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Centre for Corporate Law

MONTHLY CORPORATE LAW UPDATES (APRIL, 2022)

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TABLE OF ABBREVIATIONS

ABBREVIATIONS	FULL-FORM
AA	Adjudicating Authority
A&C Act	The Arbitration and Conciliation Act, 1996
CA	Companies Act, 2013
CD	Corporate Debtor
CIMC	Collective Investment Management Company
CIRP	Corporate Insolvency Resolution Process
CLC	Company Law Committee
CoC	Committee of Creditors
IBC	Insolvency and Bankruptcy Code 2016
IPO	Initial Public Offering
KMP	Key Managerial Personnel

TABLE OF ABBREVIATIONS

ABBREVIATIONS	FULL-FORM
NBFC	Non-Banking Financial Company
NFRA	National Financial Reporting Authority
NPCI	National Payments Cooperation of India
NRC	Nomination and Remuneration Committee
PAN	Permanent Account Number
RBI	Reserve Bank of India
SEBI	Security and Exchange Board of India
UPI	Unified Payments Interface

INSOLVENCY AND RESTRUCTURING LAW

JUDGEMENTS

1 Wages/Salaries of those employees/workers who actually worked during CIRP are to be included in CIRP costs

The IBC requires that the payment of salaries and dues of workmen of a CD should not be included in the liquidation costs. There are separate provisions in the IBC to deal with such dues. In the present case, the question raised before the apex court was whether the workmen of the CD were entitled to salaries and dues during the CIRP period.

The apex court discussed the relevant provisions of the IBC in detail and came to the conclusion that the workmen of the CD can be paid if two questions are answered- First, whether the CD was a going concern during the CIRP; and second, whether the workmen actually worked during the CIRP. The apex court opined that the Liquidator should adjudicate these questions within a period of 12 weeks. Also, till the Liquidator adjudicates such a claim, the court directed that the requisite amount should be kept aside for paying the workmen after deciding the two questions.

(Order available here.)

2 Amount Given As 'Share Application Money' Is Not Covered Under Financial Debt [Pramod Sharma v Karanaya HeartCare Pvt. Ltd]

The IBC defines a "financial debt" as a claim in respect of the provision of goods or services which is spent against the time value consideration for money. On the other hand, Share Application Money refers to the amount received by a company from the applicants who wish to purchase its share. The present case dealt with an appeal against the AA's decision which dismissed the application of the creditors to initiate CIRP. The question before the court was whether the share application money came under the definition of "financial debt". The court opined that the share application money cannot come under

INSOLVENCY AND RESTRUCTURING LAW

the ambit of financial debt as there was no debt which was disbursed by the appellant.

(Order available here.)

3 'Resolution Plan can also include a Nil Payment to the Operational Creditors [Genus Security and Allied Service v Mr. Shivadutt Bannanje & Anr.]

Under the IBC, the CoC has full authority to put forward a Resolution Plan which is meant to keep the CD as a going concern. The IBC mentions that no amount should be paid to the operational creditor when the liquidation of the CD is happening. In the present case, the CoC approved a resolution plan, which included no payment to the operational creditors. The question before the AA was whether this plan was discriminatory in nature.

The AA reiterated the importance of the commercial wisdom of CoC with respect to decisions regarding the financial aspects of the resolution plan. In this regard, it rejected the contention that the plan was discriminatory in nature. It was of the view that excluding all the operational creditors from payment was allowed under the IBC according to the waterfall mechanism under Section 53 of the IBC. Therefore, the plan cannot be termed as discriminatory in nature.

(Order available here.)

INSOLVENCY AND RESTRUCTURING LAW

AMENDMENTS

4 IBBI amends Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations 2017

The IBBI has amended the Insolvency and Bankruptcy Board of India (Voluntary Liquidation Process) Regulations, 2017. The amendment seeks to speed up the process of voluntary liquidation timelines for some specific activities undertaken during the process. It will be effective from 5th April 2022.

There are broadly three changes that the Amendment seeks to bring. Firstly, the liquidator shall prepare the list of stakeholders within 15 days from the last date of receipt of claims. Earlier, the deadline for this was of 45 days. Secondly, the liquidator will distribute the proceeds from realization to the stakeholders within 30 days of receiving the receipt. This process used to take 6 months before. Lastly, the period to complete the liquidation process of the corporate person has been reduced to 270 days from the liquidation commencement date after the creditors have approved the resolution under the IBC. Additionally, the deadline for all other cases would be 90 days from the liquidation commencement date. The previous timeline allowed it to extend up to 12 months.

(Amendment available here.)

SECURITIES LAW

AMENDMENTS

1 Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Fourth amendment) Regulations, 2022

The property of an individual who has passed away can be of several categories including securities. The procedure for inheritors of the estate of the deceased person to claim their part of the securities used to take a long time. Previously, the SEBI Rules necessitated a separate nomination process for up to three people in case of death instead of relying on the legal will of the deceased.

With an aim to simplify the procedure, SEBI has notified those transferring securities like shares would require just three documents: - the original death certificate of the deceased owner self-attested by the heir or a copy of one notarized by a public officer, a signed request form of transmission of securities by the nominee/s and a copy of their signed permanent account number (PAN) card. They have also laid down the plan for a contingency in case the person has not nominated an heir.

If the deceased does not have a nominee, holdings till 5 lakhs in physical form or holdings till 15 lakhs in dematerialized medium need a no objection certificate from all legal heirs. They would also require a notarized indemnity bond of appropriate value. SEBI has in fact increased demat limit from 5 lakh to 15 lakh rupees.

(Notification available here.)

SECURITIES LAW

NOTIFICATION

2 SEBI notifies process for paying fees through UPI apps in IPO allotments.

SEBI charges a certain processing fee for every retail investor. SEBI has recently notified that all individual investors can now avail the facility of UPI based payment options to cover the charges. As per the new notification, four categories of relevant IPO investors namely; retail brokers, depository participants, syndicate members and registrars, have to use UPI based payment gateways for allotments amounting to Rs. 5 lakh. Although the NPCI has allotted new limits on UPI payments to just two lakhs. SEBI, however, has acquired special assent for UPI use in IPOs above the payment threshold, wherein investors can now mention their UPI ids right on their application forms.

Order available here.

COMPANY LAW

NOTIFICATION

1 Company Law Committee Report: April 2022

Company Law Committee (CLC) has recently published a report suggesting changes and amendments to the Companies Act 2013. Some of them include expediting the corporate processes, improving compliance requirements, and removing ambiguities from existing provisions. The changes proposed are:-

I. Fractional Shares

Fractional shares refer to a portion of a share lesser than one unit. CLC has recommended that such shares should be issued in dematerialized form. These shares arise because of mergers, issue of bonuses, or rights issue. However, the current lacuna in the law is that there is no provision that regulates the usage of fractional shares. Therefore, the CLC has recommended an amendment in the Companies Act 2013 which would permit the issuance, holding and transfer of equity shares lesser than one unit for a prescribed class of companies. For listed companies, SEBI should be consulted.

II. Distressed Companies

Issuance of shares at a discounted price was prohibited under section 53 of Companies Act 2013. In 2017, however, this restriction was removed; thereby allowing companies to issue shares at a discount to its creditors, when their debt was converted to shares. For distressed companies, it is difficult to raise market capital because the market value of the share is less than the face value of the share. Therefore, the CLC has recommended that Section 53 needs to be amended to allow companies to issue shares at a discount to the Central Government, the State Government, or any such classes of persons notwithstanding the prohibition of Section 53. For this, it was recommended that such distressed companies be categorized as having cash losses for the preceding 3 financial years.

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III. Facilitating E-Enforcement and E-Adjudication

According to Section 398 of the Act, filing of applications, documents, inspection, etc., needs to be recorded in electronic form. But in explanation of proviso clause the filing of penalties like imposition of fines and other pecuniary penalties is not applicable under this section.

Certain adjudication related activities became problematic especially during the advent COVID-19, when all the courts and tribunals were forced to close and function virtually. The CLC recommended the omission of explanation of proviso clause and enable the Central Government to make to make rules for conducting enforcement related actions in a transparent and non-discretionary manner with proper trail through an electronic platform, under the Companies Act, 2013. The deletion of the Explanation proviso to Section 398 to further facilitate e-enforcement and e-adjudication was further proposed for amendment.

IV. Audit Framework + NFRA (National Financial Reporting Authority)

The Companies Act empowers the central government to constitute NFRA to investigate the matter of accounting and auditing standards for companies. The important principle behind the functioning of NFRA is to protect the interest of public, investors, creditors and others who are associated with the companies or body corporate.

NFRA at present can take action on only professional and specific other misconducts. But the CLC recommends that NFRA be given more power so that they can act against non-compliance of Companies Act.

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The CLC recommended that differing classes of committees may be allowed to avail non-audit services from their auditors. Hence, Section 144 of Companies Act, 2013 be amended to prescribe a differential list of prohibitions on availing non-audit services or total prohibition of the same for such classes of companies where public interest is inherent.

The CLC recommends that in order to strengthen the audit framework, the resigning auditor must assure the shareholders and other stakeholders that in his/her opinion there is nothing wrong in the company's account, which needs to be bought to their notice, and that his/her resignation was an independent decision. The resigning auditor must make a detailed disclosure report, which should contain specifically the reason for resignation, e.g., if it is due to non-cooperation from client company, fraud, severe non-compliance, or diversion of funds, etc.

Joint audit implies pooling together the resources and expertise of more than one firm to share responsibility and produce a single audit report. Currently carrying out joint audit is exclusive to company's member. The committee is of the opinion that joint audit should be mandatory to all those companies that have public interest in them. But given the expenses in carrying out joint auditing, the committee is of the opinion that it should be restricted to classes of companies as the Central Government may deem appropriate. And in case of a joint audit, the provision concerning the extent of liability of individual auditors should also be accordingly provided for in Companies Act, 2013.

V. Mergers & Acquisitions Proposals

Treasury share refers to the own stocks of the company and are categorised as assets of the company. During amalgamation of the company treasury stocks increases. The Committee feels that long-term holding of treasury stock is opposed to the principles of shareholder democracy.

COMPANY LAW

It was recommended that companies holding treasury stock will be required to completely dispose of such stock within a period of three years and report back to the central government. Such disposal may take place through sale or reduction of capital without invoking provisions of Section 66 of CA-13, considering the peculiarity of the situation and the fact that there would be no outflow of funds from the company. It was also further noted that in case the company fails to dispose of its treasure stocks within the prescribed timeline, the said shares shall stand cancelled and the share capital of the company shall be accordingly reduced in a manner as may be prescribed.

Section 233 of the Companies Act, 2013 provides for a fast-track merger/amalgamation that may be entered by two or more small companies, between a holding company and a wholly-owned-subsidiary. The threshold demands the approval persons having 90 percent of the total share in the company and not those present in a meeting and casting vote on the same. This threshold is particularly difficult to achieve in listed companies. Further this threshold requirement affects the rights of the minority shareholders' interests.

To make the fast-track merger approval process under Section 233 more robust and simultaneously continue to protect minority shareholder interests, the committee recommends a modified twin test requiring approval by:

·75% of the shareholders, present and voting at the meeting.

·Shareholders to represent more than 50%, in value, of the total number of shares of the company.

Apart from this, the report also makes recommendations to do away with affidavits under the Act, allow companies to hold meetings in electronic and hybrid modes, and to serve documents to their members in electronic form.

(Report available here.)

ARBITRATION LAW

1 SC holds that a Non-Signatory to an Arbitration Agreement can be bound to the Agreement by applying the 'Group of Companies Doctrine'[Oil and Natural Gas Corporation Ltd. V M/s Discovery Enterprises Pvt. Ltd. & Anr.]

The Group of Companies Doctrine states that a non-signatory company can be bound to an arbitration agreement if mutual intention can be seen from amongst the entities within the group of companies.

In the present case, the claimant party had awarded a contract to the sister entity of a company. After the initiation of the dispute proceedings, the claimant party contended that another sister entity of the same company should be compelled to be a signatory to the agreement because the contract had been awarded to the other party on the basic premise that it was related to the sister entity. The question before the apex court was whether the sister entity could be bound to the agreement even though it was not a signatory to it.

The apex court opined that the sister entity which is a non-signatory could be bound to the agreement with the application of the Group of the Companies Doctrine. The court also laid down factors that should be taken into consideration for the application of the doctrine to any case which includes mutual intent of the parties, the relationship of the non-signatory with the party signatory to the agreement and the commonality of the subject matter so concerned.

(Judgment available here.)

ARBITRATION LAW

2 The Scope of Section 9 of the A&C Act cannot be extended to include the enforcement of an Arbitral Award [M/S Satyen Construction v State of West Bengal & Ors]

Section 9 of the A&C Act enables a party to an arbitration proceeding to apply for interim measures for protection before or during the arbitration proceedings. In the present case, the petitioner filed an application under Section 9 of the A&C Act to withdraw the sum deposited by the Respondent upon the furnishing of appropriate security by the petitioner. The respondent contended that the relief sought by the petitioner was beyond the ambit and scope of Section 9. The question before the court was whether the scope of Section 9 of the A&C Act could be extended to enforce an arbitral award in favor of an award holder.

The court held that the scope of Section 9 cannot be extended to the enforcement of the arbitral award or granting the fruits of the arbitral award in favor of the award holder as an interim measure. Moreover, the court added that it cannot permit or allow the withdrawal of the amount so deposited by the award holder, as it would be against the concept of equity.

(Order available here.)

MISCELLANEOUS

RBI ORDER

1 RBI Issues guidelines for compensation of KMPs and senior management of NBFCs

The Reserve Bank of India (RBI) recently issued guidelines for compensation of the KMP and senior management of NBFCs. As per the guidelines, the finance companies have to constitute a nomination and remuneration committee (NRC). This committee will have the mandate to oversee the framing, review and implementation of the compensation policy of NBFCs with the approval of the board. Further, it will also have to work with the risk management committee of the company to achieve effective alignment between compensation and risks. Furthermore, the compensation packages will comprise of fixed and variable pay components aligned effectively with prudent risk taking. The compensation outcomes should be symmetric with risk outcomes and compensation pay-outs have to be sensitive to the time horizon of the risks.

(The guideline can be accessed here.)

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