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Dawn of future watchdog for foreign investment in India

By **Barnik Ghosh and Sreya Bhar**

Foreign investments in India are allowed in two routes; (i) automatic route, and (ii) approval route. Since, there was no approval necessary for the automatic route, several sectors were categorized into the approval route. Prior to the economic liberalization in 1991, it was an extremely difficult and cumbersome procedure to obtain approvals to receive foreign investments in India. The establishment of Foreign Investment Promotion Board (FIPB) in 1991 coincided with the economic reforms that were brought forward in India. The FIPB streamlined the approval route for foreign investments by introducing the concept of a single window approval for obtaining foreign investments.

The task of giving approvals was delegated to the Department of Industrial Policy and Promotion (DIPP) in 1996. Subsequently, in 2003, the authority for approval was shifted back to a newly constituted FIPB under the Department of Economic Affairs (DEA), Ministry of Finance. Over the years, India, in order to cope with the global economy, has liberalized its Foreign Direct Investment (FDI) policies. The number of sectors under approval route has been grossly reduced over a period of time and more and more sectors have been introduced under the automatic route. The automatic route, as on present date, constitutes approximately 10% of the total FDI inflow in the country.

While the industry was ripe with rumors since 2013 that the FIPB would be decommissioned, no active steps were taken with regard to the same. However, in the Budget Speech of 2017, the announcement was made regarding phase-wise abolishment of the FIPB. A future roadmap was proposed to be given by the Government. The immediate aftermath of the same, there was an apprehension regarding inflow of foreign investments under the approval route. The Government had announced the abolition of FIPB to be done over a period of time, and not immediately. It may be worthwhile to note that the Finance Minister had announced that further liberalization of the FDI policy was under consideration, thereby giving an indication to the industries about the future roadmap that the government would undertake.

In such circumstances, there were several speculations whether a greater role would be given to the Reserve Bank of India (RBI) or to the concerned Ministries. It shall be pertinent to note in this regard that in several sectors like mining, telecom, defence, civil aviation, information and broadcasting, etc. the FDI approval could be subsumed by the concerned licensing authorities. In the event, the FDI approval is actually phased out in the near future, then compliance with the relevant provisions of the FEMA will be a part and parcel of compliance with other applicable legislations. Since inflow of foreign funds would get reported to the RBI in any circumstances, an increased monitoring and supervising role of the RBI would be the natural outcome.

In our view, it may be difficult to entrust individual Ministries with the role of the FIPB. This is because there is an apprehension of severe delays by the Ministries in giving approval. This is abundantly clear from earlier experiences of companies obtaining clearances from the Ministries. Moreover, the concerned Ministry, in giving its approval, may not take a macro view of entire economic scenario, but be restricted to its own portfolio and concerns. Furthermore, the stakeholders consultations cannot be completely done away with in any Government approval process and as such, taking views of stakeholders may further delay the process and make it difficult for the Ministry concerned to take a decision. In order to curb these negatives, the FDI policy needs to be further streamlined and liberalized to remove any procedural bottlenecks.

In this regard it may be worthwhile to consider the global perspective regarding the control of foreign investments. In the United States of America (USA), an open investment policy is professed. However, the Committee on Foreign Investments in the US (CFIUS) reviews and blocks any deal which could lead to the control of any USA business by a foreigner that would raise national security concerns. It may be however pertinent to note that the CFIUS does not review majority of the FDI in the USA. In France the investment rules have been made more stringent mandating foreign buyers to get the Economy Ministry's nod of approval to be able to invest in French companies and firms operating in the fields of energy, transport, water, health and telecom. Australia has a legal framework by way of the Foreign Acquisitions and Takeovers Act, 1975 to vet foreign investments coming into the country.

In such circumstances, the Government may consider the enactment of a foreign investment promotion law wherein the issues of national security being affected by FDI inflow need to be addressed. Alternatively, an Expert Committee may be constituted to that effect. From the current framework, the National Security Council chaired by the Prime Minister with the National Security Advisor as the Secretary, may be considered for a greater role in considering the effect of FDI on national security.

We have considered certain issues which may arise due to the disbandment of the FIPB and the same have been discussed hereafter in this article.

- Any investment coming from Pakistan and Bangladesh may be looked into and considered by the Ministry of Home Affairs, irrespective of the sector.
- Foreign Investment made through Mauritius should be continued to be

vetted by the Department of Revenue, which is co-opted as a permanent member of the FIPB.

- The Ministry of Consumer Affairs, Department of Commerce and Ministry of Electronics and IT, need to be given a major role in the absence of FIPB for single brand and multi brand retail. This may severely affect the rate of inflow of foreign investments in the above mentioned sectors. The only possible solution in this regard shall be to completely abolish the FDI approval requirement in such sectors.
- Reporting of downstream investments has to be relooked into in the event FDI approval is itself done away with.
- It has been observed that the approval route for FDI does not always discourage foreign investors. While greenfield pharma sector has been put into the automatic route, no foreign investments have come in. However, brownfield projects which requires FIPB approval, has garnered foreign investments on regular basis.

In such circumstances, the following options are being suggested:

- The enactment of a law on foreign investment promotion law wherein the issue of national security being affected by FDI would have to be addressed properly;
- Increased role and involvement of the National Security Council chaired by the Prime Minister with the National Security Advisor as the Secretary in the matters of national security being affected by the FDI;
- Increased role and involvement of the RBI in supervising and monitoring the inflow of FDI in India, including introduction of the concept of reporting and inspection of downstream investment in the event FDI approval system is abolished.
- Major role to be given to the Minister of Consumer Affairs, Department of Commerce and Ministry of Electronics and IT in the absence of FIPB for single brand and multi brand retail.

In conclusion, we observe that the role of the FIPB, though negligible in the current market scenario is extremely important considering the issue of national security of the country. To quote Justice Bhagwati, *"India should not stand on the crutches of foreign jurisprudence and customs and develop its own jurisprudence and legal practice"*. The role of the FIPB is substantial and the same can be delegated to a national security council or to an expert committee to look into the same. The roadmap to be given by the Government is still a matter of speculation but we expect that the Government shall safeguard the interests of the country and its economy before allowing foreign investments from being routed into the country without any safeguard.

[The authors are Senior Associate and Associate respectively in Corporate Practice, Lakshmikumaran & Sridharan, Kolkata]

Cross-border merger provisions notified

By **L&S Corporate Law Team**

The Ministry of Corporate Affairs (MCA) has notified Section 234 of Companies Act, 2013 (Companies Act), which specifically deals with cross-border mergers concerning merger or amalgamation of an Indian company with a foreign company and *vice-versa*, and has come into effect from April 13, 2017. Under the erstwhile Companies Act, 1956, although a foreign company could merge with an Indian company, an Indian company was prohibited from merging with a foreign entity. The said prohibition was the result of a restrictive definition of "*transferee company*" under Section 394(4)(b) of the Companies Act, 1956, stipulating that a transferee company should mandatorily be a company incorporated under the Companies Act, 1956, whereas a Transferor company could be a body corporate, irrespective of the place of incorporation.

Section 234 of the Companies Act broadly states that the provisions of Chapter XV (Compromises, Arrangements and Amalgamations) shall apply *mutatis mutandis* to cross border inbound or outbound mergers. The MCA, *vide* its Notification dated April 13, 2017, has also amended the Companies (Compromises, Arrangements and Amalgamations) Rules, 2016 (Merger Rules) to insert Rule 25-A (Rule 25-A) dealing with cross-border mergers. Rule 25-A lays down the scope of the application of Section 234.

The conditions for cross border mergers under Section 234 of the Companies Act are as follows: (i) requirement of prior approval from the Reserve Bank of India (RBI); (ii) valuation of the surviving entity to be submitted to the RBI, which report must be prepared as per internationally accepted principles on accounting and valuation prepared by a valuer who is a member of a recognized professional body in its jurisdiction; (iii) provisions of Sections 230-232 to be followed for cross border mergers (thus requiring approval of the NCLT, approvals from shareholders, approvals from creditors (if any), approvals from Securities and Exchange Board of India (SEBI) (for listed companies), sectoral regulators and the income tax authorities); (iv) the scheme of merger may provide for payment of consideration to the shareholders of the merging company in the form of cash or depository receipts or partly in cash and partly in depository receipts; and (v) the foreign company should be incorporated in a permitted jurisdiction, which restriction only applies in case of outbound mergers (i.e. where the surviving transferee company is a foreign company).

Clarity has been provided to the term *'permitted jurisdictions'* listed under Annexure B to the Companies (Compromises, Arrangements and Amalgamations) Amendment Rules, 2017, (Annexure B) which shall mean a jurisdiction where the surviving entity is located being one (i) whose securities market regulator is a signatory to the International Organization of Securities Commission's Multilateral Memorandum of Understanding (Appendix A signatories) or a signatory to a bilateral Memorandum of Understanding with SEBI or (ii) whose Central Bank is a member of the Bank of International Settlements (BIS); AND (iii) a jurisdiction that has not been identified in the public statement of Financial Action Task Force (FATF) as: a jurisdiction having strategic 'Anti-Money Laundering or Combating the Financing of Terrorism' deficiencies to which counter measures apply; or a jurisdiction that has not made sufficient progress in addressing the deficiencies or has not committed to an action plan developed with the FATF to address the deficiencies.

The scope of Rule 25-A does not provide for fast track mergers under Section 233 available to domestic mergers, therefore all cross-border mergers are required to undergo the entire process as laid down under Sections 230-232 of the Companies Act.

To harmonize the scope of cross-border mergers with exchange control laws in India, RBI has released (as on *April 26, 2017*) the Draft Foreign Exchange Management (Cross Border Merger) Regulations, 2017 (Draft Regulations) for public consultation, that prescribes certain guidelines to be followed in case of both inbound as well as outbound mergers. The Draft Regulations state that:

In case of inbound mergers where the resultant company is an Indian company: (i) The issue and/or transfer of securities to a person resident outside India by the resultant company shall be in accordance with Foreign Exchange Management (Transfer or Issue of Security by a Person Resident outside India) Regulations, 2000; (ii) The existing borrowing(s) of the foreign company obtained from overseas sources shall conform to the foreign borrowing norms laid down by RBI; and (iii) The holding of assets outside India by the resultant company because of the merger or the subsequent transfer of assets shall adhere to the Foreign Exchange Management Act, 1999 or rules or regulations framed thereunder (FEMA).

In case of outbound mergers where the resultant company is a foreign company: (i) The acquisition and holding of securities in the resultant company by an Indian resident shall be in accordance with Foreign Exchange Management (Transfer or issue of Foreign Security) Regulations, 2000 or the provisions of the Liberalized Remittance Scheme, as applicable; (ii) The outstanding or impending borrowings shall be repaid by the resultant company as per the scheme sanctioned by NCLT; and (iii) The resultant company can acquire, hold any assets in India or transfer any such assets, as per the permissible limits prescribed under FEMA.

Irrespective of the transaction being an inbound or outbound merger, if such assets or securities held by the resultant company is in contravention of the provisions of FEMA, the resultant company would be required to sell the said assets/securities within 180 days from the sanction of the merger scheme and the sale proceeds to be repatriated to India or outside India, as the case may be.

Although the Draft Regulations are at the stage of public consultation, permitting a resultant company to acquire assets (which it is otherwise not permitted to acquire under foreign exchange laws) pursuant to sanction of a Scheme of cross-border merger, only to require such entity to subsequently divest such assets within 180 days from sanction of the Scheme, may entail unattractive tax and stamp duty implications. As violation of FEMA may entail penalty of up to three times the amounts involved, the feasibility of having a blanket 180-day period for divestment of such prohibited assets also needs to be examined.

To bring parity with Section 248 of the Companies Act, valuation of the merging entities is proposed to be done as per internationally accepted pricing methodology on arm's length basis, which shall be duly certified by an authorized Chartered Accountant/public accountant/merchant banker. All transactions arising due to cross border mergers are proposed to be reported to RBI as required under FEMA. Further, any transaction undertaken in accordance with Draft Regulation shall be deemed to be approved by RBI as required under Rule 25-A.

One important issue in the Draft Regulations is the explanation provided to the definition of "foreign company" which states that foreign company should mean those incorporated in jurisdictions at Annexure B. The term 'foreign company' under the Draft Regulations is used for both inbound and outbound mergers, making applicable the restrictions of permitted jurisdictions under Annexure B to even inbound mergers, in contradiction to what is stated under Rule 25-A.

Although notification of Section 234 is intended to enable cross-border mergers, a host of related concerns remain unaddressed, especially where the surviving transferee entity is a foreign company that acquires and holds business interests and assets in India of an erstwhile Indian transferor entity. Extensive amendments by the legislature and various regulators including by the Insurance Regulatory and Development Authority, the RBI, tax authorities, to name a few, are also required on numerous jurisdictional issues involved in cross-border mergers such as matters concerning recovery of taxes under the Income Tax Act, 1961, social welfare liabilities for employees, and litigations that would be inherited by surviving company, especially in outbound mergers. To protect the interests of various stakeholders involved and effectively operationalize Section 234, this legislative and regulatory void needs to be addressed in parallel. In the absence of such exhaustive legislative and regulatory changes, liberalization of the cross-border merger regime envisioned by Section 234 is not practically workable.

Notifications & Circulars

Voluntary liquidation process of a corporate person – IBBI notifies Regulations: The Insolvency and Bankruptcy Board of India (IBBI), has notified the Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017 on 31st March, 2017, which are effective from 1st April, 2017. The Regulations are in relation to the voluntary liquidation process of a corporate person i.e. companies, limited liability partnerships and persons incorporated with limited liability. As per the Regulations, a corporate person may initiate voluntary liquidation proceedings if majority of its directors or designated partners make a declaration that the corporate person has no debts or if it does have debts, make a declaration that it shall pay them in their entirety from the proceeds of the assets proposed to be sold under liquidation and that the liquidation is not being done to defraud any person. However, if the liquidator opines that the above conditions are not being satisfied, then an application shall be made by him/her to the Adjudicating Authority to suspend the liquidation process.

To be eligible for appointment as a liquidator of a corporate person, an insolvency professional is required to be *independent* of such corporate person (for instance, not be a related party, employee or partner of the corporate person). Liquidators and professionals are required to make complete disclosures, both initial and continual, about any pecuniary or personal relationship with stakeholders of the corporate person. In a step towards making liquidation a time-bound process, a liquidator is required to complete the liquidation process within 12 months from commencement of the liquidation. In the event the process continues beyond such 12-month period, the liquidator is required to present an 'Annual Status Report' indicating the progress made to the contributories (i.e. persons liable to contribute towards assets of the corporate person in the event of liquidation), every year till dissolution of the corporate person.

The Regulations *inter-alia* stipulate the manner and content of public announcement to be made regarding submission of claims by stakeholders, details regarding claims of stakeholders, registers, reports and books of accounts to be maintained (to be preserved for 8 years after dissolution of the corporate person) and submitted by the liquidator, realization of assets and their distribution, etc., to name a few.

Information Utilities Regulations, 2017 notified: The IBBI has notified the IBBI (Information Utilities) Regulations, 2017 on 31st March, 2017 (Regulations), which are effective from 1st April, 2017. The Regulations deal with the registration and regulation of information utilities (IU). As per the Regulations, an IU is responsible for storage of financial information to help scrutinise defaults and verify claims in a speedy manner, thereby ensuring that transactions under the Insolvency and Bankruptcy Code (Code) take place in a time-bound fashion.

Eligibility criteria to register as an IU: A public company with a minimum net worth of Rs.50 Crore is eligible to be a registered IU, provided it meets certain criteria. More than half of the Board should consist of independent directors. The IU, its promoters, directors, key managerial personnel, and persons holding more than 5%, directly or indirectly, of its paid-up equity share capital or total voting power are required to be fit and proper persons. Although a person is not allowed to hold more than 10% of an IU's paid-up equity share capital (with the exception of certain specified entities such as banks, insurance companies, stock exchanges, government companies, etc. that are allowed to hold upto 25% of paid up equity share capital), to begin with, a person resident in India is allowed to hold upto 51% of paid-up equity share capital in an IU during the initial 3-year period from the date of its registration. However, before expiry of such 3-year period, its shareholding must be reduced to 10 or 25%, as the case may be.

An IU is also required to seek prior approval of IBBI for transactions that may result in any person acquiring more than 5% of the paid-up equity share capital/voting power of such IU, or result in change of control, merger, amalgamation or restructuring, voluntary liquidation/dissolution, etc.

IBBI may from time to time, stipulate technical standards *via* guidelines, on matters regarding authentication and verification of information to be stored with IU, registration of users, data integrity and security, etc. The said Regulations also specify that a unique identifier shall be assigned by an IU to each registered user, who has submitted information including records of debt. To protect users' interest, IUs are prohibited from outsourcing their core services to third party service providers and are required to have a grievance redressal policy and exit management plan to enable users to transfer information to other IUs. A compliance officer (CO) is required to be appointed by every IU, who shall ensure that all the requirements and compliances under the Code are met by such IU and a compliance certificate in this regard submitted to IBBI annually.

Merger control exemptions - Expansion of scope: The Ministry of Corporate Affairs, *vide* Notification dated March 27, 2017 (2017 Notification), has expanded the scope of combinations under Section 5 and Section 6 of Competition Act 2002 (Act) which are eligible for an exemption from seeking approval of Competition Commission of India (CCI) based on certain *de-minimis* thresholds, for a period of five years. Previously, as per the MCA Notification S.O. 674(E), dated the 4th March, 2016 (2016 Notification), any enterprise whose shares, control, voting rights or assets were being acquired, was exempted for a period of five (5) years, from filing a notification with the CCI for seeking its approval, if it either had assets not more than INR 350 crores in

India or turnover of not more than rupees INR 1000 crores in India.[1] Although these financial thresholds remain unchanged, the benefit of exemption from requiring approval of CCI, which was earlier available to only certain types of combinations resulting from acquisitions, has now been extended under the 2017 Notification to combinations resulting from mergers, amalgamations and acquisition of control transactions. It may be noted that the 2017 Notification rescinds the 2016 notification prospectively and will not affect transactions entered into before such rescission.

Prior to the 2017 Notification, unless specifically exempted, CCI was required to be notified for all combinations and prior approval was required before effectuating the combination. The CCI would either approve or reject the combination based on whether such a combination would have an appreciable adverse effect on competition as per the provisions of Section 6 read with Section 19 of the Act. A negative effect of this narrow interpretation was that even relatively small-value mergers and amalgamations were required to notify the CCI, adding to costs and complexities of such transactions.

The 2017 Notification further clarifies that the asset value and turnover of only that segment/ portion of enterprise, division or business which is being transferred shall be considered for calculating the thresholds under Section 5 of the Act, instead of taking the transferor's total assets and turnover into consideration.

Furthermore, the 2017 Notification provides the method of computation of asset value and turnover for the purposes of availing this exemption. The value of assets or turnover for availing this exemption shall be determined as below:

(a) by taking the book value of the assets as shown in the audited books of accounts of the enterprise or as per statutory auditor's report where the financial statement has not yet become due to be filed, in the financial year immediately preceding the financial year in which the date of the proposed combination falls;

(b) the value of assets shall be reduced by any depreciation charged on those assets; and

(c) the value of assets shall include the brand value, value of goodwill, value of copyright, patent, permitted use, collective mark, registered proprietor, registered trade mark, registered user, homonymous geographical indication, geographical indications, design or layout design or similar other commercial rights.

Banks permitted to invest in schemes of REITs and InVITs: Previously, banks were permitted to invest in equity-linked mutual funds, venture capital funds and equities to the extent of 20% of their net worth. Expanding the scope of permissible investments within this umbrella limit, the Reserve Bank of India,

[1] Notification No. So 674(E) [F.No.5/33/2007-Cs (Part)], dated 4-3-2016

by its Circular dated April 18, 2017, has permitted banks to also invest in units issued by Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (InVITs), within the overall ceiling of 20% of their net worth for such direct investments, provided banks should not invest more than 10% of the unit capital of a REIT/InVIT, and should have in place a Board-approved policy that lays down an internal limit on such investments.

Ratio Decidendi

Date of listing of target company crucial in determining exemption from open offer obligations under Takeover Regulation 10(1)(a)(ii)

Key Points

- It is irrelevant whether the same promoters were holding the same shares for over a long period either in the target company or in the parent company or both, prior to listing the target company. The only relevant factor is date of listing the target company and the promoter holding filed by the target company as part of the listing agreement.
- The informal guidance provided by an official from the department of Security Exchange Board of India (SEBI) under SEBI's Informal Guidance Scheme, 2003 shall not be construed as an Order from SEBI under Section 15T of the Securities and Exchange Board of India Act, 1992.

In the instant case, the Securities Appellate Tribunal ("SAT") was faced with issues relating to the legal interpretation of Regulation 10(1)(a)(ii) of the SEBI (Substantial Acquisition of Shares & Takeovers) Regulations, 2011 (Takeover Regulations). In terms of Regulation 3(2) of the Takeover Regulations, if a person along with any other person acting in concert, holding shares or voting rights in the target company, acquires additional shares or voting rights more than the prescribed threshold; such person shall be required to make a public announcement of an open offer for acquiring shares of such target company in accordance with these regulations. However, the Takeover Regulations have carved out certain exemptions from the requirement of making open offers, one of which being an acquisition pursuant to inter-se transfer of shares amongst qualifying persons, which includes persons named as "*promoters in the shareholding pattern filed by the target company in terms of the listing agreement or these regulations for not less than three years prior to the proposed acquisition*".

The target company was incorporated on November 9, 2010 and listed on July 30, 2012. Thus, the target company had filed its shareholding pattern in terms of its listing agreement on July 30, 2012. Subsequently, certain inter-se promoter transfers were effected during July to October, 2014 (i.e. when the company had filed the shareholding pattern details for only 2 years post-listing). Given the said background, it was contended by the appellant that Regulation 10(1)(a)(ii) did not stipulate a minimum 3-year post-listing condition, and that the inter-se promoter transfers effected in 2014 were eligible for exemption from open offer obligations. On the other hand, SEBI argued that Regulation 10(1)(a)(ii) clearly and unambiguously mandated that the shareholding pattern filed by the target company in terms of the listing agreement should be available for a minimum of 3 years, post listing.

Thus, the question that arose was whether the period of being disclosed as promoter of the target company, prior to listing of the target company, could be considered for computing the aforesaid period of three years. The SAT answered this question in the negative and has confirmed SEBI's decision in this matter, observing that the 3-year period of reckoning of promoters in the shareholding pattern of a company shall commence from the date of the target company's listing.

Since the appellant had relied on an informal guidance submitted by a SEBI official under the Securities and Exchange Board of India (Informal Guidance) Scheme, 2003 in this matter, the sanctity of such an opinion issued by SEBI official was also brought under the scanner. The SAT concluded that the views/interpretations by an official of SEBI should not be construed as a conclusive decision or determination of any question of law or fact, and cannot be used against a correct interpretation of the law. Such interpretation cannot be binding on the Board of SEBI, neither shall it be considered as an order passed by SEBI. [*Arbutus Consultancy LLP* v. *SEBI* - Appeal No.123 of 2016, decided on 5-4-2017, SAT]

Existence of "dispute" in terms of Section 8(2)(a) of Insolvency and Bankruptcy Code bars initiation of insolvency process.

Key points

- The definition of the word "*dispute*" is not exhaustive but illustrative. A corporate debtor has the right to reject a demand on any sustainable ground other than showing a pending suit, arbitration proceeding or the breach of representation or warranty. The sustainability of such grounds shall depend on the facts and circumstances of each case.
- If the applicant of a corporate insolvency resolution process has already availed an effective remedy, the provisions of Section 10 of the Civil Procedure Code, 1908 shall come into picture and application of corporate insolvency cannot be allowed to proceed.

In the present case, an application under Section 9 (Application) of the Insolvency and Bankruptcy Code, 2016 (Code) was initiated by the applicant(s) against the respondent company for initiating the corporate insolvency and resolution process. Prior to the aforesaid application, an arbitral award had been passed on 9-9-2016 in favor of the Applicant with respect to disputes regarding a lease deed entered between the applicant and the respondent. The Award directed the Respondent to pay accrued rent along with interest and damages, which was subsequently challenged by it under Section 34 of the Arbitration and Conciliation Act, 1996 (Arbitration Act) and was dismissed by an order dated 19-12-2016 (Order). The execution proceedings to recover the amounts due under the arbitral award were filed and are pending before the Delhi High Court.

Pursuant to the above, demand notice(s) were issued by each of the applicant(s)under Section 8 of the Code (Notice), which requires that the *"corporate debtor"* should (i) bring to the notice of an *"operational creditor"* the existence of a dispute, if any; (ii) repay the operational debt, within 10 days of the receipt of demand notice. Upon receipt of the said demand notice, the Respondent(s) filed an appeal under Section 37 of the Arbitration Act against the Order. Simultaneously, the respondents disputed the existence of "operational debt" in their response to the Notice.

The Principal Bench, NCLT dwelled on the definition of *"dispute"* as stated under Section 5(6) to be read with Section 8(2) of the Code and observed that the term "dispute" has been defined under the Code in an inclusive manner, thereby giving the "corporate debtor" the ammunition to contest the demand on any sustainable ground.

A conjoint perusal of Section 8(2)(a) and Section 9(1) of the Code leads to the understanding that the existence of "dispute" shall clearly bar the initiation of insolvency process. The NCLT further observed that the arbitration proceedings are yet to attain finality, since the respondent has the right to appeal against the award within 30 days of the Order, which has been rightly availed by the Respondent. The aforesaid fact(s) coupled with the fact that the applicant(s) have already initiated execution proceeding(s) led the Bench to believe that allowance of insolvency proceedings would result in the promotion of *"forum shopping"*, which is wholly impermissible in law. Based on the above, the Principal Bench at New Delhi dismissed the application. [*Annapurna Infrastructure Pvt. Ltd. & Ors.* v. *SORIL Infra Resources Ltd.* - C.P No. (IB)-22(PB)/2017, decided on 24-3-2017, NCLT]

Territorial jurisdiction of Court when seat of arbitration determined

Key Points:

- Seat of arbitration is akin to the exclusive jurisdiction clause (if specifically stated under the 'Dispute Resolution' clause in an agreement); and
- An exclusive jurisdiction clause (stated in the disputed agreement) will oust the jurisdiction of all other courts.

The Hon'ble Supreme Court (SC) in its recent judgment dealt with the issue of 'exclusive jurisdiction' clauses. Pursuant to a payment dispute between the parties in September 2015, Respondent had issued a payment default notice to the Appellant. Subsequently, the Respondent invoked the arbitration clause and filed petitions under

Section 9 (*seeking interim relief*) and Section 11 (*appointment of arbitrator*) of Arbitration and Conciliation Act, 1996 before the Delhi High Court (Delhi HC).

Delhi HC, by its order dated September 22, 2015 granted interim reliefs by restraining the appellant from transferring, alienating or creating any third-party interests in Appellant's property (*situated in one of its establishment in Chennai, Tamil Nadu*) till the date of next hearing. Further, Delhi HC also appointed an arbitrator stating that the conduct of arbitration shall be in Mumbai. Additionally, Delhi HC held that *cause of action* did not arise in Mumbai. The courts of three territories namely, Delhi and Chennai (*to and from where goods were supplied*), and Amritsar (*registered office of Appellant*) could have jurisdiction on the matter.

Supreme Court however overruled the Order passed by Delhi HC and reiterated that when a seat is designated, it is akin to an exclusive jurisdiction clause. SC ruled that the courts in Mumbai shall have exclusive jurisdiction. SC further stated that a 'seat' is a concept by which a neutral venue can be chosen by parties to an arbitration clause. A neutral venue may not in the classical sense have jurisdiction i.e. no part of cause of action may have arisen at the neutral value, neither would any of the provisions enumerated under Section 16 to 21[2] of the Civil Procedure Code, 1908 be attracted.

Therefore, the very fact that the 'seat' of arbitration is determined would vest exclusive jurisdiction to courts situated in the place where such seat is located. With this observation, SC set aside the order passed by Delhi HC and clarified that the courts in Mumbai shall have exclusive jurisdiction, by virtue of Mumbai being the seat of arbitration. However, SC upheld the interim reliefs granted by Delhi HC. [*Indus Mobile Distribution Private Limited* v. *Datawind Innovations Private Limited and Ors.* – Civil Appeal Nos. 5370-71 of 2017, decided on 19-4-2017, Supreme Court]

Alleged FEMA violation not a valid defence against enforcement of foreign arbitral award

Facts:

A petition was filed before the High Court of Delhi, by the Petitioner in the instant case, Cruz City 1 Mauritius Holdings (Cruz City), a company incorporated under the laws of Mauritius, to enforce an arbitral award rendered under the London Court of International Arbitration Rules (Award), with respect to a dispute arising under a 'Keepwell Agreement' dated 06.06.2008 executed among the Petitioner, Unitech Limited (Unitech), a public company incorporated in India, and Burley Holding Limited (Burley), a wholly owned subsidiary of Unitech, established under the laws of Mauritius.

Cruz City had simultaneously entered into a Shareholders Agreement dated 06.06.2008

2 Section 16 to 21 of CPC deals with the provisions relating to place of suing.

(SHA) with Arsanovia Limited (Arsanovia), a company incorporated in Cyprus and Kerrush Investments Limited (Kerrush), a company incorporated in Mauritius, through which Cruz City and Arsanovia agreed to jointly pursue a real estate project in India ('Project') through their joint venture company Kerrush, which would invest through downstream subsidiaries, into entities engaged in development and construction of real estate projects. The purpose of the SHA was to govern the inter-se relationship between the shareholders of Kerrush. Burley and Unitech, although not parties to the SHA, signed the SHA confirming and accepting specific obligations, since Unitech was a shareholder of Kerrush. It may be noted that, if commencement of the said Project was delayed beyond the agreed upon period:

a. as per the SHA, a 'put option' could be exercised by Cruz City, wherein it could call upon Arsanovia and Burley, to purchase all equity shares of Kerrush, issued and allotted to Cruz City, at a purchase price that yielded a post-tax IRR of 15% on contributions made by Cruz City, and
b. as per the said Keepwell Agreement, Cruz City could call upon Unitech to cause Burley to satisfy the payment due for purchase of the said shares under option (a). That is, payment of purchase price would be liable to be made by Unitech on behalf of Burley.

Award:

Since the Project was delayed beyond the stipulated period, Cruz City called upon the respective parties and exercised the above-mentioned options (a) and (b) by issuing notices. As the said notices were not answered, Cruz City filed two arbitration requests with LCIA – the first against Arsanovia and Burley in respect of the SHA; the second against Burley and Unitech in respect of the Keepwell Agreement. The arbitration Awards were passed in Cruz City's favour, which stipulated that Unitech and Burley shall, in accordance with (a) and (b) mentioned above, pay the pre-determined purchase price for the entirety of Cruz City's equity shares in Kerrush.

Unitech's Contentions pertaining to Foreign Exchange Management Act, 1999 (FEMA):

a. Firstly, that the Award violated FEMA since Unitech had been directed to make payment against the delivery of shares of Kerrush, which was not permissible without the approval of the Reserve Bank of India (RBI), as investment by way of purchase of shares of a foreign entity without conduct of valuation of the shares, was contrary to FEMA.
b. Secondly, that FEMA bars FDI on an assured return basis and therefore, agreements for pre-determined return on equity, were illegal. Unitech claimed that as the SHA was structured in a manner to provide an assured exit to Cruz City from its investment in an overseas company (Kerrush), which had the effect of providing Cruz City with an exit option in the Project. Therefore, it was contended that

in effect, the Award enforcing such agreements violated FEMA and was contrary to the public policy of India.

Decision:

The Delhi High Court observed that the Put Option provided to Cruz City could be exercised only within a specified time period and was contingent on delay of commencement of the Project, i.e. it was not an open-ended assured exit option as sought to be contented by Unitech. The Delhi High Court observed that even if this contention were to be accepted, Unitech could not escape its liability to Cruz City, given that Cruz City had invested in Kerrush on Unitech's assurances.

Here, it is important to refer to RBI Circulars dated 9-1-2014 and 14-7-2014, as per which a foreign investor may exit its investment in India only at a valuation as on the date of exit. Delhi High Court observed that the aforesaid circulars prohibit assured return instruments brought in India under the guise of equity, and that it is doubtful whether these Circulars would be applicable to cases where a foreign investor founds its claim in breach of contract. In other words, if an investment is made on representations which are breached, a foreign investor would be entitled to remedies including in damages, such as in the present case. It was held that enforceability of the Award cannot be restricted merely due to the necessity of obtaining regulatory approval from RBI, which would not approve of the transaction if the said transaction were in violation of FEMA. It was held that the payment of purchase price for the said shares would be made by Unitech on behalf of Burley, as agreed by Unitech under the said Keepwell Agreement.

With regard to the contention that the Award was against 'public policy', the High Court observed that '*contravention of a provision of law is insufficient to invoke the defence of public policy when it comes to enforcement of a foreign award*'. Notwithstanding that Unitech may be liable to suffer consequences for violation of FEMA, to enable Unitech to escape its obligations by not enforcing the Award would be unjust and more destructive of public policy. [*Cruz City 1 Mauritius Holdings* v. *Unitech Limited*, Judgement dated 11-4-2017, Delhi High Court]

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