provide its comments on the Monitoring Agency's findings.

Consolidation and re-issuance of debt securities issued under the SEBI (Issue and Listing of Debt Securities) Regulations, 2008: To increase liquidity in the secondary market, SEBI Board has considered and approved the following proposals:

(i) An issuer shall be allowed a maximum of 12 International Securities Identification Number(s) (ISINs) per financial year for issuance of both secured and unsecured debt securities. However, the issuer may additionally be allowed to issue 5 ISINs per financial year for structured debt instruments. Debt instruments used for raising capital through Tier I, Tier II bonds, bonds for affordable housing and the capital gains tax bonds categorized under Section 54EC of the Income Tax Act, 1961 shall not be bound by the aforesaid restrictions.

(ii) To avoid accumulation of liabilities, the issuer may consider making staggered payment of the maturity proceeds within that particular financial year.

(iii) Although it is not mandatory, SEBI Board has recommended the active consolidation of existing outstanding debt securities by way of switches and conversion.

(iv) The Articles of Association of the issuer company should not contain any clause that prohibits the consolidation or reissuance of such debt securities.

Amendment to SEBI (Foreign Portfolio Investor) Regulations, 2014 (Portfolio Regulations): SEBI Board has considered the insertion of an express provision in the Portfolio Regulations to prevent resident Indians/Non-Resident Indian(s) and entities beneficially owned by them from subscribing to offshore derivative instruments.

Merger of Equity Markets and Commodity Derivatives Markets: Post the merger of Forward Markets Commission and SEBI, commodity derivative brokers are now regulated by SEBI. However, as per the existing regulations, a stock broker and/or a clearing member dealing in commodity derivatives cannot deal in other securities or vice versa unless otherwise a separate entity is set-up for this purpose. SEBI has considered this anomaly and approved the proposal to amend the Securities Contracts (Regulation) Rules, 1957 and SEBI (Stock Brokers and Sub-brokers) Regulations, 1992 to remove the restriction.

Banking Regulation (Amendment) Ordinance, 2017: The Banking Regulation (Amendment) Ordinance, 2017 (Ordinance) was promulgated on May 4, 2017 to amend the Banking Regulation Act, 1949. As per the Ordinance, Central Government may authorize RBI to issue directions to banking companies to initiate insolvency resolution process under the Insolvency and Bankruptcy Code, 2016 ('Code') in respect of a "default", as defined under Section 3(12) of the Code. Further, the Ordinance empowers RBI to issue directions to banking companies for resolution of stressed assets, if required. RBI may also appoint authorities / committees to advise banking companies on resolution of stressed assets. RBI may now intervene directly in matters in respect of resolution of non-performing assets (NPAs). The Ordinance was promulgated to remedy the situation of stressed assets in the Indian banking system, and is in line with the Government's commitment towards a speedy and efficient resolution of NPAs in the banking system.

Net Owned Fund for Asset Reconstruction Companies enhanced: The Reserve Bank of India (RBI) *vide* its Notification *RBI/2016-17/295 DNBR. PD (ARC) CC. No. 03/26.03.001/2016-17,* dated April 28, 2017 (Notification) has enhanced the minimum Net Owned Fund (NOF) requirement for Asset Reconstruction Companies (ARC). Henceforth, to be eligible for registration as an ARC, an entity is required to have a minimum NOF of INR 100 Crores on an ongoing basis. *Per* Section 3(1)(b) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002, ARCs are required to have a minimum NOF of INR 2 Crores or of a higher amount, as the RBI may specify by notification.

Accordingly, RBI has specified a significantly higher minimum NOF requirement to resolve the issue of stressed assets in the Indian banking system. Since the increase in minimum NOF requirement will attract larger ARCs, consolidation in the ARC sector can be expected in the near future. ARCs which are already registered with RBI and do not satisfy the minimum NOF criterion are required to achieve the enhanced limit latest by March 31, 2019.

Timeline for Stressed Assets Resolution: Reserve Bank of India (RBI) has issued a Circular dated 5th May, 2017 on the Timelines for Stressed Assets Resolution. Earlier in 2014, RBI had issued a 'Framework for Revitalising Distressed Assets in the Economy – Guidelines on Joint Lenders' Forum (JLF) and Corrective Action Plan (CAP)', aimed at early identification of stressed assets and timely implementation of CAP and specifies timelines for deciding and implementing the CAP by the lenders.

Considering the delays in implementing the CAP, RBI has issued the present Circular with the following measures:

a) CAP can also include resolution by way of Flexible Structuring of Project Loans, Change in Ownership under Strategic Debt Restructuring, Scheme for Sustainable Structuring of Stressed Assets, etc.;
b) Lenders must scrupulously adhere to the timelines prescribed in the Framework. The decisions agreed upon by a minimum of 60% of creditors by value and 50% of creditors by number in the JLF would be considered as the basis for deciding the CAP, which will be binding on all lenders, subject to the exit option available under the Framework;
c) Further, while voting on the final proposal, Lenders shall take unambiguous and unconditional stand and the respective Boards of banks shall empower their executives to implement decisions, without requiring the Board's further approval;
d) Any non-adherence to these instructions shall attract monetary penalties on the concerned banks under the Banking Regulation Act, 1949.

National Electronic Funds Transfer (NEFT) system: RBI has issued a Notification on 8th May, 2017 advising all participating banks to facilitate additional settlements at half-hour intervals from the present hourly intervals, which is aimed at enhancing the efficiency of the system and customer convenience.

With the new introduction of additional settlement batches (11 in number), the total number of settlement batches will be increased to 23, starting at 8.00 am and closing batch at 7.00 pm. The additional batches will be introduced from July 10, 2017.

Voluntary Liquidation and Bankruptcy provisions of Insolvency and Bankruptcy Code, 2016 notified: The Ministry of Corporate Affairs *vide* Notification 2017 REGD. NO. D. L.-33004/99, dated May 15, 2017 has notified the provisions of clauses (a) to (d) of Section 2 of the Insolvency and Bankruptcy Code, 2016 ('Code'). Section 2 lays down the entities to which the Code is applicable. In accordance with Section 2 of the Code, the entities which will henceforth be governed by the provisions of the Code (in respect of insolvency, liquidation, voluntary liquidation or bankruptcy, as the case may be) are:

(i) Companies incorporated under the Companies Act, 2013 or under any previous company law legislation;
(ii) companies governed by any special Act in force subject to applicable conditions;
(iii) Limited Liability Partnerships incorporated under the Limited Liability Partnership Act, 2008; and
(iv) such other body incorporated under any other law in force, as the Central Government may specify by notification.

Clause (e) of Section 2 of the Code (pertaining to application of the Code to partnership firms and individuals) has not been notified till date.

Companies (Acceptance of Deposits) Amendment Rules, 2017 notified: The Ministry of Corporate Affairs (MCA) *vide* Notification dated

May 11, 2017 (Amendment), has amended the Companies (Acceptance of Deposit) Rules, 2014 (Deposit Rules). Rule 2(1)(c) of the Deposit Rules excludes certain receipts by a company incorporated under the Companies Act, 2013 (Companies Act) from the definition of "deposit", thereby excluding them from the purview of Section 73 of the Companies Act. Currently, amounts received by a company from registered Alternative Investment Funds, Domestic Venture Capital Funds and Mutual Funds are excluded from the definition of 'deposit'. With the Amendment in force, now any amount received by a company from an Infrastructure Investment Trust registered with SEBI shall also not be considered as a "deposit" for the purposes of the Companies Act.

In terms of Rule 5 of the Deposit Rules, every company inviting deposit is required to enter into a deposit insurance contract at least 30 days before the date of issue of circular/advertisement or date of renewal, as the case may be. However, *vide* proviso to Rule 5, companies were permitted to accept deposits without deposit insurance contract until March 31, 2017. The said date has been further relaxed and extended to March 31, 2018.

Insurance Regulatory and Development Authority of India (Insurance Web Aggregators) Regulations, 2017: The Insurance Regulatory and Development Authority of India has notified the Insurance Regulatory and Development Authority of India (Insurance Web Aggregators) Regulations, 2017 (2017 Regulations) on April 13, 2017 which supersedes the existing Insurance Regulatory and Development Authority (Web Aggregators) Regulations, 2013 (2013 Regulations).

The objective of the 2017 Regulations is to supervise and monitor insurance web aggregators, acting as insurance intermediaries, who maintain a website for providing interface to insurance prospects, for price comparison and information of products of different insurers and other related matters (Insurance Web Aggregators).

Insurance Web Aggregators facilitate comparison of insurance products and provide interested parties with a comparative list of insurance products based on specific parameters. A few noteworthy amendments under 2017 Regulations are:

(i) Unit Linked Insurance Plans or variable insurance products were not allowed to be solicited or sold under 2013 Regulations. 2017 Regulations have done away with this restriction, thereby, permitting all types of insurance products to be solicited and sold by Insurance Web Aggregators;

(ii) The premium ceilings in case of sale of life insurance *via* telemarketing have been enhanced. An Insurance Web Aggregator can now solicit both single premium policy and non-single premium type policies whose annual premium is limited to INR 150,000 *via* telemarketing. This ticket size for single premium policy and non-single premium policy was restricted at INR 100,000 and INR 50,000 respectively; and

(iii) 2017 Regulations permit Insurance Web Aggregators to earn remuneration through rewards even in cases of zero-commission policies. In certain sectors such as health insurance, motor insurance and home insurance policies, it has been clarified that Insurance Web Aggregators are now entitled to renewal commissions. However, this renewal commission is not provided for life insurance policies as they are long term contracts.

In addition to the aforementioned, 2017 Regulations have enhanced the net-worth and capital requirements for a company engaged or desirous to be registered as an Insurance Web Aggregator. The existing market players have been mandated to comply with the revised capital and net-worth requirements within a period of one year.

These changes have, in effect, increased the number of products which are eligible to be showcased and incentivized the process for Insurance Web Aggregators. With an intention to protect the interest of customers and to ensure more equity, the guidelines prohibit Insurance Web Aggregators to promote or push a particular product or company through their website or any other form of marketing. These changes are expected to fuel the role of Insurance Web Aggregators who play an important role in comparative analysis of the insurable products, while ensuring that no single company gets unfair advantage.

Insurance - New regulations notified to regulate outsourcing activities by Indian insurers: The Insurance Regulatory and Development Authority of India (IRDAI), has notified the IRDAI (Outsourcing of Activities by Indian Insurers) Regulations, 2017 (Outsourcing Regulations) on April 20, 2017. The said regulations supersede the previous guidelines issued by IRDAI in this regard and shall be applicable to all insurers registered with IRDAI excluding entities engaged in the reinsurance business. The primary objective of the Outsourcing Regulations is to inculcate effective management of outsourcing activities carried out by insurers.

The Outsourcing Regulations define the term *"Outsourcing"* as the use of third party services for undertaking insurance activities, either now or in the future but specifically excludes activities such as legal services, banking services, courier services, medical examination, forensic analysis etc. Additionally, the Outsourcing Regulations specifically prohibits the outsourcing of activities such as investment functions, fund management, actuarial functions, KYC compliances as well as decision making in underwriting and claim(s) function. The Outsourcing Regulations mandate the formulation of an "Outsourcing Policy" by the Board of Directors as well as the constitution of an outsourcing committee which shall be responsible for the overall implementation of the approved outsourcing policy.

Within 180 days of the commencement of the Outsourcing Regulations, all existing outsourcing arrangement(s) shall either be suitably amended in accordance with the said regulations or terminated by the insurer.

RERA - Operative provisions of Real Estate (Regulation and Development) Act, 2016 notified: RERA is a legislation that has been formulated with a view to (i) protect the interest of the allottees by promoting transparency, accountability and efficiency in the construction and execution of real estate projects by promoters and (ii) establishing uniformity, standardization of business practices and transactions in the real estate sector.

Following the Notification dated April 26, 2016 through which numerous provisions of RERA were first brought into effect, the Ministry of Housing and Urban Poverty Alleviation, *vide* its Notification dated April 17, 2017 ("Notification"), has now notified the remaining provisions of RERA (tabulated below) with effect from May 01, 2017. Therefore, as of date, the provisions of

RERA in entirety are in effect and various States have formulated the applicable rules. Hopefully, in due course, the regulatory mechanism of checks and balances under RERA will ensure a paradigm change in the real estate sector by reducing the number of unfair practices, and bring in accountability of promoters.

Section Nos. notified w.e.f May 01, 2017	Key Provisions
Section 3-19	(i) registration of real estate project and registration of real estate agents, (ii) functions and duties of promoter and (iii) rights and duties of allottees.
Section 40	recovery of interest or penalty or compensation and enforcement of order, etc.
Sections 59-70	offences, penalties and adjudication and provides for the quantum of penalty to be levied and/ or the quantum of years for imprisonment, wherever applicable in case of violations committed by the (i) promoter, (ii) allottees and (iii) real estate agents
Section 79-80	(i) bar of jurisdiction and (ii) cognizance of offences, respectively. In terms of the provisions of Section 79, the jurisdiction of civil courts has been barred from entertaining any suit or proceeding in respect of any matter, over which the authority constituted for the purposes of RERA is empowered to act upon. Section 80 of RERA stipulates that no court inferior to that of a Metropolitan Magistrate or a Judicial Magistrate of first class shall have the authority to try offences punishable under RERA, save on a complaint made in writing by the authority or any officer constituted for such purposes under RERA

Employee's Compensation (Amendment) Act, 2017 notified: The Ministry of Labour and Employment, *vide* its Notification dated April 12, 2017, has notified the Employee's Compensation (Amendment) Act, 2017 ("Amendment Act"), to amend the Employee's Compensation Act, 1923 ("Principal Act"). The Principal Act provides for payment of compensation to employees and their dependants in the case of injuries, including those resulting in death or disablement, due to industrial accidents and certain occupational diseases which arise out of and in the course of employment. Through a subsequent Notification dated May 12, 2017, by the Ministry of Labour and Employment, the provisions of the Amendment Act have been made effective from May 15, 2017.

Briefly, Section 17A endows a duty on the employer to inform employees regarding their rights relating to compensation, immediately at the time of employment. This must be done in writing as well as by electronic means, in English or Hindi or in the official language of the area of employment as understood by the employee. If an employer fails to inform an employee of his rights to compensation as required under Section 17A, such employer shall be punishable with a fine which shall not be less than fifty thousand rupees, but which may extend to one lakh rupees. It may be noted that this is a significant escalation from the previously prescribed limit of five thousand rupees.

Ratio Decidendi

Corporate Insolvency Resolution Process – NCLT clarifies scope of 'operational debt'

Facts:

The National Company Law Tribunal (NCLT) has passed an order interpreting the definitions of '*operational creditor*' and '*operational debt*' under the Insolvency and Bankruptcy Code, 2016 (Code). NCLT rejected the application filed under Section 9 of the Code for initiating Corporate Insolvency Resolution Process (CIRP) and held that the remedy lay under the Consumer Protection Act, 1986 and the general law of the land. The matter arose out of non-payment of refund and the interest amount by Respondent *per* the builder-buyer agreement between the Applicants and the Respondent. The Applicants had booked a residential flat in the Respondent's construction project and made corresponding payments. The Respondent failed to hand over the possession of the residential flat within the stipulated time period. The Applicant, thus, applied for cancellation of allotment of the residential flat and refund of the deposit with interest.

Contentions:

The Applicants contended that the Respondent must be considered as an 'operational debtor' while the Applicants should be considered as 'operational creditors' within the meaning of Section 9 read with Section 5(20) and Section 5(21) of the Code. The term 'operational debt' should be liberally interpreted to include claims in respect of immovable property. Based on the aforesaid premise, the Applicants contended that they were eligible to initiate CIRP under the Code.

Order of the Tribunal:

NCLT cited and upheld the case of *Vinod Awasthy* v. *A.M.R. Infrastructures Limited* (AMR case) in the present case. In the *AMR* case, the NCLT construed the provisions of Section 9 read with Section 5(20) and Section 5(21) of the Code. *Per* Section 9(1) of the Code, CIRP can only be initiated by an 'Operational Creditor'[1] against the 'Corporate Debtor' when an 'Operational Debt'[2] is owed. The definition of 'operational debt' does not state that it also includes any debt other than 'Financial Debt'[3].

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1 Section 5 (20) of IBC defines "operational creditor" as follows:
"operational creditor" means a person to whom an operational debt is owed and includes any person to whom such debt has been legally assigned or transferred"

2 Section 5 (21) of IBC defines "operational debt" as follows:
"operational debt" means a claim in respect of provision of goods or services including employment or a debt in respect of the repayment of dues arising under any law for the time being in force and payable to the Central Government, any State Government or any local authority"

3 Section 5 (8) of IBC defines "financial debt" as follows:
"financial debt means a debt alongwith interest, if any, which is disbursed against the consideration for the time value of money and includes— (a) money borrowed against the payment of interest; (b) any amount raised by acceptance under any acceptance credit facility or its de-materialised equivalent; (c) any amount raised pursuant to any note purchase facility or the issue of bonds, notes, debentures, loan stock or any similar instrument; (d) the amount of any liability in respect of any lease or hire purchase contract which is deemed as a finance or capital lease under the Indian Accounting Standards or such other accounting standards as may be prescribed; (e) receivables sold or discounted other than any receivables sold on nonrecourse basis; (f) any amount raised under any other transaction, including any forward sale or purchase agreement, having the commercial effect of a borrowing; (g) any derivative transaction entered into in connection with protection against or benefit from fluctuation in any rate or price and for calculating the value of any derivative transaction, only the market value of such transaction shall be taken into account; (h) any counter-indemnity obligation in respect of a guarantee, indemnity, bond, documentary letter of credit or any other instrument issued by a bank or financial institution; (i) the amount of any liability in respect of any of the guarantee or indemnity for any of the items referred to in sub-clauses (a) to (h) of this clause"

Thus, 'operational debt' under the Code only covers 4 (four) categories, that is, goods, services, employment and Government dues.NCLT observed that in the present case, the debt had neither arisen out of the provision of goods or services, nor out of employment or the dues which are payable under the statute to the Centre/State Government or local body. The refund and interest sought to be recovered by the Applicants was associated with the delivery of the possession of immovable property, that is, residential flat, which was delayed. The NCLT clarified that the debt, therefore, does not fall within the definition of 'operational debt' as defined under Section 5(21) of the Code.

NCLT deliberated whether the Applicants could be regarded as 'operational creditor' under Section 5(20) of the Code. Observing that according to Section 5(20) of Code, 'operational creditor' is a person to whom 'operational debt' is owed, it was held that since the refund sought does not fall within the ambit of 'operational debt', the Applicants cannot be regarded as 'operational creditor'.NCLT held that Section 9 read with Section 5(20) and Section 5(21) of the Code cannot be construed so widely to include within its ambit even the cases where the dues are on account of advance made to purchase the flat or a commercial site from a construction company, especially when remedy under the Consumer Protection Act and the general law of the land is available.

The application for triggering CIRP was dismissed as the Applicants didn't fall within the meaning of 'operational creditor' as defined under Section 5(20) of the IBC, thereby failing to satisfy the criteria laid down under Section 9 of the IBC for triggering CIRP.

Analysis:

NCLT has provided clarity in respect of the meaning and scope of 'operational debt' and 'operational creditor'. Further, this ruling provides an insight as to which kind of cases will be subject to the Code. Failure to refund money for non-delivery of residential flat or commercial site by a construction company will not fall within the scope of the Code. By way of the present ruling, the NCLT has sought to demarcate the scope of the Code vis-à-vis consumer disputes. [*Pawan Dubey & Anr.* v. *J.B.K. Developers Private Limited* - C.P No. (IB)-19(PB)/2017 – Order of NCLT, New Delhi dated 31-3-2017]

Pendency of winding up petition cannot bar initiation of corporate insolvency process if no order passed or liquidator not appointed

Key points:

- If a notice for winding-up is served to the corporate debtor/respondent company or if the application for winding-up is pending before the High Court and no order has been passed as on date: an application under Insolvency Bankruptcy Code, 2016 (IBC) can be filed with the National Company Law Tribunal (NCLT) without any leave from the High Court.
- The objective of form(s) for statutory notice and application prescribed under the IBC is to provide and incorporate necessary information required under law. The requirement of providing a "notice" is mandatory; however, the form in which such notice is to be given is a matter of procedure and hence directory.

Facts:

The applicant company being the operational creditor was engaged in a supply arrangement with the respondent company i.e. the corporate debtor, for supply of certain diagnostic equipment(s), eye care pharma and vision care products on credit basis through its consignment agent. During the supply arrangement, the corporate debtor began to default on payments towards certain invoices and despite several reminders, the corporate debtor failed to make the payments. This resulted in huge amount of outstanding payable(s) to the operational creditor, which was duly acknowledged by the corporate debtor. Pursuant to this, the operational creditor and the corporate debtor executed an agreement of milestone including a hypothecation agreement, which specifically stipulated that failure to pay any one installment shall give rise to a material default. Consequentially, liability for the entire outstanding amount including for the supplies made till the date of default shall be of the corporate debtor. The inability of the corporate debtor to pay even the first installment resulted in the issuance of statutory notice

under Section 8 of the IBC in respect of which no response was received from the corporate debtor.

While the corporate debtor admitted that response to the notice was intentionally not given and that the outstanding amount payable was not under *"dispute"*, certain objections were raised by the corporate debtor with respect to the maintainability of the application: (i) The statutory notice received by the corporate debtor was not in accordance with the forms prescribed under IBC as well as the provisions of the IBC (Application to Adjudicating Authority) Rules, 2016; (ii) As per the hypothecation agreement, the items supplied by the operational creditor are under its ownership and any dispute arising from the agreement shall be resolved through consultation and ultimately by arbitration; (iii) The corporate debtor's liability to pay the outstanding amount cannot be construed as *"operational debt"* as per Section 5(21) of the IBC; and (iv) An application for winding-up was *sub-judice* before the High Court of Madras and a forensic audit of the corporate debtor was being conducted.

Order of the Tribunal:

The NCLT observed that both the statutory notice and the application were in accordance with the forms prescribed under IBC and rules made thereunder, stating that the said forms were meant to merely provide necessary information required under the law. The NCLT noticed that *'substance'* is more important than the *'form'* coupled with the fact that no irregularity was found between the statutory notice and the application filed by the *"operational creditor"*. In so far as the ownership of items supplied under the hypothecation agreement was concerned, the NCLT noted that it is normal business practice for sellers to have a lien over the goods supplied unless the entire payment is made by the buyer. This does not shift the obligation away from the corporate debtor for making payment towards the *"supply"* of goods. The term *'goods'* as defined under Section 5(21) of the IBC includes machinery/equipment(s), and therefore the outstanding amount owed by the operational creditor shall clearly fall within the purview of *'operational debt'* as defined in the IBC.

Section 9 of the IBC provides for the procedure for initiation of a corporate insolvency resolution process. The NCLT was of the view that the presence of an arbitration agreement between the parties does not bar the operational creditor from filing an application to initiate corporate insolvency proceedings. Similarly, the pendency of a winding up petition cannot be a bar under IBC for initiating the corporate insolvency resolution process, because the High Court has not passed any order for winding up of the corporate debtor and no Official Liquidator had been appointed. Based on the following observations, the NCLT allowed the application and ordered the commencement of the corporate insolvency resolution process which is to be concluded within 180 days. During the said period, "moratorium" as directed under Section 14 of the IBC shall come into effect without affecting the supply of essential goods or services to the corporate debtor. An interim insolvency professional as suggested by the operational creditor to oversee the insolvency process was also appointed by the NCLT.

Analysis:

Although an appeal challenging the said order has been preferred by the corporate debtor before the National Company Law Appellate Tribunal, the present NCLT order for the time being protects the right of the creditor to approach the NCLT and safeguard its interest(s) during the pendency of a winding-up petition. The underlying principle here is that the courts in India shall prefer restructuring by way of corporate resolution rather than winding-up of the entity as an option to settle operational as well as financial debts. [*Alcon Laboratories (India) Private Limited* v. *Vasan Health Care Private Limited* - C.A/1/(IB)/2017, decided on 21-4-2017]

Corporate insolvency resolution proceedings can be initiated for dishonour of post-dated cheques issued by a corporate person

Key Points:

- Issuance of post-dated cheques to any person will amount to acknowledgement of legally enforceable liability;
- Dishonour of post-dated cheques would amount to "default" under the Insolvency and Bankruptcy Code, 2016 ("Code") and can be used as a ground for initiation of corporate insolvency resolution proceedings of the corporate debtor.

Facts:

The Applicant was awarded a contract by the Corporate Debtor, which was completed to the satisfaction of Corporate Debtor. In consideration of the performance of above contract, the Corporate Debtor issued seven post-dated cheques of Rs. 5,23,016 each towards final settlement of the claim of the Applicant. Six out of seven post-dated cheques issued by the Corporate Debtor were dishonoured.

Contentions:

The Applicant relied on the judgment of Kerala High Court in the case of *Dr. K.K. Ramakrishnan Vs. Dr. K.K. Parthasaradhy & another*[4] wherein it was held that *"execution of the cheque is an acknowledgment of a legally enforceable liability and when it is dishonoured the consequences of prosecution and punishment follow"* Therefore, dishonour of cheque would be covered within the definition of "default" as provided in Section 2(12) of the Code and the Applicant would be treated as "Operational Creditor" under Section 5(20) of the Code.

Order of the Tribunal:

The National Company Law Tribunal also relied on the judgement of Kerala High Court in *Ramakrishnan's* case and accepted the contention that issuance of cheque would amount to acknowledging the liability to pay and a failure to pay such liability would amount to "default" under the Code. The Tribunal also satisfied itself of the requirements of Section 9 of the Code for initiation of insolvency resolution proceedings by an operational creditor, *inter-alia* being submission of documents by the Applicant such as, a copy of invoice demanding payment by the Applicant from the Corporate Debtor, affidavit to the effect that there is no dispute between the Corporate Debtor and the Applicant in relation to the outstanding debt, etc.

Analysis:

Unlike the recent decision of the Tribunal in the matter of *Col. Vinod Awasthy* v. *AMR Infrastructure Limited* [5], the Tribunal did not deliberate much on what may be considered as "operational debt" under the Code as the Corporate Debtor had already accepted it's liability of making payment to the Applicant by issuing post-dated cheques in favour of the Applicant. The contract between the Applicant and the Corporate Debtor was also in nexus of the business of the Corporate Debtor, therefore, the Tribunal was satisfied that the Applicant would be an "operational creditor" under the Code. In view of the same, the Tribunal admitted that it is a case fit for filing an application for insolvency resolution process. [*Prideco Commercial Projects Private Limited* v. *Era Infra Engineering Limited* - MANU/NC/0234/2017]

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4 MANU/KE/0175/2003

5 (C.P. No. (IB)-10(PB)/2017 decided on February 20, 2017

NEW DELHI
5 Link Road, Jangpura Extension,
Opp. Jangpura Metro Station,
New Delhi 110014
Phone : +91-11-4129 9811

B-6/10, Safdarjung Enclave
New Delhi -110 029
Phone : +91-11-4129 9900
E-mail : lsdel@lakshmisri.com

MUMBAI
2nd floor, B&C Wing,
Cnergy IT Park, Appa Saheb Marathe Marg,
(Near Century Bazar)Prabhadevi,
Mumbai - 400025
Phone : +91-22-24392500
E-mail : lsbom@lakshmisri.com

CHENNAI
2, Wallace Garden, 2nd Street
Chennai - 600 006
Phone : +91-44-2833 4700
E-mail : lsmds@lakshmisri.com

BENGALURU
4th floor, World Trade Center
Brigade Gateway Campus
26/1, Dr. Rajkumar Road,
Malleswaram West, Bangalore-560 055.
Ph: +91(80) 49331800
Fax:+91(80) 49331899
E-mail : lsblr@lakshmisri.com

HYDERABAD
'Hastigiri', 5-9-163, Chapel Road
Opp. Methodist Church,
Nampally
Hyderabad - 500 001
Phone : +91-40-2323 4924
E-mail : lshyd@lakshmisri.com

AHMEDABAD
B-334, SAKAR-VII,
Nehru Bridge Corner, Ashram Road,
Ahmedabad - 380 009
Phone : +91-79-4001 4500
E-mail : lsahd@lakshmisri.com

PUNE
607-609, Nucleus, 1 Church Road,
Camp, Pune-411 001.
Phone : +91-20-6680 1900
E-mail : lspune@lakshmisri.com

KOLKATA
2nd Floor, Kanak Building
41, Chowringhee Road,
Kolkatta-700071
Phone : +91-33-4005 5570
E-mail : lskolkata@lakshmisri.com

CHANDIGARH
1st Floor, SCO No. 59,
Sector 26,
Chandigarh -160026
Phone : +91-172-4921700
E-mail : lschd@lakshmisri.com

GURGAON
OS2 & OS3, 5th floor,
Corporate Office Tower,
Ambience Island,
Sector 25-A,
Gurgaon-122001
phone: +91. 0i24 - 477 1300
Email: lsgurgaon@lakshmisri.com

ALLAHABAD
3/1A/3, (opposite Auto Sales),
Colvin Road, (Lohia Marg),
Allahabad -211001 (U.R)
phone . +0532 - 2421037, 2420359
Email: lsallahabad@lakshmisri.com

www.lakshmisri.com www.gst.lakshmisri.com
www.addb.lakshmisri.com www.lakshmisri.cn