Centre for Corporate Law

MONTHLY CORPORATE LAW UPDATES (SEPTEMBER,2021)

-INSOLVENCY AND RESTRUCTURING LAW

-SECURITIES LAW

-COMPANY LAW

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INSOLVENCY AND RESTRUCTURING LAW

JUDGEMENTS

1 NCLAT expands the definition of a 'financial debt' [Sree Bhadra Parks and Resorts Ltd. Vs. Sri Ramani Resorts and hotels Pvt. Ltd.]

The instant case, yet again, raises the incessant question as to what falls squarely within the definition of a 'financial debt'. 'Time value of money" is described as the essence of a 'financial debt' and the same has always been a controversial topic under the Code.

The Applicant, in this case, alleged that he was a financial creditor owing to the default committed by the Corporate Debtor under a 'Share Purchase Agreement'. According to the agreement, the Corporate Debtor had expressed its desire to sell 100% of its shares to the Applicant. The Corporate Debtor had defaulted on its promise to repay the advanced sum paid by the Applicant. The Appellate Authority reached an 'inevitable and inescapable cocksure conclusion' that the same is not only a violation of the share purchase agreement but also the due amount falls squarely within the definition of a 'financial debt' under the Code.

(Order available here.)

2 Resolution plans approved by the AA cannot be withdrawn or modified by the Successful Resolution Applicant [Ebix Singapore Private Limited Vs. Committee of Creditors of Educomp Solutions Limited]

One of the most pertinent differences between the 2016 introduced IBC and its predecessors is that the Code provides the much needed 'speedy resolution'. This speedy resolution results in the preservation of the value of the assets of the Corporate Debtor. The Apex Court once again reiterated that the timelines prescribed by the Code are to be strictly adhered to.

INSOLVENCY AND RESTRUCTURING LAW

The Hon'ble Supreme Court held that once a Resolution Plan is approved by the Adjudicating Authority, the same cannot be withdrawn if it complies with all procedural requirements. Providing for such withdrawal forms a part of the legislative policy and if the same is not explicitly provided for, the Adjudicating bodies cannot allow it using the residuary powers under IBC.

The Apex Court also cautioned the NCLT and NCLAT to be more sensitive towards such actions that result in delays and should endeavour to stick to the timelines provided for under the Code.

(Order available here.)

3 NCLAT has no jurisdiction to hear appeals beyond 45 days [National Spot Exchange Limited vs Mr. Anil Kohli, Resolution Professional for Dunar Foods Limited]

Section 61(2) of the Insolvency and Bankruptcy Code ("IBC") allows appeals to be filed before the NCLAT within a period of 30 days. The proviso to this Section allows the Appellate Tribunal to hear an appeal for an additional 15 days if there was sufficient cause for not filing it.

In the present case, there was a delay of 44 days in preferring the appeal beyond a total period of 45 days as prescribed under Section 61(2). While pronouncing the judgement, the Apex Court opined that there may be genuine situations that arise where the party may not be able to adhere to the deadline to file appeals, however, the courts still would not have the authority to carve out exceptions to this provision as it would amount to a legislative function which squarely lies beyond their jurisdiction.

(Order available here.)

INSOLVENCY AND RESTRUCTURING LAW

4 Doctrine of Derivative Action cannot apply in Petition under Section 7 of IBC [M Sai Eswara Swamy vs Siti Vision Digital Media Pvt. Ltd.]

The doctrine of derivative action, also called the shareholder derivative suit, comes from two causes of action, firstly, it is an action to compel the corporation to sue and secondly, it is an action brought forth by the shareholder on behalf of the corporation for redressal against harm to the corporation. Thus, the action is 'derivative' in nature when it is brought by a shareholder on behalf of the corporation for harm suffered by all the shareholders in common.

In the present case, The NCLAT, New Delhi upheld the NCLT's view that a petition under Section 7 of the Insolvency and Bankruptcy Code 2016 ("IBC") cannot be filed without a board resolution from the Creditor's company.

The Appellate Court rejected the argument that the Creditor's acknowledgment of the debt in their balance sheet is enough to maintain the petition. It was opined that the doctrine of derivative action cannot be applicable unless the Company's Board passes a resolution to that effect.

(Order available here.)

5 No 'Success Fees' to Resolution Professionals [Mr. Jayesh. N. Sanghrajka (erstwhile RP of Ariisto Developers Pvt. Ltd. vs The Monitoring Agency nominated by the CoC of Ariisto Developers Pvt. Ltd.]

While the commercial wisdom is granted supremacy under the IBC, the NCLAT held that the approval of a 'success fee' to the Resolution Professional (RP) cannot be brought under the rather wide ambit of the said wisdom.

INSOLVENCY AND RESTRUCTURING LAW

The NCLAT held that the Insolvency and Bankruptcy Board of India (IBBI) has directed that the fees payable to the RP must be 'reasonable'. Further, these costs must be 'directly necessary for the CIRP' in consonance with the values of integrity and independence. The Appellate Court noted that under the Code, the RP to perform his duties with diligence and reasonable care, including incurring expenses and the CoC ("Committee of Creditors") is permitted to fix the expenses to be incurred by the RP which includes his 'fees'.

The Appellate Court held that there must be a prior consultation of minds at the initial stages of the Corporate Insolvency Resolution Process (CIRP) to decide what the reasonable fee is. Moreover, claiming a 'success' fee at the last moment is tantamount to claiming a gift/reward, which is not what the IBBI intends for the RP. The Appellate court also clarified that the term 'success fees' is more in the nature of a contingency, is speculative and not a part of the provisions of the IBC. Therefore, the same is not chargeable.

(Order available here.)

6 NCLAT holds that an amount refunded under a Performance Bank Guarantee is not a part of the Corporate Debtor's Assets [UCO Bank vs. Sudip Bhattacharya RP of Reliance Naval & Engineering Ltd.]

The IBC is a creditor centric resolution mechanism that aims to grant the creditors complete access to the assets of the Corporate Debtor. Every effort is made to expand the said pool of assets that would be managed by the CoC.

The issue, in this case, is whether the Corporate Debtor has any right with respect to the money received from the reversal of invocation of a Performance Bank Guarantee, which had been invoked prior to the initiation of CIRP.

INSOLVENCY AND RESTRUCTURING LAW

A Bank Guarantee is an independent contract between the Creditor and the beneficiary and in the event of any default, the beneficiary would realise the amount under the Bank Guarantee from the Bank and not from the Corporate Debtor. Bank Guarantees are issued for a specific purpose and for a predefined tenure which automatically gets revoked in fulfilment of such purpose or completion of such specified time.

The Appellate Court refused to include the amount refunded from the reversal of invocation of a Performance Bank Guarantee as a part of the Corporate Debtor's assets.

(Order available here.)

SECURITIES LAW

REGULATIONS

1 Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) (Fifth Amendment) Regulations, 2021

Stock exchanges serve as a platform for companies to list their securities. Entities can list securities either of the nature of equity or debt. Stocks or shares of ownership in a company are equity securities whereas bonds or debentures are issued as debt securities. On one hand, while the equity securities provide the investor with a controlling interest over the company, the debt securities are of the nature of a loan, with the investor being the lender.

Listing of any security on a stock exchange entails layers of disclosures. While a thorough framework of disclosures for listing equity securities exists, debt securities lacked the same. In this regard, the SEBI (LODR) (Fifth Amendment) Regulations, 2021 ("the amendment") has brought an overhaul in compliance requirements by debt-listed entities. The amendment imposes a stringent regulatory regime bringing debt-listed entities on par with the equity-listed counterpart.

Some of the key features of the amendment are as follows:

-Introduction of Corporate Governance Compliances

The amendment has made it mandatory for debt-listed entities to comply with provisions of corporate governance. Notably, the provisions of corporate governance did not apply to such entities in the earlier regime. The amendment, pushing corporate governance, makes applicable provisions relating to independent directors ("IDs"), setting up an audit committee, related party transactions and a stakeholder's relationship committee to debt-listed entities. These compliance requirements on the debt-listed entities are similar to those applicable on equity listed entities.

SECURITIES LAW

-Enhanced Disclosure Requirements

When it comes to disclosure requirements, the financial results of a company play a key role. In this light, the amendment requires debt-listed entities to disclose their financial results every quarter as opposed to the previous half-yearly disclosure. The increase in the frequency of financial disclosures may bring greater clarity and transparency. Further, the amendment mandates the debt-listed entities to disclose the composition of the various committees of the board of directors, terms and conditions of appointment of IDs, the establishment of vigil mechanism of insider trading and the policy on dealing with related party transactions on the entity's website.

In conclusion, while the previous regime pertaining to debt-listed entities was scattered, the amendment streamlines a robust disclosure framework. The introduction of corporate governance provisions and enhanced disclosure requirements ensure transparency. Evidently, the amendment seeks to extend provisions of corporate governance, particularly those applicable to equity listed companies, onto debt listed companies. As a result, this corporate governance regime would ensure investor protection by refining the responsibilities of key corporate actors.

(Regulation available here.)

ORDERS

1 SEBI penalises Coral Hub Limited and Directors for fraudulent trade practices

The SEBI (Prohibition of Fraudulent and Unfair Trade Practices) Regulations ("PFUTP") prohibit activities that are fraudulent or unfair in the securities market. Fabricating material information regarding the financial position of a company to mislead investors and shareholders, is in contravention of PFUTP.

SECURITIES LAW

In this regard, SEBI recently penalised Coral Hub Limited ("CHL") for fabricating its financial statement and annual report. SEBI's investigation revealed that CHL employed deceptive devices to inflate sales during Financial Years 2008-09 and 2009-10. This presented a distorted picture of CHL's financial position to its shareholders and the public.

A basic premise on which the foundations of the securities market lies is that the persons connected with it conform to standards of transparency and fair disclosures. In light of the same, the present case reflects fraud by CHL and its directors on the market and investors. Such acts of serious irregularities threaten market integrity. In light of CHL's fraud, SEBI has banned CHL from dealing in the securities market for 3 years.

(Order available here.)

2 SEBI restrains Poonawalla Fincorp MD, 7 others on account of Insider Trading

Insider trading is the illegal act of manipulating a public company's securities on a stock exchange when in possession of confidential non-public information. Such information is known as the Unpublished Price Sensitive Information ("UPSI"). Trading when in possession of UPSI is in contravention of the SEBI PIT Regulations.

In this regard, SEBI recently barred Abhay Bhutada and seven others, who were managing directors of other entities from accessing the securities market. The bar was placed after the eight entities made Rs. 13.58 crore of wrongful gains whilst insider trading in the shares of Magma Fincorp.

Earlier known as Magma Fincorp deemed to be Poonawalla Fincorp after being acquired by Rising Sun Holdings Pvt. Ltd., a subsidiary of Poonawala Finance. SEBI's investigation revealed that Mr. Bhutada transmitted the information regarding the acquisition ahead of its public announcement to the seven others banned.

SECURITIES LAW

Based on the UPSI, the insiders purchased a large volume of shares of Magma Finance, manipulating the shares of Magma Finance.

In its interim ex-parte order, the SEBI imposed a penalty of Rs.13,58,80,440 collectively on all eight entities as it directed for disgorgement.

(Order available here.)

COMPANY LAW

CIRCULARS

1 MCA extends the due date of filing the Cost Audit Report to the Board of Directors

A cost audit is a critical review undertaken by cost auditors to meet a two-fold objective. First, to examine the veracity of the cost accounts of a company and second, to scrutinize whether the statutory procedure pertaining to accounting is complied with. The Companies (Cost Records and Audit) Rules mandate that every auditor must furnish the cost audit report to the Board of Directors within 180 days from the date of closure of the financial year.

While 30 September, 2021 marked the completion of 180 days from the financial year, MCA has extended the last date of filing the cost audit report. Cost auditors can now file the cost audit report to the Board of Directors by 31 October, 2021. The extension was granted in the wake of the representations made by the audit fraternity. The representations highlighted the inability to submit the report within the stipulated time owing to the turbulent impact of COVID-19.

(Circular available here.)

COMPANY LAW

DATA & REPORTS

1 MCA extends the due date of holding AGM by 2 months for the FY 2021-22

The Companies Act 2013, mandates companies to hold an Annual General Meeting ("AGM") every year. Further, companies are required to hold an AGM within six months from the date of completion of the financial year. While 30 September, 2021 marked the completion of six months from the Financial Year 2021-22, the Registrar of Companies may grant an extension to the conduction of AGMs for any special reasons.

In this regard, MCA has extended the date of holding AGM by 2 months. Companies can now hold an AGM by 30 November, 2021. The extension was granted in the wake of representations by companies. The representations, requesting an extension, highlighted the inability to conduct AGMs within the stipulated time owing to the turbulent impact of COVID-19.

(Circular available here.)

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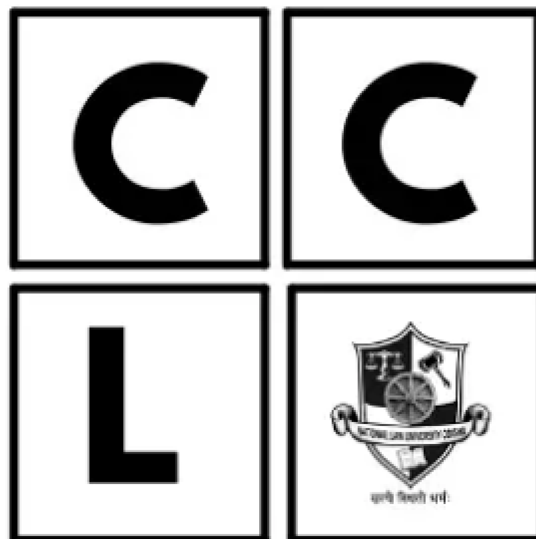

Centre for Corporate Law - National Law University Odisha

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